NEW FORMS OF INTERNATIONAL INVESTMENT: A STUDY OF ALTERNATIVE STRATEGIES TO FOREIGN INVESTMENT

BY

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DECLARATION

No portion of the work referred to in this study has been submitted in support of an application for another degree or qualification in this or any university or other institution of learning.

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ABSTRACT

This study is concerned with recent developments in international investment and the theory of the firm. The proposition that markets and hierarchies are alternative governance structures for completing related sets of transactions is less contentious. Although the literature recognizes that the choice of an appropriate organizational mode is a frontier issue in international business, however, the view that foreign direct investment is the most efficient governance structure, in transaction-cost economizing terms, remains controversial. This research identifies with this contention.

The premise of the study is that the governance structure of foreign transactions cannot be confined to or decided within the framework of hierarchy alone. The study presents a number of market (non-FDI) mechanisms that are being used to accomplish foreign investment transactions. Termed "New Forms of International Investment" (NFI), these strategies involve non-equity (i.e. contractual/ cooperative) and minority-equity arrangements.

Hypotheses concerning the transaction cost nature and the impact of managerial perceptions of several explanatory factors (identified from the literature) were developed and tested using data gathered from a questionnaire survey of executives from 47 UK MNCs, 19 Foreign MNCs (from 6 developed countries), 10 UK MNBs and 21 Foreign MNBs (from 12 developed and 3 developing countries). This was supported by interviews with 26 corporate executives drawn from 12 UK MNCs, 5 Foreign MNCs, 5 UK MNBs and 5 Foreign MNBs.

The results of the research provide evidence that while firm-specific characteristics offer firms opportunities to evaluate their strengths and weaknesses in relation to given overseas markets, host country-specific characteristics provide a complementary platform for assessing the optimum mode of entry. Also, managerial perceptions of the nature and importance of these factors and their impact on the diversification strategy of the firm were found to be significant in entry mode choices. Thus, the greater firms perceived the distortion propensities of potential host countries, the more likely resources, insofar as they would be transfered at all, would be transfered via new forms rather than via hierarchy. There was not much evidence to support the literature contention that the use of the new forms is a particular or general phenomenon of developing countries. In the main, the evidence suggests a correspondence between entrepreneurship or corporate management and foreign investment decisions. The impresssion gained from interviewing selected corporate executives suggests that managerial influences and perceptions are very crucial to whether or not an overseas operation will be embarked upon and, if so, what modality it should take.

PART ONE

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CHAPTER ONE

INTRODUCTION

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CHAPTER ONE

1.1. INTRODUCTION TO THE STUDY

Since the 1960s and 1970s, the very nature of multinational enterprises (MNES) and the general perception of their "power to overcome government restrictions in their pursuit of profits, control of resources, operations, and markets" (Rugman et al., 1986, p. 253) have made conflict with governments and multilateral regulatory agencies inevitable. Within this period also many governments have increasingly realised that any economic arrangement in which the share of the indigenous citizens is no more than supplying cheap labour force or distributing consumer goods imported by expatriate firms is the antithesis of development. With growing political independence, nation states evolve policies that tend to increasingly shift the realms of economic power from foreigners to indigenous inhabitants.

The pattern of foreign investment which has dominated the international scene, and one which has generated much controversy, is foreign direct investment (FDI). FDI has been seen to epitomize the multinationality of international production. It has also been perceived by some host governments as a potential surrogate vehicle for the infusion of 'alien' cultural, political and economic values from their home nations. Alternative investment strategies may have the potentials of mitigating these vast country concerns while providing firms with wider entry options.

The intellectual leadership for this research was kindled by exchange of correspondence with Dr. Charles Oman, Director of the Development Centre of the Organization for the Economic Co-operation and Development. In the event Dr Oman also provided some of the Centre's latest research on the phenomena of interest.

1.2 THE SETTING OF THE STUDY

The contextual background to the study of new forms of investment (NFI) is traceable to international business concern of at least three antecedent kinds. First, Williamson's (1975) "markets and hierarchies" dichotomy of the study of economic organizations is the basis of the argument of alternative governance structures. Under this tradition, the transaction - rather than technology or commodities - is emphasized as the basic unit of analysis, and governance structures, of which firms and markets are the alternatives, are assessed in terms of their capacities to economize on transaction costs (1981a). Over the years, the level of analysis has focused on the efficiency properties and superiority of the firm over other modes of microeconomic organization. For the past decade there has been a growing interest in these modes, both at firm level and macroeconomic level. Assessing the organization of economic activity via alternative governance structures requires that their identity be specified and transaction cost economizing properties be described. This task is one problem with which this study is concerned.

The second antecedent background to this study relates to Dunning's (1977, 1979) clarion call for the need to identify and/or redefine the main forms of international production or resource transfer. Addressing a meeting of European International Business Association in Sweden in 1977, Professor John Dunning stressed the need for a detailed and critical study of alternative modalities of international resource transference. About the same period, Professors Yoram Wind and Howard Perlmutter (1977) characterized entry mode choice as a "frontier issue" in international business. According to Robinson (1978) the problem stems from the fact that few firms actually make a conscious, deliberate analysis of the costs and benefits of entry mode options.

The growing consensus in the international business literature that, in recent years, the boundaries between equity and non-equity or contractual/ cooperative forms of international production have become blurred (Oman, 1984; Dunning, 1981; Hood and Young, 1986) constitutes the third antecedent this study. In particular public policy concern of multilateral bodies such as the Organization for Economic Cooperation and Development (OECD) is critical in the study of new forms of international investment. The OECD, like other multilateral government bodies, has been concerned about the controversy surrounding the behaviour of foreign multinationals, principally Western MNEs, within the North-South context (see, for example, Hyson and Weigel, 1970). The controversy relates to the extent to which the fundamental objectives and operational strategies of the MNEs correspond to, impinge upon, or interfere with host country national goals and aspirations. The magnitude of this controversy and concern led to a meeting of 'international experts' in 1979 under the auspices of the OECD. One of the topics most actively debated at the meeting was that "in the North-South context, FDI was becoming obsolete and being replaced by 'new forms of investment'" (Oman, 1984). In his preface to Dr. Charles Oman's (1984) treatise, Mr Justin Faaland, then President of the OECD Development Centre, stressed the "... importance and timeliness of undertaking a study of the new forms of international investment."

These considerations must be seen as both important and necessary for the reasons stated. However, both the descriptive literature and empirical investigations have concentrated on "new forms of investment in developing countries", apparently because the contextual genesis of the term "new forms of investment" (and of the source of the controversy) is developing countries. While the trend towards new forms may seem to be prevalent in less developed countries (LDCs) perceived to have a high degree of regulation over inward foreign investment, a considerable body of evidence pointing to the increasing use of new forms in the developed countries exists (Janger, 1980; Beamish, 1984, 1985; Harrigan, 1985; Contractor and Lorange, 1987). Thus, the notion that the use of new forms is specifically a phenomenon of LDCs (Oman, 1984; Franko, 1989) must be questionable. Some writers (e.g. Contractor, 1981, 1984; Buckley and Casson, 1985) have looked at the dimensions and empirical applicability of new forms from a wider context, rather than from a North to South perspective.

Furthermore, received theories of foreign investment have largely concentrated on equilibrium analysis of the firm (Teece, 1984) as well as the firm as a production function rather than as a governance structure (Williamson, 1975, 1981b). In both respects, not only are the economizing properties of non-hierarchical modes ignored but, more importantly, the role of entrepreneurship has been grossly suppressed (Teece, 1984). It is only recently that the assignment of transactions between firms and markets in discriminating ways has been acknowledged as the central task of corporate management (Casson, 1985; Buckley, 1989).

A study of the kind envisaged here offers the prospects of integrating entrepreneurship with the dynamics of received microtheory (e.g. the eclectic paradigm) under a transaction cost approach. This requires that the role of corporate management (as decision makers) be made central to the analysis of foreign investment decisions. This in turn requires that management be aware of, and incorporate into entry mode equations, the circumstances limiting or favouring intrafirm (as well as interfirm) transactions (i.e. ownership-specific and internalization-incentive advantages), host country characteristics, and assess the net benefits (or net costs) of using alternative governance structures in a given foreign investment operation.

1.3 THE SCOPE OF THE RESEARCH

This study is concerned with recent developments in international investment and the theory of the firm. Extant foreign investment theories have concentrated on FDI and have been projecting hierarchy as the most economical foreign governance structure. Although the elegance and comprehensiveness of FDI reasoning has provided researchers with a powerful logic (Buckley and Casson, 1976; Caves, 1982; Dunning, 1980, 1981; Hennart, 1982; Rugman, 1981; Teece, 1981, 1985), it is still deficient in some respects as a general institutional framework for deciding the integrity of foreign transactions (see also, Beamish, 1985; Beamish and Banks, 1987).

The premise of this study is that the governance structure of international transactions cannot be confined to or decided within the framework of hierarchy alone. Conceptually and practically, there are a number of alternative modes which firms can, and do, adopt in servicing foreign markets (see Vaupel and Curhan, 1973; Janger, 1980; Oman, 1984, 1986; Beamish, 1984, 1985; Harrigan, 1985; Contractor, 1985; Davidson and McFetridge, 1985; Contractor and Lorange, 1987; Franko, 1989; Welch, 1990). These studies indicate that firms often employ several different modes either separately or simultaneously in entering any particular foreign market of interest.

The focus of this study is on the alternative organizational forms, other than FDI, by which economic enterprises can, and do, sustain international private investments. A growing number of foreign investment activities are being conducted under a mix of market (inter-firm) mechanisms, involving non-equity (i.e. contractual and cooperative) and minority-equity arrangements. The importance of these forms has been kept subliminal either by research design or they were deemed too commonplace to be veritable alternative strategic avenues for sustaining foreign investments. The scope of this study is neither country-specific nor limited to a single component study. In other words, it is not intended to focus on the foreign investment behaviour of a particular country's MNEs nor is it delimited to say licensing or joint ventures. The study is also not limited to or focused on LDCs. The reason is that being an exploratory study, it is intended to elicit factors that should be included in the theorizing and research on the subject of new forms of international investment in general, as economic modes of organizing foreign transactions.

The study is different from previous studies in three respects. The first is the exploratory content just mentioned. Being an exploratory study it is not unique, rather the fact that it is an attempt at investigating empirically the phenomenon of new forms in one study differentiates it from others. As far as published literature is concerned, there has been no empirical study prior to this. Extant investigations have been largely descriptive, relying purely on archival data or anecdotal evidence (e.g. Oman, 1980, 1984a, b, 1986; Dunning and Cantwell, 1982; Franko, 1989). Some represent the subject matter as a complementary chapter of textbooks, again based on archival or anecdotal evidence (e.g. Buckley and Davis, 1981; Rugman (ed), 1982; Buckley, 1983; Ch. 3 in Buckley and Casson, 1985; Casson, 1986; Dunning, 1988 Ch. 6). Other studies which are empirical in nature are single component investigations (e.g. Killing, 1983; Beamish, 1984, 1985; Contractor, 1984, 1985; Harrigan, 1985; Davidson and McFetridge, 1985; Franko, 1989; Welch, 1985, 1990).

The third area of difference is the fact that this study extends the notion of new forms of investment to the banking industry. Both in its present formulation and extant analyses of its dimensions, the term "new forms" has been restricted to manufacturing enterprises. Yet, banks operate in foreign countries via other organizational modes than foreign branch network (which is the FDI counterpart of wholly owned subsidiary of manufacturing enterprises). It is hoped that in these three areas, this study may contribute to an understanding of the ramifications of new forms of investment.

1.4 A TAXONOMY OF NEW FORMS OF INVESTMENT

The various alternative investment strategies are termed 'New Forms of International Investment' (Oman 1984, 1986). The term itself is an OECD concept applied generically to international investments in which foreign held equity is either nonexistent or, where it exists, does not constitute majority ownership. More specifically, new forms encompass: (1) joint international business ventures in which foreign-held equity does not exceed 50 per cent, and (2) international contractual arrangements which may involve no foreign equity participation but the nature of which constitutes an investment, as is the case with licensing, technical assistance contracts, management contracts, franchising, turnkey and product-in-hand contracts, production sharing and risk-service contracts, and international subcontracting (Oman, 1984, 1986).

The new forms are heterogeneous and are better understood by what they are not. Precisely, they are not investments in majority or wholly - owned foreign subsidiaries - which constitute the traditional FDI. They are not portfolio investments either - which are purely financial operations. They are rather characterised by some 'unbundling' of the package of resources that normally accompany hierarchical arrangement. Exporting may be included in the range of methods which may be utilised in penetrating and developing markets abroad.

1.5 OBJECTIVES OF RESEARCH

The main task of this study can be clustered around five interrelated objectives:
(1) To determine the identity, and assess the transactional economizing properties, of alternative (to FDI) modes of internationalization; (2) To integrate the economic theory of entrepreneurship with received FDI theory -namely, the eclectic paradigm, since it incorporates the features of other extant theories - under a transaction cost approach. In essence, to determine the role of corporate management in the internationalization process, using the firm's ownership-specific, internalization-incentive, advantages and host country-specific characteristics; (3) To extend the arguments of the phenomenon of new forms of investment to international banking; (4) To examine the relationship between the stage of country development and the use of new forms of investment; and

(5) To evaluate the policy implications of the findings for (i) the MNE, (ii) the host government, and (iii) multilateral government organizations. The investigation of these objectives entails a wider coverage in scope of the variables affecting new forms than the previous studies, in one study.

1.6 RESEARCH APPROACH

While there may be no universally agreed theory of international investment, economic analysis of FDI have generally relied upon the two main contending theories: the internalization theorem and the eclectic framework. Because both frameworks are tautological in many respects and because the latter (i.e. the eclectic theory) incorporates many of the features of other FDI theories, the approach used in this study embodies the attributes of the eclectic theory as enunciated by Dunning (1977, 1979, 1981, 1988). Beyond the equilibrium analysis of Dunning's static configuration of ownership-specific advantages, internalization-incentive factors and host country-specific characteristics, this study attempts to integrate the economic theory of entrepreneurship into a more dynamic model for explaining the phenomena of interest than had been attempted by previous studies whose approach relied purely on the eclectic or internalization theory. The need for an integrated and/or interdisciplinary approach to the study of foreign investment has been recognized/advocated (Dunning, 1989). In particular, the omission of the role of corporate management in international investment analysis is viewed as a weakness of orthodox theory (Casson, 1985, Ch. 8 in Buckley and Casson, 1985). Earlier, Teece (1984) had observed that an analysis which incorporated the process of entrepreneurship would be of considerable importance to strategic management. The attempt to reflect these concerns in this study may be construed as a useful corrective.

Studies of new forms can be undertaken in either of two ways. One avenue is the single component study approach by which the constituents of new forms (e.g. licensing, franchising, joint ventures, etc) are studied individually or separately. Studies of this kind include the works of Bilkey and Tesar (1977), Wiedersheim-Paul, Olson and Welch (1978), Reid (1981), Cavusgil (1984), and Schlegelmilch (1986) for Exporting; Telesio (1979), Buckley and Davies (1981), Carstairs and Welch (1982), Contractor (1981, 1984, 1985), Davidson and McFetridge (1985), Horstman and Markusen (1986), OECD (1987) and Monye (1989) for Licensing; Walker and Etzel (1973), Hackett (1976), Caves and Murphy (1976), Brickley and Dark (1987), Norton (1988) and Welch (1989, 1990) for Franchising; Killing (1982, 1983), Beamish (1984, 1985), Beamish and Banks (1987), Harrigan (1984, 1985), Connolly (1984), Artisien and Buckley (1985), and Franko (1974, 1989) for Joint Ventures; UNCTC (1982) and Brooke (1985a, b) for International Management Contracts; Wright and Kobel (1981), UNCTC (1983) and Lecraw and Gordon (1984) for Turnkey Contracts; Dicken (1986) and the editorial work of Germidis (1980) for International Subcontracting.

The alternative avenue to the study of new forms of investment is the composite approach by which the new forms are studied as a composite dependent variable. In this respect, two or more strategy variants are investigated in one study. Examples of this approach include the works of Dunning and Cantwell (1982), Oman (1980, 1984a, b, 1986, 1989), Buckley (1983, 1985 Ch. 3 in Buckley and Casson, 1985), Contractor and Lorange (1987), Dunning (1988, Ch. 6) and Young et al. (1989). The approach adopted in this study identifies with this group.

1.7 STRUCTURE OF THESIS

This study is divided into three parts, namely:
(1) Literature Review of FDI theories; (2) Alternative Strategies to Foreign Investment; (3) Research Design, Analysis of Results and Conclusions.

Part One, the Literature Review Section, comprises four chapters. Theories of foreign investment are large, some providing richer explanations than others and some overlapping others. While the limitations of a study of this kind (e.g. length) do not permit an exhaustive review, if at all possible, this part of the study examines the main theoretical candidates and the empirical studies that have been undertaken in relation to them. Theories of new forms of investment may be seen as essentially extensions of the FDI theories: they are derived basically by relaxing some of the restrictive assumptions of orthodox theories.

After this introduction as Chapter 1, Chapter 2 opens the review in a three-part synthesis of foreign investment theories. Chapter two is a review based on (1) the market imperfections paradigm, (2) the product life cycle hypothesis, (3) the oligopolistic reaction hypothesis incorporating the behavioural motives notion, and (4) the currency area phenomenon.

Chapter 3 constitutes another set of theories as section 2. Literature review in this section is based on (1) international diversification, (2) the appropriability theory, (3) the internalization theory, and (4) the eclectic theory.

Chapter 4 concludes the part with an analysis of the Japanese model of foreign investment. Because the Japanese modes of foreign investment have been viewed as distinct from Western style (Kojima, 1973, 1975, 1982; Ozawa, 1979a, b) and because they embody the features of new forms - which are definitely absent in the above theories - it is thought appropriate to examine the theoretical argument of this model in a chapter of its own.

Part two of the study examines the concept of new forms through a review of the alternative strategies to foreign investment. Made up of three chapters (chapters 5 to 7), chapter 5 sets the context of discussion with an overview of corporate strategy and the foreign investment decision process. Chapters 6 is concerned with topical issues in the strategy of international investment as they relate to exporting, licensing and franchising, contractual arrangements, and joint ventures. Chapter 7 concludes this part with a review of the strategic forms of international banking. This review is in the form of an extension of the notion of the phenomenon of new forms of international investment as applicable to non-financial enterprises to the banking industry. This part also summarises the theoretical and empirical studies that have been undertaken in relation to these strategies.

Part three is the empirical part of the study and concludes it as well. It is made up of four chapters (Chapters 8 - 11). Chapter 8 discusses the research design and develops the study hypotheses. It also specifies the need for, and purpose, of the research.

Chapter 9 deals with the research methodology and statistical procedures. It discusses the approaches adopted for field research and the first part of the analysis of the research findings. This is the descriptive phase and is divided into eleven sections, covering the questionnaire administration and data reliability, description of statistical techniques, characteristics of firms (companies and banks) in the survey, and preliminary findings based on the field work.

Chapter 10 presents the second phase of the research findings. Essentially, this chapter is analytical, and is concerned with an in-depth statistical analyses of the research findings. The analyses are based seriatim on the study hypotheses. A comparison of the results is made against relevant previous research findings. The chapter concludes with an overall assessment of the relevance of a number of explanatory variables to the use of new forms of investment.

Chapter 11 concludes both this part and the study. It summarizes the study, draws its conclusions, and presents the implications of the study for the multinational firm (as the principal actor), the host government (as the representative of the recipient country) and multilateral government bodies (e.g. the OECD, the U.N.O., concerned about the behaviour and regulation of MNEs). The study concludes with recommendations for further research.

CHAPTER TWO

A SYNTHESIS OF FOREIGN INVESTMENT THEORIES: SECTION 1

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CHAPTER TWO

FDI THEORIES AND THEORIES OF THE MNE: A SURVEY

SECTION 1

> A theory is...more 'fruitful' the more precise the resulting prediction, the wider the area within which the theory yields predictions, and the more additional lines for further research it suggests.
>
> Milton Friedman (1953, p.10).

1. INTRODUCTION

An appropriate starting point in discussing the applicability of foreign investment theories to the phenomenon of "New Forms of International Investment" (NFI) is to cast the framework in terms of a synthesis of extant theories. The growth of literature on foreign direct investment (FDI) and multinational enterprise (MNE) might have been inspired by the work of Stephen Hymer (1960) published in 1976. The work provoked an immense literature and theoretical developments in the broad disciplines of international business and industrial economics. While many of the studies have expanded and refined Hymer's ideas, his original insights into the relationships of foreign direct investment and the multinational firm have nevertheless remained a convenient reference starting point for analyses.

The theoretical foundation underlying the phenomenon of FDI is as vast as the activity itself. Although reviews of theories of foreign investment and of the MNE abound in the international business literature (Balasubramanyam, 1985; Buckley, 1983, 1985; Buckley and Casson, 1976; Calvet, 1981; Cantwell, 1988; Casson, 1985, 1988; Caves, 1982; Dunning, 1981; Hennart, 1982; and Rugman, 1982), a study of this kind also justifies the need for a critical re-examination of the contending theories. At least, such an appraisal may provide general background for assessing their applicability to emerging trends in international business. Casson (1984) suggests three reasons why a review of the literature on general theories of the MNE is necessary.

The first reason is to demonstrate that, despite the volume of literature on the subject, "serious errors persist undetected in the theory for a long time" (ibid.). This may be due to the general standard of formulating theories in the field, in which the central focus has been on FDI as the essence of multinationalization. The second reason for a review is to cast extant theories within the historical context of trends in the growth of the MNE as well as in the patterns of foreign investment. Such a historical perspective may enhance the understanding and assessment of past and present developments in the field of foreign investment. For instance, several attempts are being made to revise or expand microtheories of foreign investment so as to accommodate emerging trends in corporate practice (see for example, Dunning, 1988; Buckley and Casson, 1985).

The third reason for justifying the need for a review stems from what Casson reckons as "a fundamental incompatibility between economic theories of the MNE and the managerial literature on the subject". The diversity of FDI theories implies the simultaneous existence of competing frameworks for explaining one phenomenon, suggesting therefore that one theory cannot claim to explain it all.

Cantwell (1988) identifies three reasons why there is diversity in the field of international investment theory. Firstly, he contends that each of the various kinds of international investment raises distinctive considerations and each has differential effects on both home and host countries. Accordingly, different theories are expected to be developed to explain these phenomena and are therefore bound to reflect some degree of divergence from each other. The second reason concerns identifying particular theories with the issues addressed and questions asked. Thus, if the empirical concern is with the microeconomic issue of the MNE per se, theoretical emphasis tends to be on Coase's (1937) institutional theory of the firm and its internationalization capacity. If, on the other hand, the interest is on the MNE as an alternative to free trade, theoretical focus tends to rely on markets and hierarchies (Williamson, 1975, 1981; Buckley and Casson, 1976, 1985; Calvet, 1981) or market imperfections (Kindleberger, 1968; Hymer, 1976; Calvet, 1981). The third reason why there is diversity in the theory of international investment relates to the levels of analysis. Cantwell identifies three principal levels: macroeconomic (which examines national and international trends); mesoeconomic (which considers inter-firm interactions at industry level), and microeconomic (which looks at the international growth of individual firms). Each of these requires a different set of theories to explain the phenomena of interest. Because of this growing diversity, Buckley (1985) advocates for theoretical development of the MNE in several directions before it can be seen to be adequate.

2. NATURE OF FOREIGN DIRECT INVESTMENT

FDI, as a mode of servicing a foreign market, is distinguishable from MNE, as an economic entity vehicle. For one thing, FDI is just one organizational mode of servicing foreign markets, albeit the one that offers the firm control over its foreign operations. For another, an MNE does not necessarily imply a foreign direct investor (see for example, Casson 1982; Buckley 1989, p.6). This distinction is important to permit a treatment of FDI as a mode by which firms (large or small) extend their operational strategies abroad.

FDI AS A FORM OF FOREIGN PRIVATE INVESTMENT

FDI can be described as a form of foreign private investment (FPI) which confers control and ownership over a package of resources in a foreign country. Usually, the package consists of embodied or disembodied technology, financial capital, expertise (management, financial and marketing skills), etc. This package is then transferred to a foreign country via the organization of wholly- or majority- owned subsidiary (WOS). Through this mechanism, the firm is able to exercise *de jure* control over the assets. However, control over assets can be obtained without owning them (see, for example, Casson 1985). An investor may hire and exercise control of an asset or may secure a long leasehold on it. Effectively he has acquired *de facto* control over its day-to-day usage, even though he does not own it. On the other hand, the owner of the asset may exercise no control over its daily usage. For example, portfolio investment brings ownership interest but not control. Both scenarios do not constitute FDI by definition because the crucial conditionalities - ownership and control - do not rest in the firm. Therefore, the precise significance of the 'directness' of foreign investment lies in the simultaneous presence of *both* ownership and control over the package of resources in a foreign country (Balasubramanyam, 1985; Casson 1985).

This definition has implications for the nature of FDI. First, ownership is a passive element in FDI. Outright control is an active/crucial element, in the transfer process. It is the bargaining power of the investor in a foreign country. In consequence, the establishment of WOS ensures that the investor can have the necessary control over the resources. It is an internal organizational machinery which potentially mitigates external interference in the firm's desire to maximize the advantages of asset ownership and control.

3. A TAXONOMY OF FIRMS

Another perspective of FDI focuses on firms. It is conventional to associate international investment (or production) with MNEs. Sometimes, it is regarded as the essence of multinationality (Rugman et al., 1986, p.7); hence it has been defined as that financed by FDI (Dunning 1977, 1980, 1982). In order to delineate the boundaries between domestic and international corporations, and hence the novel issues in international management, a simple framework for classifying firms is presented (Table 2.1). It categorizes firms according to their degree of involvement in both domestic and international markets.

Table 2.1 **Classification of Firms According to their Degree of Involvement in International Markets.**

Nature of Firm	Degree of involvement in domestic and international markets.				
	Product Markets	Factor Markets	Foreign Subsidiaries	Debt Capital	Equity Capital
Domestic I	D	D	-	D	-
Domestic II	D	D	-	D	D
Domestic III	I	I	-	D	D
Multinational I	I	I	I	D	D
Multinational II	I	I	I	I	D
Multinational III	I	I	I	I	I

D = High degree of domestic involvement; I = High degree of International Involvement.

Source: Derived from Holland (1986, p.7).

Domestic I type firms refer to sole proprietorships and small family-controlled businesses. The value additivity of these firms to the national economy cannot be ignored; they form a supporting retail market for large firms. A steady growth in the volume of transactions forces a transition to limited liability status. This brings it into the ambit of Domestic II type firms. Business expansion means that the family or private sources of capital may now be inadequate to support growth and competition. This group of firms may be obliged by their limited liability status to approach both money and capital markets for their funding requirements. At this stage there may be no international involvement at all. They correspond to the conventional scope of domestic business and financial management. However, these firms, especially type II, are in direct competition with large firms not only in domestic product and factor markets but also in the market for loanable funds. Medium-size firms (domestic II type) are active distributors of international products in their domestic markets via manufacturers' representation and products intermediation (wholesale activities).

Domestic III type firms correspond to large private and public liability companies. They are active participants in international product and factor markets through importation and exportation. These firms are nevertheless restricted in their capacity to borrow from the international capital markets. The creeping internationalization of this group brings it within the ambit of international financial management problems that ordinarily confront MNEs. Active competition with MNEs in the product and factor markets implies that domestic III type firms may face cash flow problems on existing investments and on new proposals. Second, active participation in the import and export markets brings these firms into contact with the foreign exchange market. This in effect makes them vulnerable to foreign exchange risk exposure. By affecting future cash flows, the value of the firm is thereby affected. The increasing involvement in international product and factor markets results in increasing international experience, acquisition of location-specific knowledge, contacts, etc., and ability to internalize many of the transactions that had ordinarily been consummated via external markets. In particular, if the transaction costs of arm's length markets are becoming high vis-a-vis growing opportunities in the host market, the firm may decide to register its international presence on a more permanent and self-controlling basis by establishing a foreign subsidiary. This is the threshold level of operation of multinational firm type I.

The decision to establish foreign subsidiaries is a major one and marks a dramatic change in the corporate investment strategy. At this stage, the firm appears inexperienced in international capital market operations. The complexity of multinationality dictates caution in the spread of corporate resources as well as in *modus operandi.* The implication is that the firm will require time and corporate adjustment to cope with the incremental problems of foreign production. For instance, in addition to the exposure problems, the firm is now exposed to other vagaries of foreign environment, including different political, legal and socio-cultural systems. In fact, the complexity of the issues involved in managing foreign subsidiaries adds novelty to the task of corporate management such that MNC I firms may be predisposed to continue to rely on domestic financial markets for their capital requirements.

Experience comes with time and involvement. MNC II and MNC III represent varying transitions in corporate organizational growth and maturity, with the latter type firm demonstrating (or completing) the full internationalization process. The foreign exchange implications of financing foreign subsidiaries and the volatility of exchange rates, inter alia, introduce the need to source from international debt markets as well as from unregulated offshore debt markets. At MNC III level, the firm can be regarded as truly universal with its group shares quoted and trading in several international stock exchanges. At this stage, the firm is even able to develop its own in-house treasury and banking operations. Multinationals in this category include Royal Dutch-Shell, Ford Motors, UniLever, British Petroleum, etc. The extent of multinationalization of this group of companies implies that their foreign investment decisions may not just be sophisticated but are intimately related to their global financing, capital structure and capital budgeting decisions.

Incremental international involvement in these markets suggests an organizational metamorphosis from domestic to international hierarchy, and clearly demonstrates the differential strengths and capacities of firms in the strategic choice of form of entering foreign markets.

THEORIES OF FOREIGN INVESTMENT: A SURVEY

SECTION 2

PART 1

BACKGROUND

Two distinct sets of assumptions underlie the theoretical explanations of foreign investment. One set, the neo-classical theory, centres on the orthodox theory of international trade and capital movements with its assumptions of perfect markets. The second set concerns assumptions about imperfections in international economic environment.

1. TRADE THEORY AND ASSUMPTIONS OF PERFECT MARKETS

International trade has historically been a vital component of the growth of nations. It serves as a major source of impetus for firms' international investment operations. International trade, at the firm level, could potentially lead to other modes of sustaining international operations, e.g. licensing, joint ventures and FDI. Up until 1981, both the value and volume of world trade far outpaced those of other modes of international operations (Rugman, et al., 1986, p.24). In 1981 the total value of world trade was about 100,000 times the size of FDI (i.e. US$4 trillion versus $40 billion)(ibid).

Until the late 1950, the received doctrine on international economic development consisted of a well-developed formal theory of international trade and a complementary theory of international capital movements (Dunning, 1988, p.13). Economic concern of international trade theorists was focused more on normative theory of international economic involvement -that is, theorizing on what would occur if certain perfect conditions were present in the world rather than with explanations of the composition of international trade and spatial distribution of economic activities. Essentially, the conditions assume a world of full and costless information, perfect competition, identical technology between trading partners, and no trade barriers.

Trade theory has been criticized in the literature on various grounds, including the unrealistic nature and impracticality of its assumptions. Its inadequacy as an explanatory power of foreign investment thus stems from three disparate factors. First, trade theory - rooted in the Ricardian orthodoxy of comparative cost advantage and Walras-Cassel factor proposition theorem - places emphasis on the differences in the relative costs of production in trading countries as the basis for sustaining trade. The theory sought to prove that differential comparative cost advantage of participating countries was based on international differences in labour productivity, which, in turn, was due to differential national advantages in technology and production functions. This macro-economic comparative cost concept offered little help in explaining the fundamental question of what determines international differences in comparative costs, or "technological inequality between countries" Hood and Young (1986, p.136).

The second limitation is that it did not explain, as it might not have anticipated it, the internationalization of business in other forms than the international movement of goods and capital (Robock, et al., 1977, p.36). Thus, contemporary forms of international business (e.g. licensing, joint ventures, FDI, inter alia) were neither anticipated nor explained by classical and neo-classical trade theorists. The third shortcoming of the trade theory is that it ignores the influence of monopolistic or oligopolistic firms on international trade. Similarly, it explicitly fails to recognize the significant influence of technology, managerial know-how or marketing skills as production functions which can form the basis for comparative advantage (See, for example, Vernon 1974). These limitations stem from the main question which the theory posed (Robock, et al., 1977, p.36):

> Trade theory asks the question, 'Why do countries trade?' This is the wrong question. Businessmen (and women) trade and, increasingly, they transfer goods across national boundaries for their own business activities without selling them outside their organization. The question should be, Why are goods and services transferred between countries?

In summary, trade theory provided the first set of neo-classical assumptions about international trade and capital movements. These assumptions have enabled international economists to develop equilibrium theories about international capital, product and factor markets.

2. ASSUMPTIONS ABOUT IMPERFECTIONS IN INTERNATIONAL MARKETS

The second set of assumptions that form the basis for theoretical explanations of foreign investment involves deviations from the idealism of the neo-classical model, and are about imperfections in international environment. To develop a framework for interpreting patterns of foreign investment (essentially FDI), international economists sought to integrate microtheory of the firm with the macrotheory of international trade and capital movements, the basic premise being that the simple model of the international economy - based on perfect market conditions in which free trade would prevail - was practically non-existent.

The theoretical developments of the market imperfections paradigm are explanatory attempts to answer the following questions:
(1) Why and under what circumstances do firms go international? (2) What operational means do they adopt in expanding abroad and why? (3) What advantages do foreign investors have over indigenous (and other foreign-competitor firms) that enable them to overcome the inherent diseconomies of foreign operations? (4) What locational advantages do countries have that make some the main source, and many others the recipients, of foreign investment? (5) Why do firms choose to internalize transactions rather than operate through markets?
These questions translate into corporate goals of the following general kind:

1. To optimize economic rents from a firm's comparative advantage in rent-yielding assets;
2. To avoid or exploit perceived externalities caused by imperfections in domestic and foreign markets, e.g. absence or failure of arm's length market for knowledge, government-imposed distortions or structural market imperfections; and
3. To meet/service international needs of clients.

Several competing theories have been developed in an attempt to rationalize these goals. For this study, only the major explanatory frameworks will be under scrutiny. The choice is based on literature references and empirical applicability.

The first of these relates to the theoretical development of Hymer (1960) and Kindleberger (1969). The premise of their work was the search for compensating advantage which foreign firms possess that enable them to compete with indigenous firms. Their approach - rooted in the theory of industrial organization in which the firm is viewed as a market agent - can be broadly grouped under the Market-Imperfections Paradigm and includes the works of Kindleberger (1969), Calvet (1981) and product differentiation hypothesis of Caves (1971).

The second group of theoretical developments takes a macroeconomic view and consists mainly of Vernon's (1966, 1971, 1974) early and later versions of the Product-Cycle Model. For continuity, these are discussed under group 1. The third framework consists of Knickerbocker's (1973) Oligopolistic-Induced Hypothesis. The thrust of this model is that the timing of foreign investment is determined largely by firm reaction to competitors' investment strategy. Included in this category is the foreign investment behavioral thesis of Aharoni (1966). The fourth strand relates to Aliber's (1970, 1971) theory of the MNE as a currency-area phenomenon. His is one of the specific frameworks that have not received much empirical support in wider international business studies. The fifth is the macro-economic development approach of Japanese firms enunciated by Kojima (1978, 1982) and Ozawa (1974, 1979, 1982). Their approach bears some semblance of the Ricardian model except that it is couched in absolute advantage terms and does not contain the unrealistic assumptions of Ricardo. Because of the distinctive nature of Japanese MNEs and of their foreign investment behaviour, the discussion will be contained under a separate chapter, chapter 4 as the concluding chapter of this part of the study.

The sixth theoretical development is based on the Risk-Diversification Hypothesis. It is postulated that the MNE is able to provide greater benefits to shareholders (i.e. reduced risk and increased return) through product diversification, size and economies of scale and scope. Included here are the works of Argmon and Lessard (1977), Caves (1971), Lessard (1979) and Rugman (1979). The seventh, termed the Appropriability theory of the MNE, is best represented by the works of Magee (1976, 1977). The central theme of the theory is that MNEs represent the best mechanism to appropriate monopoly rents arising from sophisticated and less imitable technologies.

The eighth - and a well-received one - is the Internalization Theorem. Rooted in industrial organization theory and welfare economics, the internalization concept converges upon the works of Buckley and Casson (1976), Casson (1974, 1987), Caves (1982), Rugman (1980, 1981, 1982), Teece (1977) and Williamson (1975).

The final framework, and one which has also received wide popularity and adoption in a number of research settings, is the Eclectic Paradigm. With Dunning (1977, 1981, 1988a,b,c) as the protagonist, it is a holistic framework which integrates elements of the other theories. These frameworks are discussed below, not necessarily in the order outlined.

2.1 A SYNTHESIS OF MARKET-IMPERFECTIONS PARADIGM

The market-imperfection hypothesis attempts to justify FDI from the perspective of the theory of the market. Earlier explanations of the motive for foreign investment had assumed the existence of perfect markets and perfect competition. According to this theory, FDI is only feasible in the presence of market imperfections. Imperfect market conditions open opportunities for a firm to exploit its competitive advantage in a foreign market.

The conceptual insight of Hymer's work provides the antecedent literature for the market-imperfections framework. In its original formulation, Hymer was interested in identifying the range of structural market imperfections and the role of the firm as an active superseding agent. He emphasizes that the MNE is an active creation of market imperfections and has the ability to use its international operations to separate markets and remove competition, or to exploit an advantage. He makes the following assertions about the MNE:

> ... control of a foreign subsidiary is desired in order to remove competition between that foreign enterprise and enterprises in other countries ... to appropriate fully the returns on certain skills and abilities ... The MNE is a practical institutional device which substitutes for the market. The firm internalises or supersedes the market (1976, p.48).

The market-imperfections paradigm presumes that: (1) foreign firms must possess compensating advantage over indigenous ones to make investments profitable, and (2) the market must be imperfect to enable the foreign firm exploit those advantages. Hymer's conclusions about the structural market imperfections have been flawed on several counts (see for example, Dunning and Rugman, 1985). First, his exclusive concentration on the structural market imperfections viewpoint ignored other forms of market imperfections, such as Kindleberger's (1969) elaboration, Williamson's (1975) markets and hierarchies or Dunning's (1981) micro-economic imperfections. Second, Hymer's objective appeared to be an investigation into why national firms invested abroad, rather than an evaluation of the operations of firms. The concern of modern theory of the firm is not necessarily with the why, but with the how and where of international business - i.e. the way in which foreign investments are organized as well as their locational choice (Cantwell, 1988).

Further, his thesis totally avoids the issues of market hierarchies as efficient replacement structures for imperfect markets. Hymer also neglects the importance of internalization and locational dimensions of the MNE (see Dunning and Rugman, 1975). Kindleberger (1969) refined and expanded Hymer's work. Specifically, he articulated the following taxonomy of market imperfections: (1) Imperfections in goods markets; (2) Imperfections in factor markets; (3) Economies of Scale - creating significant competitive advantage through size; and (4) Government Intervention in free market forces - through imposition of tariffs and non-tariff barriers, taxation, capital market controls, etc.

However, to encompass new developments in the field of determinants of foreign investment, Calvet (1981) proposed a somewhat different taxonomy from that of Kindleberger to distinguish among four classes of imperfections: (1) Market disequilibrium hypotheses; (2) Government-imposed distortions; (3) Market structure imperfections; and (4) Market failure imperfections.

Figure 2.1 illustrates the nature of these imperfections, associated remedial actions and organizational responses.

Figure 2.1 Classification of Market Imperfections, Market-Making Activities and Administrative Response.

Market Imperfections	Market-Making Activity	Administrative Response
Buyer uncertainty due to distance or lack of contact between buyer and seller	Information search through establishment of long-term links, or development of brand name products, or advertisements.	Managerial Control eg. to secure buyer-seller contacts, or to establish brand names through product differentiation.
Inadequate knowledge of reciprocal wants	Information-specificity and informational symmetry	Managerial Control eg. to secure bilateral knowledge of transaction details
Lack of Agreement over transactions and prices	Negotiation	Managerial Control eg. in the employment of bargaining tools
Buyer Uncertainty as to correspondence of goods to specification	Monitoring through quality control measures, warranties and guarantees	Managerial Control eg. in the provision of quality control and other ex post monitoring/ assurance devices
Mutual Uncertainty that restitution will be made for default	Assertive Antitrust Policy	Managerial Control eg. in the provision of contract reparation devices, as in enforcement contracts
Government - imposed distortions, eg. taxes, tariffs etc.	Compliance with government regulations and requirements	Managerial Response to fiscal and other regulatory demands.

Source: Adapted from Casson (1982, 1985).

MARKET DISEQUILIBRIUM HYPOTHESES.

According to the first group of hypotheses, FDI is deemed to be a transitory phenomenon. It is a reactive arbitrage response by firms to short-term disequilibrium conditions in international factor and foreign exchange markets. The notion of market disequilibrium makes the firm the centre piece of analysis. International trade is not only costly in the presence of market imperfections but is also supplanted by internal organization. Short-run disequilibrium conditions in factor and foreign exchange markets both question the validity of trade theory and provide incentives to invest abroad. Currency overvaluation, national differences in rates of return on real assets, national differences in labour costs, and national variations in technology markets, are aspects of this trend. However, this kind of short-term market imperfection does not seem to fit into the strategic nature of corporate FDI decisions. FDI is a long-term phenomenon, and would, for that matter, not be transitory as this group of determinants tends to suggest, a point acknowledged by Calvet himself.

GOVERNMENT-IMPOSED DISTORTIONS HYPOTHESES

This group of imperfections encompasses cases where government intervention policies distort, destabilize or cause disequilibrium in the markets and therefore create profit opportunities. Government disruptive policies/practices are many and varied, and can take place in product, factor, foreign exchange or, in domestic markets. Tariffs, import quotas, foreign exchange controls, wage policies, immigration regulations, national differences in tax regimes, differences in national foreign investment policies, and inter-firm trade unions, cartels , and inter-national unions (e.g. EEC, OPEC, etc.) are some of the many forms of governments' erosion of the free market forces.

Induced unnatural market imperfections (Rugman, et al., 1986, p.104) engender unstable conditions apt to foster foreign investment. This group of imperfections provides two reasons for inward foreign investment. Firstly, the raising of tariffs, other trade barriers (eg. quotas) and non-trade barriers would make external firms' exports more expensive. Secondly, production within the economy would provide access to a large protected market. The common feature of this group of hypotheses is that they are not transitory in nature. There is no market machinery which would correct the disequilibrium caused by government distortions, so as to vitiate the incentive for foreign direct investment. The scenario would conceivably arise were all governments to harmonize their policies or have none at all (Calvet, 1981).

Government-induced disruptions also encompass market imperfections of country or political risk or uncertainty of the firm's environment. In these instances, the ability of the firm to identify the constraints for corporate strategic choices and the ability to circumvent (or exploit) them through the mechanism of its internal markets largely depend on other conditions. For example, corporate perception of the degree of host government interference and its impact on the profit potentials of the market or on its overall global strategy may be important considerations in the foreign investment decision making. This in turn may depend on such other factors as size of the market, operational presence of competitor firms or their perceived strategy as well as firm-specific countervailing advantages (e.g. formal/informal linkages with the political machinery, as may often occur in third world countries, or complexity of the firm's operation and its importance to the macro-economy, especially where the host country lacks the necessary technology and technical manpower). Such monopolistic or oligopolistic advantages provide incentives for FDI.

MARKET-STRUCTURE IMPERFECTIONS HYPOTHESES

This group of imperfections refers to instances where micro-economic entities deviate from perfectly competitive market behaviour because of their power or potentials to intervene in (or interfere with) market pricing mechanisms. This explanatory approach to FDI, is rooted in the industrial organization theory.

Oligopolistic/monopolistic behaviour leads to two inter-related situations: first, it constitutes entry barriers and thus prevents market competition, and second, it offers the few firms opportunities to maximize growth and profitability through speculative interdependencies (Calvet 1981; Holland 1986, p.102). The first situation - entry barriers - can arise through product differentiation in the home market which offers an incentive to go abroad. Caves (1971) discusses the case where *product differentiation* in the domestic market can lead to control of knowledge in servicing the market. Such product control, he argues, can be transferred to foreign markets at little or no cost provided such protective means as patents and copyrights exist.

2.2 PRODUCT LIFE CYCLE HYPOTHESIS

Another important contribution to the oligopolistic feature of FDI is the *product life cycle hypothesis* enunciated by Vernon (1966, 1979). While Caves' product differentiation hypothesis helps to explain why barriers to entry/competition are essential in oligopolistic market structures (industries), Vernon's model incorporates features of the second situation, namely, the interdependence of firms in the industry. In this case, foreign investment is seen as a natural reaction to the threat of losing markets - an interdependent market response - as the firm's product matures.

Vernon characterizes FDI as a by-product of a sequence of events regarding a firm's product: a life cycle of a product from its initial launch in the home market, through stages of maturity and standardization - at which point it may be profitable to launch it in a foreign market - to its eventual decline. In its original formulation, the life cycle of a product is conceived into three stages. The first stage marks the product's novelty: it is produced by the innovating firm in its domestic market where its market profile is also established. This stage is marked by high export demand of the product, especially in high level income countries of Europe. In the second stage, maturity in production technology coupled with growth in demand, necessitates long production runs. This phase witnesses increasing competition from similar products in the domestic market and rising costs of production. Both of these factors raise the prospects of FDI. The third stage is characterized by standardization of the product as well as its production technology, loss of exclusivity of rights, diminishing domestic profit margins and increasing domestic costs of production and marketing. All of these combine to induce the innovator-firm to seek overseas production so as to exploit lower costs of production abroad and to capture the remaining rent from the product's development.

In its original form, the model has the virtues of simplicity and directness: it offers partial explanation to US investment in other advanced countries (essentially UK and other Western European countries) and the phenomenon of offshore production in low-labour cost countries (Buckley 1985). However, the predictive utility of Vernon's initial model could not justify recent developments in global foreign investment activities. Firstly, it was a framework designed to provide explanation for the early post-war expansion of US investment into Europe (Hood and Young, 1986 p.61). Secondly, the initial model appears to be essentially a defensive strategy in which the US innovator-firm is induced by (i.e. reacting to) the threat of losing its domestic market by moving abroad to reduce production costs and thereby prolong the profitable life of the product (Holland, 1986, p.102). Thirdly, the intense competition of European and Japanese MNEs in international markets can no longer be satisfactorily interpreted within the framework of the original version of the hypothesis. Above all, the programmatic decision process of the theory is an oversimplification of the complex structure of the problems facing the MNE and of its decision-making process (Buckley and Casson, 1976, p.77). Besides, its applicability is restricted to highly innovative industries.

Vernon (1971, p.65) admits the redundancy of the 1966 product cycle model when he calls it "a deliberate simplification of reality" with no pretence of capturing "the complex sociological, political and idiosyncratic factors" influencing the foreign investment behaviour. Thus, its power to explain FDI phenomenon has weakened (Vernon, 1979). To correct these shortcomings, the scope of the product cycle hypothesis has been modified and amplified several times (Vernon 1971; 1974; 1977; 1979). The new version is largely based on the analysis of competitive interaction in international markets, with emphasis now on the oligopolistic structure in which most MNEs operate and create barriers to entry by prospective entrants (Buckley and Casson 1976, p.77; Buckley 1985).

2.3 OLIGOPOLISTIC REACTION HYPOTHESIS AND FDI

The third scenario within the market-structure imperfections paradigm is an extension of the defensive investment strategy initiated by the product cycle theory. Developed by Knickerbocker (1973), this hypothesis states that FDI is a function of oligopolistic reaction. It implies that in oligopolistic industries, once one firm undertakes FDI, other competitors follow with defensive direct investments into that market. Knickerbocker argues that the follower-firms are motivated by a desire to counter any competitive advantages that the initiating firm may score from its FDI.

Knickerbocker tested this 'follow the leader hypothesis' by constructing an entry concentration index (ECI) for 187 large US MNEs. He found that the initial investments of US MNEs in a given market are 'bunched' in time and that this bunching showed a greater tendency towards more oligopolistic industries. He compared his ECI across industries (using the US industrial concentration index) and found a significant positive correlation between the two indices. He also found that profitability of FDI was positively correlated with bunching (i.e. entry concentration). He thus concluded that increased industrial concentration causes increased oligopolistic reaction in FDI, except at very high levels, where the oligopolistic structure is stable and firms are able to avoid the overcrowding of a host market.

The problem with Knickerbocker's hypothesis is that his analysis of FDI as a function of oligopolistic reaction is self-destructive, in that the advantages scored by the initial (US) FDI are neutralized by the responding foreign investment activities of other countries' (e.g. Canadian, European and Japanese) MNEs in the respective host markets (Agarwal, 1980). There is thus a vicious circle trend in the oligopolistic reaction theory: increasing FDI leads to increasing international competition via the process of oligopolistic reaction, vice versa. A corollary of Knickerbocker's hypothesis is that this self-limiting oligopolistic reaction should lead to a decline in the flow of FDI.

MARKET FAILURE IMPERFECTIONS

The first three groups of market-imperfections paradigm concern market disequilibrium hypotheses, government-imposed distortions, and market structure imperfections. The last strand of market imperfections is characterized by deviations from the technical assumptions that underlie perfect markets; that is, perfect market assumptions about production techniques and commodity properties (Calvet, 1981). Essentially, market failure imperfections refer to situations where it is not possible to create a market in knowledge. Knowledge in the context of exchangeable commodity takes the form of technical and managerial know-how.

Calvet identifies three types of imperfections which lead to market failures. The first type encompasses those phenomena which forestall efficient allocation of resources via external markets, known as EXTERNAL EFFECTS. The second type, termed PUBLIC GOOD EFFECTS, refers to the failure of an external market to price knowledge efficiently. The last type, called ECONOMIES OF SCALE EFFECTS, refers to those characteristics which create disequilibrium in the relationship between social efficiency and market performance.

External effects, include a range of environmental factors which are exogenous to the firm. These are generally classified into economic, noneconomic, and governmental variables. The MNE can practically do little to make fundamental changes in the economic, political, social, and cultural environment within which it operates (Rugman, et al., 1986, p.100). Apart from host country external effects, MNEs are also confronted by those externalities that originate from their home countries.

The next category of market failures concerns the nature of knowledge as a public good. A commodity is deemed a public good if the consumption of it by one party does not debar other parties from consuming it. Examples include public roads, parks, bridges and schools. An externality exists in them when the consumption actions of one party have effects on other parties who are not charged (or compensated) via the price mechanism. Any time property rights are invested in them or established to overcome externality (ibid. p.106), they lose their public goods image characteristics and thus become private goods. The common feature of private goods is the presence of a regular market to price them. For example, private goods such as cars, radios, watches, apples, bread, etc., can be priced in a regular market. A public good, such as knowledge, public road, bridge or school cannot be priced in a regular market, although privatization can create an arbitrary assignment of property rights over them. Because of absence of efficient market mechanisms to price knowledge, profit-seeking firms attempt to reap rewards for their private investment by acquiring property rights over it. Additionally, the idiosyncratic nature of firm-specific knowledge in conjunction with competitive disadvantage likely to result from dissipation or leakage actively induces firms to internalize rather than contracting out.

Thus, the absence of arm's length external markets for knowledge leads to internalization (of the markets) within the firm, the firm's objectives being: (1) to provide channels for the transfer of this knowledge at lower costs than via external modes; and (2) to reduce the possible leakage or dissipation of this knowledge to competitors.

2.3.1 BEHAVIORAL MOTIVES FOR FOREIGN INVESTMENT

Conceptually, the decision to extend corporate investment beyond national borders is not a simple one: it results from a complex process that has incremental dimension to that conventionally met in a domestic setting. The decision is governed by a wider and more complicated set of considerations: some economic, some behavioral, and some strategic. It is difficult to isolate one from the other in an international context. The behavioral approach is principally associated with the work of Aharoni (1966). According to Aharoni, foreign investment is affected by two sets of motives: external stimuli and managerial stimuli. External stimuli motivate serious search for overseas opportunities. Individual managerial goals potentially lead to a pursuit of 'undesirable projects'. In effect, the proposensity to invest abroad depends on the strength and frequency of these stimuli in conjunction with the way management reacts to them (i.e. converts them into investment decisions).

Ex hypothesi, Aharoni argues that the behavioral approach is not a search for profit opportunities, as suggested by the profit maximization model of the firm (see, for example, Cyert and March, 1963; Stevens, 1974). But the 'serious search for overseas opportunities' have profit maximising potentials. Clearly, if project opportunities offering returns significantly above the cost of capital were not identified, then managerial behaviour could not be reconciled into profit maximization. In effect, Aharoni's analysis of foreign investment as a behavioral process is broadly consistent with the profit maximization hypothesis (Buckley and Casson, 1976, p.81; Hood and Young, 1986, p.96). Dunning (1973) characterizes his refutation of profit maximization as "a confusion of ends and means"; the behavioral process he describes is not, in general, incompatible with the rational choice in profit maximization.

2.4 FOREIGN INVESTMENT AS A FUNCTION OF DIS-EQUILIBRIUM IN THE FOREIGN EXCHANGE MARKET.

An important facet of the market imperfections paradigm is disequilibrium in the foreign exchange markets. This theory is particularly associated with Aliber (1970, 1971) and deals with the influence of currency areas on foreign investment decision. Essentially, the MNE is viewed as a 'currency area phenomenon'. The advantage of operating in a particular currency area is one which is not specific to particular firms but to all firms based in that area. According to Aliber, MNEs with access to international financial markets have an advantage over local firms. He argues then that FDI can take place even if the market for alternative modes (e.g. licensing) is perfect.

Aliber's hypothesis depicts the role of foreign exchange rate in foreign investment decisions. While currency fluctuations may influence the timing of FDI and might well have predicted the direction of the post-war expansion of US MNEs (to Europe from the 1950s through to the early 1970s), a number of criticisms have been levelled on the currency area hypothesis (see, for example, Buckley and Casson, 1976).

First, his analysis of FDI is based on the transitory nature of disequilibrium conditions in the foreign exchange markets. Yet, such a short-run feature is not consistent with the strategic context within which the integrity of FDI is decided. Second, his assumption that investors are unable to adjust the risk of a firm's foreign earnings is inconsistent with the notion of efficient market hypothesis. Third, while Aliber's theory offers explanation to the existence and direction of FDI between currency areas, it does not explain FDI flows within the same currency area, as for example, the investment of UK firms within sterling area (Buckley and Casson, 1976, p.71; 1985, p.6; Agarwal, 1980). Further, it offers little or no explanation to cross-investment between currency areas (ibid), nor does it explain the reluctance of large MNEs in maximizing profitability in foreign investment by capitalizing on such investors' ignorance.

SUMMARY AND CONCLUSION

The purpose of this chapter is to present a brief survey of the literature on the conceptual issues of foreign investment and multinationality as a prelude to a brief review of the theories of foreign investment. The chapter is divided into two sections. Section 1 deals with some conceptual and background issues which form the basis of the issues with which Section 2 is concerned.

The theoretical foundation underlying the phenomenon of foreign direct investment is as vast as the activity itself. Several reasons account for this, including changing structure of modes of foreign investment, divergence in backgrounds of antecedent literatures from which the theories are derived, and divergence of the issues addressed. Most of the available literature on international investment has focused on FDI. The precise significance of the directness of foreign investment lies in the simultaneous presence of both ownership and control of the package over resources in a foreign country. In order to establish the boundaries between domestic and international firms, a framework for classifying firms is developed. It categorizes companies according to their degree of involvement in both domestic and international markets, and allows an identification of the novel issues posed for corporate management.

Section 2 brings the objective of this survey in perspective. It is the first part of the survey of foreign investment theories. Two distinct sets of assumptions underlie the theories of investment: assumptions of perfect markets under the trade theory and assumptions about imperfections in international markets. Because the trade theory is impractical by reason of its assumptions, its utility in explaining FDI is grossly impaired. Accordingly, theoretical focus has shifted to the market imperfections paradigm.

Several competing theories have been developed in an attempt to explain fdi phenomenon. At least nine major theories can be distinguished: (1) Market Imperfections Paradigm; (2) Product Life Cycle Hypothesis; (3) Oligopolistic-Induced hypothesis; (4) Currency-area phenomenon, (5) The Japanese model, incorporating features of 'new' forms; (6) Risk-Diversification Hypothesis; (7) Appropriability theory; (8) Internationalization theory, and (9) Eclectic theory.

This chapter centred on the first four theoretical frameworks. According to the first group of theories, FDI is only feasible in the presence of market imperfections. Under the product life cycle model, foreign investment is seen as a natural reaction to the threat of losing markets as the firm's product matures. The third set of hypotheses states that FDI is a function of oligopolistic reaction - a kind of 'follow the leader' defensive strategy. Included here is the behavioral hypothesis which postulates that FDI is motivated by external stimuli and managerial behaviour. Finally, foreign investment is thought to be a function of disequilibrium in the foreign exchange market. This strand of thought views the MNE as a currency area phenomenon.

CHAPTER THREE

A SYNTHESIS OF FOREIGN INVESTMENT THEORIES: PART 2

CONTENTS

CHAPTER THREE

INTERNATIONAL DIVERSIFICATION AND FOREIGN INVESTMENT

SECTION 1

3.1.1. BACKGROUND

A plethora of market imperfections, which weaken incentives to engage in international diversification, has been reviewed in chapter 2. These were seen to manifest in both goods and factor markets, and range from imperfect correlations between national capital markets through environmental uncertainties and government-imposed distortions to transaction costs. The imperfections also constitute barriers to free trade as well as inhibit private international real assets investment.

At the same time, extant studies suggest that the potential for investment benefits (in terms of risk reduction and/or improved returns) through international diversification is large, but that investors exploit it only to a limited extent. Because the capacity of individuals and small firms to engage in 'home-made' (that is, self-conducted) international diversification is constrained (by these market imperfections), a large literature has developed to examine ways by which investors can circumvent the obstacles and simultaneously achieve the benefits associated therewith. One mechanism which is claimed to be a potential surrogate vehicle for individual international asset diversification is the multinational company (MNC).

The intuitive appeal of the MNC in this regard is attributed to three main factors. First, multinationals are claimed to be diversified internationally in their real cash flow streams, and can, for practical purposes, serve as a proxy for foreign asset investment (Grubel, 1968; Levy and Sarnat, 1970; Rugman, 1979; Rugman, et al., 1986, p.430). Second, the MNC is seen as a more efficient institutional mechanism for overcoming many of the market imperfections than the private investor (Rugman, et al., 1986). Finally, individual (as well as institutional) investors can secure international diversification benefits at a much lower transaction cost by investing in the shares of a multinational (Rugman, 1979).

The object here is to review the literature in terms of matching internal governance structure of the MNE with the attributes of diversification. Achieving this starts critically with the rudiments of diversification strategy. The context of this review and the intuition behind it has been sketched as section one. Section two sets out the rudiments of diversification, including the various forms in which it is pursued. Applications of its dimensions to risk reduction through foreign investment conclude the discussion in section three.

SOME RUDIMENTS

To diversify assets, means to spread investment/resources over several enterprises, markets, products or services. In an international context, this involves a combined set of operations, including sales, location of production facilities, raw material sources, and financing base. Diversifying a firm's operations internationally predisposes management to recognize the occurrence of a disequilibrium and to react competitively (Eiteman and Stonehill, 1982, p.195).

An active diversification strategy may permit the firm to make marginal shifts in sourcing raw materials, intermediate, or finished products. Or, if there is idle or spare capacity, production runs can be stretched in one plant with demand elasticity, thus curtailing costs in unproductive ones. Alternatively, the firm can step up its global marketing efforts where the disequilibrium condition has rendered its products more price competitive. In all of the conceivable scenarios, the observations of Eiteman and Stonehill are instructive:

> Depending on management's risk preference, a diversification strategy permits the firm to react actively or just passively to opportunities presented by disequilibrium conditions in the foreign exchange, capital, and product markets. Furthermore, such a strategy does not require that management predict a disequilibrium condition but only recognize it when it occurs (ibid.).

The foregoing contrasts with undiversified domestic firm. The difference is this: although the pure domestic firm might experience the full impact of international disequilibrium conditions (eg. foreign exchange effect even though it does not have foreign currency cash flows), the firm is not predisposed to react to it in the same manner as a multinational counterpart, simply because it lacks comparative information from internal sources (ibid., p.196).

3.1.2 PARADIGMS OF DIVERSIFICATION

Two major types of diversification can be distinguished: (1) portfolio and (2) real. The dimensions of the latter include horizontal, vertical and conglomerate diversifications. To appreciate how and why this distinction leads to differential forms of foreign investment, a brief consideration of each type may be insightful.

PORTFOLIO DIVERSIFICATION

The investment distinction here is that portfolio or financial investment is not matched with control. Generally, it takes the form of debt or equity, implying a commitment of financial capital to a foreign locale with no controlling interest in the foreign facility. To the extent that it involves a low level of commitment (and control), portfolio investment warrants lower transaction costs than direct investment, where ownership of a controlling interest accompanies high level of commitment. Given that firms would prefer to have a controlling interest in their foreign investment operations, what benefits are then derived from foreign portfolio investment?

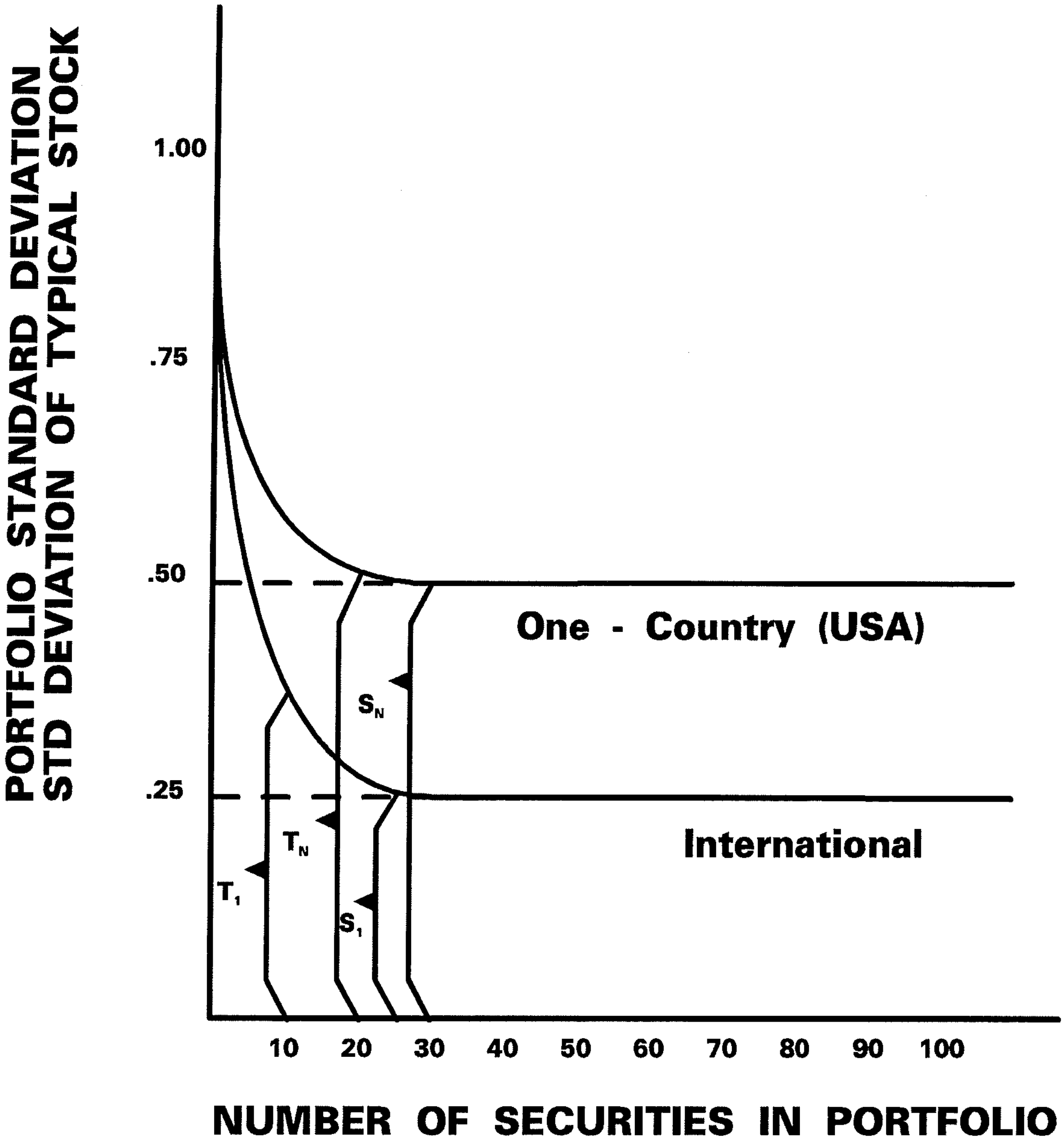
Foreign portfolio investments are important especially for firms operating extensively internationally (Daniels and Radebaugh, 1986, p.16). They are used primarily for financial purposes, by which firms with extensive international operations routinely transfer funds from one currency area to another to secure a higher yield on short-term investments (ibid). Broadly speaking however, modern portfolio investment offers improved risk versus return performance in comparison with a domestically diversified portfolio (See, for example, Grubel, 1968; Levy and Sarnat, 1970; Lessard, 1976; Rugman, 1979). Incentives for internationally diversified portfolio investment arise as transactions become progressively risky in the domestic market relative to returns. Conceptually, when diversification is extended across national boundaries, a substantial proportion of the risk which is systematic within each country can be diversified (Lessard, 1977). Lessard demonstrates this, as illustrated in Figure 3.1, by comparing the risk reduction through diversification within one country (U.S.A.) to that obtainable through international diversification

As Figure 3.1 shows, both the total portfolio risk (T_N) and the systematic risk (S_N) in a single-country case drop to T_I and S_I, respectively, through international diversification. Lessard shows the drop to be about one-third less than a single-country (U.S.) figure. This drop in portfolio risk is attributed to the fact that returns on diversified single-country portfolios display considerable independence as opposed to the correlations between returns on internationally diversified portfolios (Solnik, 1974; Lessard, 1973, 1976).

Most available evidence suggests that a considerable proportion of the investment risk which is systematic within a country can be diversified away internationally. Empirical evidence further suggests that the potential for such risk reduction through international diversification is even greater for Less Developed Country investors. In short, there is less uncertainty about the relevance of diversification motive to FDI. What is less certain, though, is the extent to which financial diversification motive *per se* is a sufficient, albeit a necessary, incentive for FDI.

Indirect evidence - the likes of Grubel (1968), Levy and Sarnat (1970), Hughes, et al. (1975), Lessard (1973, 1977), and Argmon and Lessard (1977) -at best provides international market judgement, suggesting that investors recognize the international diversification provided by MNCs through their firms' security price behaviour. It may be argued therefore that, beyond mere financial or portfolio motives, firms seek to secure international diversification in 'real' assets, the reason being that corporate international diversification in real assets provides a more strategic incentive and competitive advantage for multinationality.

Figure 3.1 Risk Reduction Through National and International Diversification



Source: Lessard, D. R. (1977) *International Diversification and Direct Foreign Investment* in Eiteman, D. K. and Stonehill, A. I. (ibid) pp. 274-287

T_1 & T_N = Total Risk Reductions through diversification: national (one-country) versus international cases

S_1 & S_N = Comparative Systematic Risk Reduction Profiles in national versus international diversification

INTERNATIONAL DIVERSIFICATION IN REAL ASSETS.

The second category of international diversification relates to pursuit of risk reduction and, ultimately, multinational expansion via diversification in goods and factor markets. Economic theory distinguishes three main types of real asset diversification: horizontal, vertical, and conglomerate diversifications.

A firm is said to be *horizontally diversified* if it produces the same product/s or provides the same service/s in several different plants or locations, regardless of whether these are in the same geographic region or not (Buckley and Casson 1976, p.20). Examples of firms in this category include soft drinks giants such as Coca Cola, and Pepsi Cola, international hotel chains such as Holiday Inn and Sheraton and financial services industry (e.g. banks and insurance companies).

Vertical integration, on the other hand, is the case where the firm produces intermediate products which are either complementary or correspond to different stages of the same production sequence. Typical examples are found in the oil industry where, for instance, exploration-drilling-refining-marketing (filling-stations) operational/ownership sequence seems to offer multinational oil companies allocative efficiency. The idea is to avoid or overcome potential factor distortions that may be induced at the various intermediate stages of the firm's global operations (See, for example, Williamson, 1975).

The last category, *conglomerate diversification*, seems to be the most complex pattern and epitomizes universal multinationality. It is represented by MNCIII in Table 2.1. A firm is 'conglomerately diversified' if it produces in more than one production sequence. The capacity to engage in this form rests upon the firm's internalization advantages of general management skills, or "upon the pursuit of portfolio gains of the kind realised by a mutual fund" (Pearce, 1983). Examples of conglomerates include, Royal Dutch/Shell, BP, ICI, and most Japanese MNEs.

3.1.3 DIVERSIFICATION, RISK REDUCTION AND THE MNE.

The object of this concluding part is duo-fold. First, it sketches the relationship between diversification and multinationality. Second, it reviews diversification in the context of risk reduction through foreign investment. It is observed straight away that the complementarity of diversification and multinationality, on the one hand, and diversification and risk reduction, on the other hand, makes any conceptual separation difficult.

DIVERSIFICATION AND MULTINATIONALITY

Broadly speaking, each of the economic paradigms of diversification can provide opportunities for achieving multinationality. However, while portfolio diversification may provide firms with some exploitable ownership specific advantages, "they do not seem to be sufficiently important to be other than permissive factors in foreign investment" (Hood and Young, 1986, p.52). Multinationality by diversification can be achieved via incremental process or through the establishment of wholly owned foreign subsidiaries.

As an incremental strategy, the firm may move rapidly into some foreign markets and gradually increase its commitments. This could be pursued through contractual modes (e.g. licensing or turnkey contracts) or via cooperative modes (eg. joint ventures or other strategic alliances). In these cases, both multinationality and international diversification can be achieved without establishing wholly owned foreign subsidiary. Table 3.1 illustrates product/market conditions which may determine the kind of diversification approach firms may adopt. The concentration strategy approach involves strong commitment and competitive position in one or few markets before moving into other foreign locations. Both forms are, however, varying degrees of operations in the diversification spectrum, the adoption of any one or combination being determined by, *inter alia*, transactional considerations.

Table 3.1 Product/Market Factors Affecting Choice of Diversification.

	PRODUCT/MARKET FACTOR	Prefer 'Simple' Diversification if:	Prefer 'Concentration Diversification if:
1.	Sales response function	Decreasing/Concave	Increasing/S-Curve
2.	Growth rate of each market	Low	High
3.	Sales stability in each market	Low	High
4.	Competitive lead time	Short	Long
5.	Spillover effects	High	Low
6.	Need for product adaptation	Low	High
7.	Need for communication adaptation	Low	High
8.	Economies of scale in distribution	Low	High
9.	Programme control requirements	Low	High
10.	Extent of constraints	Low	High

Source: Ayal, I and J. Zif (1979), "Marketing Expansion Strategies in Multinational Marketing", Journal of Marketing, Vol. 43, Spring.

Incentives for multinationality via diversification increase as transactional considerations and firm-specific advantages merge towards a hierarchical governance structure. For example, imperfections in markets for technology or other real factors of production provide strong incentives for multinationalism. Further, the possession of firm-specific advantages has been shown to motivate diversification and foreign investment (Lessard, 1977; Dunning, 1979, 1980, 1987, 1988; Rugman, 1980, 1981, 1982). Two advantages of product differentiability and managerial capacity (Caves, 1971, 1985; Buckley and Casson, 1976, 1985, 1989) are specially significant in the equation of diversification and multinationality.

3.1.4 DIVERSIFICATION, RISK REDUCTION AND FOREIGN INVESTMENT

Empirical investigations into the benefits of risk reduction by international diversification began with Grubel (1968). Subsequent efforts include Levy and Sarnat (1970), Solnik (1973), Lessard (1973, 1977), Hughes, et al. (1975), and Argmon and Lessard (1977). The focus of these studies was on financial assets (bonds and equities). Although they provided evidence about the benefits of risk reduction by international diversification, they however ignored the effect of real assets diversification and associated benefits. Their evidence has been described as "indirect at best" (Lessard, 1977) because they were based on financial assets.

Exceptions to the above began with Severn (1974) who first applied the diversification principle to foreign direct investment. Lloyd (1975) quickly followed, then came Rugman (1975, 1976, 1977, 1979, 1980). Rugman extended Lloyd's work by distinguishing between international diversification in financial assets and international diversification in real assets. Rugman made the analysis within the framework of international trade. Under international trade theory financial diversification is referred to as portfolio investment, while real diversification is termed direct investment (Rugman 1979, p.21). This framework enables Rugman to argue that direct investment is not motivated by financial variables but rather undertaken through the specific mechanism of the MNE.

Modern portfolio theory postulates that the investor is risk-averse, and will choose that portfolio which minimizes risk (see, Markowitz, 1970). However, this theory has been used with limited success to explain diversification of individual shareholdings by industry or by country, and diversification of financial asset holdings (Buckley and Casson, 1976, p.82).

The arguments against the theory of portfolio choice are the same as those which challenge the ability of individuals to engage in 'home-made' direct investment. In the main the objections centre on market imperfections (discussed in chapter two). These make it transactionally inexpedient for small or individual investors to engage in international investment.

The complex twin tasks of reducing risk through international diversification, on the one hand, and achieving foreign investment, on the other, can be seen as one of "transaction-cost economics" or " the economics of organization" (Williamson, 1975, 1979, 1981a). Under this proposition the central role of the firm is to economize on transaction costs, using its internal organization. In the absence of markets for firm-specific advantages (Rugman, 1979, p.35), the internal organization becomes a potentially useful corrective for real assets diversification, risk reduction and foreign investment.

Unfortunately, the modelling apparatus of received microtheory (i.e. the capital asset pricing model - CAPM) is insufficiently microanalytic to deal with international risk dimensions and other transactional considerations (including problems of externality) associated with foreign direct investment, for the reasons already discussed. Besides, the absence of international risk-free asset, one of the variables assumed in CAPM, questions its applicability.

3.2 THE APPROPRIABILITY THEORY

The appropriability theory of the MNE derives from, and consolidates, a dichotomy of constructs: the industrial organization framework and the neoclassical concept of appropriability of returns from private investment in knowledge. Under the former stream of thought, the MNE is portrayed as a more efficient governance structure for accomplishing transactions than arm's length market. Such a configuration facilitates empirical attempts to assess the purposes served by hierarchical modes of organization. This perspective owes its origins to the antecedent contributions of Coase (1937), Simon (1957, 1961, 1972), Chandler (1966) and Williamson (1975). The second stream of thought is embedded in the public goods nature of knowledge first identified for the MNE by Johnson (1970) and Magee (1976, 1977a,b).

Magee's work consolidated both views under the appropriability concept and brought same to the fore as an explanatory power of FDI or multinationality. Essentially, the MNE is characterized as a specialist in the creation and dissemination of knowledge (technology). Magee distinguishes five stages by which the MNE generates knowledge or information: new product discovery, product development, creation of the production function, creation of market for the product, and appropriability (1976). The basis of the theory is that, because of market failure, or more generally organizational failure (Williamson, 1975), MNEs resort to internal organization in servicing foreign markets. Through this avenue the MNE can ensure greater appropriability of the private returns to its investment in new knowledge. The argument is that research and development costs of knowledge are high, moral hazard problems are posed under markets; therefore, internalization offers opportunities of recovering costs and avoiding risk of dissipation and associated competitive disadvantage. The argument of using patent system to protect the appropriability of private returns is thereby suppressed by FDI proponents.

SECTION 3

3.3 THE INTERNALIZATION THEORY

> ... it is argued in this study that the existing theories are basically subsets of the *general theory of internalization* ... Internalization is a synthesizing explanation of the motives for FDI ... The process of internalization explains most *(and probably all)* of the reasons for FDI ... It is now time to recognize that internalization is a *general theory* of FDI and a *unifying paradigm* for the theory of the MNE (Rugman, 1980, with emphasis mine).
>
> Modern economic analysis of the multinational enterprise relies heavily on the theory of internalization. This book is firmly with the tradition of internalization theory .... This is effected by taking the modern theory of the MNE - which encapsulates most of the insights of internalization theory ... (Casson, 1987, p vii).

3.3.1 SOME BACKGROUND

The internalization concept derives from Commons-Coasian institutionalistic perception of the internal organizational structure of the firm as an alternative efficiency (ie. cost-economizing) mechanism for completing a related set of transactions. Williamson (1975) expanded and brought modern day realism to this economic thought. He synthesized their works and those of other antecedent contributors (see Table 3.2) into the *Markets and Hierarchies* dichotomy of economics of organization, which regards the transaction as the basic unit of analysis and holds that an understanding of transaction cost economizing is central to the study of organizations. However, Williamson restricted his analysis to the domestic context, and addressed the economics audience, *in stricto senso*. It was Buckley and Casson (1976) who first applied the transaction-cost approach to the study of multinational enterprises and the phenomenon of foreign direct investment. Since then several researchers have addressed themselves to one or another of the theoretical issues surrounding the internalization concept. These include Hymer (1976), Dunning (1977), Teece (1977), Rugman (1980, 1981), Caves (1982), Rugman ed. (1982), Casson (1984, 1987), Buckley and Casson (1985, 1989) amongst others.

However, the internalization theory, in its present formulation and popularity as a general paradigm of FDI, has been advanced by Rugman (1980, 1981, 1982), and, in a rather less extravagant but persuasive way, by Casson (1982, 1984, 1985, 1987). This is exemplified in the above affirmative remarks. Considering therefore that transaction-cost economizing is central to the internalization approach, it is not surprising that it features prominently in propositions that favour internal organizational structure as a pre-eminent mechanism for accomplishing international investment. The transaction cost approach to the study of organizations is wide, basic to the arguments of this study, and has been discussed in greater detail by Williamson (1975, 1979, 1981a, b). Only issues of a specific kind are addressed here.

Table 3.2 summarizes the major antecedent literatures and future developments expected in the transaction cost theory cum internalization theory. The basic premise of the relationship between transaction cost theory and the internalization concept can be summarized as follows: (1) The proposition that the firm is a production function to which a profit-maximization objective has been assigned is less illuminating and self-limiting (Williamson, 1981a). (2) The economic world is circumscribed by a plethora of market imperfections which, for practical purposes, impair the efficient completion of transactions through autonomous market mechanisms. (3) Arising from 2, environmental factors in combination with a related set of human behavioral factors prospectively impede exchanges between firms (i.e. across a market). (4) In consequence (of 2 and 3), the external arm's length market is costly and inefficient for completing certain types of transactions. (5) The transactional sources of market failure describe both the transactional limits of the market and the costs associated therewith. (6) In consequence (of 4 and 5), the firm is an institutional response to varying degrees of externality, and hence a superior mechanism for accomplishing a related set of transactions than alternative governance structures, in transaction-cost economizing terms.

The above propositions are informed by growing international consensus (in economics and international business) that contemporary developments in international activities and spread of the MNE have followed the path of an assessment of the operations of the internal market of the firm (Buckley and Casson, 1976, 1985; Casson, 1979, 1984; Rugman, 1980, 1981, 1982; Williamson, 1975, 1979, 1981a,b). This assessment is facilitated by the organizational failures framework (Williamson, 1975). Within this framework there is a general perception that the frictions associated with market modes can be prospectively attenuated by shifting transactions into the firm.

Table 3.2 SOME ANTECEDENTS AND FUTURE DEVELOPMENTS

AUTHOR/YEAR	ORIGIN	MAIN OBJECT OF ANALYSIS
Commons 1934	Industrial/Institutional Economics	Significance of transaction costs for economic analysis
Coase 1937	Industrial/Institutional Economics	Nature of the firm and significance of transaction costs
Hayek 1945	Industrial/Institutional Economics	Economic institutions and role of knowledge
Arrow 1964	Industrial/Institutional Economics	Economics of market failure and transaction costs
Barnard 1938	Industrial Organization	Attributes of human factors and the rationality of internal organization
Simon 1947	Industrial Organization	Limits of the organization man and the rationality of internal organization
Chandler 1962	Business History	Strategy of MNEs and hierarchical forms of business organization
	CONTEMPORARY CONTRIBUTIONS	
Caves 1971	Institutional/Industrial Economics	Economic Analysis of MNEs and Market imperfections.
Williamson 1975	Institutional/Industrial Economics	Source and Nature of transaction costs and their role in markets and hierarchies
Dahlman 1979	Institutional/Industrial Economics	Role of transaction costs and externality in economic exchange
Buckley & Casson 1976	Economics and International Business	The MNE and Internalization
Rugman 1980	International Business	The MNE and Internalization
	FUTURE DEVELOPMENTS	
?	?	Operationalization of transaction costs in both firms and markets
?	?	Explanation of alternative governance structures and their boundaries
?	?	Explanation of how markets and hierarchies boundary changes

This is accomplished by either creating a market for the firm's products/services where none already exists and/or substituting arm's length market with a unified governance structure (i.e. the internal market). This ability is presumed to attenuate (1) environmental factors of uncertainty and small-numbers exchange relations, and (2) human factors of bounded rationality and opportunism, that lead to prospective market failure (Ibid.).

3.3.2 A PRELIMINARY STATEMENT ON TRANSACTIONAL CONCEPTS

Explicating the relation between these transactional concepts - bounded rationality, uncertainty/complexity, opportunism, small-numbers bargain, information impactedness and atmosphere - is rather long and involved, as Williamson himself acknowledges (1975). Suffice it however to observe that:

1. *Opportunism* is an extension of the conventional assumption that economic agents are suboptimal in their organizational relationship, by reason of miscandour or dishonesty, but also self-interest seeking with guile (Williamson, 1975, 1979, 1981). It is a moral hazard problem that obtains under an "ecology of micromotives" (Schelling, 1971).

2. *Bounded rationality* is a human behavioral problem of limited competence which affects the capacity of the "organization man" to deal with complex economic situations, in particular complex exchange relations as in contracts. The term does not connote irrationality. Instead, although boundedly rational agents experience limits in formulating and solving complex problems, they otherwise remain "intendedly rational" (Williamson, 1975).

3. *Small-numbers exchange relations* obtain under monopolistic and/or oligopolistic market conditions. In these situations opportunistic propensity is almost inescapable due to lack of competitive (large-numbers) exchange relations arising from market thinness, sensitivity to tradeoffs, uncertainty/complexity, bounded rationality, opportunism, or information impactedness.

4. *Information impactedness* refers to asymmetric informational relationship between parties to an exchange relation. It is a market condition, by reason of the above factors, in which one or more parties to a transaction possess superior (or inside) knowledge about the true underlying circumstances of the transaction, the knowledge of which cannot be costlessly discerned by or divulged to others, or, if obtained, might be too late for the party to adjust *a posteriori*

5. Under conditions of *uncertainty/complexity*, parties to an exchange relation possess insufficient knowledge of the transaction, profit functions or constraints facing each other.

6. *Atmosphere* refers to a condition which provides for attitudinal interactions and systems consequences that are associated therewith. These factors are illustrated in Figure 3.2; they can be seen as causing friction in exchange relations. Friction results in transaction costs which, in turn, affect the governance of contractual relations.

The object of transaction cost analysis is to supplant the usual emphasis on technology with an assessment of the comparative costs of completing transactions or a related set thereof under alternative governance structures (ibid). The central focus of the theory is transaction, and, in particular, the differential cost of transacting in markets and hierarchies (firms).

3.3.3 NATURE OF TRANSACTION COSTS

From Commons and Coase to Williamson, and from Buckley and Casson to Rugman (Table 3.2), a deeper understanding of the nature and ramifications of transaction costs has progressively emerged with the conclusion that markets do not function costlessly, but rather are circumscribed by a range of externalities termed transaction costs. The relevance of externalities lies in the fact that it is they that ultimately indicate the presence of transaction costs (Dahlman, 1979).

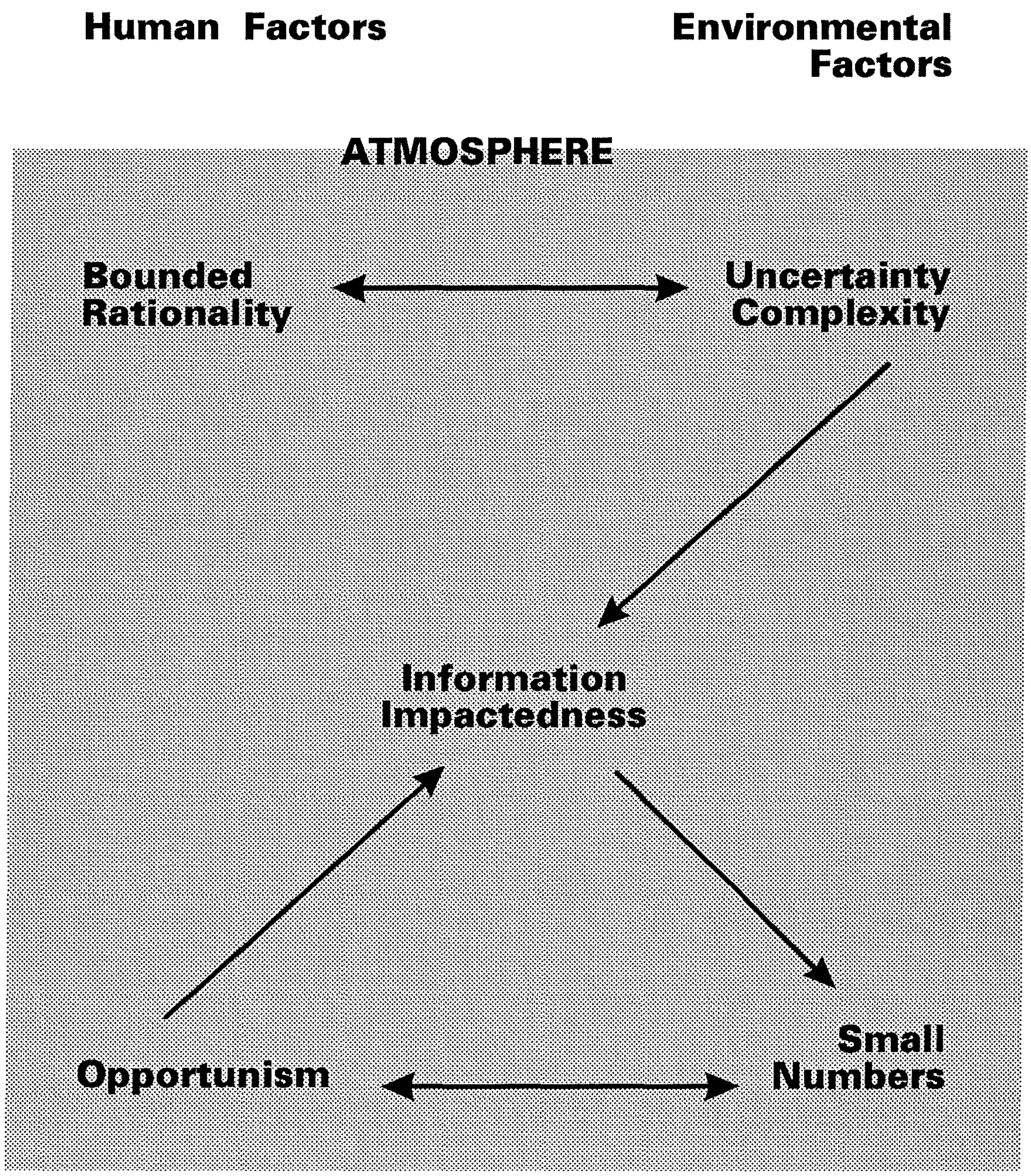
Transaction costs, in one word, mean the costs of running the organization. Specifically, they include all of the following: search and information costs; bargaining and decision costs; quality control costs, dimensions of which include monitoring or auditing costs, metering costs, policing and enforcement costs; associated transactional risks, e.g. default risk; 'transaction-inspired' costs or the so-called government-imposed costs, e.g. taxes, tariffs, and non-tariff barriers, political risks, etc. These are contingent upon effecting a transaction and would not have otherwise arisen, hence the term, 'transaction-inspired'.

All transaction costs can then be seen as resources expended to counteract externalities. Specific sources of these costs can be identified with interactions between human factors of opportunism and bounded rationality with environmental factors of uncertainty and small numbers exchange relations. By themselves alone, these factors do not generate transaction costs, rather it is when they join or interact that costs occur (Williamson, 1975, 1979). Figure 3.2 illustrates possible interactions between these factors. The factors can interact in all aspects of economic exchange and generate transaction costs (see, Dahlman, 1979, p.148).

Transaction costs result in two types of internalization: internalization of a market and internalization of an externality. The first type refers to the substitution (i.e. replacement) of an arm's length market with internal organization. Internalization of externality is concerned with the creation of a market where none already exists. Thus, under the first type the firm is induced by circumstances (eg. mispriced goods or competition) to shift transactions out of the market into the firm because thereby it can realize a strategic advantage in the use of its resources and over rivals. But, the second type can be associated, not with the notion of non-existence of market in the first place, rather with strategic attempts by firms to bypass the market and resort to their internal mechanisms. In so doing, an externality is internalized by replacing existing institutional arrangements (markets), presumed to have high transaction costs, with a new set of institutions (firms), deemed to have lower transaction costs.

It is the existence of these transaction costs in various organizational modes (e.g. markets and firms) that creates a major strategic choice problem for managers of MNEs (Holland, 1986, p.158). The strategic options open to the firm include: (1) internalize market transactions when the firm has transaction cost advantage over a market; (2) generate internal transaction cost economies where the firm does not have such an advantage; (3) use markets when they offer superior transaction cost advantages over the firm. Market participants also face the same choices. The result of such choices will determine the boundary between firms and markets. It will also identify the factors that permit transactions to be classified as one kind or another, as well as identify and match the alternative governance structures within which transactions can be organised.

Figure 3.2 Nature of Transaction costs and Organisational Failures



Source: Williamson, O.E. 1975. *Markets and Hierarchies: Analysis and Antitrust Implications,* New York: The Free Press, p.40.

3.3.4 STRENGTHS AND WEAKNESSES OF INTERNALIZATION THEORY

It has been postulated (from the preceding discussion) that the critical factors which impede exchanges between firms manifest in bounded rationality, opportunism, uncertainty, small numbers, information impactedness, and atmosphere. Williamson uses these factors to evaluate the strengths or advantages of hierarchy. Since hierarchy, internal organization or internalization are synonymous terms, the same rationalization can be made here. After all, it is in a bid to avoid or overcome these factors that both external and internal markets evolve. The way in which internalization affects each of these factors may be summarized as follows:-

1. *Bounded Rationality*: Internalization serves to attenuate bounded rationality by permitting the specialization of decision-making and economizing on communication costs (p.257). In effect, internalization permits the bounds on rationality to be extended through efficient codes and specialized training or other measures that will propel individuals to behave in a more calculating manner.

2. *Opportunism*: Internalization weakens opportunistic inclinations through administrative fiat. The fact that, in relation to autonomous contractors, the parties to an internal exchange are less able to sustain micromotives or appropriate subgroup gains at the expense of the organization, the incentives to behave opportunistically are accordingly attenuated.

3. *Uncertainty*: Internalization promotes convergent expectations, thereby serving to absorb uncertainties associated with autonomous decisions by interdependent parties in the event of changing market circumstances (Malmgren, 1961).

4. *Small numbers*: Internalization permits small-numbers bargaining indeterminacies to be resolved by administrative fiat. It can create its own market where none exists just as it can bypass existing ones.

5. *Information impactedness*: The attenuation of the interaction between opportunistic behaviour, market uncertainty, and small numbers bargain,

prospectively reduces the asymmetric distribution of relevant information between parties under a unified governance structure.

6. *Atmosphere*: Internalization permits organizational effectiveness to be viewed, not in strict calculative relations of a transaction-specific sort between the parties, but more broadly in a less calculative exchange atmosphere.

Theoretical analysis of these factors predicts that the costs of using the market mechanism to coordinate the exchange of an intermediate product are likely to be high under those circumstances (see for example, Williamson, 1975, 1979, 1981a,b). Thus, they act as incentives for firms to internalize. However, internalization may have its drawbacks which make contractual (market-mediated) alternatives desirable in certain circumstances.

3.3.5 LIMITS OF INTERNALIZATION

A symmetrical analysis of the limitations of internalization requires an acknowledgement of the transaction forces that may impede the process of internalization. Such a comparative analysis is necessary whenever the distinctive powers of internal organization are impaired and/or transactional diseconomies are warranted by reason of firm size, limitations of internal control, and managerial diseconomies of scale (see, for example, Williamson, 1975, p.117; Blair and Kaserman, 1983, p. 25). Coase (1937, p 340) first identified the possibility of a cost disadvantage attending to internalization as the firm's size increases. He observed that "as a firm gets larger, there may be decreasing returns to the entrepreneur function, that is, the costs of organizing additional transactions within the firm may rise". Further, although internalization may reduce the incentive to engage in opportunistic behaviour, it may not eliminate it altogether (Blair and Kaserman 1983, p. 24). Williamson is also critical of the distortion propensities of internalization. Specifically, he notes:-

> Internal organization ought to be regarded as *a syndrome of characteristics:* distinctive strengths and distinctive weaknesses, in a comparative institutional sense, appear nonseparably - albeit in variable proportions - as a package. Although the existence of market failure constitutes a presumptive basis for internalizing transactions, the "defects" associated with market exchange may

> need to exceed a nontrivial threshold before internal organization offers a clear cost advantage (1975, p 130).

The concern here is less with progressive distortions of internalizing by hierarchy than with the limitations of internalization theorem as a general paradigm by which foreign investment is to be understood Casson (1988) espouses a generalized view of the limitations of internalization and, in view of its broad coverage, coupled with the fact he is one of the progenitors of internalization as a general theory, his ambivalent position is reproduced as Exhibit 3.1

In conclusion, Casson's views as well as others suggest that the proximity of the transactional relationships that exist between markets and hierarchies lies on a continuum, with spot market exchange and hierarchy as extremes and a range of contractual alternatives falling in between. As transactional relationships shift from 'low-level' spot market through 'middle-level' contractual alternatives to 'high-level' hierarchical mode, the metric that varies along this continuum is the degree of control that one party to the exchange exerts on the other. But there are other variables in the equation of exchange relations and transactional control.

These other variables form a holistic approach to the study of international investment. This approach, termed "Eclectic paradigm", recognizes internalization as one of a three-way determinant of international investment, the other two being ownership and location specific advantages. This theoretical framework is the subject of the next section.

Exhibit 3.1 Limitations of Internalization Theory

(1) Although internalization theory is a general theory applicable to all markets, in practice applications have tended to focus on just a single market, namely that for technical know-how. Enormous emphasis has been placed on the role of FDI in technology transfer. Although this is appropriate in the context of US high technology FDI, it is too restrictive when dealing with recent developments in off--shore processing and in service industries. Internalization of markets in components and semi-processed materials, and in information services, needs to be considered as well.

(2) Internalization issues are usually studied from the standpoint of a single firm. The firm is assumed to be surrounded by arm's length markets, and the strategic issue is how far the boundaries of the firm should be pushed out by internalising these markets. In practice, however, the boundary to the expansion of one multinational is often set by the boundaries already established by other multinational firms. A more appropriate perspective from which to study internalization begins with the industrial production system as a whole. Given a configuration of production activities, one firm's internalization of a market through the acquisition of some facility denies the other firms the opportunity of internalising other (related) markets by acquiring that facility themselves. A pre-emptive struggle may therefore ensue between rival multinationals for the acquisition of key facilities.

From this alternative perspective, joint ownership of key facilities, which is difficult to explain using the conventional approach, emerges as a natural method of resolving conflicts of this kind. A related point is that when the ownership of a production system is divided up between a small number of multinational firms, there may be several markets where the same multinationals face each other as buyers and sellers and yet other markets where they compete on the same side of the market. Thus any pair of firms may interact on several fronts, on some of which they cooperate through trading intermediate products, while on others they compete in buying from, or selling to a third party (which might well be yet another multinational firm). This raises complex strategic issues, such as whether competitive behaviour of the latter kind will spill over to undermine cooperative behaviour of the former kind, or vice versa. Only a 'systems view' of production allows a satisfactory analysis of these issues.

(3) Internalization theory tends to suggest a polarised view of contractual arrangements, in which pure arm's length trade is contrasted with complete hierarchical control. In practice, there are many intermediate arrangements - such as joint ventures -and also a variety of implicit understandings built up as a result of long-term trading partnerships (so-called quasi-integration). The two often coexist: for example, the formal ambiguity over control implied by 50:50 equity joint venture is typically resolved by implicit agreements between the two parties. A theory which encompasses the social as well as the legal aspects of contractual arrangements is necessary to account fully for such phenomena.

Source: Casson, M (1988). Recent Trends in International Business: A New Analysis, Unpublished Discussion Papers in International Investment and Business Studies, University of Reading, No. 112.

SECTION 4
THE ECLECTIC THEORY OF INTERNATIONAL INVESTMENT

3.4.1. INTRODUCTION

The eclectic theory, whose protagonist is Professor John Dunning, is a synthesis of other theoretical developments (explored thus far). It is largely drawn from three major strands of thought: the organizational failures literature, the industrial organization theory and location theory. Together with internalization theory it is the most widely accepted theoretical candidate for explaining foreign direct investment. At the same time, both concepts offer stiff opposition to each other in terms of being competing paradigms. Both schools of thought make definitive statements about the generalizability and predictive powers of their theories (See, for example, Casson, 1987 for the former, and Dunning, 1988 for the latter).

The crucial questions with which foreign investment theories are concerned are compactly stated as:- *What*, *How*, and *Where* to produce (or invest) (Dunning 1977, 1979, 1980, 1988). An examination of these requires a reformulation of the following general analytical kind:-

1. Why do firms engage in international investment? Put differently, why do firms domiciled in one country (home country) choose to invest (or produce) in other (foreign) countries rather than in their home country?
2. Given the incremental costs of operating abroad, how are they able to compete with their indigenous counterparts? In other words, how do investing firms overcome the competition and other transactional frictions associated with operating in a foreign country?
3. Generally, which organizational modes of servicing foreign markets do firms adopt? This assumes that firms have alternative modes for operating in foreign markets. It also precludes any *a priori* declaration that one particular mode is superior to the other/s, in efficiency terms. This stream of thought seeks to identify the differential organizational forms by which international investments are completed, and the differential capacities (i.e. advantages) that underpin such forms.

4. Is multinationality an exclusive preserve of few large (dominant) firms? If so, why? If not, why is it that certain firms dominate others in the international market place?

The above questions have been asked in different ways and contexts. The specific historical perspective adopted in the literature is that which attempts to explain post-war US corporate investment in Western European manufacturing industry. In seeking answers to the questions, several theoretical developments, as surveyed in preceding chapters, have sprung up: some with limited applicability, some contradictory to others, and some complementary aspects of the same general phenomenon.

The common feature of these competing paradigms is that they all provide partial explanations to foreign investment and multinationality. Thus, none can claim closure or complete satisfaction in explaining the phenomenon. There are missing links of one kind or the other in all of them. For instance, explanatory frameworks that derive from the industrial organization literature did not address the 'Where' of foreign investment. That is, while recognizing the efficiency of internal organization of the firm in economizing on international transactions, this group stopped short of explaining 'where' such firms' advantages (i.e. efficiency properties of internal organization) would be exploited. On the other hand, location-related theories, while offering explanations to the 'Where' of foreign investment, ignored issues of 'How' and 'Why' of it. The concept of the eclectic paradigm can therefore be seen as supplying the missing links in an effort to identify and evaluate the factors that influence multinationality.

The main task of this section is to review the theory and application of the eclectic paradigm. Discussion is pursued in six sections, after this introductory part as section 1, and progresses in the order of Ownership advantages (section 2), Location Advantages (section 3) and Internalization advantages (section 4). Section 5 provides some empirical evidence while Section 6 concludes with its linkage with other received microtheories.

3.4.2. OWNERSHIP ADVANTAGES OF MNEs

BACKGROUND:

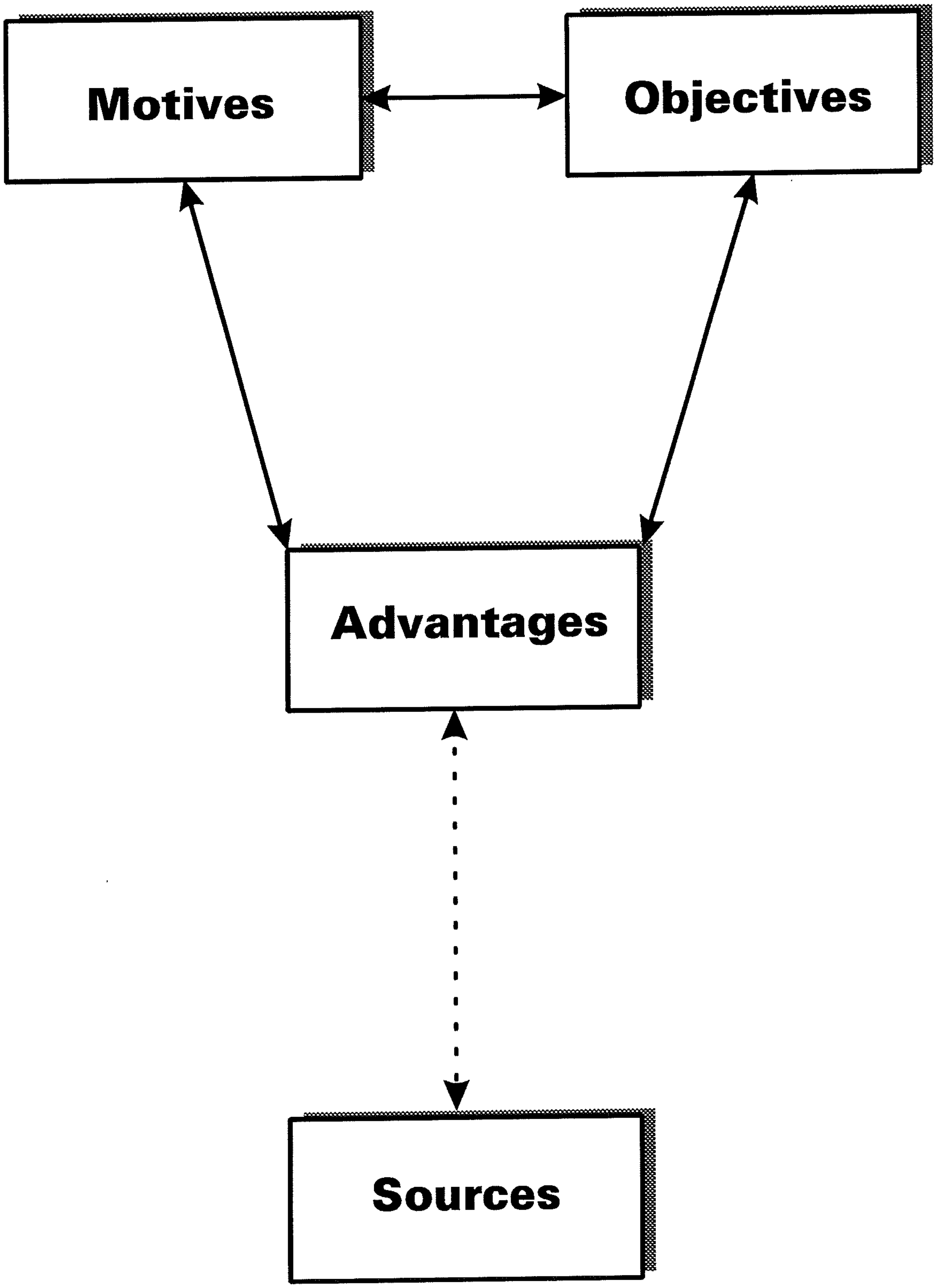
The notion of ownership-specific advantages is explicitly introduced into the discussion of multinational enterprises in an attempt to decipher what intrinsic properties firms have that inspire them to venture and sustain operations in foreign countries. The goal of a firm is an end desired (an objective to be attained); the quest for international market share, profit maximization, global positioning, or growth are all aspects of this. Couched as objectives, they represent distinctive features of something lacked and wanted by the firm.

Explicating the relation between advantages (or capabilities) and the interplay of motives (an incentive force) and objectives (desired ends) may provide an interesting insight into the discussion. At the risk of oversimplification, the formulation of this relation can be summarized by the schematic in Figure 3.3. The main pairings indicate motive and objective on the inverted triangle's base, motive and advantage, on the left side of the triangle, and objective and advantage, on the right side. That a firm's advantage has its origin somewhere - springing from within the firm or from without or a combination thereof - is denoted by the broken line that joins them.

The logic of figure 3 can be substantiated at any level of human endeavour, individual or corporate. Advantage is defined here to mean capacity or something possessed/owned that gives the holder superiority in a particular respect over another/others.

Such a superiority gives rise to a favourable or beneficial condition, under appropriate usage. Thus, advantages possessed by a firm provide incentives to pursue certain goals. The interaction in each pairing is a necessary reinforcement, it is designed to inspire management to consider alternative actions. For example, if the firm's advantage lies in superior management skills or product innovation, incentives to protect and maintain the advantage become increasingly stronger the more profitable their use prospectively becomes. On the other hand, incentives to protect and maintain a dormant asset weaken as the transactional rewards become progressively unprofitable.

Figure 3.3 The Relation Between Advantages, Motives and Objectives



This philosophical background underscores the crucial role of ownership advantage to the growth and success of a firm and to the possibility of multinationality. It also sets the stage for considering the dimensions of ownership-specific advantages.

DIMENSIONS OF OWNERSHIP-SPECIFIC ADVANTAGES (OSAs)

Dunning's (1988) remark aptly summarizes the properties of OSAs.

> ... Rarely, in seeking to identify the reasons for business achievement, is one able to find a single common denominator. Sometimes excellence is primarily based on innovatory ingenuity; sometimes on aggressive or novel methods of advertising and marketing; sometimes on super-efficient capital budgeting; sometimes on dynamic and imaginative entrepreneurships; sometimes on the diversity of operational experiences and capabilities; and sometimes on an unusual aptitude to manage human relationships ...

Dunning's observation summarizes the dimensions of OSAs. In simple terms, OSAs are monopolistic advantages unique to a firm which enable the firm to compete successfully in the market place. The ability of the firm to compete successfully in an "unfamiliar" foreign environment rests *inter alia* on its OSAs. The advantages, which may be tangible or intangible proprietary assets, are designed to overcome market imperfections. Incentives to develop OSAs increase as the opportunities of exploiting, *ceteris paribus.*

The range of advantages that prospectively lead to and/or sustain successful multinationalization is large, and is compactly summarized by Rugman, et al., (1986, p. 119) as follows:-

1. Proprietary technology due to research and development activities.
2. Managerial, marketing, or other skills specific to the organizational function of the firm.
3. Product differentiation, trademarks, or brand names.
4. Large size, reflecting scale economies.
5. Large capital requirements for plants of the minimum efficient size.

To the above must be included advantages of the following kind: market/ political connection, through contacts/dealings with large international clientele, politicians, bureaucrats and other informal links; and product market pre-emptive or oligopolistic privileges, as in the case of national companies operating under international cartels (e.g. OPEC), or companies in strategic industries (e.g. defense).

SOURCES OF OSAs

OSAs can arise in any number of ways. However, the literature distinguishes three main sources from which a firm can develop or acquire OSAs (Dunning, 1976, 1979). Figure 3.4 highlights the sources and the types of advantages that can be derived from each source.

3.4.3 LOCATION-SPECIFIC ADVANTAGE THEORY

The second stipulation for multinationality, under the eclectic theory, is location-specific advantage. OSAs are monopolistic advantages which offer the firm the constitutional authority and transactional access to use of facilities in a location-specific manner. Those advantages provide a necessary, but not a sufficient condition for multinationality. Essentially, they do not provide answer to the '*where*' of foreign investment. That is the gap which location theory seeks to fill.

The role of location theory in the general rubric of the MNE received little attention until lately (Buckley and Casson, 1985, p. 13). Yet, it is in the location theory that any complementary explanation of the strategic contexts of foreign investment (i.e. growth, organizational mode, etc.) are to be found. The entry of location theory into the FDI phenomenon finds its antecedent in the Ricardian endowments orthodoxy. In this connection, the MNE is seen primarily as a vehicle for the transfer of mobile resources (e.g. technology, financial capital, and managerial know-how) to locations of immobile complementary resources (raw materials, cheap labour, markets, etc.) (Ibid.).

Location-specific advantages (LSAs) refer to the set of advantages which accrue to a certain location by reason of differences in location-specific endowments between countries, or between geographical locations in a country. The specificity of this set of advantages resides in the particular location. A firm can only acquire them simply by operating in that location.

Figure 3.4 Sources of Ownership-Specific Advantages

1. PRIVILEGED SOURCES
   - Independent of Multinationality.
   - Exclusive possession of, or access to, idiosyncratic assets.
   - Transactional advantages resulting from firm size, established market position, product differentiation, brand names, or trademarks.
   - Transactional advantages due to bank power or financial connections, reflecting plant capacity, or scale/scope economies.
   - Transactional advantages arising from exclusive or privileged access to factor inputs (e.g. raw materials, natural resources, human resources, etc.), information and products markets.
   - Transactional advantages due to government protection.

2. OSAs DUE TO COMMON GOVERNANCE (Commonly enjoyed by subsidiary/associated firms, as opposed to *de novo* firms)
   - Advantages of credit rating, in-house facilities, established reputation or brand name.
   - Access to functional capacity (managerial, marketing, financial, production, and R & D).
   - Economies of joint supply of factor inputs, finished products, etc.

3. COROLLARY ADVANTAGES OF MULTINATIONALITY (Those induced by geographical or product diversification).
   - Transactional advantages of wider market opportunities.
   - Transactional advantages of size, market power, economies of scale or scope.
   - Transactional advantages of informational economies, arising from access to political and economic information networks, etc.
   - Capacity to diversify production and products in different countries.
   - Transactional advantages of risk diversification through the capacity to invest in different currency areas.
   - Transactional capacity to exploit international differences in factor endowments, production techniques, and markets.

Advantages which may be linked with a country or location include the following:

1. Natural endowments and national production functions.
2. Market size and growth.
3. Government controls and regulations.
4. Political, legal, economic, and socio-cultural conditions.
5. Host country's similarity to investor's home country.
6. Home government's role.

The types of advantages that may be derived from each source are identified in Figure 3.6.

Figure 3.5 **The Advantages to Firms of Undertaking Different Types of Foreign Production.**

Type of Foreign Production	Ownership advantages	Location advantages	Internalization advantages	Types of Activity which favour MNEs
1. Resource-based	Capital; access to markets, managerial skills; experience in similar markets	Resource (for example availability and cost skilled labour, information); customization to local tastes	To secure supply of skilled labour; protection and exploitation of specialist information; quality control	Engineering design, insurance and re-insurance, management consultancy, investment banking.
2. Import-substituting services	Capital; specialist knowledge; reputation and image; access to multi-national clients	Labour and other costs; size of local market; local government regulations; need for on-the-spot contact with clients	Exploitation of knowledge and business contacts; buyer uncertainty; high information costs	Reinsurance, executive search and accountancy management and engineering consultancy, branch banking
3. Trade and distribution	General merchanting knowledge; access to suppliers and market outlets	Size of market; access to customers, suppliers and commodity exchanges; liberal attitudes towards trade	To protect market share; exploitation of business and market contacts to avoid underperformance or misrepresentation by sales agents; to assist price discrimination	Import and export merchanting
4. Efficiency seeking	Economies of specialization, scope and geographical diversification; access to multinational clients	Few import barriers	To exploit economies of common governance	Investment banking management consultancy information technology

Source: Dunning (1988), *Explaining International Production, London: Unwin Hyman, p.273.*

Figure 3.6 Sources/Types of Country (Location)-Specific Advantages.

1. NATURAL ENDOWMENTS AND NATIONAL PRODUCTION FUNCTIONS:-
   - Spatial distribution of natural and created resource endowments and markets.
   - Cost-effective production factors, e.g. skilled manpower, energy supplies, materials, components, semi-finished goods.
   - Infrastructural resources, e.g. international communications and transport facilities.
2. MARKET SIZE AND GROWTH:-
   - Size and growth structure of national economy.
   - Existence of multinational enterprises of varying nationalities.
   - Strong and efficient capital markets, high degree of banking development, including a strong international bank market.
3. GOVERNMENT CONTROLS AND REGULATIONS:-
   - Kind and structure of artificial barriers, e.g. tariff and non-tariff barriers to trade in goods and service (e.g. import and export controls)
   - Tax structure and incentive regimes
   - Financial controls, e.g. profit repatriation controls.
   - Other investment incentives and disincentives, e.g. expatriate quotas, immigration controls, performance controls, etc.
4. POLITICAL, LEGAL, AND SOCIO-ECONOMIC CONDITIONS OF HOST COUNTRY:-
   - Political system of a country - Is it a stable democracy, socialist/communist, or an unstable military government?
   - Economic system - a free-market, centrally-planned, mixed, etc.
   - Legal system - corollary of political, economic and cultural systems.
   - Cultural ethos of the citizens - proximity to foreign investing firm's home country.
   - Educational and commercial systems.
   - Institutional framework for harnessing resources and for resource allocation.
5. HOST COUNTRY'S SIMILARITY TO INVESTOR'S HOME COUNTRY:-
   - Psychic proximity, e.g. language, cultural, business, customs, educational, etc., similarities or differences.
   - Political and economic, etc., interest parities between the investor's home government and the host government, e.g. investment, trade, and other economic and political agreements, or regional and international co-operative arrangements, e.g. cartels such as OPEC, EEC, ECOWAS, etc.
   - Territorial/Colonial interest parities, e.g. the Commonwealth, the Anglo-American ties, etc.
6. HOST GOVERNMENT'S ROLE
   - Foreign investment incentive or disincentive schemes
   - Nationalization programmes, e.g. indigenization programmes, anti-trust policies, interplay of political and economic policies, etc.
   - Privatization and other free-market policies.
   - Other forms of government intervention in private enterprising, including bureaucratic bottlenecks and red-tapes.

3.4.4. INTERNALIZATION ADVANTAGES OF MULTINATIONALITY

The first two stipulations of the eclectic paradigm - the OSAs and LSAs - attempt to explain *which* firms will service a particular foreign market (using their ownership-specific advantages), and *where* such OSAs might be best utilized in transaction-maximizing terms (by complementary location-specific endowments), respectively. As simultaneous explanatory powers, these two conditions are insufficient in explaining international investment, for they do not explain *why* a firm should choose to exploit its OSAs abroad or which organizational mode is most efficient in exploiting the advantages in a given foreign location. This stream of explanation is the context of the internalization advantages.

The internalization theory, discussed in the preceding chapter, suggests that the incentive to internalize the firm's FSAs is the raison d'etre for multinationality. This immediately suggests that MNEs perceive the international market as an inferior transaction mode. The reasons for the internalization of markets have been explored in section 4. Essentially, market failures of two kinds were identified: (1) internalization of a market, referring to the supplantation of market mediated exchanges by internal organization; and (2) internalization of externality, that is, the replacement of alternative contractural modes by the internal structure of the firm. The linkage between internalization and multinationality lies in the potentials of internalising markets for control and for transaction-cost economy through a unified governance structure. The factors that favour internalization are identified in Figure 3.7.

3.4.5. EMPIRICAL APPLICATIONS

Table 3.3. illustrates some recent empirical applications of the eclectic model. Not surprisingly, available literature evidence suggests a preponderance of Dunning's research effort in propagating the eclectic model. Initially, empirical application of the model, as with the other frameworks, concentrated on the manufacturing industry. Recently however, its applicability to other spheres of international economic activity has come under scrutiny. This has been pursued through theoretical adaptation or empirical extension or both. For example, Boddewyn (1981) adapted the model to examine the reasons for corporate divestment. She concludes that: (1) The reasons for FDI, as suggested by the eclectic theory, can be reversed to explain international divestment. (2) Divestment occurs when a firm loses its FSAs, or when the reasons for internalization terminate. (3) By the same configuration of three types of advantages that explain the initial decision to invest abroad, disinvestment (or subsequent decrease in FDI) requires simultaneous violation of the same. Thus, the absence of one of the three conditions, or an adverse change thereof, is sufficient to bring about negative FDI or disinvestment.

Figure 3.7 Factors Favouring Internalization Advantages

1. AVOIDANCE OF HIGH TRANSACTION COSTS.

- Need to avoid the high costs associated with searching, negotiating, and enforcing contracts across markets.
- Need to control elementary attributes of human decision makers, namely opportunistic tendencies and bounded rationality.

2. OVERCOME MARKET UNCERTAINTY AND PROBLEMS OF SMALL-NUMBERS EXCHANGE RELATIONS

- Need to reduce buyer uncertainty and information impactedness problems.
- Need of seller to protect quality of products.
- Need to guarantee market outlets
- Need to guarantee supplies and conditions of sale/purchase
- To provide or compensate for absence of markets or future markets.

3. CONTROL THE USE OF PRODUCT/TECHNOLOGY

- To eliminate the possibility or resale, product-knowledge dissipation by, or leakage to, competitors or potential ones.
- To control supplies and conditions of sale of technology
- To control market outlets, including those which might be used by competitors or potential competitors.
- To capture economies of vertical integration (of interdependent activities).

4. OVERCOME/EXPLOIT UNNATURAL MARKET IMPERFECTIONS

e.g. Tariffs, foreign exchange control, regulations on foreign investment.

5. NATURAL RESPONSE TO IMPERATIVES OF CAPITALISM

- Ability to engage in practices consistent with competitive (or anti-competitive) strategies, e.g. tax avoidance, transfer-pricing, price discriminations, predatory pricing, leads and lags, cross-subsidization.

6. TO ACQUIRE MARKET POWER

- E.g. through mergers and acquisitions, to control either the sources of and/or the markets for primary resources, intermediate products or final products.
- To engage in monopoly or oligopoly practices.

The eclectic model has also been used to explain multinationalization in the banking industry. Gray and Gray (1981) are credited as the first to apply Dunning's eclectic theory to multinational banking. Although their work and that of Yannopoulas (1983) were largely descriptive, they provided a strong theoretical insight into, and have become a useful reference for, the study of international banking. Following them, Cho (1985) and Nigh, Cho and Krishnan (1986) have adapted the eclectic model to examine the determinants of multinational banking performance as well as the role of location-specific advantages in international branch banking. Although these studies relied on US data, their findings affirm the predictive utility of the eclectic paradigm.

Latterly, Dunning has widened the predictive scope of his original formulation as well as its empirical applicability. Evidence for this can be found in his most recent writings (see, for example, 1988, chapters 2, 6, 13) where he discusses some possible extensions of the eclectic paradigm. He also adduces empirical evidence on multinationalization in the hotel industry, and business and professional services industry.

Table 3.3 **Selected Recent Empirical Applications of Eclectic Paradigm.**

	Year of Publication	Researcher/s	Research Context	Specific Research Objective	Research Methodology
1.	1980	John H. Dunning	Manufacturing Industries in 7 countries: 5 DCs and 2 LDCs.	To evaluate the significance of O- and L-specific variables - variables in explaining industrial pattern and geographical distribution of the sales of US affiliates in 14 manufacturing industries in 7 countries in 1970	Regression analysis - Linear and - Multiple
2.	1981	Jean J. Boddewyn	US Manufacturing industry	To examine via the eclectic model whether foreign disinvestment theory is the reverse of foreign direct investment	Survey Study
3.	1981	H. Peter Gray & J. Gray	US Multinational commercial banking	To apply the Eclectic theory to explain the multinationalization of non-financial corporations, with emphasis on multinational commercial banking	Exploration survey and historical analysis
4.	1981	John H. Dunning & Matthew McQueen	International Hotel industry	To examine the relevance and applicability of the eclectic paradigm to explaining the extent, structure and form of involvement by MNEs in the international hotel industry.	Historical survey and analyses
5.	1983	George N. Yannopoulos	US Transnational banking	To examine the transnationalization of US banking using the eclectic theory	Historical data analyses
6.	1986	Kang Rae Cho	US Multinational Banking in Asia Pacific Region	To identify major determinants of MNB performance in Asia Pacific Region, exemplified by Singapore and South Korea	Cross-sectional analyses, and pooled time-services cross-sectional tests
7.	1986	Douglas Nigh Kang Rae Cho	US Banking involvement abroad	To examine the role of location-specific advantages in US international branch banking.	Pooled time services, and cross-sectional regressional analysis.
8.	1988	John H. Dunning	International hotel industry	Same as in 4 - An update	Same as in 4
9.	1988	John H. Dunning	Business and Professional Services	To evaluate the locational determinants of MNE business	Survey study

3.4.6. SUMMARY AND CONCLUSION

This chapter has attempted a review of key theories: diversification, internalization and the eclectic paradigm. The eclectic concept offers a holistic approach to explaining foreign direct investment. The logic of eclecticism suggests that a 'full' explanation of international investment cannot be accomplished through a microtheoretic approach. Aspects of extant mainline theories implicitly fall in this category. The common threads that tie these explanatory approaches are: (1) an evolving consensus that received microtheory, as useful and powerful as it may be for analytical purposes, operates at too high level of parochialism to permit many important international investment phenomena to be addressed in an uncontrived way; (2) a growing realization that the extent, form or pattern of foreign investment activities cannot be confined to or measured in terms of hierarchical mode alone; and (3) a sense that FDI is just one of a number of possible organizational mechanisms by which foreign economic involvement can be accomplished.

The eclectic concept therefore derives from the notion that an explanation of the ramifications of foreign investment requires wider considerations and needs to lean upon several strands of related theory. Precisely, it states that the extent, form and pattern of international investment is determined by the configuration of three sets of firm-specific advantages. The paradigm avers that, given the spatial distribution of location-specific endowments and the firm's complementary ownership-specific advantages, enterprises which have the greatest opportunities for, and derive the most from, internalizing transactions will be the most competitive in foreign markets. The later recognition that these advantages and their mode of utilization will differ according to industry, country and enterprise characteristics seems to be a useful corrective.

CHAPTER FOUR

A SYNTHESIS OF FOREIGN INVESTMENT THEORIES: PART 3

JAPANESE MODEL OF FOREIGN INVESTMENT

CONTENTS

CHAPTER 4

JAPANESE MODEL OF FOREIGN INVESTMENT:

4.1. INTRODUCTION

Japanese model of foreign investment is sometimes linked with the product cycle hypothesis and sometimes thought as a macroeconomic development approach (see, for example, Hood and Young, 1986, p. 67; Cantwell, 1988). Some however think that it is different from Western patterns of foreign direct investment (see, for example, Kojima, 1973, 1975, 1982; Ozawa, 1979a, b). The differences are attributed to (a) the late arrival of Japanese MNEs, (b) the regional concentration of the MNEs in Asia and Latin America, (c) the greater labour intensity of Japanese investments as compared with those of the West, (d) the flexibility and willingness of Japanese MNEs to adopt contractual and cooperative forms of investment, and (e) the existence of group-controlled investment (Buckley, 1983).

The distinctiveness of Japanese mode of foreign investment has been recognised by academics, corporate executives, national governments and multilateral institutions. For example, in his preface to Kojima and Ozawa's (1984) "Japan's General Trading Companies: Merchants of Economic Development", Just Faaland, then President of Development Centre of OECD, had this to say: "The spectacular growth and development of the Japanese economy has brought increasing worldwide attention in recent years to Japan's unique economic institutions". This study accordingly identifies with this distinction and will proceed with an assessment of the nature of the country's "economic giants".

One of the economic institutions which have played a major role in Japan's postwar economic transformation is the *sogo shosha* or *general trading company*. International economists have been trying to rationalize the success and investment behaviour of the *sogo shosha* within the context of received microtheories of investment. Before discussing the theoretical frameworks commonly associated with the Japanese model of foreign investment, it may be insightful to review of the investment behaviour of the *sogo shosha.*

4.2. INVESTMENT PROFILE OF THE SOGO SHOSHA

Japan's large general trading companies (GTCs) have been described both in Japan and abroad by all sorts of terms, ranging form "Japanese-type conglomerates," "Japan's new *zaibatsus*", "Japanese-type multinationals", "modern monsters with worldwide communications networks rivaling that of the Pentagon", "mammoth traders handling 10,000 commodities, from instant noodles to missiles", "speculators in stocks, rice, land, lumber and other necessities", to "action think tanks". These characterizations may be bewildering, but, they do represent, even if partial or exaggerated, varying descriptions of the complexity of the business, organizational structure, resources, and behaviour of the sogo shosha (ibid).

In general, the central element surrounding the business of the GTCs has traditionally been trading. However, in order to understand the complexity and diversity of investment profile of the GTCs, it is necessary to look beyond their identity as mere traders and trade intermediaries. They are active generators of long-term demand and supply in a vast range of products. The big nine GTCs (Table 4.1) are reportedly handling literally an infinite number of products (Kojima and Ozawa, 1984).

The scale of operations of GTCs and the magnitude of their investments make them leading Japanese multinationals, not only in overseas trading but also in manufacturing, resource extraction and other non-trading ventures (ibid.). As Table 4.1 shows, five of the six largest Japanese MNEs in 1981 were GTCs; ranking among the first four largest MNEs.

Table 4.1 Japanese 9 Largest General Trading Companies and How They Rank Among Japan's Top 25 MNEs.

		CATEGORY	CUMULATIVE VALUE OF INVESTMENT US $ M	RANKING
1.	Mitsui & Co	GTC	1,176.5	1
2.	Mitsubishi Corporation		790.5	2
3.	Marubeni Corporation		776.0	3
4.	C. Itoh & Co		631.0	4
5.	Japan Asahan Aluminium	Other	435.0	5
6.	Sumitomo Corporation	GTC	344.0	6
7.	Matsushita Electric Industries	Other	337.0	7
8.	Nissan Motor		298.0	8
9.	Nissho-Iwai	GTC	284.5	9
10.	Torray	Other	284.0	10
11.	Tomen	GTC	239.0	11
12.	Honda Motor	Other	219.5	12
13.	Kawasaki		211.0	13
14.	Sanyo Electric		193.0	14
15.	Shin Nihon Steel		190.5	15
16.	Sony		188.0	16
17.	Mitsubishi Heavy Industries		176.5	17
18.	Ishikawajima - Harima Heavy Industries		175.0	18
19.	Kanematsu Goshu	GTC	170.0	19
20.	Japan Usiminus	Other	162.5	20
21.	Kawasaki Heavy Industries		157.0	21
22.	Tokyo Kyuku Dentetsu		150.0	22
23.	Teijin		146.5	23
24.	Nichimen Jitsugyo	GTC	144.5	24
25.	Tokyo Shibaura Electric	Other	141.0	25

Source: Adapted with modification from Kojima and Ozawa (1984, p.17). The authors' original compilation was in Japanese Yen, but given the (authors') average exchange rate of 200 Yen to $1 at the time (1981), the equivalent dollar values of the cumulative investments are thus computed from the original Yen values.

Altogether, the top nine GTCs were all among Japan's 25 largest MNEs. The commercial success of the trading companies can be traced beyond sheer commercial intermediation in wholesale business. A macroscopic assessment of the scale and complexity of the GTCs's overseas operations reveals a four-way functional classification: (1) transactional intermediation, (2.) financial intermediation, (3) information-brokerage, and (4) auxiliary functions. This grouping is merely for academic convenience; it, in no way, captures the immense diversity of their operations, for, according to some observers the *sogo shosha* "buy and sell everything under the sun except people and coffins" (ibid).

4.2.1. TRANSACTIONAL INTERMEDIATION

One of the fundamental features of the GTCs is their capacity to intermediate in a vast range of commercial and noncommercial transactions. This ability stems from, and is nourished by, their network of multinational information-collection machinery. Externally generated information about prospective and extant operational environment is internalized within the company's global network system. The sophistication and cost of the information-gathering machinery as well as their scope of coverage constitute potential entry and exit barriers to small and/or ill-equipped companies. In consequence, the GTCs are able to put this advantage of market-knowledge into extensive commercial use by acting as transactional brokers both for other traders and non-traders.

In order to optimize customer services and, in turn, maximize rent from this advantage, GTCs strive to economize on transaction costs. They offer "trader-specific marketing or procurement cost advantages and/or provide a particular type of qualitative (non-price) marketing service required for a specialized line of product, such as technical and promotional services (i.e. offer product-specific non-price marketing advantages)" (Kojima and Ozawa, 1984, p.84). Trader-specific marketing/procurement cost advantages can be realized both through scale economies in transactions and specialized knowledge about a particular market. The ramifications of the intelligence network cum their specialized nature enable the GTCs to reduce the search and information costs of procuring customized range of inputs and components as well as selling the finished products.

An important corollary of product intermediation is the potential it offers to intermediate as well in production techniques. A significant aspect of the transactional brokerage function of the GTCs lies in technical development and services. GTCs maintain a large crew of technical experts as well as a complement of special sales force to provide technical services in plant exports. Kojima and Ozawa observe that "in the absence of these advantages, non-trader firms will use either pure market (i.e., direct market transactions without the intermediation of traders) or hierarchy (i.e., non-traders themselves set up marketing units within their own organizations)...implying that the "departure-from-trader" phenomenon will occur in either case". (p.85).

4.2.2. FINANCIAL INTERMEDIATION

Drucker (1975) provides an approximate description of the financial intermediation role of the GTCs. He notes that "in many ways, the trading company is not a 'trading company', but a 'finance company'". He traces the historical development of this role to the early stages of industrialization, following the Meiji Restoration in 1868, during which the government gave little concern to distribution services and establishment of medium-term money markets. The development of the trading company was conceived as "one way in which the Japanese company manages its medium-term credit problem, for the trading company optimizes the need for medium term credit". Peter Drucker elaborates as follows:

> "The trading company creates its own money pool, or what bankers call a 'float' - a reservoir of money that can be used whenever the need arises and that can be turned over a great deal faster than money invested in any one distribution channel or cycle. It creates a medium-term money market, and does so very effectively. It represents the most rational optimization of the existing structures, under which medium-term finance is critically short and inadequately taken care of by the existing banking system ... Just as the *zaibatsu* bank is the capital market of Japan, so the trading company is its money market."

Describing the GTCs as quasi-bankers is simply an understatement; in practice, they behave like institutionalized bankers. They provide not only in-house full-scale banking facilities, but equally extend the services to outside parties. According to Kojima and Ozawa, contemporary trading companies are active intermediaries in both money and capital markets - supplying short- to medium-term loans to facilitate their trade-intermediating activities, as well as equity capital to foster their own suppliers.

Table 4.2 illustrates the magnitude and proportion of debt and equity capital investments of the top nine trading companies as of 1981. Despite the huge investments, the return on such (equity) investments is typically low, with modal return on equity around 2 per cent. The exception is Mitsubishi Corporation with a high ROE of 9.4 per cent - arising from its lucrative investment in Brunei natural gas (ibid.). However, it would appear that from a strategic point of view, the interest/concern of the GTCs is not so much on the return on a particular investment project so long as it fosters transaction intermediation which generates commissions. Overseas investment projects provide opportunities for intermediating activities which in turn enhance the prospect of economic rents via commissions, management consultancy, technical supplies and services, etc. Kojima and Ozawa draw the interesting contrast in the functional attributes of Japanese GTCs as financial institutions vis-a-vis institutionalized arrangements found in the western world.

> ... as financial institutions, Japan's GTCs are unique. They combine the rules of the British merchant bank, which was founded to provide medium-term loans for foreign trade, and the German universal bank, which is heavily committed to financing its affiliated industrial group. But the important difference is that Japan's trading companies are quite willing to accept an extremely low rate of return on financial investment in exchange for other business transactions that enable them to earn commissions. (p.25)

Table 4.2

Magnitude and Percentage of Equity and Debt Capital Investments by Top Nine Japanese Trading Companies. 1981.

	A Equity Investment (at home and abroad) Amount	%	B Debt (at home and abroad) Amount	%	C Total (A + B) Amount	%	D Overseas Financing (Equity&Loans as % of C) Amount	%	E ROE %	F E/D Ratio
Mitsubishi Corp	889.775	38.6	1,416.805	61.4	2,306.580	100	701.0	30.4	9.4	4.0
Mitsui & Co	1,417.680	39.0	2,215.280	61.0	3,632.960	100	1,243.5	34.2	3.1	1.9
C. Itoh & Co	1,199.790	42.1	1,648.125	57.9	2,847.915	100	576.5	20.2	2.2	4.6
Marubeni Corp	798.635	53.5	693.475	46.5	1,492.110	100	630.5	42.3	2.2	9.0
Sumitomo Corp	547.770	63.8	310.265	36.2	858.035	100	296.5	34.6	2.0	6.7
Nissho Iwai	326.085	40.9	471.625	59.1	797.710	100	305.0	38.2	2.0	1.8
Tomen	211.880	43.3	277.285	56.7	489.165	100	208.5	42.6	2.0	8.1
Kanematsu Gosho	172.305	31.8	370.105	68.2	542.410	100	126.0	23.2	1.3	6.1
Nichimen Jitsugyo	122.690	33.2	246.595	66.8	369.285	100	148.0	40.1	1.2	10.1

Source: Kojima and Ozawa (1984, p.89). The amounts have been converted into US dollars at the exchange rate of 200 Yen to $1 (the approximate rate at the time). Another modification is the incorporation of column F, with the ratios transformed from their original presentation, e.g. 87 to 13 is transformed to 6.7, rather than as notations as in the authors' own.

In effect, they conclude, the financing services of the GTCs may be likened to a 'loss leader' situation in a marketing context, whereby return-to-risk considerations of a particular investment project are somewhat underplayed in favour of possible linkage effects whose high earning potentials would, in turn, mitigate the original loss. But, the ability to make strategic decisions of these kinds depends in part on knowledge of the markets.

4.2.3 INFORMATION-BROKERAGE

Another important characteristic in the development of transactional prowess in the international arena is related to the high propensity of the GTCs to gather information - economic, political and otherwise. It is reportedly claimed that a GTC's capacity to collect economic, social and political information is "far superior to that of the Japanese Government, as far as both geographical and topical coverage is concerned" (ibid.). The hub of the trading company's intelligence service is its home office in Japan. The home office is the "debriefing" point for company employees returning from overseas, as well as the centre of a telex network.

The ability to spin a vast web of information-gathering entails huge expenditure of human and material resources. Heavy commitment of resources in communications network is the corporate investment counterpart of R&D found in R&D-oriented manufacturing companies. The difference, however, is one of kind and mode: whereas trading companies' comparative advantage resides not in initiating or generating but in collecting, processing and disseminating information, R&D-oriented companies generate and internalize knowledge. This distinctive characteristic has an important theoretical implication for the behaviour of GTCs as MNEs, as will be discussed shortly.

Table 4.3. presents the differential patterns of investment in communications among the top nine GTCs. The data shown in the table clearly illustrates the importance of communications to the trading companies. The capital outlay and its relation to sales is comparable in size and proportion to the average R&D expenditure in such technology-intensive manufacturing industries as electronics (about 3.9%) (ibid.). For instance, with an expenditure level of $59,680,000 in telex, telephone, facsimile, postage and computer

time, Mitsui is acclaimed to have the most comprehensive, sophisticated system (the global on-line network system) with telex-cum-computers strategically installed in five key cities around the world. The company handles an enormous volume of information through regular intra-firm and other 'covert' communication channels.

Table 4.3 Communications Expenditures of the Top Nine GTCs, 1978

(converted to US$m; 200Y=$1)

GTC (in spending order)	Communications Expenditure	Communications Expenses As a % of Sales
Mitsui & Co	59.680*	9.60%*
Mitsubishi Corporation	21.685	3.04
Marubeni Corporation	17.965	3.78
C. Itoh & Co	17.640	3.87
Sumitomo Corporation	17.640	4.31
Nissho Iwai	16.930	4.68
Kanematsu Gosho	7.470	4.47
Nichimen Jitsugyo	7.370	3.82
Tomen	3.425**	1.87**

* Includes computer expenses estimated at about $US30m.
** Only Head Office expenses

Source: Ibid, p.90.

Economizing on intelligence activities is accomplished by assigning transactions to geograhic regions in a discriminating way. The approach applies both to the determination of efficient boundaries of information-gathering and investment and to the organization of communications network. For instance, the organizational cost of information-gathering, (including transmission) in developed countries is less and more efficient than in LDCs because of the relative ease and efficiency of communications and transportation and the availability of information media (e.g. publications, broadcasting, lectures, public meetings, etc.). Correspondingly, the rate of return on investment in information-gathering (intelligence activities) will tend to move in tandem with both the organizational and locational (geographic) cost of transacting, i.e. it will be much higher in DCs than in LDCs. The irony of their operations is that information of a strategic nature about a developing country (e.g. political changes, etc.) filters into, and is collected more effectively in, developed countries. For instance, subsequent to the fall of the Shah of Iran, all the major trading companies established liaison offices in Washington, D.C. from where they assessed the implications for Japan's investment interests in the region.

Assigning transactions to geographic regions provides a partial explanation to the heavy concentration of Japan's manufacturing and extractive investment in developing countries (about 70 per cent) contrasts sharply with the relatively small (about 33 per cent) commerce-related investment in these countries. The low rate of return on investment in intelligence activities in LDCs is attributed to a number of factors, including: acquisition, bureaucratic bottlenecks frequently leading to bribery, unwillingness of officials to grant interviews or even discuss matters, reluctance to respond to letters and all forms of inaccessibility. All of these constructively act as a disincentive to invest except, in a "loss-leader" context discussed earlier.

4.2.4 AUXILIARY FUNCTIONS OF GTCS

The auxiliary functions can be viewed as a development of specialized management skill compatible with the traditional managerial task of organization and co-ordination. The basic difference here is that the organization/co-ordination role is a new business function established by the GTCs to meet the challenges of a new economic environment. It is not the same as corporate business unit or strategic business unit either, rather the organization/co-ordination role represents an amalgam of strategic business unit and corporate strategic unit in the sense that it integrates in a synergic context the trading companies' major traditional functions (discussed above) into corporate strategy.

As set out by Kojima and Ozawa (p.26), the critical dimensions for describing GTCs' organization/co-ordination function are (1) conversion or 'downstream' operation, and (2) development or 'upstream' operation. The first dimension is a reflection of the GTCs' propensity to cultivate consumer markets on their own by engaging in material procurement, product design and marketing as a *vertically-integrated* operation that moves downstream through different stages of production. The *modus operandi* of the 'downstream converter' role is in many respects consistent with 'internalization of a market' by which external market (i.e. arm's length contractual relationship) is replaced with internal market (see, for example, Casson, 1984).

As a diversification strategy, it provides an opportunity to expand the traders' operations beyond the traditional producers' goods in the upstream stages. Kojima and Ozawa describe the strategy as follows:

> The trading company secures necessary raw materials or intermediate inputs and organizes a production team by tying up with a manufacturer who will be in charge of producing the newly designed products specified by the trading company. Usually, the manufacture is a small- or medium-sized company which, because it has not yet developed its own market, is willing to become a captive supplier or a production division of the trading company. If the manufacturer's production skill is inadequate, the trading company brings in the necessary technology from the outside under a licensing agreement.
> (p. 26).

The converter formula is highly relevant and profitable as a market entry mode and international market diversification strategy. It can be used to span different segments of a market, both vertically and horizontally. Table 2.4. illustrates how the trading companies operationalize the converter formula. Basically, they diversify abroad by adopting a 'subtle' strategy in capturing perceived or 'informed' (through their network) market opportunities.

The second dimension for describing GTCs' organization/co-ordination function is development or 'upstream' operation. Basically, this involves developing, in collaboration with another company or companies affiliated with a particular industry, expertise which may otherwise be costly for the GTC. This investment strategy enables trading companies to diversify into such industrial complexes as petrochemical and electronic manufacture. The practice appears to have a historical pattern consistent with 'imitative investment' or 'follow-the-leader' hypothesis. For instance, once Mitsui Co. ventured into construction of a petrochemical complex (or *kombinato*), at Iwakuni, Mitsubishi Corporation and Sumitomo Corporation followed suit by setting up similar petrochemical *kombinatos* at Yokkaichi and Niihama, respectively (ibid.). The 'follow-the-leader' investment behavioural pattern tends to be systematic and pervasive. When one GTC makes a move in any direction, it stimulates the interest of others. Like the western-type oligopolistic market reaction (see chapter 2), the tendency is to generate and/or capture external economies or economize on transaction costs by forging cooperative arrangements.

What clearly emerges from the investment 'ubiquity' of Japan's MNEs is that they are, in the words of Kojima and Ozawa, "willing bearers of, and capitalizers on, uncertainties and risks". If this were true, then, the crucial question is: why do they exhibit such a peculiarity towards foreign investment? Put differently, what distinguishes Japanese 'trade-oriented' model of foreign investment from western 'anti-trade' (the so-called American type) FDI? In what theoretical framework can an explanation of their pattern be assessed? The next section attempts an answer.

Table 4.4 Illustrative Industrial Application of the Converter Formula

INDUSTRY	MODE OF OPERATIONALIZATION	ILLUSTRATIVE GTCs
1. CLOTHING	Marketing through affiliated retail outlets clothing items manufactured under a joint venture or contractual arrangement eg. licensing with either home or foreign manufacturing companies.	Mitsui & Co, with Daitobo Co under imported know-how from Friedman-Marks Co. of USA OR Mitsubishi Corp., with a Korean firm, with technology licensed by the Takahara Shirt Manufacturing Co. of Japan.
2. CATERING-RESTAURANTS & FAST-FOOD CHAINS	Operating restaurants and fast-food chains through franchise arrangements; transforming these into successful chain of instant-noodle restaurants, known as "Larmen Dosanko" in New York.	Mitsubishi Corp., under a partnership arrangement with American Kentucky Fried Chicken.
3. TECHNOLOGY BASED	Advancing into technology-oriented sectors or industry, such as personal computers and computer peripherals, by marketing abroad products of a manufacturer which it (the trading company) supports either as its subsidiary, joint venture or contractual partner.	C. Itoh & Co. marketing overseas, under its own house brand, small printers produced by a manufacturer which it has successfully supported as a subsidiary.

4.3 CONCEPTUAL EXPOSITION OF JAPANESE MODE OF FOREIGN INVESTMENT.

The object here is to elicit theoretical explanation to the empirical analysis sketched above. There is less disagreement in the literature that the *modus operandi* of Japanese foreign investments suggests a distinct characterization than there is agreement in how to analyze it or justify it within extant FDI theories. Consequently, Japanese academics/analysts, notably Professors Kiyashi Kojima and Terutomo Ozawa, have proposed alternative explanations. Both have been at the vanguard of theoretical developments of Japanese mode of foreign investment since the early 1970s. Their individual and collective works constitute the antecedent literature from which both the preceding and prospective discussions derive.

The common feature in their proposition is the extension of the neoclassical theory of trade. By integrating trade theory with FDI theory, they view the MNE as a mechanism by which the comparative advantage of nation states may be better advanced. Using the standard two-country, two-factor, two-product Hecksher-Ohlin model of trade, Kojima (1978) prescribes that investments should flow from a comparatively advantaged 'home' country to a relatively disadvantaged 'host' country. He further prescribes that such investments should be made in sectors which require internationally mobile intermediate products that can be combined with non-transferable inputs in which the host country is relatively well endowed. This way, foreign investment may be conceived both as a catalyst to trade and as and arbitrager for improving the efficiency of international allocation of economic activity (Dunning, 1988, p.50).

Kojima recognizes that FDI, as a package involving technical knowledge and human skill components is to some extent industry-specific. Foreign investment, he argues, is able to proceed because of possession of this industry-specific comparative advantage, which can be exploited overseas. His model, which rests on the disproportionate effect on productivity when sector-specific capital moves from capital-intensive industry of the home country into the host country's labour-intensive industry, assumes that the latter experiences more productivity through direct investment than in the former "due to the smaller technological gap and a greater spill over of technology to local firms" (1978, p.126). In this process, while precipitating a change in the host country's industry the production frontier remains unaffected because the home industry's comparative advantage (in technology and managerial skills) does not fritter away simply because it is applied abroad nor are other internationally mobile factors (labour and capital) adversely affected. Kojima adopts the line of argument to explain the industrial structure of Japanese FDI. But Buckley (1985) observes that "Japanese FDI represents a search for location specific inputs (stable environment, low transport costs, but chiefly cheap labour) to complement the skills developed by Japanese enterprises".

In many respects the literature accepts that: (1) the firm-specific advantages -namely, access to a world-wide distribution network, transactional ability and managerial skills, and other intrinsic organizational qualities - of Japanese MNEs differ significantly from those of their American or European counterparts; (2) the industrial structure and distribution of Japanese FDI are markedly different from those of other industrialized countries; and, (3) the modelling apparatus of received microtheory (e.g. the product life cycle or the eclectic paradigm, although Dunning (1988, p.50) disagrees with the latter association) is insufficiently microanalytic to deal with many of the transactional phenomena of Japanese foreign investments (see, for example, Buckley, 1980).

In recognition of these, Ozawa (1979a,b) proposed a four-way classification for characterizing as well as distinguishing Japanese-type FDI, namely (1) the later takeoff of Japanese foreign investment, (2) regionalization of foreign investments, (3) labour intensity of Japanese investments, and (4) the openness of Japanese companies to other forms of international investment than FDI. Further joint investigation by Kojima and Ozawa (1984) reveals two additional distinctive features, namely (5) the high propensity to invest in their own commercial facilities, and (6) the prevalence of group-controlled investments. These must be seen not just as explanations rooted in the Ricardian orthodoxy of trade theory but, quite importantly, as peculiarities in the behaviour and approach of Japanese firms towards foreign investment. In this way, they may well be regarded as the *raison d'etre* for Japanese mode/pattern of foreign investment.

4.3.1 LATE ARRIVAL IN INTERNATIONAL ARENA

The first distinguishing characteristic can be associated with the later (than western countries) takeoff of Japan in the field of international investment. Japanese investors (including individual and institutional, portfolio and direct) are late-comers to the world arena of multinationalism in comparison to USA, UK, West Germany and other Western European countries. This late arrival vis-a-vis its potentialities (in terms of manpower and organizational skills) coupled with 'discrete' desire to 'catch up' with trends in international development must have provided a strong impetus to launch into the international market with such a rapidity. It must not be isolated, however, that the 'soft spot' which USA has had for Japan since after the Second World War - for obvious reasons - would have been somehow contributory, even if in moral supportive terms, to the phenomenal growth of Japan. With US influence over its western allies, any affirmative actions towards Japan were bound to rub off on both the economic and political relations.

4.3.2 REGIONALIZATION OF FOREIGN INVESTMENT

Another distinguishing feature of Japan's foreign investment behaviour is the tendency to cluster overseas investments by locational proximity. Regional concentration of overseas investments in Asia and Latin America provided Japanese firms first experience of FDI. Regionalization of foreign investments would seem to be a logical and prudent approach to 'attacking' the international arena, especially given the technological and other competitive strengths of US and European MNEs. At least, it serves as an FDI threshold in terms of geographical and socio-cultural proximity.

4.3.3 LABOUR-INTENSIVE FOREIGN INVESTMENTS

The third characteristic derives from the relative labour intensity inherent in the structure of Japanese industries. This can be attributed to three main factors. First, from a historical perspective, pre-war Japan was characterized by industrial backwardness and technological bereavement. Even the immediate post-war lacked the necessary infrastructure to support manufacturing and capital-intensive activities. Although all that is now history, they form the antecedent basis of labour intensity of contemporary commercial and industrial activities. Second, and also from historical development, Japan is largely a trading nation, and a feature of trading activities is the relative dependence on labour. As sketched above, the spectacular growth and development of postwar Japan and its present outward-oriented strategy of industrialization have been facilitated largely by the *sogo shosha*. Given the country's "almost complete dependence on overseas resources" (Kojima and Ozawa, 1984, p.12) on one hand, and the interest of labour-abundant developing countries (especially of neighbouring countries of Asia and Latin America) in attracting relatively labour-intensive manufacturing activities, on the other hand, Japanese firms - anxious to capture markets from western MNEs - tend to establish relatively small and medium sized ventures. These are modelled to offer LDCs a combination of labour-intensive, locally congruent technologies and a more friendly competitive industrial environment than large-scale, capital-intensive and overtly competitive American-type industrial ventures (ibid.).

Finally, the labour-intensive characterization of Japanese firms might have also stemmed from their cultural dependence on people rather than technology. This point is underscored by Ouchi (1981) in his analysis of Theory Z that, "success in terms of productivity, under Japanese culture, depends upon a company's ability to coordinate people, rather than technology".

4.3.4 OPENNESS TO NEW FORMS OF INTERNATIONAL INVESTMENT

The fourth way of distinguishing Japan's approach to international investment is the openness of firms to other modalities of foreign investment than FDI, in particular minority-equity interests and/or joint ventures. Japanese MNEs are generally viewed as more accommodating to the demands of host countries and more willing to accept 'new' forms of outward investment than their western counterparts (Ozawa, 1984). The high propensity to depart from foreign direct investment and to engage in minority-owned operations and/or non-equity contractural types is attributable to the combination of factors described above.

4.3.5 PROPENSITY TO INVEST IN THEIR OWN COMMERCIAL ACTIVITIES

Another important distinctive feature of Japanese overseas investments is the propensity of the *sogo shosha* to invest in their own commercial facilities. Kojima and Ozawa (1984, p.81) observe that unlike technology-based manufacturers, trading companies do not invest in research and development themselves; they do not generate knowledge internally, rather, they gather both cross-sectional and inter-temporal information about supply and demand conditions in commodity markets (from raw materials to intermediate and finished products) as well as services. The information set is then transformed and internalized as ownership advantage of the trading companies. Thus, as with western

MNEs, the more extensive the network of trading and marketing facilities, the easier and more effective it is for the *sogo shosha* to collect information. Effectively therefore, the ownership advantages and internalization capabilities of the *sogo shosha* derive from the multinationality of their operations. This contrasts with western MNEs whose multinationality (ability to multinationalize) depends in part on ownership and internalization advantages (see chapters 2 and 3 above).

The theory of Japanese trading companies' involvement in international production begins with their multinational trade-intermediating operations (of the co-operative and afiliative type and not of the internalization type). These give birth to ownership advantages that enable the firms to become effective organizer/co-ordinators of overseas ventures. Furthermore, in exploiting such ownership advantages, the trading companies do not show preference for, or interest in exercising, intra-firm, hierarchical controls of the sort observed in the western-type multinationality. Rather, they resort to variants of co-operative and affiliative modes: a loose integration of firm and market antecedent of Richardson's (1972) theory of co-ordination through cooperation.
Nevertheless, it is also observed that the conventional western-type FDI by internalization does apply to most of the overseas investments made by trading companies in *their own* global networks of branch offices and trading subsidiaries (such as Mitsubishi International, U.S.A., Mitsui & Co., Europe S.A., Sumitomo Corporation Italia, among others) (Kojima and Ozawa 1984, p.82). But, the internalization is of parametric information which the *sogo shosha* consider "crucial for their intelligence operations" (ibid.).

The crucial investment distinction here lies in the mode of generating the internalization advantage. As can be discerned from the various analyses of Kojima and Ozawa, the Japanese mode of generating internalization advantage appears to be non-idiosyncratic, information-specific, exogenously generated, and purely for intelligence purposes. It is rather the *effect* than the *cause* of multinationality. On the other hand, the western MNE type of internalization advantage is idiosyncratic, asset-specific, endogenously generated, and purely for monopolistic investment purposes. It is rather the *cause* than the *effect* of multinationality (for explanation of these terms, see chapter 3, section 3.3).

Clearly, the orientation and investment profile of Japanese merchants of foreign investment are markedly different from those of their western counterparts. The conceptual explanation under a transaction cost analysis framework, discussed in chapter 3, is consistent with empirical analyses (e.g. Ozawa, 1974, 1979, 1980, 1984; Kojima 1973, 1978, 1982,; Kojima and Ozawa, 1984; and Kujawa, 1986). One factor which is however common to both investment atmospheres (Japanese and Western worlds) is the prevalence of competition. Potential competitive disadvantage in a monopolistic production/marketing context attenuates the incentive to depend on contractual arm's length market mechanisms for future streams of earnings. Essentially related to prospective market failure problems of moral hazard (e.g. opportunism, externality and dissipation), western MNEs are empirically shown to prefer to internalize their firm-specific knowledge. As for their Japanese counterparts, while rivalry can be exceedingly fierce among the general trading companies for a particular piece of valuable information acquired by one of them, because the advantage possessed in the form of information is generated externally, internalization of such advantage is rather precarious (Kojima and Ozawa, 1984, p.82). Further, because the trading companies are in active competition both amongst themselves and with other countries MNEs, they generally adopt an approach, exhibiting a high propensity towards group investments.

4.3.6 GROUP INVESTMENT STRATEGY IN THE CONTEXT OF COMPARATIVE ADVANTAGE.

The last distinctive feature of Japanese overseas investment is the prevalence of group-controlled investments (ibid. p.83; Buckley, 1985). Kojima and Ozawa ascribe this peculiarity to the industrial organization of Japanese industry. The proclivity to establish intimate business relationships with a large and diverse number of companies (including banks, insurance and shipping companies) - in essence become an active member of a particular *keiretsu* group - is a commonality of Japanese MNEs. Both the transactional and financial intermediation features discussed earlier offer trading companies the opportunity to intermediate in a vast range of commercial and industrial transactions. Together with their information brokerage ability, trading companies are able to assist their own manufacturing subsidiaries and affiliates in economizing on production activities by relocating in a discriminating way. Their comparative transactional advantage enables them to shift production activities of subsidiaries from home to overseas whenever the benefits of home-based production are lost.

For instance, it was the trading companies that first detected a decline in Japan's comparative advantage in low-skilled, labour-intensive goods in the early 1960s and then urged Japanese manufacturers to establish overseas ventures in neighbouring Asian countries with lower wages (ibid). As organizer/co-ordinator of overseas ventures, the orientation of GTCs is clearly based on the doctrine of comparative cost advantage, whether it is to do with their subsidiaries wholly or a consortium within the affiliated *keiretsu* group.

Group integrated/controlled investment is particularly found to be an efficient mechanism of accomplishing transactions that are huge in scale, complex and resource-intensive. Generally, under western orientation of investment, such transactions will be pursued via consortium arrangements - a form of group-integrated/controlled investment. Here, there appears to be less systematic emphasis on governance structure (control) than there is on establishment of capitalized vehicle either as an entry mode and/or a diversification strategy. For Japanese firms, it is a 'pooling' of firm-specific comparative advantages of participating companies. It represents in efficiency terms a group integrated package of resources which offer a superior transaction cost economy over intrafirm arrangements.

Kojima and Ozawa clearly perceive the concept of group investment as transactionally superior to hierarchically integrated investment from a dichotomy of scale economies: "genuine" and "pseudo-" economies of scale. Both are defined in terms of pareto-optimality - that is, an equilibrium condition in which welfare maximizing decisions of firms simultaneously maximize (economy-wide) social welfare. Genuine economies of scale "are those that arise from the saving of real resources and the reduction of production or selling costs" (Kojima, 1978, p.225). They are pareto optimal since they are beneficial to both firms and society at large. Pseudo-economies of scale, on the other hand, increase private benefits at the expense of the society (through incremental social costs). An example is corporate transfer pricing practice which enables companies to potentially avoid or minimize taxes - an increase in social welfare costs or loss of social revenue - and thus enlarge private profits (for other illustrations, see ibid., pp. 225-227).

A limiting boundary between western-style of group investment and Japanese style is therefore one of degree of susceptibility to pseudo-economies of scale, according to these authors. Japanese group investment strategy organized under comparative advantage governance structure is seen to be less susceptible to pseudo-economies (both in structure and direction) than hierarchically integrated investments of Western MNEs.

4.4. SUMMARY AND CONCLUSION

In conclusion, a transactional interpretation of Japanese mode of foreign investment, in which the neoclassical theory of international trade based on comparative cost advantage is implicit, reveals interesting features about the structure and *modus operandi* of Japanese multinationals. Essentially constructed around the general trading companies, it is shown both empirically and conceptually that their overseas investment activities are distinct from those of the traditional "western" form of foreign direct investment.

A macroscopic analysis of the scale and complexity of the overseas operations of Japanese firms also reveals a facilitation based on integrated functional classification of (1) transactional intermediation, (2) financial intermediation, (3) information-brokerage, and (4) transactional organization/co-ordination. These enable the firms to develop the criteria and define the "efficient boundaries" (of an operating unit) for economizing on overseas transactions.

Finally, a conceptual explanation of these is surveyed through six interrelated frameworks, namely: (1) late arrival to international investment arena, (2) regionalization of foreign investment, (3) labour-intensive structure of foreign investment, (4) propensity to adopt new forms of international investment, (5) propensity to invest in their own commercial activities , and (6) the prevalence of group-controlled investment.

PART TWO

ALTERNATIVE STRATEGIES TO FOREIGN INVESTMENT

CONTENTS

PART TWO

ALTERNATIVE STRATEGIES TO FOREIGN INVESTMENT

This part explores the dimensions of new forms of international investment. The object here is twofold: to examine the identity of the alternative strategies, in terms of their dimensions, characteristics and strategic importance as foreign market entry modes, and to review related empirical studies.

As defined in Chapter One, new forms of international investment encompass a whole range of international operations that are thought of constituting a grey area between exports and direct investment. Precisely, they are not investments in majority or wholly owned foreign subsidiaries which conventially define foreign direct investment. Excluded also from this definition are bank lending and other financial operations, although these may be used to finance new forms of investment. They are therefore to be seen from their strategic implications for the firm's growth, profitability and/or global pursuits. Not all known forms of alternative investment strategies can be usefully addressed in a study of this kind nor are they all necessarily relevant within the definition of new forms.

The part consists of three chapters: chapters 5 to 7. Chapter 5, which is the first chapter of this part, is concerned with the dynamic structure of entry mode determinants and the influence of corporate development strategies. Chapter 6 overviews the strategic roles of exporting, licensing and franchising, contractual arrangements, and joint ventures on international investment. Chapter 7 concludes the part with an examination of the applicability of new forms to international banking.

PART TWO

CHAPTER FIVE

CORPORATE STRATEGY AND THE FOREIGN INVESTMENT DECISION PROCESS

CONTENTS

5.1 INTRODUCTION

The growth of international business may be said to have followed a three-stage historical cycle. The first cycle is the prewar pattern of international business, dating back to the Industrial Revolution, which was essentially in trade form. This period witnessed a massive worldwide expansion of trade and significant increases in the amount of non-equity foreign investments.

The second cycle in the growth of international business is the postwar emergence of multinationals. The postwar period, particularly during the 1950s and 1960s, was accompanied by a continued rapid growth of multinational, mostly U.S.-based, firms through the establishment of wholly-or majority-owned foreign subsidiaries. The third period of the historical cycle is the contemporary rapid expansion of international investment. This period dates back to the 1970s and has seen significant increases in the flow of foreign investment worldwide. In particular, since the mid-seventies the flow of financial capital has shown more rapid growth than that of FDI, but also the variety of forms of international involvement has witnessed enormous expansion and has consequently assumed an increasingly important role in the world economy. What is less clear though is the significance of the growing diversity of forms which such investment has taken since the early 1970s, and more prominently in the 1980s.

Until the 1980s a disproportionate amount of attention was given to the growth and development of companies by forms other than direct investment. The term "new forms of international investment" is an OECD concept applied to the organizational modes of international business operations which lie between simple exports and direct investment (in the form of wholly-owned foreign subsidiaries) (Oman, 1984). Generically, they are defined as international investments in which foreign participation does not involve a controlling equity interest or constitute majority ownership. More specifically, new forms of international investment (NFIs) encompass:

(a) joint international business ventures in which foreign-held equity does not exceed 50 per cent; and

(b) international contractual arrangements in which the foreign firm may have no equity involvement, but the nature of its participation constitutes an investment, such non-equity participation will involve some element of risk on the part of the foreign firm, provide it with some control, and yield returns in future periods (see, for example, Oman, 1984, pp. 22-23, for a distinction between investment and sale).

All these arrangements are typically referred to as 'alternatives' to FDI or, more generally, 'markets'. In terms of historical usage/significance, foreign investment in forms other than foreign direct investment is not a new phenomenon, nor are such modes of investment particularly a less developed country phenomenon (Cf. Oman 1984). Although the tendency to adopt new forms may be more transparent in developing economies, their usage in and between developed countries has been documented in a number of studies. For example, joint ventures (an aspect of NFIs) have been found to be frequently used by Fortune 500 companies in developed countries (Janger 1980; Harrigan, 1985). Also, foreign investments in forms other than wholly-owned subsidiaries (e.g. licences) have been found to predominate in U.S.-based companies by a ratio of 4 to 1 (Contractor and Lorange, 1987).

The reasons for the increasing adoption of the new forms are varied: they are partly firm-specific (i.e. relating to factors internal to the enterprise); they are partly country-specific (host and/or home), or they may be influenced by managerial perception of the significance of the factors or their perceptions of the impact of entry made choices on shareholders' wealth. In terms of host country influences, the growing tendency to favour new forms in LDCs in part reflects strategic macro-economic aim of acquiring technological transfer and the development of indigenous skills and technology. Growing nationalism, global competition, changing fortunes in financial markets, economic and political integration of regional markets (such as the EEC, OPEC, the US-Canada Free Trade Agreement, etc), and the increasing democratization of the Eastern and Communist bloc are all aspects of environmental stimuli (or distortions) that are prospectively associated with changes in corporate foreign investment strategies.

This chapter, which is the first in part two of the study, explores the alternative modes of international market entry and development. Internationalization of business operations has become particularly engaging in the process of providing a wider context within which corporate expansion goals are pursued. The dynamics of the international environment force changes both in the direction and method by which economic activities are organised. As a result, increasing importance is being attached to the modes of market entry and development strategies employed by firms in foreign markets. These are the subject of exploration in this and next five chapters.

The object of this chapter is to discuss the dynamic structure of entry mode determinants and the influence of corporate development strategies. These are pursued in sections 1 and 2, respectively. The chapter concludes with a typology of new forms, as a prelude to a more detailed discussion of their structures in ensuing chapters.

5.2. A DYNAMIC STRUCTURE OF ENTRY MODE DETERMINANTS

The theory of New Form of Investment (NFI) may be described as a re-assessment of the explanatory/predictive powers of markets and hierarchies. It is a re-assessment in the sense that traditional frameworks (discussed in part 1) have been found inadequate in addressing divergent foreign investment practices. The reason is that they focused on one mode of organization, namely FDI. In particular, it has been recognized since the early 1980s that a variety of forms of investment and industrial cooperation have assumed an increasingly important role in the international investment and diversification strategies of firms. The growing importance of these forms, which, have largely been perceived in a North-South context, has raised a considerable interest in the future of FDI, the changing division of roles of the major participants, and their implications for small and medium-sized firms (See, Oman 1984, 1986), among others.

The phenomenon of interest concerns the choice and impact of entry modes on the success of foreign operations. Theoretical recognition and redirection has warranted a reformulation and/or relaxation of the underlying assumptions of extant paradigms in order to accommodate positive trends in the use of non-FDI entry modes by firms. A dichotomy of issues lies at the substratum of the analysis (Figure 5.1):

1. the locational structures which encourage or support foreign firms to establish corporate presence in the host country; and

2. the governance structures necessary to exploit opportunities, or to overcome obstacles, existing or potential.

These two structures are discussed the context of the dynamic features of host countries' perceptions of the impact of firms' choices of modes of entry on their economic, social and political fabrics.

5.2.1 LOCATIONAL STRUCTURES

To encompass positive developments in host country attitude towards foreign investors, a somewhat different taxonomy from Dunning's may be proposed to distinguish among natural locational endowments and unnatural (contrived) set of institutional arrangements that both characterize the politics and set the context within which the integrity of foreign investment transactions are decided. This set of structures relates, but not restricted, to conventional location-specific advantages enunciated by Dunning.

The literature states that country-specific features have to be strongly attractive in order to lure firms of one or more national origins to locate in another. Traditional FDI perspective regards locational factors as consisting mainly in tangible resources (e.g. raw materials), human and material infrastructure. However, practical events in many countries lead to the conclusion that this view is not only simplistic but, in fact, beclouds the structures that decide such advantages. The imperatives of political independence makes complex foreign structures in the form of inward direct investment to be circumspect, and, in some ways, characterized as imperialistic.

Failure to recognise this, and constant reference to locational advantages as deriving from a firm's oligopolistic propensity (Knickerbocker, 1973; Flowers, 1976; Graham, 1978, 1985; and Dunning, 1977, 1981, 1988) among others, is to ignore the growing concern and hostility of host country political systems toward what they perceive as 'imperialistic tendencies'. This feeling is not peculiar to LDCs. Consider America's grudge over Japan's inward investment practices. Pat Choate, in his book "Agents of Influence", describes how the Japanese have penetrated the US economic, political and education systems while keeping their own closed to outsiders. He expresses "the concern shared by American politicians and academics" about Japan's outward investments and how they protect and promote these by erecting a complex infrastructure of political and strategic influence throughout America. If America can be so disturbed by the scale and complexity of inward FDI, how much more would small nation states?

While a country's natural immobile resources are its provenance structures and have to be utilised *in situ*, however, the politics that surround their utilization, and which, in fact, decide whether a foreign investor may be able to internalise or externalise their usage are subject to human contrivance and thus negotiable. The distinction between *ex ante* and *ex post* locational advantages, which had not previously been made, is crucial to the argument. It is therefore argued that it is the local politics which unlock economic advantages of any location. A complete treatment of locational structures requires that the limits as well as the powers of country-specific properties be assessed. The properties of a country that commend locational structures as inward-investment enabling factors would appear to fall into three categories: incentives, controls, and what may be referred to broadly as 'innate structural advantages'.

INCENTIVE STRUCTURE

In an incentive sense, locational structures manifest in those government policies which foster inward investments. Incentive schemes are significant in that although a country may possess natural endowments, if it pursues policies which progressively attenuate the bargaining power of inward foreign investors, then there is a risk that the attractive properties of its tangible resources may be lost. In circumstances where hard bargaining between government agencies and the firm over locational utilization of resources is crucial, the foreign firm's oligopolistic propensity may be in active conflict with the host government, especially if wider issues about control are strategic to both parties.

CONTROL STRUCTURE

Closely related to incentive investment scheme is the sensitivity of control instruments that are attached to a set of locational structures. A clear example is the sort of inward investment policies pursued by India where, regardless of the sophistication or attractiveness of the investment, control is rarely abdicated to the foreign firm (See, Desai, 1984). Control has traditionally been associated with the firm, in terms of its constitutional authority over intra-firm activities and of possessing an efficient conflict resolution machinery. However, control instruments can be assigned to locational resources by virtue of their nature, strategic importance to national economy, or a combination thereof. An example is the banking sector or defence industry where active government controls preclude, or at least monitor very closely, the possibility of foreign domination.

Furthermore, there is a considerable number of measures which, regardless of how open or developed a country's economy may be, represent obstacles on the ability of foreign investors to engage in certain investment practices. Country control instruments come in the shape of laws, regulations and administrative practices which affect the ability of non-residents to undertake direct investments, or, even, to participate in certain investment activities exclusively reserved for indigens.

The common feature among host country investment policies is the politics that surround foreign equity investment. While the economic advantages of a foreign investment are acknowledged, the often unspoken concern of many host governments is the degree to which their economic and, perhaps, social fabrics may be eroded by 'unguarded' foreign domination of enterprises. Take this away, and inward direct investment will be less of an issue in respect both of economising properties and bargaining potentials.

INNATE STRUCTURAL ADVANTAGES

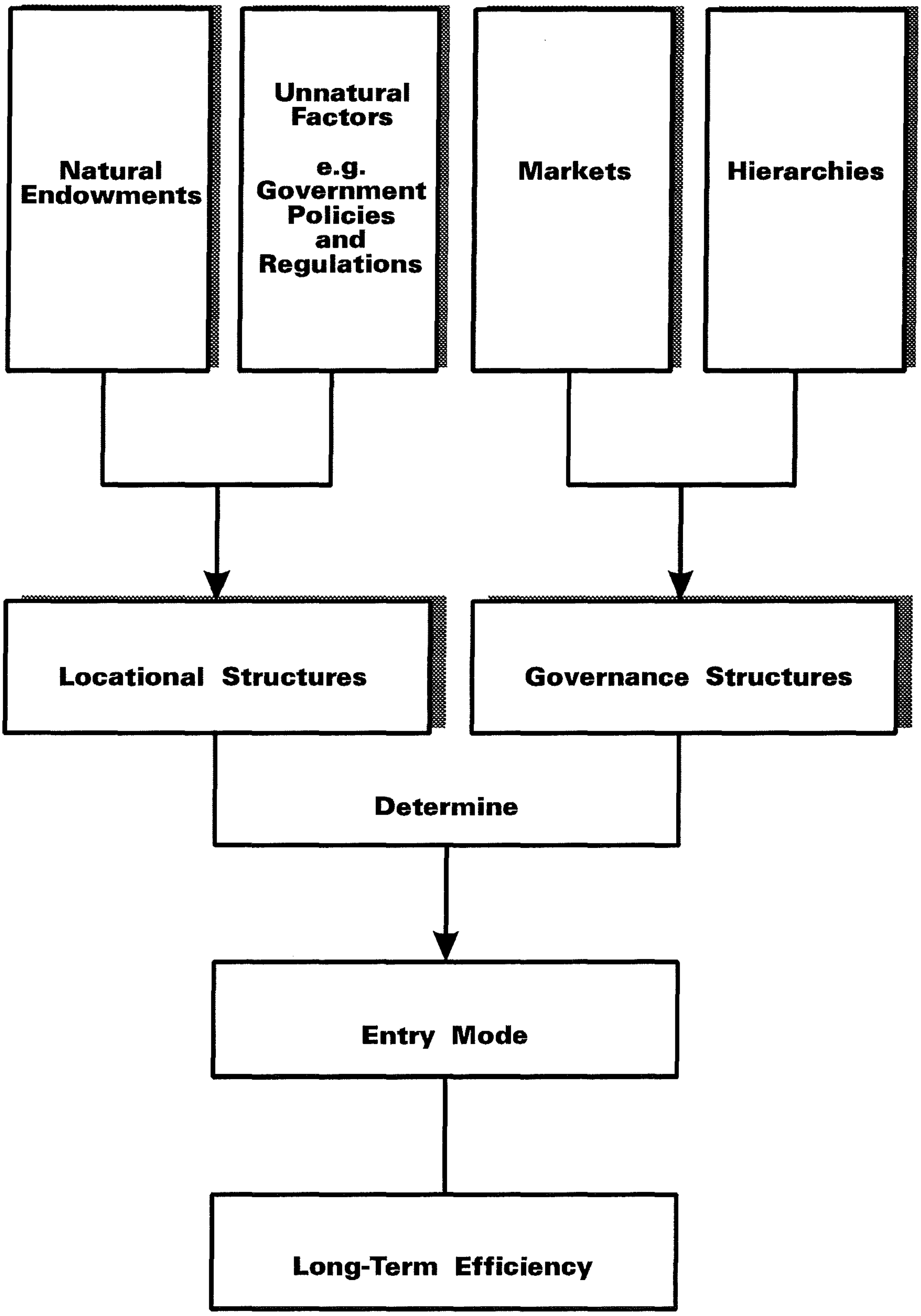
Innate structural advantages reside mainly in what is regarded in economics as 'comparative advantage'. The idea that economic inputs, especially immobile natural resources, are most efficiently employed in their place of origin, *ceteris paribus*, is both interesting and engaging. The importance of innate structural advantage is that it suggests that, even if there are institutional bottlenecks, it could still be efficient to invest in the domain. Examples of innate structural advantage abound in the oil and extractive industries, such as offshore oil deposits, gold and other mineral mines, etc. They are often a source of firm-government bargains and the degree to which the balance tilts depends on the incentive and control differences described above as well as the coordinating properties for organizing economic exchanges. The firm needs to assess two primary sets of variables in order to engage in effective decision making about its entry mode strategy.

5.2.2 GOVERNANCE STRUCTURES

The notion of governance structures is conducive to a study of, or a sensitivity to, transaction-cost issues. It seeks to supplant the conception of the firm as a production function by one of the firm as a governance structure (Williamson, 1975, 1986). The traditional notion of the firm as a production function to which a profit-maximization objective is assigned has had good economics following. By governance structure is meant the institutional framework within which the execution of transactions is accomplished and their integrity is decided (Williamson, 1986, p. 155). The literature recognizes markets and hierarchies as two main alternatives.

The theory of governance structures seeks to address the transactional properties of alternative modes of organizing foreign business operations. The thesis of alternative governance structures is concerned mainly with (1) growing corporate propensity to depart from traditional powers of internal organization as a means of accomplishing foreign investments, (2) recognizing the declining properties of vertical integration as a strategic means of achieving international diversification, and (3) providing, in a comparative institutional sense, the efficiency properties of alternative modes. The emphasis on internal governance is on the distinctive strengths of FDI, but fails to acknowledge its distinctive weaknesses. Because of these reasons, issues concerning alternative governance structures have become particularly engaging in recent international investment practices and international business research.

Figure 5.1 A Framework of Entry Mode Determinants



The firm needs to assess two primary sets of variables in its entry mode Strategy: Location and Governance Structures

NFI propositions seek to explain divergent practices in the market place which offer alternatives to FDI, on the one hand, and both technological interdependence and technical complementarity, on the other hand.

There are merits, in political and transaction-cost economizing terms, in assigning internal governance structure to certain foreign investment operations. The affirmative argument is encapsulated in the theoretical frameworks reviewed in Part One. In summary, the general proposition is that the firm is a superior mechanism for allocating resources. The efficiency powers of the firm reside in its internal governance structure by which it is able to control allocation of resources, resolve conflicts by fiat and economize on transaction costs. As for alternative governance modes, general references to market failures are frequently employed to justify substitution of internal organization for market-mediated exchange.

The object of this study is to present the potential capacity of new forms of investment to offer a wider variety and greater sensitivity of the strategic contexts that describe foreign investment activities. In the discussions that follow, the term 'alternative' is used both in the sense of replacement choice, and in terms of available option from several possibilities. Claims of alternative governance structures are therefore claims of complementary operational entry modes of accomplishing foreign investment activities.

In short, but for the control differences between NFI and FDI, (see Table 5.2 below), the operational and strategic complementarity of markets and hierarchies will challenge any orthodoxy that seeks to discern the supremacy of one mode over the other. It has been argued that markets and hierarchies framework, while being a powerful paradigm for discussing alternative modes of accomplishing transactions is static in nature (Calvet, 1981). The author advocates the need for an understanding of the forces that compel transactions to be internalised or externalised as well as the political and social implications of the international spread of hierarchical forms. It is in this context that the arguments of locational and governance structures are constructed. The taxonomic implication of locational structures is the opportunity it offers to introduce political and social considerations into the location theory. According to Calvet, these issues have been carefully and purposely avoided. But, for how long will they be excluded from the equation when the imperatives of growing nationalism are challenging the control structure of FDI? An inclusion of this awareness and recognition of transactional properties of alternative governance structures may add dynamism to the static configuration of the markets and hierarchies framework.

5.3 DEVELOPMENT STRATEGIES OF THE FIRM

In considering strategic alternatives, three key corporate objectives would appear to be significant in relation to adaptive, sequential decision-making. These are: (1) To consolidate businesses and operating presence in the home market. (2) To develop interests in key strategic foreign markets. For a UK enterprise, principal strategic foreign markets may include Western Europe, North America and Far East (in particular, Japan). (3) To enter new, high growth product markets or sectors compatible with the enterprise's specific advantages.

These objectives provide a framework for adopting a policy of 'business focus' in the market place. Three critical questions are raised in a policy of business focus: (1) Where, within its business segment, can a firm achieve the best competitive advantage in the market place? (2) Where does the firm see the greatest market growth? (3) Where can it leverage its resources and expertise (FSAs) most effectively?

Translating corporate objectives into business focus, as sketched above, simplifies the complexity associated with the development of strategies. The process provides a perspective that is pragmatic and complementary to the four-way taxonomy of Young, et al (1989). Under the heading of broad development strategies, the authors make a distinction between the following constructs:

- Stability: implying that the firm remains in the same business with no difference in the pursuit of existing objectives and in the level of commitment. This is consistent with objective (1) and question (1) above, namely, consolidation.
- Expansion: suggesting diversification into new markets or business areas (product, geography or both), with the aim of increasing sales,

profits, market share or taking up a competition position. This is consistent with objective (3) and questions (1) and (2) above.

- Rationalization: or what the authors term 'retrenchment', by which unprofitable markets (product and/or geography) are pruned off, resulting in a leaner and more efficient management structure. Liquidation, sell-out and divestment are development approaches of corporate rationalization or retrenchment strategies. This is consistent with objective (2) and question (3) above.
- Combination: implying a combination of the above, either as a sequential and adaptive process or a simultaneous process. This is mainly relevant to large, divisionalized companies.

The preceding discussion can be summarized by the schematic in Figure 5.2. It should be noted that these broad strategies are not mutually exclusive. Thus, it is possible to find an enterprise stabilizing its operations in the domestic or a particular foreign market; expanding into new product/service lines or geographic areas; scaling down its operations in some other markets; completely divesting of its activities in some product lines or markets; or executing all or some combination of the above, simultaneously. However, it is also possible, given the firm's size and scope of operations, to pursue any of the broad strategies independently.

5.3.1 DIRECTIONS OF DEVELOPMENT STRATEGIES

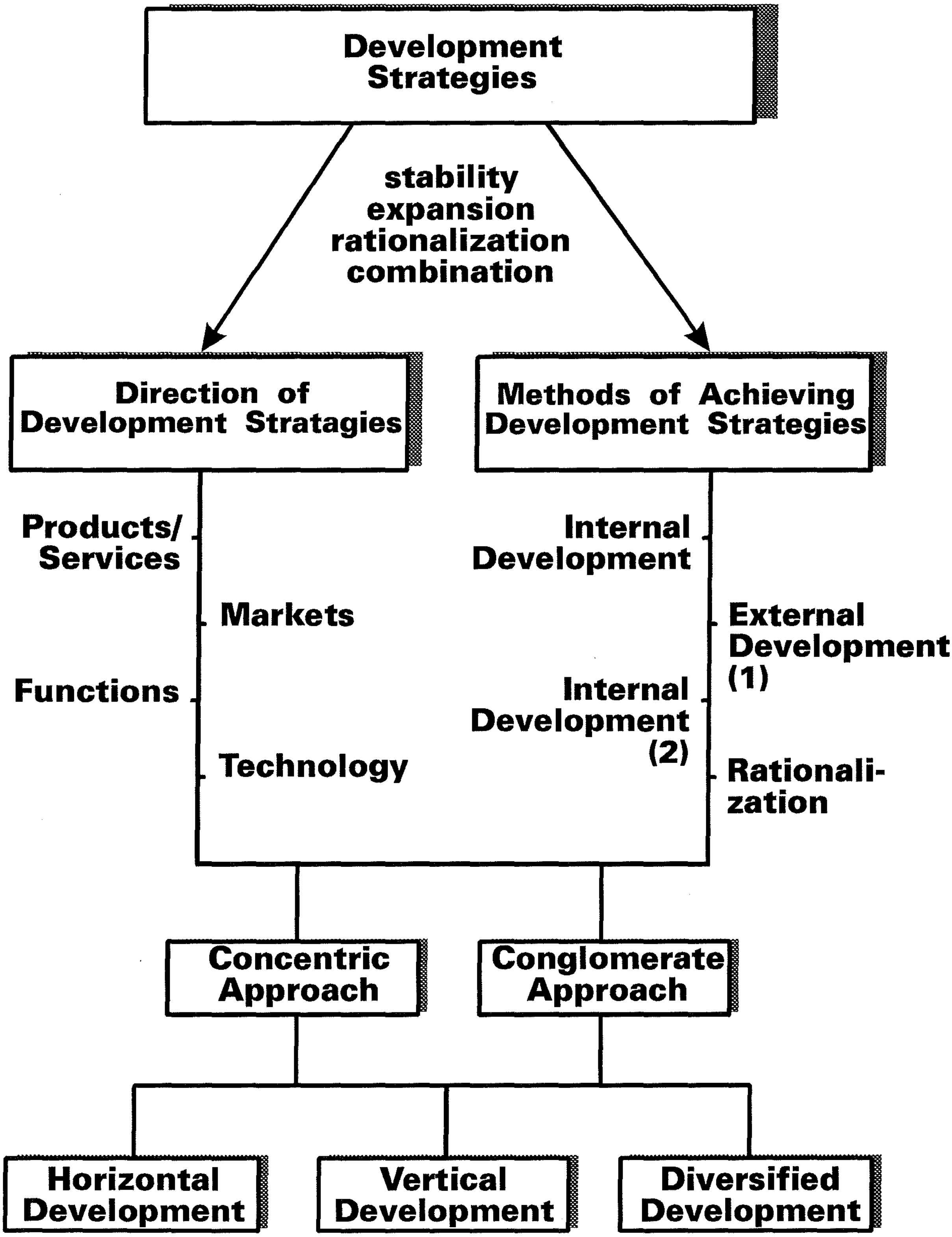
The next step for corporate management is to decide upon the direction of development that is compatible with its chosen strategy. A firm may choose to develop any or a combination of the broad strategies by product or service, by geographic market, by line functions, by technological application, or by a combination thereof. For instance, a UK bank wishing to stabilize and/or diversify its operations in say, Spain, may extend its credit card facilities and cashline services to its Spanish customers. It may also diversify into non-bank services such as trustee and insurance services, investment banking services, portfolio management services, and so on.

Consider further the following extracts from the chairman's statement of the undernoted companies:

> ... From the strong platform (of annual sales of over £3 billion and almost 300 stores covering the UK market), we are now committed to the next phase of our development. We shall reinforce Safeway's historic strengths in unprocessed fresh foods and we shall become significantly better in a number of areas where we have identified scope for improvement. These include supply chain management, detailed merchandising and store replenishment, own brand development and consumer marketing ... (Alistair Grant, Chairman, Argyll Group PLC, 1990).

> ... GEC's strategy for the 1990s was set out in the circular sent to shareholders on 17th August 1989. A principal objective was to develop a substantial and profitable presence in European markets in advance of 1992 through acquisitions and international alliances ... (The Rt. Hon. Lord Prior PC, Chairman, GEC PLC, 1990)

Figure 5.2 Development Strategies of the Firm



Source: Adapted with modification from Young, et al.(1989, Figure 1,1)

The preceding statements exemplify generalizations of strategy development paths followed by most firms. The series of interviews carried out by this researcher as part of this study reflect this general approach to corporate development. Having determined the direction upon which it is going to pursue, the next step for the firm is to determine how best to accomplish it. Precisely, how will it achieve its development strategies?

5.3.2 METHODS OF ACHIEVING DEVELOPMENT STRATEGIES

There are basically two methods of achieving firm strategy. One is *internal development*; and the other is *external development*. Internal development encompasses rationalization and offers a firm a distinct opportunity to review its existing operations, markets (product lines and/or geographic bases), production techniques/facilities, marketing and management functionalities, financial position and so on. In effect, internal development method presents a picturesque account of the balance sheet of the firm: it provides corporate management and shareholders a graphic account of the strengths and weaknesses of the firm, with respect to its specific competitive advantage as well as to competitors.

Through internal development, a firm may also be enabled to take stock of the performance of subsidiaries and business units as well as line functions. Available evidence may suggest plant/market closure, product/project abandonment, or some form of structural adjustment. Thus, it may be instructive, before resorting to external development method, to review present firm activities - markets and products - with a view to ensuring that the fabrics of the corporate profile are consistent with the type of development it seeks to pursue.

Achieving corporate strategy through external development methods is exciting, promising and demanding. Several options are available in the market. However, factors both endogenous and exogenous the firm present limitations on its ability to devise methods that are particularly suited to its purpose. In general, the firm's ability to use any particular method is a function of its specific characteristics, including industrial belonging, market forces and political processes (host and home) and managerial perceptions.

External development methods are market-mediated mechanisms. They include mergers and acquisitions, joint ventures, licensing, and all forms of inter-firm collaborative and contractual alliances. External methods can be used in conjunction with internal mechanisms. The capacity to utilise both avenues is a powerful test of the firm's strength in the market place, but depends, however, on the same set of factors, as already mentioned. Each of these groups (that is, directions and methods) leads to either a concentric or a conglomerate approach. Where the direction of corporate development or the method thereof involves related products, related markets, etc., that approach is regarded as *concentric.* A *conglomerate* approach, in contrast, is a strategic development involving unrelated products or markets.

Further classification of these approaches distinguishes between vertical (forward), horizontal (backward) and diversified integrations or developments. *Vertical integration* is a common investment feature of the petroleum and extractive industry. The tendency is to use the internal mechanisms of the firm to establish control and hopefully minimize transaction costs. The type of firm-specific advantages (FSAs) that the firm seeks to control or protect is always generally determined by external market imperfections (Rugman, et al., 1986, p. 112). The pairing of environmental factors of uncertainty and small-numbers exchange relations with human factors of opportunism and bounded rationality (Williamson 1975, 1980, 1981) are especially important. Transactional economies, externality reduction, and the propensity to control via the administrative fiat prospectively lead to vertical integration. Thus, an international oil company, such as Shell or Mobil, would choose to control and co-ordinate the extraction, transportation, refining, and marketing of petroleum instead of employing the services of autonomous market agents.

The argument of lower transaction costs and efficiency, while justifiable and credible, may, in *stricto senso*, not be the driving force, for those can be achieved via market mechanisms. I contend within the framework of Stigler (1968) that if transactional economies and efficiency are removed from the equation, an argument for plausible antisocial consequences can be forcefully engaged. Anticompetitive effects of two types are commonly attributed to vertical integration: price discrimination and entry barriers

(Williamson, 1975). Where the companies are large and conglomerate, a third anti-trust public policy issue arises, namely monopoly.

Horizontal expansion, on the other hand, is a development strategy in which the firm expands its product/service market in different geographic areas. Thus, rather than locate different stages of the production or marketing process in various countries (vertical expansion), a UK company can expand into US and/or other European markets on the same product line. Banks and professional/consultancy firms, (e.g. accountants, architects, etc) adopt horizontal diversification. Most large MNEs have expanded both vertically and horizontally. Ford Motors is a common example. ICI and Nestlé exemplify strategic movements from vertical to horizontal, vice versa, as this is common with conglomerate firms.

Conglomerate diversification is the zenith of corporate growth and diversification. The major multinational companies - of which there are really few in the UK but many in US and Japan - are all conglomerately diversified. A firm qualifies as a conglomerate if it produces (i.e. manufactures or services) internationally a diversified range of products. Take ICI Plc, as an example. Headquartered in the UK where it has over 50 production sites, the company is spread all across Continental Western Europe with 97 manufacturing/research/administrative bases and across Eastern Europe with production facilities in 11 countries. In North America, it has 137 operational facilities with USA accounting for 106 and Canada the remaining 31. In Latin America, it has 48 operational bases, 39 in Asia Pacific, 127 in Australasia (Australia 118 and New Zealand 9), 17 in Indian sub-continent, 10 in Middle East, and 54 in sub-saharan Africa. In all, ICI employs over 130,000. Its principal activity sectors include: Agrochemicals and Seeds, Pharmaceuticals, Petrochemicals and plastics, General chemicals, Paints, Fibres, Industrial explosives, and other effect products (such as colours and fine chemicals, specialty chemicals, films, electronics, etc.).

Another example is the ITT, a giant US conglomerate. Its scope of diversification includes electronics, telecommunications, pharmaceuticals, cosmetics, insurance, food, electricals, sanitary fittings, leisure and hotels, etc. Most conglomerates develop from purely resource-based enterprises and spread both horizontally and vertically. The need to economize transaction costs and the desire to internalize related set of transactions, thereby ensuring that they are governed by administrative processes of the firm, prospectively leads these firms to create in-house markets (e.g. credit and finance). Some conglomerates extend their interests into banking and finance, insurance and shipping, etc. Although Western MNE's have produced some of the world's largest conglomerates, however the rapidity with which Japanese firms, the *sogo shosha* (or general trading companies, GTCs), have metamorphosed into giant conglomerates is outstanding. Indeed, they are fast overtaking US giants not only in the scope of their product diversification, but also in their geographic spread. Table 5.1 illustrates the extent of product or sectoral diversification of top nine Japanese GTCs.

Table 5.1 Scope of Economic Activities of Top 9 Japanese Conglomerates

ACTIVITY SECTOR	KITSUI	MITSUBISHI	MARUBENI	C.ITOH	SUMITOMO	NISSHO	IWAITOMEN	KANEMATSU	NICHIMEN	TOTAL VENTURES	
										No	%
Agricultural, Marine and Forestry products	12	2	5	1	0	1	3	0	2	26	10.6
Minerals and Fuels	2	0	1	1	0	1	2	0	0	7	2.9
General Commerce	2	3	1	1	2	3	2	1	1	16	6.5
Manufactures: Food and Beverages	4	0	0	0	0	0	1	1	0	6	2.4
Textiles	6	1	5	6	0	0	3	1	3	25	10.2
Metal Products	6	4	2	2	4	2	2	0	0	22	9.0
Motor Cars, motorcycles and Parts	5	3	8	9	5	1	1	0	1	33	13.5
Chemicals	2	1	0	0	0	1	0	1	0	5	2.0
Electrical Machinery	0	17	4	3	0	0	2	1	1	28	11.4
Non-electric Machinery	3	0	11	5	4	2	1	1	3	30	12.2
Sundries	16	10	8	4	1	1	6	0	0	47	19.2
Total by company	58	41	45	32	16	12	18	12	11	245	100.00

Source: Kojima and Ozawa (1984)

Within the framework sketched in Figure 5.2 and described above, it can be seen that a variety of options are open to a firm seeking diversification and growth either in product market or geographical market or both. While the expansion strategy can be pursued within the firm's home country, the context of multinationalization is inharmonious with domestic (market) diversification. For analytical purposes, however, it is useful to present both strands as Figure 5.3 demonstrates.

5.3.3 CLASSIFICATION OF DIVERSIFICATION ALTERNATIVES

Two questions are fundamental to a firm's decision to engage in diversification? Consider these in turn.

1. Does it seek to diversify in the domestic market or foreign market? The consideration of this question is invariant to whether or not the firm already operates in foreign markets. Rather, the overriding consideration hinges on the firm's global strategy or future development. Consider, for example, the excerpts of the diversification strategies of the following three companies, drawn from three different industrial sectors.

(a) ... For some time, both we and Banco Santander Group have recognised the importance of increasing our presence beyond our traditional domestic frontiers.... In short, we are embarking on the implementation of a strategy for European development. We believe that strategy to be viable and flexible and that it will allow us entry to Europe at low cost and with low risk ...
The Royal Bank of Scotland Group plc "Announcement of Unique European Alliance with Banco Santander Group", 6th October 1988.

(b) ... Our principal objective is to develop a substantial and profitable presence in European markets in advance of 1992 through acquisitions and international alliances ...
GEC plc, Annual Report and Accounts, 1990.

(c) In common with other retailers, Argyll relies upon effective trading relationships with a wide range of suppliers. The creation of the Single European Market is encouraging many leading manufacturers to operate on a pan-European basis affecting their procurement, production, marketing and selling strategies. For this reason, Argyll has formed two important associations in order to establish progressively a pan-European retail grouping with a network to match the European scale of the manufacturers ...
Argyll Group plc, Annual Report and Accounts, 1990.

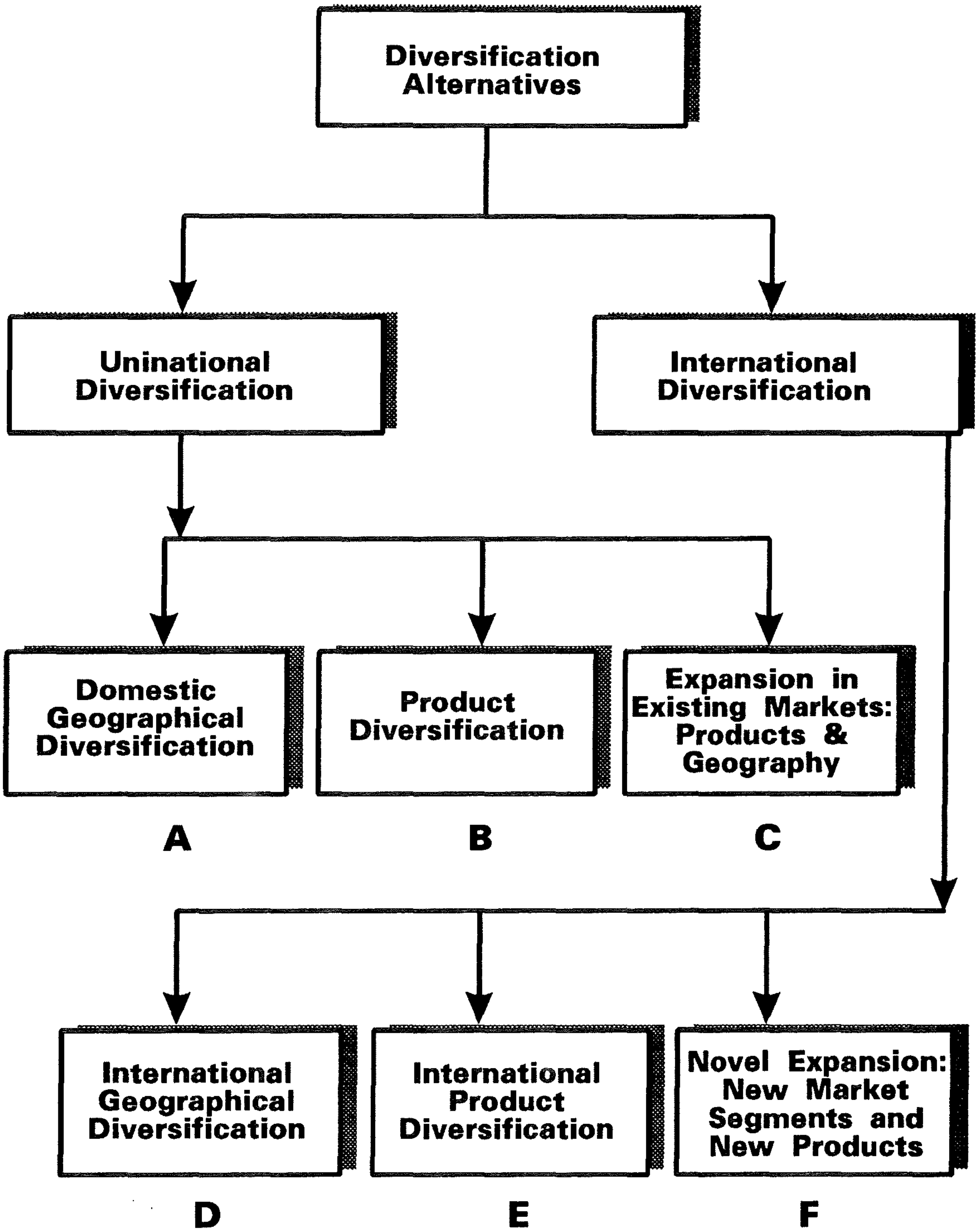
2. Assuming that the company has decided the geographic domain of the diversification move, will it then be market segment based, product/service based, or a combination of both?

A geographical diversification *per se*, whether domestic or international, involves expansion into new market segments while holding product/service constant. A product/service diversification, on the other hand, involves expansion into new product/service market while holding the geographic segment constant. In this case, the company launches new products or services into its old and existing markets. A third variant involves a combination of the above two, namely launching into new market segments with new products. This may be regarded as a novel diversification or expansion strategy.

Johnson Mattheys plc exemplifies a strategic consideration that incorporates the features of Figure 5.3.

> ... Our objectives are: to consolidate our core businesses and operating presence in our home market, to develop interests in key strategic foreign markets, e.g. Europe, North America and Far East, and to enter new, high growth sectors such as networks and services ...
>
> Johnson Mattheys plc, Annual Report and Accounts, 1990.

Figure 5.3 Classification of Diversification Strategies



Notation:

A: Involves same product/services in new market segments
B: Involves new products/services in present/existing market segments
C: As the strategy implies
D: Same as A but in foreign market(s)
E: Same as B but in foreign market(s)
F: As the strategy implies

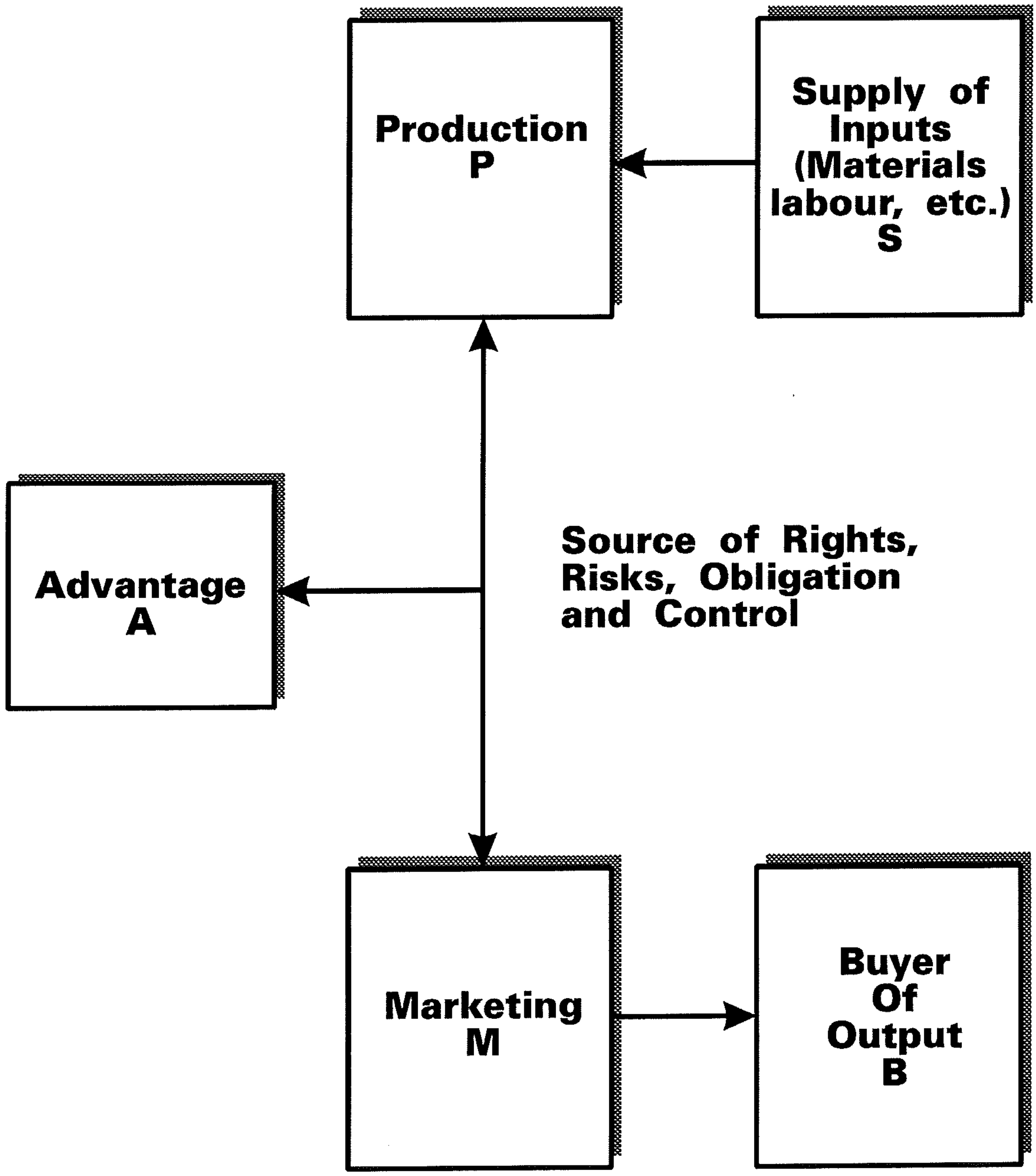
5.4. A TYPOLOGY OF NEW FORMS

International business arrangements can be classified in any number of ways. Common literature classification dichotomizes between equity and non-equity arrangements or, more technically, between hierarchy and market. The usefulness of this polarization lies in its analytical simplicity, namely: the relative ease with which risk is linked with control and ownership. Under a hierarchy, risk is assumed to be progressively attenuated via administrative fiat of a common governance structure. Under a market structure, the ratio of risk to control and to ownership is assumed to be high in each case. The reason is often associated with the transactional limits of markets and the sources of market failure. In relative terms, markets are assumed to lack the efficiency of sequential adaptations to uncertainty and risk and, as such, are an inferior administrative process for accomplishing transactions.

The missing thread in this argument, and one which is central to a possible resolution, is the inadequate symmetrical analysis of markets. Williamson recognizes this fact but uses the inadequacies of markets as an alibi to invoke hierarchy. Basic to such a comparative analysis is the following proposition: Just as hierarchical structure matters in assessing the efficacy of internal organization, so does market structure matter in assessing inter-firm transactions. In the end, whether a set of transactions ought to be executed across markets or within a firm depends on the relative efficiency of each mode vis-a-vis the firm's goal.

Several possible 'markets' are identifiable, depending on whether the environment of operations is products/services or finance. It is important to make this clarification for the following reasons. First, literature emphasis on multinationality has long centred around manufacturing/extractive industry, although application of extant theories to financial and service industries, such banks, and hotels, is now growing.

Figure 5.4 The Structure of Entry Mode Arrangements



Source: Derived with modifications from Casson(1986)

Second, different nomenclatures distinguish foreign entry modes of financial institutions from those of non-financial enterprises, although some commonalities exist. For example, joint venture operation is regarded in banking as 'consortium'. Finally, since this study is about the identity of 'alternative' forms of international investment, its scope is not restricted to any particular industry; it covers banks, as financial enterprises, and non-financial enterprises, broadly defined.

A TAXONOMY OF NEW FORMS

For analytical purposes, it maybe convenient to distinguish nine main types of 'markets' or contractual arrangements. Variants of some these are discernible. The various permutations are derived from the schematic, Figure 5.4, and their structure is indicated in Table 5.2. The structure of entry modes illustrated in Figure 5.4 represents non-financial enterprises, although interpretations apposite to the financial sector can be deduced. These are discussed in greater detail in the following chapters.

Table 5.2. Control Structure of New Forms of International Investment as Applicable to Non-Financial Enterprises

	MODE OF INVESTMENT	CONTROL ALLOCATED TO PARTNERS FOREIGN	LOCAL	COMMENTS
A	JOINT INTERNATIONAL BUSINESS VENTURES:			
1.	Equity Joint Venture	A.P.S.M.	A.P.S.M.B.	Both partners contribute to the assets of the venture, share risks and profits, and participate in the ownership of the enterprise.
2.	Non-Equity Joint Venture	A.P.S.M.	P.S.M.B.	Here the foreign partner has no equity stake in the venture, but brings resources which contain some element of risk sufficient to command or warrant control.
3.	Industrial Co-operation Agreement	A.P.S.M.	P.S.M.B.	Similar to 1, but with time limit on equity and possible restriction on terms (e.g. payment)
B	INTERNATIONAL CONTRACTUAL AGREEMENTS			
1.	Export/Overseas Agency	A.P.S.M.	M.B.	The relationship may be more than that of a casual seller-buyer. Has become an age-long and the easiest route to foreign investment.
2.	Licensing	A.P.S.	P.S.M.B.	Foreign licensor provides local licensee right or access to technology in return for financial compensation.
3.	Franchising	A	P.S.M.B.	A particular type of licensing, and often seen as part of the parent chain than a single business enterprise, except that the franchisee retains control over production in exchange of royalties to the franchisor.
4.	Management Contracts	A.P.S.M.B.	A	Performance rights and control are shifted by contract to foreign management in return for a fee.
5.	Turnkey/Product-in-Hand	A.P.S.	M.B.	The foreign contractor's responsibilities generally include the design and engineering of plant, provision of basic technology and know-how, supply of a completed production outfit and the training of local personnel.
6.	International subcontracting Contract Manufacturing	A.P.S.	M.B.	Otherwise known as Contract Manufacturing or offshore production/assembly. Similar to 5, but the principal provides the contractor with design and product specifications.
7.	Assembly Plant/Technical Assistance Contracts	A.P.S.	M.B.	Similar to 5. The package comes completely-knocked-down.
8.	Production-Sharing Contracts	A.P.S.B.	P.M.B.	Similar to non-equity JV, but for a specified period of time in return for a predetermined share of the output, once the foreign partner has recovered its costs.
9.	Acquisition & Mergers	A.P.S.B.M.	-	Similar to outright control.

Notational inferences in columns 2 and 3 derive from Figure 5.4

CHAPTER SIX

ALTERNATIVE STRATEGIES TO FOREIGN INVESTMENT

CONTENTS

CHAPTER SIX

6.1 EXPORTING AS A BASE FORM OF INTERNATIONAL MARKET ENTRY

Descriptions of foreign investment strategies assume a wide spectrum of entry mechanisms, ranging from export modes through variants of contractual and cooperative modes to wholly-owned subsidiaries. Exporting has a historical following: it has been the entrepreneur's primary method of entering into foreign markets; a means of opening up new markets; an avenue of circumventing domestic market constraints; and a strategic means of increasing turnover and profit. It is often generalised as the least risky means of internationalization and represents what Young, et al. (1989, p. 19) see as the 'toe-in-the-water' in international business.

Over the years, exporting has grown both in scale and importance. It is vastly seen as a strategic necessity of international business and, as such, is supported by national and supranational governments via a number of institutional arrangements such as Export Promotion Councils, Export-Import banks, Export Credit Guarantee Schemes, etc. For example, in 1934, the U.S. government agency - Export-Import bank - was established for the purpose of encouraging U.S. trade by supplying credit at subsidized rates of interest and financial guarantees to customers of U.S. exporters as well as export insurance covers. In the U.K. there is the Export Credits Guarantee Department (ECGD), set up in 1930 as an independent department, that has authority, under Treasury control, to issue insurance policies to cover risks met by exporters, such as insolvency or default of importer, refusal of goods on delivery and political and foreign exchange risks.

Regional and inter-governmental bodies of various sorts are also actively engaged in developing markets for products and services through varying degrees of cooperative export arrangements. Inter-governmental export and cooperation agencies of the kinds found among member states of North America, EEC, ECOWAS, GCC, ASEAN, to name a few, are examples of pervasive international recognition of the strategic role of export operations in international business.

6.1.1. REASONS FOR EXPORTING

Although sales, costs, and risk factors may be important motivating forces for developing export activity, studies about the export behaviour of firms have shown that the actual initiating factors in export involvement are either internal or external to the firm.

6.1.2. INTERNAL DETERMINANTS

The most important internal determinant of export marketing tends to be corporate management. Cavusgil (1984) independently and with Nevin (1981) identified organizational and management characteristics as very important in explaining variations in export activity and in the export initiation process. In the study of differences among exporting firms based on their degree of internationalization, Cavusgil found that expansion of export activity is significantly related to the following four behavioural factors:

- *Management's expectations*, concerning the effects of exporting on firm's growth, market development and profits;
- *Managements' perceptions* of and attitudes towards risk and desire to develop new markets;
- *Technology orientation* of the firm; and
- *Extent of resource allocation* to exporting, such as systematic exploration of foreign market opportunities and formulation of corporate export policy.

In an earlier study, Bilkey (1978) had argued that whether or not management was interested in and enthusiastic about exporting depended on the following four factors:

- <u>Management's Impression or Perception</u> of the overall attractiveness of exporting. This is an abstract idea which is independent of any contributions exporting might make to the firm.
- <u>International Orientation of the firm</u>: Several attitudinal factors have been found to be significant for the degree of international orientation that a firm may exhibit. The firm's background and traditions and foreign attitudes of its top management may be special cases. For example, Bilkey notes that the foreign attitudes of top managements correlate, in turn, with whether or not: they studied a foreign

language in school, lived abroad sufficiently long to have experienced cultural shock, and had an attractive foreign experience.

- Confidence in the firm's competitive advantage: Managerial perception of the strength and significance of its ownership advantages is a measure of its confidence and ability to compete in foreign markets. Composite proxy factors include: management's perception of whether or not the firm's products have unique qualities; management's perception of whether or not the firm has technological, marketing, financial or price advantages; whether or not the firm possesses exclusive information about a foreign market or customer; whether or not the firm has a patented product; and whether or not the firm has an efficient distribution network; and
- Adverse home market conditions: Adverse domestic macroeconomic and/or political conditions may cause management to explore export opportunities as a means of sustaining the firm's survival and growth. Government regulations (such as sectoral ceilings or increased local taxes) and saturated or depressed domestic market may all, in varying degrees, determine whether or not management decides to initiate exports.

6.1.3. EXTERNAL DETERMINANTS

Internal factors are immanently related to a firm's efforts to exploit market opportunities abroad. However, in many cases firms begin export sales in a passive manner, that is through unsolicited orders. In their study, Simpson and Kujawa (1974) found that 70 to 80 per cent of the sample companies' first export order was unsolicited. In cases where the initiating force is passive there is usually not an articulated export policy or a formal plan of action, rather the firm resorts to its bankers for advice and guidance.

Unsolicited export orders might come to a firm as a result of information which the foreign buyers might have obtained about the firm's product or price advantages. Sources of such information include: trade journals, chambers of commerce, banks, industrial associations, spillover in advertising or systematic buying procedures of foreign buyers. Alternatively, foreign buyers could obtain information about the firm's products or price advantages through the firm's embassy in the buyer's country, through trade fairs and indirect enquiries through friends abroad, mail order catalogues or by word of mouth. In this researcher's experience, all of these have proved to be credible sources of information.

6.2. LICENSING IN THE STRATEGY OF INTERNATIONAL INVESTMENT

The term 'licensing' is often used in a generic sense to describe a wide range of contractual arrangements involving a transfer of knowledge (technology), rights and resources between parties located in different countries. For example, licensing is frequently associated with management contracts, franchising, and contract manufacturing (see, for example, Rugman et al. 1986, p 94). Monye (1989) employs the term in a much broader context to include the above as well as joint ventures, turnkey contracts, etc. The submission here is that such a generalised usage tends to distort the true nature and practical subtlety of international licensing. Moreover, that kind of umbrella usage can be confusing because each of those organisational modes is a distinct strategic form of servicing foreign markets. Here, however, the term is employed in a more precise way to refer to a contractual arrangement in which a foreign company (the licensor) grants, on a *quid pro quo* basis, a local company (the licensee) the rights to exploit its know-how. The rights are generally to manufacture and market the licensor's product in the licensee's home market. In effect, licensing is simply a legal permission from one firm to another that enables the latter to use the know-how or proprietary rights of the former.

In general, the right to appropriate another firm's assets (tangible or intangible) is intricately linked with the fact that such assets are legally protected. In particular, intangible properties such as copyrights, patents or trademarks are legally sanctioned monopolies or proprietary rights of a company. To use them therefore without the permission of the owner tantamounts to an actionable violation. For instance, in a recent US case, an artiste successfully pleaded that another had plagiarized his tune. Hence, it is this transfer of intangible property rights that is the fulcrum of a licensing agreement and distinguishes licensing from the other associated contractual arrangements (Root, 1987). It is that which also establishes the form which a license may take.

6.2.1. MOTIVATIONS FOR LICENSING

There are many reasons why a firm may wish to license abroad. In their surveys of international licensing strategy, Telesio (1979) and Contractor (1986) studied the reasons for licensing from the perspectives of the licensor (Table 6.1) and licensee (Figure 6.1), respectively.

Table 6.1. Average Occurrence of Reasons for Licensing Abroad

Rank	Reasons for Licensing	Percentage of Companies Citing Particular Reason Has Been of Importance	Total Number of Companies Giving a Response
5	Shortage of funds for Investment	55	46
7	Did not have management for investment	36	39
6	Lacked knowledge of market	48	41
2	Market too small for profitable investment	73	45
4	Entry in market difficult because of strong competitors	58	45
3	Politically risky situation for investment	66	35
1	Government pressure for licensing	90	42

Note: Replies were to the question: Considering your recent licensing decisions, which of the factors below have been of importance in determining whether you license to an unaffiliated company or a minority-owned affiliate instead of investing with a controlled manufacturing facility? The possible replies were (1) has been of importance, (2) occasionally of importance, and (3) never of importance. In this table, the first two possible replies were combined into one.

Source: Telesio, P. (1979). Technology Licensing and Multinational Enterprises, New York: Praeger Publishers, p.38.

The first three reasons of Table 6.1 are firm-level factors (ranks 5, 7, 6); the fourth, sixth and seventh (ranks 2, 3, 1) reasons are host country-level factors, while the fifth reason (rank 4) is internalisation or product/ industry - level factor. From the licensor's point of view, host government pressure was the utmost reason for licensing, with 90 percent of the sample firms citing it.

Following it was the size of the host country's market. Seventy three percent of the respondents felt that the reason they used the licensing mode was because the host market was too small for a profitable investment. Surprisingly, firm size, proxied by managerial expertise, knowledge of host market (or lack of it) and financial constraint, are in descending rank order of importance the least reasons for licensing abroad.

From the licensee's point of view, the reasons for entering into licensing arrangements range from cost of research and development through selling international brand name to the prestige effect of associating with an international company (Figure 6.1). These reasons are more likely to influence licensing arrangements between developing country licensees and developed country licensors. The former are less likely to have access to, or expertise in, technology and are more likely to benefit from association with established brand names or internationally recognised companies than their developed country counterparts.

Figure 6.1. Reasons for Licensee's Need for Licensing

1. Avoid R & D costs.
2. Upgrade Technology.
3. Receiving valuable brand name.
4. Selling internationally through licensor.
5. To pre-empt licensor competition.
6. Reproduce proven manufacturing techniques.
7. Future links/other business with licensor.
8. To receive future technology from licensor.
9. Prestige effect of associating with international company.

Source: Contractor, F.J. (1985), Licensing in International Strategy, West Point Conn Quorum Books, p.178.

6.3. FRANCHISING IN INTERNATIONAL INVESTMENT STRATEGY

A franchise is a special type of licensing or technical-assistance agreement in which one party, known as franchisor, provides another, called franchisee, the use of a 'package' that incorporates both the trademark and technical know-how as well as local exclusivity and support service, including supplies and financial assistance. Franchising has had a historical following with U.S. enterprises since the nineteenth century. It is generally believed that the first franchise ever to be established was by the Singer Sewing Machine Company in the USA in 1863 (Young, et al, 1989, p.227). Since then, it has become a popular mode of international establishment among many enterprises including hotels, breweries, soft drink companies, motor dealers, petroleum marketers (filling stations), and fast food restaurants. For instance, Holiday Inn grants to the various national franchisees its trade name as well as local exclusivity, management assistance, ranging from appraisal of a proposed hotel site to the provision of reservations services and training programmes. Oil companies attach their trade names to the refined petroleum, as in Gulf oil, Mobil oil, Shell oil, etc., and in turn franchise these trade names to filling stations.

In addition to its popular use as a form of international business, franchising is also used very frequently between domestic firms. It is also used to achieve market segmentation, without necessarily creating intra-firm competition. Franchising benefits the host country through the package of training and technology transfers; on the other hand, it affords the firm a means of international entry/expansion with minimum risks and commitment of resources.

6.3.1. INTERNATIONAL GROWTH PATTERNS

Franchising has seen a phenomenal growth in both the domestic and international fronts since after World War II. In the last two decades, US MNEs have played a leading role in this form of international business expansion (Welch, 1989). It is estimated that one third of retail sales in the US are handled by franchising, with three quarters of the sales in three areas: car and truck dealers, filling stations, and soft drink bottling (Daniels and Radebaugh, 1986 p.517). In terms of international growth pattern, the fastest growth areas of the franchising industry have been in the food (mainly fast food and hotels) and business services, with US firms forming the lead also. For example, in the early 1980s, it was estimated that there were 295 international franchisors in the USA and about 23,500 outlets abroad, with 30 per cent of this total in Canada, 25 per cent in Europe (primarily in the UK) and 20 per cent in Japan (Kacker, 1985). Mcdonald's alone had over 1000 foreign franchises in 1980, and expected to derive over half its sales from abroad by 1990 (Business Week, 1981 p.162). In fact, the entry of McDonald's into the Soviet Union is indicative of the extent of corporate reliance on franchising as an entry mode choice.

There is also a growing number of franchisee countries, including some developing countries, whose local firms have developed their own franchise systems and are pushing these into the international market. For instance, Pronuptia, a French bridal wear franchisor, has 250 foreign outlets. Wimpy's and Bake 'N' Take from the UK and Winerwald from Germany are some of the earliest and most successful international food franchisors (Daniels and Radebaugh, 1986, p.518). There are, according to one estimate, 80,000 businesses running on a franchised basis in Britain, many of these as filling-stations and fast-food outlets. The industry is simultaneously witnessing a steady growth and encouragement from home governments. Australia, which by 1986 was ranked only behind Canada and Japan as host countries to US franchisors, is now the home of a growing number of international franchise systems (Welch, 1990). Malaysia is also part of this evolving pattern. With the Malaysian government supporting the development of small businesses via franchising, a small number of Malaysian food franchising operators have begun to go international (Dusevic, 1989).

In terms of operational patterns, two types of franchising are distinguishable: 'product and trade name' franchise and 'business format' franchising, also known as 'full business system'. As the name suggests, the first type of franchise involves the MNE's product as well as its trade name, as for example, when Coca-Cola sells its syrup along with the right to use its trademark to independent bottling companies (franchisees). The business format franchising involves much more than product and trade name. It additionally involves marketing strategies, operating procedures and quality control; and continuing direct association between the franchisor and franchisee in the operation of the business (Young, et al. 1989, p.230). Thus, it is a more comprehensive package than product and trade name type, hence it is called full business system. It is also the form which dominates the international market and actually separates franchising from licensing. Fast-foods, hotels and filling-stations are examples of industries using the business format system. Although in practice it is difficult to trace the line that divides product and trade name franchising and basic licensing, following that Coca-Cola example, nevertheless, the literature provides evidence concerning subtle features that separate franchising from licensing.

6.3.2. DISTINCTION BETWEEN FRANCHISE AND LICENSE

Franchising has traditionally been regarded as a form of licensing. Conceptually, many of the principles of licensing apply equally to franchising: both are contractual agreements which, for a fee, involve the transfer of proprietary rights form one firm to another. Practically however, franchising involves more than nominal transfer of rights: in the main, it entails the provision of a wider package of services on a continuing basis than would be the case with licensing in the operation of the business. Although opinions vary as to the precise difference between the two types of agreement. The summary presented in Figure 6.2 captures many of the differences.

6.4. CONTRACTUAL ARRANGEMENTS IN INTERNATIONAL INVESTMENT STRATEGY

The discussion so far has focused on a spectrum of contractual arrangements used by firms independently as entry modes into foreign markets. Because the manifestations of contractual arrangements are so wide-ranging and because some of them are not only in mutual or reciprocal relationship but also are commonly found in combination, it is appropriate, within the scope of international market development, to consider these for aggregate discussion within a single chapter. A management contract may be a by-product of licensing, franchising or a turnkey agreement. For example, most breweries in Nigeria, as in many developing countries, were established as, but not limited to, turnkey arrangements. Even those established over ten years ago still operate under some form of foreign management contract and depend on their foreign partners for equipment repairs and component supplies.

The formal purpose of this section is to complete the roster of international contractual investment strategies by accounting for other establishment modes under which the foreign firm may contribute no equity capital, but which provide it with some control or returns, even after the project has been completed. Specifically, these include: management contracts, turnkey contracts, product-in-hand contracts, market-in-hand contracts, international subcontracting, production-sharing and risk-service contracts. These are considered *seriatim*.

Figure 6.2. Distinction Between Licensing and Franchising

	Licensing		Franchising
1.	The term 'royalties' is normally used.	1.	Management fees are regarded as the most appropriate term.
2.	Products, or even a single product, is the common element.	2.	Covers the total business, including the know-how, intellectual rights, goodwill, trademark and business contacts. (Franchising is all-encompassing, whereas licensing concerns just one part of the business).
3.	Licenses are usually taken by well-established businesses.	3.	Tends to be a start-up situation, certainly as regards the franchisee.
4.	Terms of 16 to 20 years are common, particularly where they relate to technical know-how, copyright and trademarks. The terms are similar for patents.	4.	The franchise agreement is normally for five years, sometimes extending to 10 years. Franchises are frequently renewable.
5.	Licensees tend to be self-selecting. They are often an established business and can demonstrate that they are in a strong position to operate the license in question. A licensee can often pass his license onto an associated or sometimes unconnected company with little or no reference to the original licensor.	5.	The franchisee is very definitely selected by the franchisor, and his eventual replacement is controlled by the franchisor.
6.	Usually concerns specific existing products with very little benefit from ongoing research being passed on by the licensor to his licensee.	6.	The franchisor is expected to pass on to his franchisees the benefits of his ongoing research programme as part of the agreement.
7.	There is no goodwill attached to the license as it is totally retained by the licensor.	7.	Although the franchisor does retain the main goodwill, the franchisee picks up an element of localized goodwill.
8.	Licensees enjoy a substantial measure of fee negotiation. As bargaining tools, they can use their trade muscle and their established position in the marketplace.	8.	There is a standard fee structure and any variation within an individual franchise franchise system would could cause confusion and mayhem.

Source: **Perkins, J.S. (1987). "How Licensing, Franchising Differ", Les Nouvelles, December 157.**

6.4.1. MANAGEMENT CONTRACTS

Management contracts are a growing form of foreign market development. Managerial talent is one of the most important ownership-specific advantages of a firm. It plays a distinct role in the economic and political development of a nation. One of the hallmarks of national development is the availability of adequately trained management. Thus, although a country may be endowed with natural resources, without skilled indigenous manpower it will depend on foreign management to harness such resources. Management talent is one important dimensions which is often used to differentiate between developed less developed countries, with the latter depending largely on the former for the supply of expert skills.

The term 'management contract' is used imprecisely to refer to transfer of management skills. Yet, "rarely are management contracts purely concerned with transferring management skills" (Buckley, 1985). For the most part, an infusion of technology is involved (Gabriel, 1967; Ellison, 1975, 1976). Some conceive of it as a form of licensing or subcontracting arrangement under which the contractee pays for training in production and, in return, is "allowed to produce as much as he likes of the product" (Casson, 1986). The operational dynamics of contemporary management contracts however make this definition infamous, which is why Casson himself feels that "no rational profit-maximising firm would be willing to pass on its advantage to a potential rival on these terms unless its management believes that the partner will never learn sufficient to become a serious rival or that the advantage is about to become obsolete in any case".

Management contract, as the name implies, is a contractual arrangement whereby a firm provides management expertise in general or specialised functional areas to another firm or organization, for a specified period of time, for a fee. This definition is consistent with Ellison's broad conception:

> Management contract is an arrangement under which a certain degree of responsibility for the operations of one enterprise is vested in another. The latter undertakes the usual management functions, makes available a whole range of skills and resources and trains personnel. The contract covers payment to the company and the handing over of authority to the locals once trained (Ellison, 1975, p. 25).

Construction management contracts are conventionally excluded from the above definition, even though there is not much dissimilarity between the two, at least conceptually. In the construction industry, the term 'management contract' refers to a contractual arrangement between a construction project client and an external management firm under which the latter operates as the project's management contractor with responsibility for the management and co-ordination of the design and construction phases of the project. The management contractor does not participate in the project's construction work, rather provides management services to control and co-ordinate site activities, which are normally sub-contracted to other construction firms (CIRIA, 1983, p.6).

A common feature of management contracts is the operational control it confers on the foreign contractor as regards the enterprise or a crucial phase of it. Such control would otherwise be invested in, or exercised by, the contractee's internal management. The operational control may be with respect to general management of a project or an enterprise, personnel training and administration, production, financial services and administration, provision of inputs and services, and/or distribution and marketing.

The control element embedded in management contracts gives the foreign firm the opportunity to control the amount and type of information that is divulged as well as the level of expertise offered. Through this influence, the firm is able to maximize its earnings by widening indirectly the scope of its remit. For instance, a foreign contractor engaged to manage a state airline does not generally restrict itself to 'mundane' management. The operation may involve rationalization, selling off obsolete aircraft, acquiring or leasing new aircraft, improving or restructuring reservations services, including computerization and control, and any other activity it deems fit for the realization of the objectives.

Management contracts often supplement other forms of international business such as licensing, turnkey projects, joint ventures, or subcontracting. In their pure form, the foreign firm provides managerial services to a local project, without equity interest or ownership claim. Nevertheless, they may be used to facilitate control in the other forms and can also serve as a means of avoiding political risks. In particular, in less developed countries, management contracts tend to be interlocked with the political process, but are less likely to be volatile to its changing fortunes than dividends from fdi operations. In short, the characteristics of management contracts - which make them appealing to host countries - are to be found in their residual property. That is, they tend to be employed mainly for project redemption purposes and/or for projects in which local resources (broadly defined to include know-how, technology, and factor inputs) are either unavailable or inadequate.

The emergence of management contracts in international market development has been widely linked to changing international investment strategies in the North-South context (Oman, 1986) and reflects judgements of the following general kinds by the developing country: (1) a preference for local ownership over foreign ownership, even if that ownership is nominal, that is, not accompanied by control over operational activities; (2) a lack of local technical and managerial skills to set up and operate the project; and (3) a recognition that the project carries with it, at least for the short term, a valuable socio-economic cost benefit, regardless of the nationality of the foreign contractors (UNCTC, 1983, p.1).

These generalizations apply to all types of management contracts, be it hotel management, chemical plant operation or procurement of special services. The judgements embody a realistic appraisal of corporate deficiency, on the one hand, and corporate capabilities, on the other hand, as a unique element of such transactions. The transactional implications of this for international investment are:

(a) an increasing willingness of MNEs to assume 'managerial' role rather than 'ownership' in overseas operations;
(b) the opportunity this role provides the MNE to enter and establish operational presence in foreign markets that are increasingly inhospitable to direct investment;
(c) the opportunity this device offers Western MNEs to establish in markets traditionally closed to foreign private capital; and
(d) the flexibility this managerial role provides MNEs to adopt their commercial strategies to changes in international markets brought about by global competition, fluctuating fortunes in macroeconomic development and environmental pressures against foreign direct investment.

6.4.2. TURNKEY CONTRACTS

Turnkey projects have become particularly significant in the economic development process of less developed countries (LDCs). LDCs are characterised by problems of political democracy and leadership, economic development, rapid industrialization, inadequate infrastructure, and management of changing fortunes (eg poverty, ethnic tensions, prolonged civil wars, depression, high unemployment, hyperinflation, and affluence). Their natural resources however provide some sort of 'potent alchemy' to the economies. The inter-dependence of LDCs and DCs is not in doubt, and is not at issue here. For obvious reasons, the political machinery of most LDCs views FDI of some Western MNEs as a potent intervention in their political/economic governance. Consequently, they tend to encourage industrialization processes which potentially offer technological transfer whilst minimizing the subrogation of economic or political independence. Contractual arrangements are deemed to be pro-active in the industrialization process, and in this context turnkey projects are particularly significant.

A turnkey contract is an investment arrangement whereby a foreign contractor has overall responsibility for 'setting up' a complete production facility for eventual transfer to the host country owner. Projects executed under this sort of arrangement are thus termed turnkey projects. Implicit in this definition are the following features:

1. By 'setting up' is meant construction of the production unit/facility and bringing it ready for commissioning.
2. Ownership of the facility is transferred to the local owner, after a period of test-runs, signalling the completion of the first phase of the project.
3. The production facility may be factory, industrial plant, refinery, public infrastructure such as airport, seaport or railway facilities.
4. The local owner/contractee may be a firm or government. The notion that the customers are usually governments (mainly developing country governments) who have decreed that a given product or service must be produced locally and under its auspices (Daniels and Radebaugh, 1986, p.520) is a sweeping generalization. This author has been associated with two turnkey arrangements in Nigeria neither of which involved the government. There is also abundant evidence about the use

of turnkey arrangements in other LDCs' private sector contracts (see, for example, country cases in Oman (ed.) 1984).

Turnkey arrangements are usually accompanied by management contracts, licensing or franchising, whereby continuing relationships with the foreign contractors or their principals/agents are maintained. In fact, in certain types of industries such as breweries licensing is essential. A look at the labels of most beers brewed in developing countries depicts an assignment of German or other foreign brands. Implicit in the above definition are two types of turnkey contracts: 'light and heavy'. A 'light' turnkey contract is one which comes to an end once the physical construction of the project has been completed. A 'heavy' one, on the other hand, contains clauses which provide for the extensive training of local personnel.

A common feature of turnkey contracts that distinguishes them from most other international business operations is the size of the projects involved. Size is in respect of both the scale or complexity of operations and the amount of money involved. Related to this feature is the specific nature of turnkey projects. While differing from project to project and country to country, the crucial investment distinction of turnkey contracts is this: they are idiosyncratic, meaning that they are transaction-specific, specialized, and nonmarketable (see Williamson, 1975, 1979, 1981a, for explication of these terms).

6.4.3. PRODUCT-IN-HAND CONTRACTS

Product-in-hand contracts are variants of turnkey operations. Under the arrangement, the contractor's responsibility goes beyond project completion and commencement of operations, as is the case with turnkey projects. The incremental dimension here is that the turnkey installation must be completely operational with local personnel. Product-in-hand contracts are analogous to the 'heavy' type of turnkey contract referred to above in that they contain provisions which confer legal responsibility on the foreign contractor to train local management and workers to take over the running of the installation. In a pure turnkey contract this provision does not form part of the original remit. An example of product-in-hand contract is what is termed 'Completely-Knocked Down' (CKD) assembly plant. As the name suggests, it is a subassembly plant. Under the terms of the contract, the contractor brings the components of the plant into the host country in a semi-assembly form. The contract often stipulates that local input components be utilised as much as possible in place of imported components. The feature of product-in-hand contracts is that their products are often meant for the host country and/or regional market. Major international motor manufacturing companies adopt this mode. In Nigeria, for example, Peugeot Motor Company of France, Volkwagenwerk Ag of Germany, and Mercedes Benz of Germany, all operate CKD assembly plants.

6.4.4. MARKET-IN-HAND CONTRACTS

Another form of turnkey contractual arrangement is the market-in-hand agreement. In this form, the foreign contractor is additionally required to take responsibility, wholly or partially, for the sale of the project's output. This type of arrangement often characterises projects in which the foreign participant has a stronger incentive to establish in the host country than his local partner. In this case, the foreign partner/contractor may have developed home market for the product but may be concerned about production costs. With a host country partner providing transactional economy, for example, through cheap labour and provision of infrastructure, the foreign partner may undertake to market the project's output outside the host country.

Market-in-hand contracts are found in fishing projects, petroleum projects, rubber products and in projects where there is a greater demand and utility in developed countries. In this regard the local partner/contractee provides the administrative support and 'software' inputs while the foreign partner/contractor is obliged under the terms of the contract to establish market for the products.

Where the market, if any, for the project's output in the host country offers an inadequate incentive to establish the project, or where local promoters lack necessary production, managerial and marketing skills, market-in-hand provisions in the contract, enable the multinational partner to yield optimization privilege to the host country (See, Ozawa, 1984).

6.4.5. INTERNATIONAL SUBCONTRACTING/CONTRACT MANUFACTURING

International subcontracting, also known as contract manufacturing or offshore production/assembly, is an arrangement in which a firm based in one country (termed the principal contractor) places an order with a firm based in another country (termed the subcontractor) to produce components or assemble finished products. The subcontract is typically limited to production to the principal's specifications and brand name. Generally, the responsibility for the marketing of the product lies with the principal, with sales normally taking place in the principal's home and/or third-country markets.

One writer describes subcontracting "as a kind of half-way house between arm's length transactions on the open-market and complete internalization within the firm ... The subcontracting relationship is symbiotic - a technical division of labour between independent firms - in which each partner contributes to the support of the other". (Dicken, 1986).

OTHER CONTRACTUAL/COLLABORATIVE ARRANGEMENTS

A number of other contractual/collaborative arrangements exist that are either encompassed within the same package, too industry-specific for common identification or involve government agencies in the main. These are generally referred to as <u>industrial cooperation agreements</u> (ICA), although references to licensing, technical assistance arrangements, turnkey projects and joint ventures come under this heading. Since these other forms have precise signification as discussed above, it may be appropriate to restrict ICA to other contractual/collaborative arrangements that are industry-specific or firm-cum-government. Arrangements under scrutiny here include production-sharing contracts and risk-service contracts.

6.4.6. PRODUCTION-SHARING CONTRACTS

These are primarily found among oil and extractive industries. Under the contract the foreign firm prospects for oil or minerals in specified fields and, if a successful find is recorded, undertakes production in conjunction with the host country's state-owned company. Specific features of the agreement include pre-determined production percentage share, pre-determined share of the physical output, and length of time required to recoup pre-production costs and to hand over contract rights to the state company.

Pre-determined share of costs and revenues between the foreign firm and the host government agency varies from country to country, and ranges from 15 per cent host-government share, as in Chile, to 85 per cent host-government share, as in Egypt (Oman, 1984, p.16). Similarly, other considerations, such as technical and financial responsibilities of the parties, are carefully specified in the contract.

6.4.7. RISK SERVICE CONTRACTS

Risk service contracts are similar to production-sharing contracts in many respects. Both are used primarily in the petroleum and extractive industries. The crucial investment distinction between the two is that under a risk service contract the foreign company's share of output is paid in cash rather than physical output. However, the agreement may also contain a provision which permits the contractor to exchange its cash receipts for equivalent amount of output (e.g. crude oil) determined at international prices. Another important feature of risk service contracts is that the burden of risk rests solely on the foreign contractor, who must also provide the investment capital for exploration and production.

What then is the attraction in this type of foreign investment, given that if no oil is found the contract terminates? With a production-sharing contract, the foreign contractor is at least paid a pre-determined fee for exploration services if no oil is found. Under a risk service contract, the foreign contractor's compensation package is made up of capital reimbursement, interest on the capital and a pre-determined percentage of risk fee, out of production revenues.

Risk service contracts may be particularly appealing to the large multinational oil companies for the following reasons First, their very nature constitutes an entry barrier. The requirements of such agreements (including production-sharing contracts) prospectively increase the difficulty of entry by new firms or small-and medium-size firms. To be able to compete for these contracts the firm must possess the capital and knowledge (technical and managerial) necessary to conduct these types of operation.

Second, sequel to the entry empendiments, the few participating firms may successfully effectuate collusion as a prelude to establishing dominance either in the industrial sector and/or market segment. This may account for the global domination of the petroleum industry by few large MNEs, such as Royal Dutch-Shell, British Petroleum, Exxon, Mobil, Texaco, etc. For the same reason these companies are found in virtually every country that produces oil.

The monopolistic incentives of these factors progressively lead the firms to integrate vertically across national boundaries into markets that could otherwise be competitively organised. Even if integration (backward or forward) does not capture all aspects of the market, the residual (nonintegrated) sector may be so reduced that only a few firms of efficient size can service this area. In other words, firms that would otherwise be prepared to enter into the initial stage of the market may be discouraged from coming in by the prospect of having to engage in small-numbers bargaining, with all the hazards that this entails, with the few market-mediated-exchanges (Williamson, 1975, p.116).

6.5. JOINT VENTURES IN THE STRATEGY OF INTERNATIONAL INVESTMENT

If direct investment (through wholly-owned subsidiary) is viewed as the ultimate in the hierarchical route of resource transfer in which there is a de jure control over foreign operations, then joint ventures (JVs) may be categorized as next in the ladder. The term 'joint venture' implies the sharing of assets, risks and profits, and participation in the ownership (i.e. equity) of a particular enterprise or investment project by more than one firm or economic 'group' (Oman 1984, p.14). It is a contractual arrangement whereby two or more parties collaborate in an economic activity under joint control. Reference to 'control' is intended to underline the power to govern the financial and operating policies of an economic activity with the prospects of yielding benefits. 'Joint Control' therefore is the contractually agreed sharing of control over an economic activity. It presupposes joint contribution to the venture in accordance with contractually agreed proportions. The notion of 'joint control' is to be distinguished from 'significant influence' and/or 'joint venture investor'. By 'significant influence' is meant the power to participate in the financial and operating policy decisions of an economic activity without control or joint control over those policies (IAS No 31, 1991). An investor in a joint venture is by definition a party to a joint venture with no joint control over that venture. The investor may be a firm, government agency or an economic group with significant influence but not joint control over the venture.

This definition immediately distinguishes between three forms and structures of JVs: jointly controlled operations, jointly controlled assets and jointly controlled entities. The first type encompasses cases where two or more venturers combine their operations, resources and expertise in order to manufacture, market and distribute jointly a particular product. Some JVs involve the joint ownership and control of the assets, the use of which results in joint profit sharing. A jointly controlled entity is a JV which involves the establishment of another entity ('a child') in which each venturer has an interest. The child operates in the same way as other enterprises, except that a contractual arrangement between the parties establishes joint control over the economic activity of the entity.

Implicit in the above JV view is a notion of an all party equity participation commonly referred to as 'equity joint venture' (EJV). However, all joint ventures cannot, both conceptually and practically, be regarded as EJVs. There amy be instances in which a collaborating partner has no equity stake in the venture, but, nevertheless, is an important lifeline in the organization and success of the project. Where the JV partners are drawn together by equity contribution, the distribution of equity shares may be determined by each partner's financial contribution, or it may be related to other forms of capital contribution, such as technology, management or access to world markets. The latter form of participation may be described 'narrowly' as non equity joint venture (NEJV).

Where the joint venture partnership is between parties resident in different countries, it is known as international joint venture (IJV). IJVs under scrutiny here are those in which the host country partner holds at least 50 per cent of the equity. Thus, joint ventures which are majority foreign owned are excluded from the category of new forms. In practice, however, the type of venture and the relative nature of equity contribution coupled with host country inward investment regulations may determine the composition of interest.

In general, the common features of IJVs are:

1. incorporating a separate enterprise in which investors from two or more countries have a mutual interest and share a common economic purpose;
2. joint commitment of resources to the venture;
3. joint management responsibility;
4. sharing of business risks and losses;
5. joint participation in the profits of the enterprise; and
6. enduring cooperation in the venture.

6.5.1. FACTORS FAVOURING THE GROWTH OF INTERNATIONAL JOINT VENTURES

The factors underlining the growth of JVs in international business range from cost and risk considerations through international competition to host government regulations. Traditionally, investors are risk averse, and the specific nature of JVs suggests that firms pursuing global strategies might evaluate both the cost constraints and country cum investment risks and seek to reduce them when operating in foreign countries.

Figure 6.3 derived from a study of JV arrangements in developing countries, lists five factors, in no particular order of importance, contributing to the diversity in the use of JVs. Host government regulations are significant in determining the use of JVs or any governance structure. The issue of control is central both to the regulations and to the growth of new forms of investment. Host countries would wish to acquire foreign technology and know-how with minimum foreign control of its resources. The exercise of foreign control and potential costs of wholly owned subsidiaries are a source of friction between host governments and foreign MNEs. Accordingly, investment laws are enacted to restrict or prohibit entry modes that place the locus of control of certain classes of enterprises on foreign multinationals (See for example, Nigeria's Indigenization Decree 1972 or India's Foreign Exchange Regulation Act of 1974).

For the profit-seeking MNE, the desire to maximize global returns has to be matched with loss of control and ownership of foreign subsidiaries. This balance is prospectively attained via JV creation whereby the equity in the foreign subsidiary is shared with host country interests (Bivens and Lovell, 1976).

Another factor in the growth of IJVs is the increasing participation of small and medium-size firms (SMFs) in international business.

Figure 6.3. Factors Contributing to the Growth of Joint Venture Activity

- Government legislation, especially in developing host countries, requiring local equity participation
- The increasing participation of small to medium-sized companies in international business, with joint ventures being used to reduce the capital cost and risks associated with international expansion.
- A greater diversity in the source country distribution of MNEs and the greater willingness of non-US MNEs to enter into joint ventures.
- The increasing costs of technological development, with joint ventures being used to reduce risks and the costs of R&D.
- The growing intensity of competition, with joint ventures being used for strategic/competitive reasons.

Source: Derived from UNCTC, Arrangements between Joint Venture Partners, UNCTC Advisory Studies, No.2, Series B, UN, New York, 1-13.
Culled from Young, et al (1989, p.342)

The attraction of JVs for SMFs lies in the sharing of investment costs and risks which, otherwise might pose entry barriers to this group of enterprises. Associated with cost and risk considerations are entry constraints of the kinds posed by size limitations. SMFs are conventionally thought of lacking in the package of corporate resources required to embark upon foreign investment. In this regard JVs could potentially mitigate this obstacle.

Related to the influx of SMFs is the increasing diversity in the growth of non-U.S. MNEs and their willingness to adopt flexible approaches to foreign investment. In particular, Japanese MNEs have eroded many of the host countries traditionally served by U.S. MNEs, and have done so by adopting non-equity forms that match host countries' control desires.

Costs of technological development and growing competition in the international marketplace are other factors contributing to the growth of JV modes of operation. The British telecom video telephone project described above is a classic example of how IJVs might be created in response to high costs of R&D and strategic/competitive forces.

Harrigan's (1985) three way analysis of the motivations for JV formation (Figure 6.4) covers the factors described above by distinguishing whether JVs are used for internal, competitive or strategic purposes. Buckley and Casson (1989) illustrates how different motives for internalization manifest themselves in various JV contexts (See Figure 6.5).

Figure 6.4. Motivations for Joint Venture Formation

A. Internal uses

1. Cost and risk sharing (uncertainty reduction)
2. Obtain resources where there is no market
3. Obtain financing to supplement firm's debt capacity
4. Share outputs of large minimum efficient scale plants
a. Avoid wasteful duplication of facilities
b. Utilise by-products, processes
c. Shared brands, distribution channels, wide product lines and so forth
5. Intelligence: obtain window on new technologies and customers
a. Superior information exchange
b. Technological personnel interactions
6. Innovative managerial practices
a. Superior management systems
b. Improved communications among SBUs
7. Competitive uses (strengthen current strategic positions)

B. Competitive uses (strengthen current strategic positions)

1. Influence industry structure's evolution
a. Pioneer development of new industries
b. Reduce competitive volatility
c. Rationalise mature industries
2. Pre-empt competitors ("first-mover" advantages)
a. Gain rapid access to better customers
b. Capacity expansion or vertical integration
c. Acquisition of advantageous terms, resources
d. Coalition with best partners
3. Defensive response to blurring industry boundaries and globalization
a. Ease political tensions (overcome trade barriers)
b. Gain access to global networks
4. Creation of more effective competitors
a. Hybrids possessing parents' strengths
b. Fewer, more efficient firms
c. Buffer dissimilar partners

C. Strategic uses (augment strategic position)

1. Creation and exploitation of synergies
2. Technology (or other skills) transfer
3. Diversification
a. Toehold entry into new markets, products, or skills
b. Rationalization or (divestiture) of investment
c. Leverage-related parents' skills for new uses

Source: Harrigan, K.R. (1985), Strategies for Ventures, Massachusetts: Lexington Books, D.C. Heath & Co., 28.

Figure 6.5. Internalization Motives for Joint Venture Creation

A. Lack of Confidence in Long-term Arm's-Length Contracts

1. Hedge against intermediate product price movements
2. Avoid recurrent negotiation under bilateral monopoly over the price of a differentiated intermediate product
3. Integrate upstream and downstream operations

B. Quality Uncertainty

1. Insure against defective quality in jointly used components
2. Adapt a product to an overseas market
3. Management training and transfer of technology
4. Buyback arrangements in collaborative R&D

C. Collusion

1. Reduce cost
2. Enhance sales and profitability
3. Economize on monitoring costs
4. Control output

4. Hostages: Internalising the Implementation of Counter threats

1. Counteract imbalance in vulnerability of two parties in a collaborative venture
2. Avoid breakdown in confidence and mutual trust
3. Establish an atmosphere of consummate cooperation

Source: Derived from Buckley and Casson (1989). "A Theory of Cooperation in International Business" in Buckley (1989), The Multinational Enterprise: Theory and Applications, London: Macmillan, pp. 46-74

CHAPTER SEVEN

STRATEGIC FORMS OF INTERNATIONAL BANKING

CONTENTS

CHAPTER SEVEN
STRATEGIC FORMS OF INTERNATIONAL BANKING

INTRODUCTION

7.1 BACKGROUND AND OVERVIEW

One of the most significant developments in world economy within the last two decades is the rapid growth of international banking activities following the phenomenal growth of international business. In its traditional form of providing foreign exchange and financing imports and exports, international banking has become an enterprise unto itself, for not only has it become massive in scale, but has also come to exercise a significant influence in both national and international economies. To appreciate the importance of growth of banking activity across national boundaries and the rise of the multinational bank (MNB) is to cast it within the historical context of the macro-economic environment in which the development has occurred.

International banking is a logical extension of a cross-border mercantile operation. It existed in the medieval ages, principally to finance joint ventures between merchants involved in multiple cross-border voyages. International business transactions (in which cross-border agency and partnership or joint venture were the predominant forms) can be traced back to Genoa between 1156-1158 AD. This trend, albeit rudimentary, signalled the evolution of international banking as an obvious corollary of international business.

However, the growth of modern forms of international banking may be traced to three-stage periods of development. The first period, referred to as the pre-World War I decade, saw banks headquartered in Great Britain as very dominant market leaders in the international arena. At the start of the war, UK domiciled banks had 2,000 foreign branches while French and German-based banks, altogether, had five hundred foreign branches (Aliber, 1984). This trend could be associated with the financial exigency of the war and its overseas financing requirements. During this period, US banks had a very modest profile in the international arena. While in 1913, there were only six US-based foreign branches, by 1920 the number had increased to 100 and remained unchanged until the end of the 1950s (Pecchioli, 1983).

The second period, referred to as the post-World War II, saw the emergence of US-based banks as major leaders in the international branch network system. Their foreign banks' networks had blossomed from a modest pre-World War I position through 124 foreign branches by 1960 to over 500 by the end of the decade. At the same time, other European- and Japanese-based banks had embarked on a substantial expansion of their foreign networks. The emergence of foreign branch networks of banks from US, Japan, and Europe resulted in global competition in the international capital markets on a scale unprecedented in the history of international business. The ensuing competition led to shrinking of foreign domination of UK, French and German banks. By the end of 1960 the total number of foreign branches, subsidiaries, etc. had reached 4,500 (UNCTC, 1981).

The last period in the evolutionary process of international banking occurred in the 1970s. While the 1960s brought an increased awareness of the scale of problems that arise when business operations extend beyond national boundaries, the 1970s witnessed enormous developments in international banking. Not only did the number of participants and volume of business increase tremendously, significant developments also occurred in international capital markets and instruments. Table 7.1 shows the growth of global network of overseas branches and agencies of different countries and geographic regions as of 1978. The arrival of oil - producing countries and the massive injection of petrodollars in the international financial system led to dramatic increase in the role of banks in the emerging world economy. The OPEC members were deemed good credit risks in the 1970s and bank lending surged to stem the tide of petrodollars pouring into the international economic system. The intermediation role of international banks (in absorbing and re-channelling surplus funds) within this period has been described as "the greatest achievement of international banking in recent years" (Houthakker, 1984).In short, since the 1960s, international banking has become very important not only in the scale of lending and borrowing, but also in the number and size of outlets owned by banks domiciled in other countries. This trend, which was largely in response to macro-economic developments in the world economy, has been immense and significant in both

Developed (DCs) and Less Developed (LDCs). The number of participants and volume of business increased tremendously in tandem with the increasing number of domestic banks and interpenetration of national economies by foreign banks. In addition, the emergence of resource-rich Organization of Petroleum Exporting Countries (OPEC) in the early 1970s as major new actors on the world financial markets increased the role of MNBs as primary international financial intermediaries.

Despite these developments, much of the emerging literature has concentrated on the growth of MNEs. Published literature indicates that studies on the phenomenon of multinational banking have been comparatively scanty. Indeed, there are only a few studies that have applied the theories of Foreign Direct Investment (FDI) and MNEs to explain multinational banking. These include the works of Gray & Gray (1981), Cho (1983), and Nigh, Cho and Krishnan (1986). The earlier works of Aliber (1976, 1980, 1984), Brimmer & Dahl (1975), Fieleke (1977), Germidis and Michalet (1984), Goldberg & Saunders (1980,) Grubel (1977), Odle (1981), and UNCTC (1981, 1982) are largely descriptive. Conclusions reached from these studies are mainly from U.S. point of view. Furthermore, there is no published study on the application of "new forms of investment" to the banking phenomenon. Yet studies of this kind may enhance an understanding of the operational modes of banks' diversification strategies. Banking is a highly regulated enterprise as Table 7.2 and Exhibit 7.1 indicate. Strict restrictions on certain types of entry mode in conjunction with deregulation and competition in international financial markets mean that banks pursuing global strategies may have to adopt a flexible approach to foreign markets. It is the contention here that while the preferred entry route is one that provides an optimum mode, returns to risk and control, however, variations among nations may indicate different modes of servicing the needs for various markets. Thus, banks may have to change their operating strategies abroad in the light of country risk levels, competitive regulatory constraints, and intensified political opposition overseas. These indicate that the future market and product expansion in the international banking industry may become highly selective, with greater dependence for international expansion in countries with proximal political and economic relationships.

Table 7.1 Global Network of Overseas Branches and Agencies in 1978

Country of Origin	Banks	US	UK	Fra.	Ger.	Switz.	Other Europe	Other Latin Amer.	Jap.	Far East	Mid-East	Africa	Carib. area	Total
United States	136	-	56	21	22	8	67	85	32	126	30	16	207	670
	(8)	-	(11)	(3)	(3)		(4)	(52)	(14)	(18)	(4)	(7)	(12)	(128)
United Kingdom	20	19	-	21	8	8	72	102	8	503	142	148	83	114
	(16)		(2)	(24)	(2)	(1)	(30)	(64)	(7)	(845)	(49)	(2182)	(81)	(3287)
France	24	11	13	-	16	10	48	30	7	31	23	30	7	226
	(16)		(2)	-	(5)	(1)	(44)	(45)		(13)	(14)	(232)	(5)	(361)
Germany	12	13	6	2	-	1	1	5	12			7	47	
	(2)	-	-			(1)	(1)	(1)						(2)
Switzerland	12	8	8	-			4	3	2	1			7	33
	(3)	(2)				-		(1)						(3)
Netherlands	7	8	5		2		8	28	3	10	10	2	10	86
	(2)						(1)	(9)	(3)	(11)	(8)	(4)	(3)	(39)
Italy	6	11	4				6	6	1	1	5	1		35
	(5)	(2)	(1)	(7)	(2)			(3)	(11)		(26)			
Other Europe	32	18	158	79	7	1	21	22		3	6	1	1	317
	(13)		(6)	(9)	(3)	(1)	(19)	(12)		(2)	(18)	(33)		(103)
Canada	7	28	15	2	6		7	26		11	7	1	140	243
	(5)	(14)	(10)	(1)	(1)	(2)	(11)	(31)					(84)	(154)
Japan	23	49	22	1	12		6	3	-	29			-	122
	(6)	(8)	(3)		(2)			(4)	-	(8)	(2)			(27)
Australia	9	7	17							528				522
	(4)		(4)							(12)				(16)
Latin America	15	16	4	2	1		4	39	2	1	1	1	18	89
	(2)	(2)		(1)			(1)	(1)						(5)
Other Far East	47	36	130	4	5		3	1	18	257	81	24	6	565
	(17)	(2)	(4)				(6)		(10)	(108)	(4)	(12)		(146)
Mid-East	21	17	20	6	8		3			4	106	10	3	177
	(6)	(2)		(1)							(23)	(11)		(37)
Africa	15		8	4							13	15		40
	(6)										(9)	(38)		(47)
Caribbean	1							13						13
	(1)							(7)					(2)	(9)
Total	387	241	466	142	87	27	250	356	79	1518	425	249	489	4329
	(112)	(34)	(40)	(39)	(16)	(6)	(123)	(229)	(34)	(1018)	(134)	(2530)	(187)	(4390)

Source: OECD (1983). The Internationalization of Banking: The Policy Issues. Paris: OECD, p. 59

Table 7.2 Legal Restrictions on Foreign Bank Entry

Country	Form of foreign bank presence: Representative Office	Branch	De-novo Subsidiary	Situation in mid-1981 Participation in indigenous banks: Subsidiary (1)	Affiliate (2)	Main Changes 1960-1981
Australia	*	F	F	F	p(10%)	None
Austria	..	-	-	-	-	None
Belgium	*	*	-	-	-	Implementation of EEC Directive of 12/12/1977
Canada	..	F	R	F	p(10%)	Some liberalization for de-novo foreign subsidiaries in the 1980 Bank Act
Denmark	..	-	-	F	p(30%)	Liberalization of foreign bank entry as from 1/1/1975. Implementation of EEC Directive of 12/12/1977
Finland	+	F	+	F	p(20%)	Liberalization for de-novo foreign subsidiary in 1980
France	..	-	-	-	-	Abolition of special register for foreign banks and remaining discriminatory provisions in 1975
Germany	..	-	-	-	-	
Greece	..	-	-	F	p(49%)	None
Iceland	..	F	F	F	p(49%)	None
Ireland	R	R	R	R	R	Liberalization of policy with regard to foreign bank branching in 1977. Implementation of EEC Directive of 12/12/1977
Italy	..	-	-	-	-	Implementation of EEC Directive of 12/12/1977
Japan	..	R	R		p(5%)	
Luxembourg	*	-	-	-	-	Implementation of EEC Directive of 12/12/1977. Liberalization with regard to foreign representative offices in 1980
Netherlands	..	-	-	R	-	Implementation of EEC Directive of 12/12/1977
New Zealand	*	F	F	F	F	None
Norway	*	F	F	F	F	None
Portugal	*	F	F	F	F	Restrictions introduced in 1975 with the nationalization of banks
Spain	*	P	R	R	-	Substantial liberalization of de-novo entry in 1978
Sweden	R	F	F	F	F	None
Switzerland	..	-	-	-	-	Reciprocity principle introduced in 1969
Turkey	*	R	F	F	F	

Table 7.2 Legal Restrictions on Foreign Bank Entry Continued..

Country	Form of foreign bank presence: Representative Office	Branch	De-novo Subsidiary	Situation in mid-1981 Participation in indigenous banks 1960-1981: Subsidiary (1)	Affiliate (2)	Main Changes
United Kingdom	..	-	-	R	P	Banking Act of 1979
United States	..	-	-	-	-	International Banking Act (1978)

(1) Majority interest; (2) Minority interest.

<u>Key to symbols</u>

- .. No authorization required
- * Licensing under general authorization procedures
- \- No specific restriction; entry provisions apply equally to both domestic and foreign applicants. In the latter case, a reciprocity test is applied by some countries.
- R Requires case-by-case authorization/approval, with some provisions applying differently to foreign applicants.
- P Permitted within certain specific limits. Figures in brackets refer to maximum percentages permitted.
- F Forbidden by law or not permitted under government policy.
- \+ Requires case-by-case authorization.

For a detailed description of legal restrictions on foreign bank entry, see Exhibit 7.1.

Source: OECD (1983). <u>The Internationalization of Banking: The Policy Issues</u>. Paris: OECD, p. 72

Exhibit 7.1 Home-Country Control on the Opening of Domestic Banks' Establishments Abroad

Australia	The establishment of overseas branches by Australian banks is not subject to specific authorization requirements but the central bank is generally notified. Banks are required to consult with the Reserve Bank before establishing subsidiaries, whether domestic or foreign.
Austria	The opening of a bank's first branch abroad requires prior authorization by the Austrian National Bank acting as foreign-exchange authority. Prior to 1979, any opening of a branch was subject to approval. Any acquisition of participation in foreign banking institutions is subject to approval by the supervisory authority.
Belgium	Prior authorization is legally required for the opening of branches or the acquisition of banking subsidiaries though, in practice, banks have to inform the Banking Commission in advance.
Denmark	Establishments abroad require approval by the Danish National Bank. In the case of establishment of subsidiaries abroad, approval by the supervisory authority is also required.
Finland	Prior to 1979, there were no special provisions governing establishments abroad by Finnish banks. As from 1979, only commercial banks, mortgage banks, and the post office bank are entitled to establish branches or representative offices abroad. In the case of branches, approval by the Ministry of Finance is required; for representative offices, notification to the Ministry of Finance is sufficient. Subject to permission by the Ministry of Finance, a Finnish commercial bank may purchase shares in a foreign financial or credit institution up to a total of 20 per cent of the bank's equity capital.
France	The establishment of French banks' offshoots abroad and the acquisition of participation in foreign banks are free up to an amount of Frs. 1 million per calendar year. For larger amounts, prior authorization by the Treasury is required.
Germany	German banks are not subject to specific authorization requirements for the opening of establishments abroad, but the supervisory authority must be notified.
Ireland	Domestic banks are required to consult with the Central Bank with regard to the opening of new branches, acquisitions, or the establishment of subsidiaries abroad.
Italy	The establishment of overseas branches of Italian banks and the acquisition or establishment of subsidiaries are subject to prior authorization by the Central Bank.
Japan	Both the establishment of overseas branches of Japanese banks and the acquisition or establishment of foreign subsidiaries are subject to prior approval by the Ministry of Finance. Capital transactions concerning the opening of foreign establishments stated above require prior notice to the Ministry of Finance.
Luxembourg	A formal authorization is legally required for the opening of a foreign branch. The establishment or the acquisition of subsidiaries abroad is not subject to prior authorization, but banks will inform and consult the Banking Commissioner in advance.
Netherlands	The opening of branches or subsidiaries abroad by Dutch banks is not subject to any formal requirement but in respect of subsidiaries a declaration of no-objection is required for participation in other enterprises (including banks) in excess of 5 per cent of the own resources of the enterprise concerned.
Portugal	The opening of subsidiaries, branches, representative offices, or any other form of banking presence abroad is subject to prior approval by the Ministry of Finance.
Spain	The authorization of the Ministry of Economy is required for the opening of branches abroad, which is, in any case, subject to exchange control provisions. The establishment or the acquisition of subsidiaries abroad are not specifically subject to limitations, other than exchange control authorization and the general provision that the total amount of fixed assets and share holdings must not exceed the bank's own resources.
Sweden	Swedish banks are not allowed to have branches abroad. The opening or acquisition of foreign subsidiaries require authorization by the government.
Switzerland	Swiss banks require no specific authorization for the opening of establishments abroad.
United Kingdom	British banks require no specific authorization for the opening of establishment abroad. They are, however, asked to notify the Bank of England of intentions to expand abroad.
United States	The establishment of banking offshoots abroad is governed by Regulation K. A member bank may establish a branch abroad subject to prior approval by the Board. Prior authorization is not required for the establishment of additional branches in any foreign country in which a bank operates one or more branches. The Board must be notified about the opening, closing, or relocation of a branch. The same regulations apply to the opening of branches abroad by an Edge Corporation. Prior specific consent of the Board is required for a bank's investment in its first subsidiary, joint-venture, or portfolio investment. The Board grants a general consent for any investment abroad if the organisation is not engaged in business in the United States and the total amount invested does not exceed 5 per cent of the investor's capital and surplus. Any investment in a subsidiary or joint-venture that does not qualify under the general consent procedure is subject to prior notification to the Board if the total amount to be invested does not exceed 10 per cent of the investor's capital and surplus. Any other investment is subject to the specific consent of the Board.

Source: ibid. p. 54

7.1.1 ON THE CONCEPT OF STRATEGIC FORMS OF BANKING

From a technical point of view, banks have a wide range of organizational forms from which to choose when establishing presence in foreign countries (see, for example, Robinson, 1972; Lees, 1974).

The concept of 'strategic forms of banking' used in this study is a logical extension of new forms of investment in the manufacturing sector, but defined somewhat differently because of industry structure differences. Thus, the term refers to international banking establishments incorporated under host country law in which foreign held equity may confer direct or indirect controlling interest. In other works, foreign-held equity in such overseas banks does not constitute control under home-country regulations. Branch banking is therefore not envisaged by this definition. More specifically, new forms of banking refer to:

(1) Various co-operative banking arrangements established under host-country law in which the foreign bank may have a direct or indirect controlling interest; and

(2) Joint venture and consortium banking arrangements with local banks in which the foreign bank partner may or may not control majority equity interest in the venture. This type of foreign banking strategy is to be distinguished from the first category. In the first group, the parent bank often retains its corporate identity and/or control as in, say, The Royal Bank of Scotland, New York, in USA. In a joint venture or partnership with a local bank, the foreign bank usually brings its bank-specific advantages to bear upon the venture and uses these as a bargaining power to retain a measure of control in the arrangement, especially in situations where the foreign partner has a minority stake in the organization.

(3) The last category may form a separate group by itself because of its specialised nature and scope. Included here are merchant banking and a range of near-banking and non-banking services. This categorization serves as a convenient means of identifying the nature of various organizational forms of banking (or entry) in foreign markets. The first category encompasses international co-operative arrangements and include: agencies, correspondent relationships, representative offices, affiliates and subsidiaries. The second

category comprises international joint venture and consortium banks. Loan syndicate arrangements are excluded from this group, because they are more of financial investments (similar to portfolio investment) than real investment. The last category has become distinct in its own right due to the specialised nature of services provided and activities covered. It encompasses a whole range of merchant banking and non-banking activities including, equipment leasing, factoring and discounting, insurance, tourism and holiday services, mortgages and other specialised trade finance operations.

This introductory section provides a historical perspective on the strategic forms of international banking. The rest of the chapter is divided into five sections. Section 2 explores the taxonomy of strategic forms of international banking, while its dimensions are the subject of Section 3. The ramifications of the global strategy of the multinational bank are examined in Section 4. Applicable theories of the MNE are extended to multinational banking. These are reviewed in Section 5 as are their empirical applications. Summary and conclusion bring the chapter and Part 2 of the study to a close.

7.2 A TAXOMONY OF STRATEGIC FORMS OF INTERNATIONAL BANKING

Given that this study is about organizational forms of international investment other than foreign direct mode, which in the case of banking means establishing foreign branches, included in the following taxomony are types of international banking operations which may, in any case, fulfil the definition of "new or strategic forms of international banking" cited in Section 1. Figure 7.1 illustrates the organizational forms of international banking and the associated control structures. Category I is included for completion of analysis since by definition overseas branch banks are the banking industry counterpart of foreign direct investment. Concern here therefore is on Categories II, III and IV of Figure 7.1. Tables 7.3 and 7.4 illustrate the growth of various modes of foreign banking over a period of two decades (1960 - 1981) in OECD member countries as homes and hosts of foreign banks, respectively. Clearly, other modes than branch banking have grown rapidly within the period.

Figure 7.1 Organizational Forms of International Banking and Associated Control Structure

CATEGORIES OF ORGANIZATIONAL FORMS

CATEGORY I	CATEGORY II	CATEGORY III	CATEGORY IV
Overseas Branch	International Cooperative	International Merchant	International Joint
Network Arrangements:	Banking services;	Venture and Consortium	
International Mergers	Representative offices	Leasing	banking
and Acquisitions	Agencies	Factoring	Shell branches
	Correspondent arrangements	Discounting	
	Affiliates	Insurance	
	Subsidiaries	Travels	
		Mortgages	
Direct control under Home Country Law	Direct or Indirect control under Host Country Law	Depends: Direct or Indirect: Home or Host	Depends: Generally under country of operation

HOME/HOST COUNTRY STRUCTURE

Table 7.3 Organizational Modes of Foreign Banking by Banks Selected OECD Member Countries as of Dec.

OECD MEMBER COUNTRIES AS OF DEC

	1960				1970			
HOME COUNTRY/ORG. MODE	RO	B	S	A	RO	B	S	A
1. Australia (1980)	-	16+	3	-	6	18	3	-
2. Belgium	N/A	1	4	15	N/A	1	5	26
3. Denmark	-	-	-	-	-	-	-	-
4. Finland (1982)	N/A	-	-	-	N/A	-	-	5
5. France (1979)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
6. Germany	-	3	-	N/A	-	5	3	N/A
7. Greece	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
8. Ireland	1	111	(*)	N/A	1	130	(*)	N/A
9. Italy	22	13	-	-	43	21	-	-
10. Japan	-	31	5	-	-	58	6	-
11. Netherlands	-	-	-	-	-	-	21	35
12. Portugal	-	1	1	-	8	1	-	5
13. Spain (1962, 1979)	9	5	N/A	-	7	25	N/A	-
14. Sweden (1982)	-	-	-	-	11	-	-	26
15. Switzerland	N/A	9(*)	-	N/A	6(*)		-	
16. United Kingdom (1982)	8	2676	8(**)			-	-	--
17. United States	N/A	131	39		N/A	534	141	-
Total	40	2997	60	15	76	799	179	97
% increase (decrease)	-	-	-	-	90%	(73%)	198%	547%

OECD MEMBER COUNTRIES AS OF DEC

	1981			
HOME COUNTRY/ORG. MODE	RO	B	S	A
1. Australia (1980)	17	34	5	5
2. Belgium	42	13	16	49
3. Denmark	15	23	8	19
4. Finland (1982)	12	-	7	16
5. France (1979)	24	22	22	36
6. Germany	-	87	56	N/A
7. Greece	N/A	26	N/A	6
8. Ireland	7	188	(*)	N/A
9. Italy	140	57	8	-
10. Japan	196	151	81	-
11. Netherlands	13	68	42	62
12. Portugal	8	15	3	14
13. Spain (1962, 1979)	166	80	N/A	-
14. Sweden (1982)	29	-	12	43
15. Switzerland	N/A	38(*)		-
16. United Kingdom (1982)	185	1280	68(**)	
17. United States	N/A	841	960	-
Total	804	2923	1288	25
% increase (decrease)	958%	266%	620%	(74%)

- N/A Figures Not Available   RO = Representative Office
+ Includes Agencies   B = Branch
(*) Branches & Subsidiaries combined   S = Subsidiary
(**) Subsidiaries and affiliates   A = Affiliate

Source: Compiled by the author from several tables from OECD (1983), The Internationalization of Banking, Paris: OECD

Table 7.4 Organizational Modes of Foreign Banking in OECD Countries as of 1960, 1970 & 1981

	1960				1970			
HOME COUNTRY/ORG. MODE	RO	B	S	A	RO	B	S	A
1. Australia (1980)	1	6	-	1	27	8	-	28
2. Austria (1971)	-	2	-	-	1	3	11	2
3. Belgium	1	7	7	N/A	9	11	15	N/A
4. Denmark	-	-	-	-	-	-	-	-
5. Finland	-	-	-	-	-	-	-	-
6. France (1979)	12	19	14	-	38	27	31	-
7. Germany	31	21	3	-	73	47	30	-
8. Greece	-	3	-	-	-	5	15	-
9. Ireland	-	164	(*)	-	-	229	(*)	-
10. Japan	N/A	34	-	-	N/A	38	-	-
11. Luxembourg	-	3	-	-	-	8	15	-
12. Netherlands	-	-	-	-	-	17	6	10
13. Portugal	1	1	1	-	2	1	1	-
14. Spain	9	4	-	-	37	4	1	10
15. Switzerland	15	8	N/A	N/A	56	13	84	123
16. U.K. (1982)	N/A	N/A	51	N/A	N/A	95	(*)	-
17. United States	-	-	-	-	-	-	-	-
Total	70	272	76	1	243	506	209	173

	1981			
HOME COUNTRY/ORG. MODE	RO	B	S	A
1. Australia (1980)	88	20	-	89
2. Austria (1971)	13	3	10	6
3. Belgium	20	26	29	1
4. Denmark	10	4	1	-
5. Finland	2	-	3	-
6. France (1979)	67	55	61	-
7. Germany	285	101	47	-
8. Greece	17	65	1	-
9. Ireland	2	258	(*)	-
10. Japan	103	94	-	-
11. Luxembourg	-	18	84	-
12. Netherlands	11	24	16	9
13. Portugal	11	2	1	-
14. Spain	155	27	6	3
15. Switzerland	26	16	91	145
16. U.K. (1982)	163	274	(*)	-
17. United States	249	377	46	30
Total	1222	1364	396	283

(*) Branches and Subsidiaries combined

Source: Ibid.

CATEGORY I

This group of organizational forms of international banking can be seen as involving varying degrees of co-operation between the foreign bank and a host country entity. Co-operative arrangements can be on a reciprocity basis or on commission basis. Alternatively, they could simply be a corporate form of banking.

REPRESENTATIVE OFFICES: These serve as contact points for providing business and economic information about the host country or a prospective regional market. Such points of contact lead to business connections. In the main representative offices act as intermediaries between the parent bank and the host country customers, without serving as booking stations, that is, accepting deposits and making loans. Where host government regulations disallow branch banking or direct foreign participation, foreign banks can use the medium of representative offices to scout out business opportunities in the host country. Alternatively, they can be used as preparatory grounds while waiting for approval for operations. Usually, representative offices do not require authorization and in many cases are licensed under general authorization procedures (see Table 7.2). Ireland and Sweden were for a time the only two OECD member countries that required authorization, with differential provisions for foreign applicants. Sweden abandoned this policy in 1985 (Business Week, June 4, 1984, p.41).

AGENCIES: represent a more active organizational presence in foreign countries than representative offices. First, agencies are able to accept certain types (specific-use or short term) deposits, generally from wholesale (i.e. corporate) customers. Second, they are allowed to make loans to local firms. Third, they can raise funds in the host country, usually through local loans or short term deposits although they can be supported by their parent banks. However, agencies are not permitted to operate current accounts (demand deposits) other than credit balances.

CORRESPONDENT ARRANGEMENTS: A correspondent bank is a bank with which another bank maintains banking relationships. The relationship is created on a reciprocity or symbiotic basis. It allows both banks to avail one another the use of its resources to service the other's customers. For example, a correspondent bank relationship with a German bank will enable a British Bank to make payments in Deutsche Mark on behalf of its domestic clients. Correspondent banking has been at the substratum of the growth of international business. As might be expected, the growth of international business (and of MNEs) resulted in an expansion of traditional domestic banking services. Many banks had to open international departments as special units to handle the overseas needs of their domestic clients. As businesses increased and as transactional delays through host country foreign exchange bureaucracy or international clearing systems, were unrelenting it became more exigent to maintain reciprocal deposits with commercial banks located in the countries with majority of their corporate clients.

Additionally correspondent banks provide advisory services, using their local knowledge. They provide a first hand survey of overseas market potential for their customers. Banks maintain a database on economic and political structure of most, if not all, countries where they have correspondent relationships. With that they can advise a prospective exporter client on such matters as host government regulations, economic and political structure of the potential host market, its monetary and fiscal regimes, etc. Correspondent banks are able to assist and advise on the marketing and product development of their customers For instance, with their knowledge of local conditions, they can recommend reputable agents or distributors in their local area. They also provide holiday and travel advisory services.

AFFILIATES: are local banks incorporated under host country law in which the foreign bank holds a minority equity interest. The term 'affiliate' is broadly used to cover a wide range of investments in associated companies. Associated companies are related companies in respect of which a parent company is in a position to exercise significant influence. Technically, the distinction between an affiliate and a subsidiary is generally based on the extent to which the parent company (or bank) holds a controlling interest in the associated company (OECD, 1983, p.57). The issue of controlling interest is explored in the next section.

SUBSIDIARIES: refer to local banks incorporated under host country law in which the foreign bank has a direct or indirect controlling interest. A subsidiary is a corporate form of banking next to foreign bank branch. In some countries, the establishment of foreign branches are not permitted for legal and political reasons. However, local banking organization can be set up in which the foreign bank enters into a partnership with a local bank or holds a majority equity in it. But, it should be remembered that, unlike manufacturing subsidiary, here majority equity participation does not necessarily imply a controlling interest, vice versa.

CATEGORY III

These activities enable banks to register presence in foreign markets through the specialised activities. The involvement of banks into these activities is seen as a breakdown of the wall that has historically divided banks and nonbanks Foreign involvement in both affiliates and subsidiaries may be with respect to purely commercial banking activities. Alternatively, it might be related to specialised services as in the provision of merchant banking and near-banking services. Such subsidiary affiliations may be with leasing organizations, factoring, and discounting, consumer credits, brokers and agents, insurance, mutual funds, investment banking, travel agencies, etc.

INVESTMENT/MERCHANT BANKING: An investment (US) or a merchant (UK) bank is a financial intermediary which performs a variety of securitisation and financial services, including acceptance of bills of exchange, the issue and placing of loans and securities, portfolio and unit trust management and some banking services. Also called <u>Issuing houses</u>, they provide, risk capital for firms, deal in gold bullion, insurance, hire purchase and are active in the EUROCURRENCY market.

Merchant banking has diversified from its historical role of financing overseas trade and accepting bills of exchange. From these traditional functions, they have developed a range of other banking services connected with foreign trade, e.g. dealing in gold and foreign currency and assisting borrowers to raise money on the stock exchange. Nowadays, while such functions are still part of their portfolio of services, they are more of institutional (corporate) finance houses, issuing houses, accepting houses or investment trusts. They are most prominent in the mergers and takeovers markets where they act as institutional advisers. For example, the Corporate Finance division of Kleinwort Benson Group plc was involved in some of the largest and most complex corporate finance transactions which took place during 1989, including advising Beecham on the £8 billion merger Smithkline Beckman, regarded as "the largest cross-border merger ever completed" and a host of other multimillion pound acquisitions and mergers (Annual Report, 1989). Following the big bang, there has been a growing trend in which commercial banks (and even building societies) offer merchant banking services through associated institutional mechanisms.

SECURITISATION AND DISINTERMEDIATION: Deregulation has brought about changes in the boundary between banks and markets in international capital and credit markets. The effect is that the basic business of corporate banking is shrinking with the securitisation of assets and of the Euromarkets. The creation of a single European market prospectively increases the trend towards securitisation and decline in the growth of cross-border lending. In this case, the shift from internalization of transactions (which entails financial intermediation between international borrowers and lenders) to externalization of transactions (which involves direct borrowing from international lenders via the security markets) underscores the underlying difficulties with intermediation. These can be traced to transaction cost origins in which Eurosecurity markets are regarded as more operationally efficient (i.e. lower transaction costs) than syndicated bank loans.

High internal transactions by MNBs, problems of third world debt, increasing international competition (arising from deregulation and involvement of non-bank banks) and the growth of in-house banks by large MNEs (especially the Japanese) are some of the catalysts for the shifting of transactions away from the internal organization of MNBs. For example, the rescheduling costs of sovereign debts and the associated increase in bad debt provision in the books of MNBs increased the policying and enforcement costs of existing debt contracts but have also affected expectations about future contracts. Not only that, the transaction costs of searching for good credit risks and the subsequent negotiation costs have escalated considerably since the debt crisis.

In contrast, the emergence of Euronotes and Eurocommercial paper has drastically reduced market transaction costs. For example, the less dependence on syndicated term lending implies less need for standby facilities, a combination of which leads to reduced transaction costs. Furthermore, the relative decline in petrodollars juxtaposing major new capital flows from Japanese private and institutional investors has contributed immensely to the decline in the relative importance of traditional commercial banking. In response, banks have diversified into other non-bank areas in the hope of both only enlarging income source base and capturing the clientele.

LEASING ORGANIZATIONS: have now generally become affiliates or subsidiaries of banks. The leasing business is particularly linked to tax efficient schemes but has grown in scope and importance as the process of obtaining commercial loans from banks becomes increasingly lengthy and costly. Leasing activity covers a wide range of markets, from individuals to industries and property and from aircraft to xerox machines. In an integrated single market, international leasing will become increasingly important to service a European rather than a national clientele. By being affiliated with leasing firms, banks of one national origin can establish operational presence in a foreign country without the necessity of a direct establishment.

FACTORING : Liquidity problems and the need to sustain a stable working capital have forced small and medium-size firms to transfer the responsibility for credit sales collection to debt collecting firms. This service is relatively young in the UK compared with the US. The factor has to have a strong support of a bank or other financial institutions to be able to discount credit invoices and make immediate payments. In many cases, factoring companies are affiliates or subsidiaries of banks. Through international factoring companies, factors can offer services to exporters by protecting their customers from bad debts overseas and by giving advice on foreign exchange transactions. These can be seen as an integrated package of resources which a bank can claim as ownership and internalization advantages and through which a bank can register presence in foreign markets.

CONSUMER CREDIT: The consumer credit sector covers mainly asset-based financing such as cars, boats, household furniture and property. Also included are various kinds of instalment credit such as hire purchase. In these cases, the loan is secured on the goods. This sector offers products similar to those of savings and loans organizations. Not only are they becoming integral part of a commercial bank structure but are directly in competition with specialised consumer credit organizations owned by the manufacturers of the assets financed, e.g. Ford Credit Finance, IBM Credit, GMAC, Renault Finance, GE Credit, etc. This in-house financing has put a strain on the competitiveness of traditional HP companies as well as rendering the role of commercial banks redundant. For example, a person wishing to buy a Ford car need not go to an HP company or a commercial bank since the Ford dealer will raise the necessary credit at the often advertised "0% financing". Banks are therefore having to acquire HP companies as complementary businesses, using their cheap funding sources and wider economic base.

OTHER CO-OPERATIVE MODES: Other service areas which banks actively use to penetrate into foreign markets include insurance, travels and mortgages. By acquiring controlling interests in these industries, banks are able to increase their corporate base and enhance profitability on a global basis.

CATEGORY IV:

JOINT VENTURE & CONSORTIUM BANKS: Joint banking venture is an association established for the purpose of carrying out specific business of mutual interest to the participating banks. Joint venture banks are also called consortium banks, for which two main types can be distinguished. The first type comprises those set up by member banks who do not feel strong enough to act independently. The second type encompasses those which specialise in a particular type of business. The first type of consortia is formed by banks who feel too small and/or inexperienced to go it alone.The distinguishing feature of this category is the transitory nature of the association. As the individual partners gain in strength, the continued existence of this category might be at risk. For example, in 1984 the Nordic Bank Consortium was bought out by one of the shareholders, Den norske Creditbank - Norway's largest bank. The other shareholders - Kansallis Osake Pankki of Finland and Copenhagen Handelsbank - have since set up on their own in London (World Banking, 1986). Similarly, Ibero Partners now represent only three banks instead of the original six.

Also, Scandinavian Bank lost two of its shareholders in 1984, and the setting up of a London branch by one of the remaining partners (Union Bank of Finland) suggests that it too might be considering leaving the consortium (Ibid.). These and several other cases illustrate the transitory nature of this category of joint banking ventures.

Anecdotal evidence tends to suggest that the long-term future of the consortia lies in their provision of specialist services. This implies that the JV entity must not compete with its shareholders or transact actively in each other's market. The following examples are illustrative. Sir John Hall, chairman of the Association of British Consortium Banks as well as of European Brazilian Bank Ltd., describes the operational objective of his bank as follows: "We are finders of niche business by and large, not lenders or innovators in capital markets. Otherwise we would be facing competition from our shareholders - and that of course would be fatal". Nicolo Dubini, managing director of ITAB notes that "when a consortium bank starts to do what its members already do, then its days are numbered".Clearly joint venture banking is created for specialist services and this view is reflected in the fact that none of the London-based consortia have yet participated in the City Revolution - the 'Big Bang' (ibid.). It is also perceived as a useful way for the first category of consortia - those members not large or established enough to go it alone - to diversify. This is even moreso because the medium-term lending for which consortia were originally established can now be easily handled by individual banks.

Apart from diversifying services into areas not already covered by parent banks, the success of consortia also lies in absolute clarity of purpose. Where the partners to a consortium have divergent objectives or incongruent goals, the bank is bound to fail. An example is the closure of the Paris-based Franco-Algerian consortium bank (Union Mediterranee de Banques) in 1985. The major reason for its closure was the disagreement between the French and Algerian partners on the role of the bank. While the French wanted the bank to be primarily a retail bank for France's many Algerian workers, the Algerians saw it as an international bank specialising in trade finance and merchant banking (ibid.). The conflict of policies and roles exacerbated the bank's problems.

Finally, consortium banking can be seen as performing a role similar to JV in the manufacturing sector, namely, providing small and medium-size banks opportunities to compete in foreign markets, especially in international financial centres like London, New York and Tokyo; providing banks of one nationality opportunities to develop new products and markets such as underwriting, merger brokering, and financial management; providing banks a launching pad into competitive or prohibitive markets, which otherwise they would be unable to venture on their own individually; and serving as a collective investment mechanism for diversifying risks and costs, especially in financing sovereign projects.

7.3 DIMENSIONS OF INTERNATIONAL BANKING

In the previous section, international banking was described in terms of jurisdiction of legal control. Because of the strategic importance of banks in macro-economic development, they are generally constituted as local legal institutions and, depending on the host government regulations, may operate as legal extension of the parent bank or as local institutions operating under host country law. Unlike foreign affiliates and subsidiaries, foreign branches are by contrast a legal extension of the parent bank in a foreign country. Accordingly, they are not separately constituted or locally chartered companies. Rather, they are an integral part of the parent bank; they have no separate legal identity, and are subject to the parent bank's home country control and regulation. They are therefore the foreign subsidiary counterpart of the manufacturing industry. Thus, foreign direct investment in banking refers to foreign branch banking.

For political, legal and economic reasons, some countries restrict the opening of foreign branches. Exhibit 10.1 presents the kinds of national controls applied by member countries of OECD on the opening of domestic banks' foreign branches. Some countries adopt a liberal approach that is usually linked to reciprocal considerations. In developing countries, government restrictive policy is traditionally linked to a sensitivity to the problem of foreign bank presence and its impact on the indigenous banking system (OECD, 1983). Another point of technical clarification in the definition is 'controlling interest'. The practical application of the term varies from country to country and is not necessarily equivalent to the concept of "majority" equity interest and participation (ibid.). Although a foreign bank can have a direct or indirect controlling interest in a local bank, as in affiliate or subsidiary, that does not technically constitute a branch status because the establishment is incorporated under local law.

7.3.1 COMPARATIVE BANKING AND THE MULTINATIONAL BANK

International banking - also called multinational or transnational banking - has been described as one of the least understood aspects of finance and one of the most diffuse as well (UNCTC, 1981). There is no consensus definition of the term: different researchers adopt different working definitions, perhaps to fit the context of their research. Literature perusal suggests two approaches to the discussion of international banking. One approach is silent on conceptual issues. Included in this category are the descriptive works of Aliber, 1984; Brimmer and Dahl (1975), Khoury (1979), Goldberg and Saunders (1981), and Nwankwo (1988).

The second approach addresses conceptual issues and consists of several working definitions. One school of thought in this group perceives it as a currency phenomenon. Thus, a multinational bank is one which deals in two or more currencies. Specifically, Aliber (1984), posits that "...from the point of view of industrial organization, US banks (or more generally, banks) engage in international banking when they sell deposits and buy loans denominated in currencies other than the US dollar" (or their home currency). Another school of thought defines it as one which operates in, and is subject to the laws of, at least two countries.Other wider views exist. One such view defines a transnational bank as one which has global operations which involve "not only ... ordinary commercial banking ... but also merchant banking, leasing, factoring, and consulting ...". (UNCTC, 1981). The snag with this global perspective is that if a UK bank operates mainly in USA for example, it will not qualify as a MNB for the purposes of this and Aliber's definitions. The UNCTC provides an alternative definition, namely deposit - taking "banks with branches or majority-owned subsidiaries in five or more different countries and/or territories" (ibid.) This view is both exclusive and restrictive for the reason stated immediately. It only permits number-counting and numerical locations of transnational banks (Aliber, 1984). Adopting this definition enabled the UNCTC researchers to recognize only 84 MNBs by 1975.A conceptual exploration of comparative banking (i.e. domestic versus international) and the nature of multinational bank (MNB) can be pursued in any or all of three ways. The first is a generic description of the traditional role of banks. The second is a classification of banks that identifies a metamorphosis of involvement in financial markets and client structure. The third conceptual process seeks to distinguish between MNBs and MNEs. These are briefly surveyed in turn.

TRADITIONAL ROLE OF BANKS

In their basic form, banks are financial institutions which act as intermediaries between 'surplus-saving units' (depositors) and 'deficit-spending units' (borrowers). As financial intermediaries they (1) acquire funds from depositors and savers in return for safety, liquidity assurance and higher net return; and (2) in turn sell the acquired funds to borrowers at a much higher rate of interest, thereby earning a margin of spread. In other words, banks borrow at one level of interest rates (i.e. rates paid to depositors) and lend at another level (i.e. rates charged on credit facilities). In performing this financial intermediation role, banks have a unique ability to bring together individual borrowers and lenders to the mutual advantage of both parties. They are legally equipped to guarantee safety and liquidity and can diversify risk on a global basis.While retaining this basic feature, contemporary banking has however widened the intermediation process as Figure 7.2 illustrates. This model presents a simple framework for understanding the dimensions of financial intermediation, including maturity intermediation, denomination intermediation, portfolio diversification, professional management, liquidity assurance and securitisation. These functions are structured to suit two types of customers: retail group and wholesale group. In this figure, multinational banks can be seen as evolving from the domestic market through increasing diversification of traditional functions to a view of active participation in international financial markets.

DEGREE OF INTERNATIONAL INVOLVEMENT

Another approach to international banking distinguishes between types of banks and their degree of involvement in international markets. This is 'a stages of development' approach based on market matrix in which the degree of involvement is matched by type of services and clientele group, etc. Figures 7.3 and 7.4 illustrate different aspects of this classification.

Figure 7.2. A Framework of Financial Intermediation

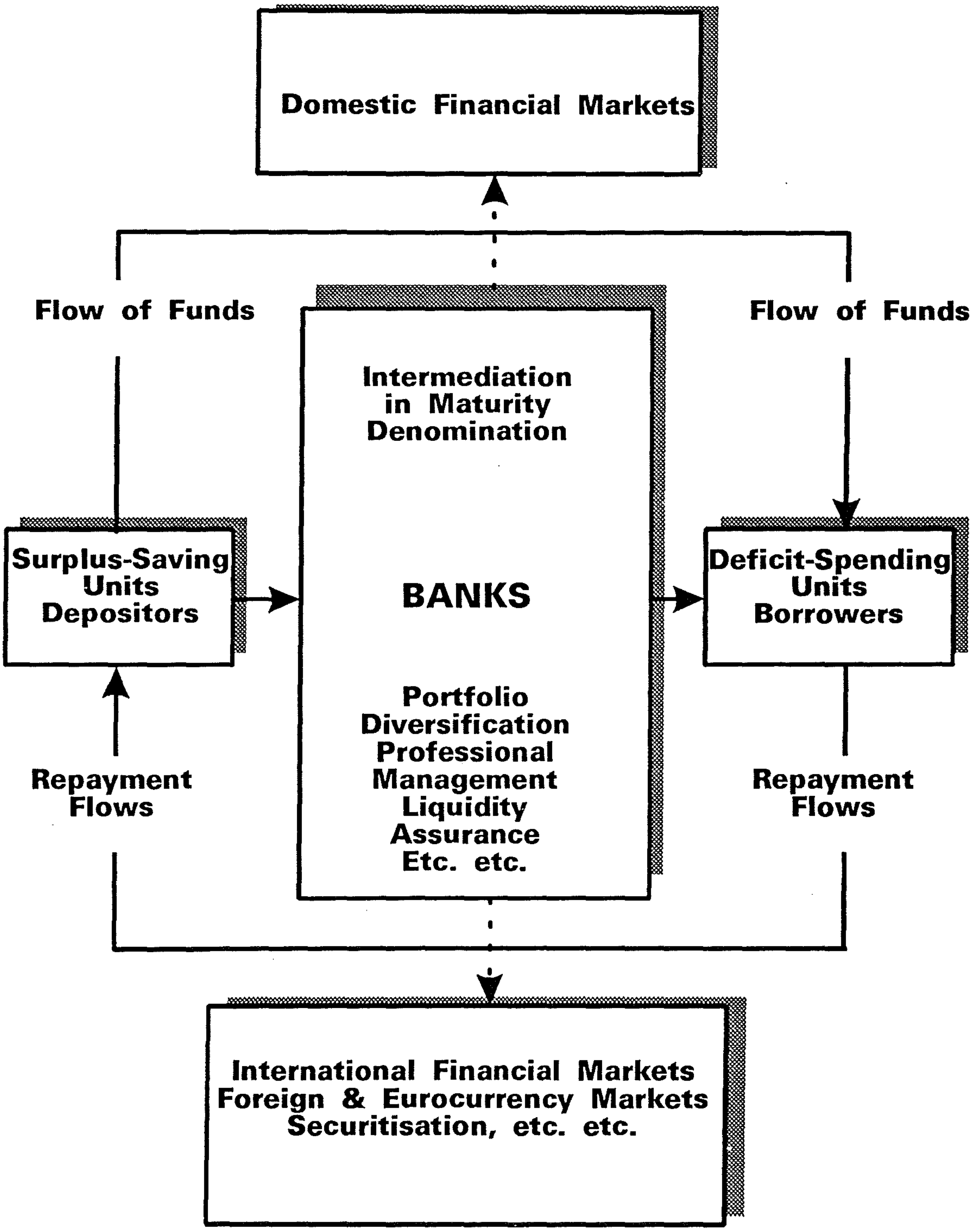


Figure 7.3 Degree of Banking in Domestic and International Markets

		DOMESTIC MARKETS			INTERNATIONAL MARKETS		
		RETAIL MARKETS	MONEY MARKETS	CAPITAL MARKETS	FOREIGN EXCHANGE MARKETS	EUROCURRENCY MARKETS	EUROBOND MARKETS
Domestic Bank	1	D	D	-	-	-	-
Domestic Bank	2	D	D	D	-	-	-
International Bank	1	D	D	D	I	-	-
International Bank	2	D	D	D	I	I	-
International Bank	3	D	D	D	I	I	I

D = High Degree of Domestic Involvement
I = High Degree of International Involvement

Both figures portray the various stages of involvement in domestic and international retail (and wholesale) money and capital markets. The extent of a bank's commitment to international activities is simplified in Figure 7.3 while Figure 7.4 amplifies this metamorphosis, specifying in each category the type of services, major customers, possible competitors and the kinds of customer service needs. This taxonomic explanation is similar to Giddy's (1983) framework, but differs from his not only in scale and scope but also recognizes implicitly the barriers to international banking in the stages of development.

A CONCEPTUAL CONTRAST WITH MNE

A third and last conceptual exploration of international banking contrasts multinational banks (MNBs) with multinational enterprises (MNEs). MNBs can be distinguished from MNEs in at least three ways. First, they belong to different activity industries: the former engage in service activities while the latter produce goods. Accordingly, their production functions are fundamentally different from one another. Second, MNBs (like the industry in general) are labour-intensive, providing financial and other specialised informational services. On the other hand, conventional MNEs are capital intensive, albeit combining labour, capital, and technology in their production function. This is not to suggest that MNBs are not technological in the production of financial services, but relatively speaking, MNEs are more capital intensive (Rugman, 1979). Third, MNBs have the unique ability to perform financial intermediation. Although MNEs can provide in-house financial intermediation and other financial services, such as treasury management and consumer credit, they are limited in the scope of such services.

Figure 7.4 Market Matrix of Degree of Involvement in Domestic and International Markets.

DEGREE OF DOMESTIC MARKET INVOLVEMENT & SERVICE GROUPS	MAJOR CUSTOMERS	MAIN BANK SERVICES	MAJOR COMPETITORS	CUSTOMER SERVICE NEEDS
1 - DOMESTIC MARKET 1 - CONSUMER FINANCIAL SERVICES	Individuals Households Sole Traders Non-profit Organizations Self Employed	Savings Accounts Current Accounts Cash Line Services Term Deposits Safe Deposit Investment Accounts Credit Lines: Overdrafts Personal Loans Mortgages Credit Card Facilities Budget Accounts Professional Advisory Services: Investment Services - stocks and shares Tax Management Insurance Services Travels Advice General Business Advisory Services Mainly Domestic Currency Business	Other Banks: Commercial Savings Mortgage Building Societies Non-bank Organizations: Finance Houses Insurance Companies Post Offices Brokerage Firms Accountants Solicitors Credit Companies Money Lenders	Convenience Security Efficiency High Savings Interest Low Borrowing Rates Professional Advice at Minimum Cost Personal Financial Planning General Business Advice General Information

Figure 7.4 Contd.

2. DOMESTIC MARKET 2 - MIDDLE MARKET & CORPORATEFINANCIAL SERVICES DOMESTIC BANK 2	Partnerships Large Sole Traders Small- and Medium-Sized Companies Small Local Authorities Governments and their Agencies	Same as Above Plus: Short and Term Loans Hire Purchase and Instalment Credit Cash Management Leasing Factoring Registrar Work Foreign Services Computer Services Credit References Merchant Banking Import Export Finance Mainly Domestic Currency Business with some Foreign Exchange Currency Investment and Currency Lending	Same as Above Plus: Foreign Banks Merchant and Investment Banks Leasing Companies Factors Foreign Exchange Brokers Computer Bureaux Development Agencies Government Departments Local Authorities	Same as Above Plus: Corporate Planning Foreign Exchange Services Business Finance
3. DOMESTIC MARKET 3 - BANKS AND FINANCIAL INSTITUTIONS DOMESTIC BANK 3	Large Retail and Wholesale Customers - Large Companies Foreign Banks - Correspondent Relationships Banks Governments and their Agencies	Same as Above Plus: Automatic Teller Machines Interbank Market Home Banking Correspondent Banking ServicesDomestic Currency Business With Active Involvement in Foreign Currency Business and Euromarkets International Portfolio Investment Advisory Services Cheque Transactions	Same as Above Plus: Central Bank Discount Houses	Same as Above Plus: International Investment Advice:- International Portfolio Investment Advice

Figure 7.4 Contd.

1. INTERNATIONAL MARKET 1: CONSUMER FINANCIAL SERVICES	Individuals Households Self-Employed Sole Traders Non-Profit Organizations Mainly with Interest in International Transactions, the Scope of which is Small and Limited	Same as Domestic Bank 3 Plus: Electronic Banking Currency Accounts Eurocheques Travellers Cheques Negotiable Order on Withdrawal (NOW) Facilities Foreign Accounts Payment Services Foreign Exchange General Information and Introductions	Foreign International Banks Travel Agencies Credit Card Companies Other Banks: Commercial Savings Cooperative Building Societies Post Office Information Professional Advice Travel Planning Security Convenience Efficiency Low Cost Competitive Interest Rates	
2. INTERNATIONAL MARKET 2: MIDDLE MARKET AND CORPORATEFINANCIAL SERVICES	Partnerships Large Sole Traders - Importers and Exporters Small- and Medium- Sized Companies Local Authorities Governments and their Agencies	Accounts in Foreign Countries Foreign Exchange Deposits Foreign Currency Loans Merchant Banking Project Finance Electronic Funds Transfer Correspondent Banking Services	Other Banks: Commercial Savings Merchant/Investment Foreign and International Multilateral Agencies Multinational Companies	Same as Above, but in greater international scope plus: Corporate Planning International Transfers
3. INTERNATIONAL MARKET 3: 3 BANK AND FINANCIAL INSTITUTIONS	Multinational Companies Large Companies Large Corporate Bodies Foreign Banks Other Financial Institutions Governments and their Agencies	The Above Plus: Euro-currency Syndications and Deposits Financing International Trade Foreign Investments Promotion of Foreign Trade and Investments Economic and Financial Consultative Services International Bond Issues Sovereign Lending World Net Work Systems	Central Banks Other Large Banks Discount Houses Company Treasurers	Same as Above Plus: International Fundings at Low Cost

Giddy (1983) extends the industrial organization theory of FDI to distinguish among three types of international banking: arm's length international banking, offshore banking, and host country international banking. Arm's length international banking is the most basic form; is home based and corresponds to International bank type 1 and domestic bank 3 of Figures 7.3 and 7.4, respectively. They maintain correspondent account balances in foreign banks for the purpose of clearing their customers' international payments. But for regulatory barriers and other imperfections in the international financial markets, all international banking would take the form of arm's length (ibid.).

An offshore bank is a bank incorporated overseas, usually in a tax-haven country, whose function is to provide funds other than those of their own country. The financial markets are generally not regulated in the same way as domestic markets. The transactional emphasis in offshore banking includes purchase and placement of eurocurrency funds, eurocredit activities, and foreign exchange deals. These are conducted in offshore or eurocurrency centres. Finally, host country international banking refers to banking with local residents in a foreign country where a parent bank may establish presence in the form of representative offices, subsidiaries or branches. Instances of this type include Glasgow based Bank of China and Bank of Pakistan which are primarily designed to cater for the Chinese and Pakistani communities in Glasgow and environs, respectively. Apart from providing banking services to a 'culture-fast' community such as these, the banks have become an important employer for British communities of these countries. This point was emphasised during the interview sessions of this research.

Arm's length international banking can be regarded as the banking counterpart of exporting and international trade. Offshore banking can be likened to offshore assembly plant while host country banking or foreign branch banking is the equivalent of foreign direct investment.

7.4 GLOBAL INVESTMENT STRATEGY OF THE MNB

Theories of the economic behaviour of the multinational enterprise are conventionally employed to rationalise foreign investment decisions of banks. The framework is based on the neo-classical assumptions about imperfections in international environment markets. These assumptions create an option for the firm to act in a passive direction, by accepting the imperfections, or to react in a manner that will potentially avoid or overcome them.

The basic premise of these theories is that the simple model of the international economy, based on perfect market conditions in which free trade would prevail, is practically non-existent. Therefore, the symmetry between free trade and the MNE (Rugman et al, 1986, p.98), is the result of the latter's response to the imperfections. In turn, the type of response adopted by a firm is dependent upon the firm's strategy. The general characteristics of the theories and their applicability are as relevant to the manufacturing/extractive industries as they are to the banking industry. This section of the chapter examines the role of the global investment strategy of the multinational bank as a prelude to discussing the theories.

7.4.1. MOTIVATIONS OF GLOBAL INVESTMENT STRATEGY

The various theoretical models that have been developed to explain foreign direct investment (FDI) are attempts at rationalising the differential capacities of firms in the choice of optimal modes of servicing foreign markets. The starting point for examining the models and the structure of the firm's strategy is an enquiry into why banks headquartered in a particular country should seek to establish operational presence in foreign countries.

PRESERVATION OF OSAs AND BUSINESS RELATIONSHIP

A growing body of empirical evidence supports the hypothesis that the international expansion of banks is based on the need to preserve their ownership - specific advantages (OSAs) as they follow their customers abroad. (Grubel, 1977; Fieleke, 1977; Terrell, 1979; Goldberg & Saunders, 1980, 1981; Gray & Gray, 1981;

Tschoegl, 1982; and Yannopoulos, 1983). MNBs are able to do this more competitively than local banks due to their pre-established relationship with and better access to information on their clients at home (Pringle, 1966; Brimmer & Dahl, 1975; and Rugman, 1981). Besides, the banks may need to follow their clients abroad in order to ensure a continuing business relationship with the home parent of the foreign subsidiaries. Failure to do so may force foreign subsidiaries to turn to foreign banks or domestic business relationships. (OECD, 1983; Nigh, et al, 1986).

REGULATORY FORCES

Banks are also found to react to regulatory forces which seek to restrict their capacity to exploit perceived domestic market imperfections. As profit seekers, on the one hand, and a vital mechanism in the transmission of government's monetary policy as well as financial intermediaries, on the other, banks can find themselves playing ambivalent roles in national economy. Where regulatory pressures prevail, they may resort to foreign markets to exploit favourable or less restrictive foreign banking environments. (Brimmer & Dahl, 1975; Aliber, 1976; Fieleke, 1977; Goldberg & Saunders, 1980; and Gray & Gray, 1981). In some developing countries there are restrictions on branch banking (see Figure 7.2 and Exhibit 7.1).

ACCESS TO CHEAPER FUNDS ABROAD

Broadly speaking, banks are motivated to optimise returns by seeking overseas markets where they have access to cheaper funds. A substantial foreign banking presence in various offshore banking and some onshore banking markets of developed and developing countries seems to suggest the significance of such motivation (Nigh et al, 1986).

INCENTIVE TO ARBITRAGE IN FOREIGN COUNTRIES

Where a bank's specific advantages can be employed to capture perceived failures in a segmented market, the host government may even be willing to pay the MNB a premium for contributing to improve the country's international capital flows. Incentives may take the form of tax havens, less restriction in organizational set-up (including removal of quotas), or removal of costly barriers to portfolio flows.

Although the lessening of entry restraints and the liberal stance of home and host country regulations are likely to have played a role in the growth of multinational banking, a much more important factor relates to regulatory incentives that offer greater freedom from supervision than the home country, or special advantages, or both (OECD, 1983). Exchange controls, taxation, monetary policy, and prudential supervision are aspects of this policy.

SCANNING ADVANTAGES OF THE MNB

In a world of imperfectly diffused information, the scanning advantages of an MNB may widen its set of investment opportunities. The information - and profit - scanning functions of a multinational network are effective parameters for success in foreign markets (Vernon, 1979).

INTERNATIONAL DIVERSIFICATION OF RISKS

Banks may be motivated by imperfections in capital markets to reduce risk through foreign diversification of investments. Diversifying a bank's asset holding over several countries can potentially lead to risk reduction and ultimately to an improvement in risk/return ratio (see, Fieleke, 1977 and Rugman, 1979).

POLITICAL MOTIVES

Finally, there may be political motives behind international expansion of banks (ibid.) These political motives drive banks to avoid or exploit various externalities in both home and foreign markets. Some of these are a consequence of the natural - and unnatural - market imperfections explored in part 1 of this study.

9.4.2 NATURE OF GLOBAL STRATEGY OF THE MNB

A contextual analysis of the global investment strategy for the MNB may proceed from a consideration of the nature of strategic problem in general.

NATURE OF STRATEGIC PROBLEM

Schoderbek, et al (1975, p.143) characterised the organizational task of building associations between particular environmental changes and accommodative organizational actions as the "strategic problem". This construct is shown in Figure

7.5. Given the international environment in which the subject strategic problems exist and the market imperfections and parity deviations that describe them, the ability to adapt to environmental demands and opportunities constitutes a *conditio sine qua* non for firm's survival. This is the context in which a firm's strategy is set.

The scenario created in Figure 7.5 can be traced to a firm/market relations in which the transaction cost differences between existing firms and existing markets are emphasized (see, for example, Holland, 1986, p.158 and Rugman et al, 1986, p.329). In general, and for profit-seeking firms in particular, the transactional interdependencies of the firm-environment system are a function of the perceived nature and importance of the relationship between the firm (as hierarchy) and the environment (as market). Such a relationship can be either symbiotic and/or synergistic. The former is functionally necessary for the survival of both systems (firms and markets). A synergistic relationship, on the other hand, is not functionally necessary, but its existence enables the firm and the market to achieve a relatively greater performance (see for example, Schoderbek,1975, p.145).

Behind the interdependencies are a vast range of environmental constraints which the firm has to overcome in order to survive. These include increasing turbulence of the international environment, structural balance of the payments disequilibrics, worldwide economic recession, volatile exchange rates, volatile interest rates, and technological change. In addition, the banking industry is facing increased competition; deregulation which has expanded the financial services of non-bank banks; sophistication and demand - diversity of bank customers; and the growth pattern of the financial services sector.Overall the real issue facing MNBs and, for that matter, all firms, is SURVIVAL. Survival, expressed as long-term profitable growth, means securing quality earnings from net interest income by intelligent asset/liability management, and by generating fee income from value-added services, while controlling costs vigorously. This demands a careful and articulated development of business strategy.

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APPROACHES TO GLOBAL INVESTMENT STRATEGY

The global investment strategy for the MNB can be explained from two approaches: the normative and the pragmatic. The normative approach is theoretical: it is based on Dunning's eclectic model of foreign investment. This model rests on three simultaneous conditions: ownership-specific, location specific, and internalization-incentive advantages. In combination, they provide an analysis of what an MNB should do in order to "survive",

ACTUAL PRACTICE OF MNBs

Descriptive views of actual strategies adopted by MNBs are attempts to explain the response of banks to changes in the competitive environment. Kenyon et al(1985) provide an analytical evidence of a survey of practice in five countries: USA, UK, Germany, France and Japan. From their analyses, banks are seen to evolve strategies as a response to intensified competition and growing environmental pressures. The various strategies of individual banks in the five-country study can be grouped into: (1). those that deal with or require changes in management priorities and (2). those that warrant changes in marketing and global strategies.

CHANGES IN MANAGEMENT PRIORITIES

MNBs were shown to modify their priorities in response to competitive pressures. Such environmental influences included the birth of the eurocurrency market, constraints on domestic markets, deregulation, and possibility of arbitrage with domestic markets. The 1970s witnessed the upsurge of inflation, OPEC activities, volatility in the markets, technological advancement, etc. Coupled with global competition, changes in management priorities were seen to occur in the areas described below.

CHANGE IN PERCEPTION OF UNIQUENESS OF BANKS & THEIR ROLES

Banking is no longer seen as a unique role, especially in the USA and UK. Dergulation has widened the scope of the activities of non-bank banks and caused an erosion into the traditional domain of banks. Technological advancement among other factors, has contributed largely to the perceived changes in the culture of banking.

CHANGE OF OBJECTIVE

Changes are seen to be taking place in the objectives pursued by bankers. In a bid to increase profitability, banks are having to set profitability criteria. Consequently, they now pay more attention to activity returns than overall returns, as was the case.

CHANGE IN MARKETING FOCUS

Bank customers, especially corporate clients, are much more sophisticated than in the 1960s. Large MNEs have treasury departments and in-house finance establishments which compete in varying degrees with banks, with the result that the latter are now forced to evolve a new marketing focus. There is also a shift in the fragmentation of banks' services to customers. The attempt is to match the growth in the sophistication of demand for banks' services and the capacity of competing firms to unbundle the delivery of bank products. For a bank to survive in this kind of area, management must be prepared to match the skills of competitors not only in the existing fragmented packages, but also to create a clientele - product match for its own unbundled packages. Corporate treasurers may be willing to accept intramarginal products if they are offered other marginal products e.g. loans.

The second group of responses by MNBs to competitive environmental pressures consists of strategies formulated expressly in terms of global product range, focus by products, customer segment or geography. Others have to do with expansionist-driven responses and responses propelled by financial policies rather than products or markets.

GLOBAL PRODUCT STRATEGIES

This group of strategies is designed to cover a wide range of banking products/services across a wide range of customers in a well diversified geographical location. It is a maximising strategy which seeks to optimise the international returns of individual divisions of the bank. To be able to implement this strategy a bank must have certain comparative advantages, e.g. in organization, management information systems, etc. And to operationalise the strategy, global relationship officers are appointed "to coordinate and monitor the worldwide activities of their global customers, the bank's exposure to each and the bank's return from each" (ibid.).

FOCUS STRATEGIES

Rather than adopt a global product strategy, some banks adopt strategies which seek to concentrate their activities either on particular products, customer segments or market segments, on a global basis.

PRODUCT FOCUS

A bank that has skills to specialise in products may ignore promoting a full range of bank services. Instead it will develop differentiated services for competitive offerings on a worldwide basis. Again, such banks must possess some advantage in management information services that enable them to track down information on product profitability across a broad spectrum of customers in a fairly diversified geographical coverage.

CUSTOMER FOCUS

Where the focus is on customer, banks in such specialism seek to widen their international return through selecting and concentrating on customer segments. As opposed to product strategy, this category consists in either putting together a suitable package of products for special customers or highlighting common products and offering them with greater efficiency.

GEOGRAPHY FOCUS

An alternative strategy in this group for maximising international returns of a bank's divisions is to focus on certain geographic segments. Where some form of affinity exists between geographical parts of the world, as is the case with Britain and its former colonies, that can be a natural basis for international diversification of divisional activities. This approach is found among British banks on the basis of anecdotal evidence.

EXPANSIONIST STRATEGIES

This class of strategies characterises the model of globalisation adopted by Japanese banks. As relative 'late-comers' in the international banking business, the strategy of Japanese banks is not to sell any particular product or target particular customer or market segments, but to catch up with leading Western banks. "Late-comers who are determined to catch up cannot afford to be choosy at a time of intense international competition" (Ibid). These banks have been found aggressive and have loss-leading policies, albeit with credit control and long-term profitability. The pattern and dynamics of Japanese MNBs are similar to their MNEs, described in Chapter 4.

STRATEGIES MOTIVATED BY FINANCIAL POLICIES

This group of strategies is adopted by banks in response to either financial motivations or short-run tactical pursuits. The response to financial motivations is associated with the activities of some American banks that found the domestic environment to be intensely competitive, resulting in an erosion of profit margins. "The new strategy consisted of altering the balance sheet nature of he business, seeking overseas opportunities and ambitious profit objectives" (Ibid). The strategy employed the tools of standard costing for individual expense items.

On the other hand, the tactical responses are found to be a feature of some major German and French banks. This approach is dissimilar to the earlier strategies in the sense that it is no strategy per se. Rather, it is a short term retreat by these banks into their traditional markets. As observed by the authors, it may well be that these banks are not under any competitive pressures, or that they are yet to evolve a strategic response.

7.5 INTERNATIONAL BANKING THEORIES & EMPIRICAL EVIDENCE

To build a theory of international banking, the same parameter of considerations surrounding FDI and MNEs may be applicable. In the attempt, a number of theories have been extended to explain international banking phenomena. These include: trade theory, comparative political advantage hypothesis, colonial vintage hypothesis, market imperfections paradigm, product life cycle hypothesis, industrial organization theory, transaction cost theory, and the eclectic theory, combining location and internalization theories. An overview of these theories follows, seriatim.

TRADE THEORY

Aliber (1976) suggests trade theory as one of two possible explanatory approaches to the theory of international banking. The other approach is the industrial organization theory, which is discussed later on. Trade theory argues that banking will be most efficient (and therefore more substantial) in those countries that have comparative advantage in producing bank products, in particular the core products (services) of money transmission and payment, deposit facilities and bank loans. The theory also appraises comparative banking costs and trade barriers in different countries (Lees, 1974, p.99). Large differences in loan-deposit spreads can induce multinational banking (Aliber, 1976). The trade theory does not however provide an insight into the sources of these advantages or why a bank would want to internalize them by itself.

COMPARATIVE POLITICAL ADVANTAGE

Niehans (1983) contends that the international trade theory is not very helpful in explaining international banking. The principal determinant of the international location of financial services, he argues, seems to be government action, namely legislative, administrative or judiciary. Banks are in the business of financial services and since these are strongly dependent on comparative advantages in the pure trade sense, they tend to be influenced rather by the regulatory environment. Differences in legislation, banking regulation, etc can determine certain activities in a given country. Niehans sees these factors as 'comparative political advantage', and these can be likened to the notion of 'locational structures' discussed in chapter 5 (section 5.2).

COLONIAL VINTAGE HYPOTHESIS

The early establishment of many foreign retail networks depicted colonial vintage proclivity, especially British and European banks. Colonial ties provided a head start in the drive for global retail and wholesale banking market. These may well explain the dominance of Barclays bank and Standard Chartered bank in the Commonwealth region or French banks in Franco-phone countries of Africa.

MARKET IMPERFECTION PARADIGM

Various sources of imperfections in international financial markets (explored in part 1) are often cited as giving rise to multinationality in banking. Externalities in the markets, which are rooted in market failures, market structure imperfections, market disequilibria and government-imposed distortions, create opportunities for a bank to go abroad either to avoid or exploit them externalities. Merger and acquisition of banks and consortia are examples of market imperfections causing international banking. Similarly, use of correspondents, agencies and representative offices can be viewed as a response to varying degrees of market imperfections, including host country restriction on branch networks. Brimmer and Dahl (1975) and Kelly (1977) show that government regulations on capital flows were primarily responsible for US banks' expansion into European markets during the 1960s and 1970s.

PRODUCT LIFE CYCLE HYPOTHESIS

Goldberg and Saunders (1981) extended the principles of Vernon's product life cycle model (explored in part 1) to foreign bank branch decisions of US commercial banks.

Thus, American banks went from domestic service and trade financing to the 'exporting' of loan commitments in tandem with the movement of MNEs from exporting to international investment. His emphasis on the importance of non-competitive advantages of US banks in servicing US multinationals in foreign countries is similar to the argument of the industrial organization theory discussed next.

Niehans (1983) uses the product life hypothesis to propose a three stage development of international banking. The first stage is where a bank accepts deposits from foreign sources and/or makes loans to foreign borrowers in its domestic currency. This is the foreign customer stage. The second stage, called foreign currency stage, is where the bank accepts deposits and/or makes loans in the foreign currency. In the third or foreign branch stage, the bank maintains its own foreign branches, which epitomizes multinational banking. The shortcoming in Niehans' proposition is that it paints a simplistic picture of the complex process of foreign establishment.

INDUSTRIAL ORGANIZATION THEORY

The emphasis of this school of thought is on the ability of a foreign bank to compete with its indigenous (and other foreign) counterparts in their domestic market, on account its net ownership-specific advantages. These advantages are fully acknowledged under Dunning's eclectic paradigm. According to this theory, banks that originate from countries with well developed capital markets and with tight controls over entry of foreign banks will have a strong tendency to develop ownership-specific advantages.

TRANSACTION COST THEORY

The transaction cost approach to the study of economic organization regards the transaction as the basic unit of analysis and holds that an understanding of transaction cost economizing is central to the study of organizations (Williamson, 1981a). Unlike most extant theories, this theory has not been extended to the international banking phenomena. Economizing is accomplished by (1) making transaction - rather than commodities - the central focus of analysis, and (2) assessing governance structures, of which banks and markets are the leading alternatives, in terms of their capacities to economize on transaction costs. This in turn highlights the strategic choices facing the bank: Will it transact internally through foreign branch or externally through correspondents, agencies, affiliates or joint ventures?

The nature of transaction costs and the associated arguments have already been discussed in part 1. Essentially, the theory suggests that the interaction of human factors of opportunism and bounded rationality with environmental factors of uncertainty, small numbers exchange relation and informational impactedness generates costs. The externality generated by this interaction can only be mitigated via the administrative machinery of the bank's internal organization because external markets are ill-equipped to deal with it. However, as has been argued in chapter 5, under appropriate conditions, markets can be a more efficient mechanism for accomplishing international transactions than the firm. Securitisation is a typical example in which transactions are removed from the bank into the market, involving direct borrowing from lenders via the securities markets. Concern over sovereign debt, carrying heavy bad debt provisions, high policying and enforcement costs of the existing debt contracts, and the high costs of searching for good credit risks are all aspects of the inadequacy and limits of internal organization which prospectively lead to use of markets.

ECLECTIC THEORY

Dunning's eclectic model is an integration of the above theories. It is based upon three conditions: (1) ownership-specific, (2) location-specific, and (3) internalisation-incentive advantages (OLI Theory). These advantages must be simultaneously present to consummate a FDI activity. otherwise, "if the enterprise possesses only (1) and (3) advantages, it will export ..." (Boddewyn et al, 1986). Exhibit 7.2 presents various sources of these advantages in the banking industry.

OWNERSHIP-SPECIFIC ADVANTAGES

The basic question which this model seeks to answer is: What advantages does a bank have which allow it to compete against local and/or other foreign banks? Ownership-specific advantages (OSAs) are embedded in industrial organization theory. This theory states that a firm (in this case a bank) must possess net ownership advantages vis-a-vis other banks in serving particular foreign markets. Net ownership advantages of a bank include ownership and control of resources (size of the bank), wide banking network, scale economies, ability to tap reliable and quality sources of funds, control of and/or strong relationship with large corporate clients whose subsidiaries dominate particular foreign markets, and strong informal relationships between key executives of the bank and foreign government functionaries.

The last two examples have been employed in Nigeria and other LDCs. For instance, the active presence of Standard Chartered Bank and Barclays Bank in West African sub-region followed the industrial domination of large British banks like Shell, B.P., ICI, Unilever, etc. Strong personal and religious affinity between some Northern Nigerian Emirs and their Arab counterparts have been known to stimulate commercial ties, resulting in the establishment of certain Arab banks in Nigeria.

Ownership-specific advantages in the control of resources have also been known to play an important role in the internationalization process of banks. For instance, Morgan Guarantee Bank of New York was reported to have entered into Nigeria through a loan syndication between some Western banks and Nigerian Government in which it acted as leader. Some Japanese banks sprang partly due to the active involvement of the Japanese refinery construction companies in Nigeria. The same goes for West German banks' entry into Nigerian market following the involvement of West German breweries. Certain World Bank project loans to LDCs require that a major international bank be appointed as the financial representative for loan disbursements and repayments.

Exhibit 7.2 Multinational Banking in the Context of the Eclectic Paradigm

Ownership Advantages

Skilled personnel, access to other managerial resources; access to favourable financial sources; access to, or possession of widespread and efficient networks; scope and efficiency of services offered; product differentiation ability; size; international reputation and image; Specialist knowledge and experience in international operations; specialist knowledge in servicing the banking needs of particular customer groups; ability to package tailor-made services; size stature and composition of clientele; scale economies (in wholesale and retail banking, foreign exchange and exposure management, and in international clearing services), ability to lure customers through cost-effective, efficient, and good marketing services.

Location Advantages

3 source areas are distinguishable.

1. General level of national economic system:- size of national economy; degree/level of economic development; stature of national capital markets; level of banking developments; degree of concentration of both home and foreign banks; degree of FDI activities.

2. Political and general socio-cultural systems:- Similarities in language, social, political, educational, and business system.

3. National regulatory systems:- Banking Regulations; fiscal regimes; foreign exchange regulations;credit allocation policies; degree of openness to international markets and level of concentration of foreign banks; interest rate policies; degree of asymmetry or symmetry of capital markets with other national markets.

Internalization Advantages

Availability and efficiency of intra-bank funds transfers; efficient customer contacts; efficient international networks of market information and commercial intelligence; potential for reduced earnings variability; transfer pricing mechanism; flexible asset/liability management's exploitation of knowledge and business contacts; exploitation of economies of common governance; protection of global market share; maintaining supply of skilled labour and other managerial resources.

Finally, a bank may develop ownership advantages in an attempt to either out- perform competitors and/or overcome the impact of deregulation. This may perhaps explain the motivation for the development of advanced electronic systems to move funds and information, the development of home banking system, or the development of PRONTO services in 1980 by Chemical Bank of New York to explore technologically advanced alternatives to the traditional delivery of retail banking service.

INTERNALIZATION-INCENTIVE ADVANTAGES

The internalization theory, explored in chapter 3, can be extended to the banking sector to explain why a bank should choose to exploit its advantages itself rather than selling them to local and/or correspondent banks. Rugman (1981, p.89) asserts that: in the same way that the MNE creates an internal market to overcome imperfect good and factor markets, so does the MNB use internalization to overcome imperfections in international financial markets.

The central theme of this theory is that the transactional model of the bank arises to evade transaction costs and market imperfections in international financial markets, especially failures of arm's-length markets for bank knowledge in overseas markets. The theory also highlights the symbiotic relationship between banks and capital markets in which both forms of organizations act as possible substitutes for each other.

Following the organizations failure framework, MNBs find it transactionally cost effective to create implicit market for their products/services in overseas markets. Because of the unique characteristics of the banking industry (e.g. absence of patent products, ease of imitation of banking services/products etc., the MNB creates and uses its internal market to produce and market its products/services. Imperfections in the national markets and government-imposed distortions (regulations) all create incentives to resort to internal organization.

LOCATION-SPECIFIC ADVANTAGES (LSAs)

The opportunities offered by virtue of establishing in a particular country constitute the location advantages of the firm. The underlying theory explains that existence of country-specific advantages may be combined with bank-specific advantages to rationalise a bank's decision to locate abroad. If this were not so then alternative forms of servicing foreign markets may be costless. The absence of control in a correspondent bank relation on the one hand, and the need to optimise global profitability from a bank's ownership advantages on the other, underpin the complexity of the opportunities offered by location characteristics.

The role of location-specific advantages in the U.S. banking involvement abroad was the subject of the empirical study by ho (1983, 1986) and Nigh, Cho, and Krishman (1986). As implied in their studies and others, location-related characteristics can be firm-specific, polycentric or a natural result of bilateral/multilateral relations. For instance, interest rate differentials and market competitiveness are seen as being firm-specific. Polycentric factors are those that affect all banks by reason of locating in a particular country. These include political risk, level of development of capital markets, foreign exchange/money transmission controls, trade restriction barriers, etc.

Additionally, foreign branch network may be encouraged by home cum host country relations. Thus, banks may take advantage of relations (economic and/or political) between their home country and another country or other countries. The above studies confirm this hypothesis. The unique nature of banks and their impact on national economy makes them highly susceptible to governmental interference. Because government intervention policies can be politically and/or economically motivated, and because banks have national (home-country) identities, location-related factors occupy a strategic position in the foreign investment decision of MNBs generally. Headquarters management are therefore sensitive to the opportunities offered by location characteristics in both the domestic and foreign markets.

Trade theorists however argue that 'banking will be most efficient and more substantial in those countries that have a comparative advantage in producing bank products, specifically, the core products (services) of money transmission and payment, deposit facilities for savers and bank loans for borrowers'. Against this background, Cho individually and collaboratively with Nigh and Krishman hypothesised that such FDI activity (i.e. foreign branch banking) was positively related to the local banking market opportunities, *ceteris paribus*. Their studies however provide partial evidence on the hypothesized relationship. Cho's study contains disaggregated evidence on the role of LSAs. On the one hand, the net effects of LSAs are found to be negative for the growth of MNBs, despite various incentives offered in the host countries' markets. On the other hand, the study documents the differential effects of location advantages across banking activities and markets. Also it is found that LSAs are largely responsible for the types of MNB activities, although ownership-specific and internalization advantages are more relevant for the level of involvement of such activities. While the evidence of these studies is inconclusive, one would imagine that the appeal of London or other money centers for FDI banking could be associated with factors inherent in the 'local banking market opportunity hypothesis'. It is perhaps the intuitive appeal of the LSAs more than inchoate corollary empirical findings that underpins its relevance as a determinant of international banking.

7.6 SUMMARY AND CONCLUSIONS

The study is about alternative strategies of international investment. International banking is within its scope and is shown historically to be a logical extension of international business. International banking is not amenable to any precise definition. However, foreign branch banking is shown to be the FDI counterpart of foreign subsidiary of MNBs. Banks employ a wide range of organizational forms in servicing foreign markets. Within the purview of 'new forms of international banking,' three categories of organizational modes are distinguished: cooperative arrangements, joint venture or consortium banking, and merchant banking and associated services.

The dynamics of international banking are explored through a survey of global strategy of MNBs in two phases: the pragmatic phase, which examines the global practices of banks; and the theoretical reviews of FDI theories applicable to the banking industry.

PART THREE

RESEARCH DESIGN AND ANALYSIS OF RESEARCH FINDINGS

CONTENTS

PART 3

RESEARCH DESIGN AND ANALYSIS OF RESEARCH FINDINGS

This study is divided into three parts. The first two parts were concerned with Literature review on two levels. The first level, which was the subject of Part One, reviewed the literature on foreign investment theories. This provided the basis for assessing the applicability of extant theories in explaining wider dimensions of international investment than had been contemplated by the theories in their original formulation. A taxonomy of the new forms of international investment established the parameters for examining the second level, in Part two, the structure and dimensions of alternative strategies to foreign investment. The application of markets and hierarchies paradigm was made more microanalytic than previous international business studies of these matters.

This part of the study (Part 3) is the concluding part and is concerned with empirical investigation into the phenomena of new forms of international investment. The part is divided into three chapters. The first chapter, which is chapter eight of the study, establishes the purpose of this research, formulate the hypotheses and discusses the research design. The second chapter is chapter nine of the study and is concerned with research methodology, the methodology used in the statistical analysis, and the first phase of the analysis of research findings. The second phase of the analysis of research findings is the focus of chapter ten. It deals with the statistical analyses in relation to the stated hypotheses. Chapter eleven concludes the study with a summary and policy implications as well as suggestions for further research.

CHAPTER 8

RESEARCH DESIGN AND STUDY HYPOTHESES

CONTENTS

CHAPTER 8

RESEARCH DESIGN

8.1 INTRODUCTION

The purpose of this chapter is to generate testable hypotheses for the statistical data collected in the field work.

For ease of readership it may be helpful to state the study hypothesis in advance of the argument. These are:

H_1: The adoption of new forms by a firm in foreign market development is significantly influenced by managerial assessments of firm-specific characteristics.

H_2: The adoption of new forms in the internationalization process is positively related to the firm's global strategies/objectives, *ceteris paribus*.

H_3: The choice of new forms in the internationalization process is not significantly influenced by the size of the firm.

H_4: New forms of investment are more likely to prevail in firms with a 'dynamic foreign investment posture' than in firms with a 'static posture'.

H_5: The choice of new forms in foreign market development is significantly influenced by managerial perceptions of host country charactawistics.

H_6: Firm choice/use of new forms in the internationalization process is independent of competitors' mode of organising foreign transactions.

H_7: Firm choice of new forms in the internationalization process is independent of stage of host country development.

H_8: Firm choice of new forms is dependent upon their perceived net benefits by corporate management.

The premise for all the tests in this enquiry is that common, or at least similar, factors are at work in driving the several routes of international entry. While hypothesis-testing remains a very crucial undertaking in behavioral science researches, evidently research can have a variety of purposes, and the research design which is most appropriate for any given project will depend on its purpose. (For a detailed discussion of the purposes of social science projects and their implications for research design, see Selltiz, Wrightsman and Cook, 1976, pp 89-112). The divergences of opinions, approaches, and values between corporate foreign investment practice and international business research can lead to four types of research projects; exploratory, descriptive, normative, and explanatory.

The common features of exploratory researches are (Manheim and Rich, 1986, p.68): (1) their utility when the phenomena of under investigation are new or have not been studied before, and (2) the familiarity which they provide about such phenomena, thus enabling more precise research questions to be developed and hypotheses formulated. Group 2 type researches - descriptive - characterize investigations which are designed to provide an unbiased representation of the phenomena of interest so that research questions and hypotheses may be better developed. Such studies are labelled descriptive or positive because they attempt to justify what already is. In contrast to this type of research, a normative research is essentially theoretical: the aim is to present or justify what ought to be, rather than what is. Finally, explanatory researches are geared towards casual investigations, the objective being to explain why a phenomenon exists or why an event occurs. An explanatory research design provides a basis for causal inferences when it allows the researcher to rule out any plausible explanations for observed results that represent alternatives to the causal hypothesis being tested (ibid).

The significance of the above typology is that each type requires different sets of research design. For example, exploratory research emphasizes flexibility more than precision, while descriptive and explanatory researches emphasize accurate measurement of phenomena, and require unbiased and reliable observations (ibid). This study, while embodying some of the elements of descriptive and explanatory research, conforms more with the requirements of an exploratory investigation.

Regardless of the purpose of a study, a research design should include the following basic elements (ibid.):
(1) a statement of the purpose of the research; (2) a statement of the hypothesis to be tested (if any); (3) a specification of the variables to be employed; (4) a statement of how the variables are to be operationalized and measured; (5) description of data collection

and analysis; and (6) a discussion of analysis of the data collected. This chapter is devoted to items 1 to 4, while items 4 and 5 are the subject of chapter 9.

8.2 A STATEMENT OF THE PURPOSE OF THE RESEARCH

The study of alternative strategies to international investment may be viewed *instricto senso*, as a study of non-FDI modes of entry into foreign markets. The choice of mode of foreign market entry and development strategy is vital to the success of foreign operations, hence Wind and Perlmutter (1977) identify it as a "frontier issue" in international business. Analytical enquiries in this area can take any number of approaches (as shown in parts 1 and 2) for the same reason that entry modes differ in their mix of advantages and limitations. Much of the empirical literature has been based on the theoretical framework of the eclectic model and internalization theorem. The inadequacy of these theories, as originally formulated is evident in their later versions which have sought to accommodate divergent modes of foreign investment (see, for example, Rugman, 1982 and Buckley and Casson, 1989, and Dunning 1988, for internalization and eclectic streams of research, respectively). General explanation of non-equity forms of foreign investment and specific applications to the international hotel industry and the business-service sector, etc., are both theoretical and empirical ways of recognizing the diversity of strategic forms of foreign involvement and the need for a redefinition of central concepts of received microtheory.

Recently, the transaction cost theory has emerged as a strong explanatory candidate in the foreign investment phenomena. Like the internalization concept, the transaction cost approach has its antecedent in the industrial organization literature, but, unlike the former, it regards the transaction as the basic unit of analysis and transaction cost economizing as central to the study of economic organizations. Both in its original formulation in the economics literature (Williamson, 1975) and extension into the international business literature (Casson, 1982), structural differences of the firm are assumed to arise primarily to: (1) promote economy in transaction cost by assigning transactions to governance structures in a discriminating way, (2) determine the efficient boundaries between firms and markets, and (3) match internal governance structures with attributes of transactions.

As applied to foreign market entry and development strategy, transaction cost considerations explain why a firm should engage in direct investment rather than using contractual or cooperative modes. Clearly, corporate choices are most usefully and tractably treated as one of common governance costs (i.e. costs of establishing a wholly owned foreign subsidiary) versus disintermediation costs (i.e. costs of transacting across markets). Another view is one of a tradeoff between control and cost of resource commitment (Anderson and Gatignon, 1986).

Implicit in the assumptions underlying current theoretical developments and accompanying public concern is a view of foreign investment practices in which the traditional FDI via wholly owned subsidiary is no longer made the centrepiece of analysis. Spearheaded by the OECD in the 1980s, although it has been recognized much earlier (Hyson and Weigel, 1970), the literature developed as "new forms of investment" with specific orientation to developing countries. Its popularity as a line of research investigation is commonly credited to Dr. Charles Oman (the Director of the Development Centre of OECD) whose 1984 and subsequent publications have brought realism to the significance of changing international investment strategies, albeit in the North-South context.

8.2.1 THE NEED FOR THE RESEARCH

This study is concerned with recent developments in international investments and the theory of MNE. Extant foreign investment theories have concentrated on FDI and have been very successful in projecting wholly owned foreign subsidiary as the most efficient governance structure. Despite the elegance and comprehensiveness of FDI reasoning, it is still deficient in some respects as a general institutional framework for deciding the integrity of foreign investment (see for example, Beamish, 1985; Beamish and Banks, 1987).

The need for a detailed and critical study of this kind was highlighted by Professor Dunning and others in the late 1970s. Addressing a meeting of European International Business Association in Sweden in 1977, Professor Dunning stressed the need for a detailed and critical study of alternative modalities of international resource transference. Subsequently, the OECD and other multilateral organizations have advocated for a rethinking on the package of FDI (see for example, Germidis, 1981; Oman, 1984 and Contractor, 1985). Also, Mr Faaland, President of OECD Development Centre underscored the "... importance and timeliness of undertaking a study of the new forms of international investment" (1984). In short, there is virtual unanimity in the international business and investment community that, in recent years, the boundaries between equity and non-equity/cooperative forms of international investment have become blurred (see Dunning, 1981; Oman, 1984a, b, 1986; Hood and Young, 1986.). The proposition by a number of economists that traditional FDI was becoming obsolete and was being superseded by new forms of investment (Oman, 1984, p.26) is the context upon which this research is based.

Although the trend towards new forms may appear to be prevalent in developing countries, it is frequently being adopted in developed economies as well. (see for example, Janger, 1980, Harrigan, 1985). Contractor and Lorange (1987) show that various modes of NFIs (such as licenses or joint ventures) in U.S.-based companies outnumber wholly-owned subsidiaries by a ratio of 4 to 1.

Setting aside the fact that most existing studies are U.S. based and/or have relied on U.S. MNEs as data base, what is somehow surprising is the paucity of synthesis and empirical investigation of the "rather disparate literature on a topic which is currently identified as an important area in the international trade and development - the growth of 'new forms of international industrial co-operation' (Buckley, 1985). In the manufacturing industry, and to a partial extent in the banking/services sector, economic rationale for multinationality is perceived and pursued through wholly owned subsidiary (or foreign branch network in the case of banks). The central questions with which foreign investment studies are concerned revolve around two issues: (1) Why firms headquartered in one country establish strategic operational presence abroad; and (2) whether the establishment pattern is random or systematic with respect to factors that owe their origin to the firm, to environmental influences, or to the interaction of both.

The first set of questions emphasizes governance structures in which the attributes of the firm's ownership-specific as well as internalization advantages are significant and expressed in ways in which their transaction-cost economizing properties are made dynamic, rather than regarded as a datum. The second set of questions is rooted in external stimuli or operating environment structures. These include the institutional arrangements that characterize the politics and set conext within which economic activities take place in a country. They include not just 'dormant' location-specific advantages-about which conventional location orthodoxy is emphatic-but more importantly unnatural (i.e. contrived) set of environmental factors that potentially affect the configuration of inter-country relations and ultimately decide whether firms of one country should be allowed to establish in another country regardless of their competitive advantages.

The premise of this study therefore is that the extent of international economic activities cannot be confined to or measured in terms of FDI alone, as represented by wholly owned foreign subsidiary (or branch banking network). Conceptually and practically, there are a number of strategies which firms can use in servicing foreign markets. Through these mechanisms, firms can potentially overcome or avoid many of the disabilities that have been conventionally associated with the market modes.

Despite these concerns, published literature indicates that research response has been rather scant and disaggregated in the main. NFI researches have been mainly carried out as single component studies, although some of these are dichotomous - that is, equity verses non-equity. As far as published empirical literature is concerned, there has been no empirical investigation of new forms of international investment. Published works are generally descriptive or conceptual propositions. This study is an attempt to bridge the perceived gap.

8.2.2 PURPOSE OF THE RESEARCH

The purpose of the study is fivefold: (1) To determine the identity, and assess the transactional economizing properties, of alternative (i.e. non FDI) modes of internationalization; (2) To integrate the economic theory of entrepreneurship with the eclectic paradigm under a transaction cost approach. In other words, to determine the role of entrepreneurship (corporate management) in the internationalization process, using firm-specific and country-specific advantages; (3) To attempt to extend the phenomenon of new forms of investment to international banking; (4) To examine the relationship between the stage of country development and the use of new forms of investment; and (5) To evaluate the policy implications of the findings for (i) the MNE, (ii) the host government; and (iii) multilateral governments.

Specifically, the study: (1) investigates the extent and significance of, and the motivations behind corporate choice of new forms of investment in both financial and non-financial enterprises; (2) examines the factors that determine the choice of form and their relative importance, from the perspectives of both governance and locational structures; (3) assesses the impact of managerial perceptions of the significance of ownership-specific advantages, internalization-incentive advantages and host country-specific characteristics on foreign market entry mode choices; and (4) offers empirical evidence of the costs and benefits of new forms.

One hypothesis of interest concerns the extent to which new forms offer small and medium - size firms (SMFs) a creeping opportunity to internationalize their activities. Multinationality is conventionally associated with large MNEs deemed to possess sufficient firm-specific advantages (FSAs) to countervail externalities in international markets. Conversely, the structure of SMFs is portrayed as being insufficiently equipped to deal with or overcome international market imperfections. Therefore, an understanding of the ability of SMFs to assign foreign transactions in a discriminating way has remained somewhat elusive for the above reason. An empirical verification of new forms as a vehicle by which SMFs are able to express their specific advantages but also sustain foreign transactions is a potential useful corrective.

Related to this is the question concerning the significance of determinants of governance and location structures - namely FSAs, internalisation-incentive advantages and location-specific advantages - as rationales for adopting NFIs. According to Rugman, et al., (1986, p103), there is little difference in FSAs between firms under oligopolistic competition, leading firms to differentiate their products from those of their rivals, but also guard against dissipation via hierarchy. This argument presents new forms as a residual concept of governance, implying that firms will resort to their usage only when the dissipation cost of FSAs is commensurate with royalties from contractual dependence (Cf. Coase, 1937).

Another important question concerns the attitudes of corporate management towards the impact of entry mode choices on firm value. Such attitudes reflect differences or agreements in their perceptions of the significance of firm-specific (ie. ownership and internalization) and host country-specific factors on the mode of entry into particular foreign markets. The relevance of economic theory of entrepreneurship to entry mode choices has received little attention in international business literature. In short, analysis of entrepreneurship has been very much neglected by economists (Casson, 1985; p.172) and by international business researchers, broadly defined. Yet, whether transactions will be assigned between firms and markets at all, let alone doing so in discriminating ways, is, with little doubt, the central task of corporate management (see for example, Teece, 1984; Casson, 1985 p172; Buckley, 1989, p154). These theories suggest that firms will be sensitive to market and political pressures to the extent that future cash flows, share prices, and ultimately, firm value may likely be affected. In particular, what are the perceptions of firms about the costs and benefits of alternative entry mode choices and what are the policy implications?

Entry mode choices are yet to be assessed in this problem context. Previous studies have concentrated on Dunning's eclectic theory and Buckley and Casson's internalization theorem (popularised by Rugman as a general theory of international investment). This study aims to introduce into the entry mode literature aspects of the economic theory of entrepreneurship in the hope that it will add to the international business research agenda as well as respond to Dunning's (1989) call for a more interdisciplinary approach (see also Buckley, 1990).

This study covers both financial enterprises (banks) and non-financial enterprises (as generally defined); therefore, references to firms contemplate both types of enterprises.

8.3 SPECIFICATION AND DEFINITION OF HYPOTHESIS

The aim of the empirical research is to obtain answers to questions about reality. Questions may be practical (as with case studies, participant observation studies or evaluation of events and behaviour), or they may be principally of academic interest (as with normative research or conceptual development studies). In either case, they will probably be stated in abstract terms, even though the answers sought are usually concrete and specific. One of the first problems in research is to devise ways of getting from the abstract level of questions to some concrete observations which will hopefully provide answers to the questions. That is what a hypothesis is about. Essentially a hypothesis is a statement of what may be believed to be factual.

This section of study is concerned with the specification and explanation of hypotheses. It specifies the facts (variables, logical constructs) and the relations among them that offer a logical description or explanation of the conditions or events that give rise to the problem. Some variables or relations in hypotheses are known and others are 'devised' or 'invented' to complete and systemize the explanation. Thus, by logically relating known facts to "intelligent guesses" about unknown variables or relations, hypotheses are able to extend and enlarge our knowledge. In short, hypotheses have been described as "your (our) eyes as you (we) try to approach problems in a scientific manner. Through them you (we) look into the disorder that is a problem and see the possibilities of order" (Hodnett, 1955, bracket replacements are mine).

Studies of new forms can be undertaken in either of two ways. One avenue is the single component study approach by which the constituents of new forms (e.g. licensing, franchising, joint ventures, etc.) are studied individually or separately. Studies of this kind include works of Bilkey and Tesar (1977), Wiedersheim-Paul, Olson and Welch (1978), Reid (1981), Cavusgil (1984), and Schlegelmilch (1986) for Exporting; Telesio (1979), Buckley and Davies (1981), Carstairs and Welch (1982), Contractor (1981, 1984, 1985), Davidson and McFetridge (1985), Horstman and Markusen (1986), OECD (1987), and Monye (1989) for Licensing; Walker and Etzel (1973), Hackett (1976), Caves and Murphy (1976), Brickley and Dark (1987), Norton (1988), and Welch (1989) for Franchising; Killing (1982, 1983), Beamish (1984, 1985), Beamish and Banks (1987), Harrigan (1984, 1985), Connolly (1984), Artisien and Buckley (1985), and Franko (1974, 1989) for Joint Ventures; UNCTC (1983) and Brooke (1985a, b) for International Management Contracts; Wright and Kobel (1981), Lecraw and Gordon (1984) and Dicken (1986) for Turnkey Contracts; and the editorial work of Germidis (1980) for International Subcontracting.

The alternative approach to the study of new forms of investment is the composite approach. In this respect, two or more strategy variants are investigated in one study. Examples of this approach include the works of Dunning and Cantwell (1982), Oman (1980, 1984a, b, 1986) Buckley (1983, 1985 ch.3 in Buckley and Casson, 1985), Contractor and Lorange (1987), Dunning (1988, ch.6), and Young et al. (1989). The approach adopted in this study identifies with the latter.

8.3.1. A TRANSACTION COST ANALYSIS OF NEW FORMS OF INVESTMENT

The study evaluates the relationship between NFI (mode of entry or form of foreign involvement), on the one hand, and the factors that influence their choice, on the other hand. By definition new forms of international investment are heterogeneous. For analytical purposes, they can be most usefully and tractably viewed as 'new forms' or 'markets' under a 'markets and firms' dichotomy. It should be made clear at the outset that this dichotomy is for analytical purposes since, strictly speaking, included in the taxonomy of new forms are international investment strategies in which there is equity interest, albeit such foreign-held equity does not constitute majority ownership and control. This approach is consistent with a composite analysis of the kind represented by the studies cited above. Thus, rather than isolating each mode for analysis - an approach for which single component studies are designed - the attempt here is to examine the factors which induce or propel firms to establish operations in foreign countries via the mechanisms of new forms. This avenue of research offers a complementary strength to single component studies such as the ones cited above for, after all, the single modes of entry they investigated comply with the definition of new forms of investment.

To encompass new developments in the field of determinants of foreign investment and to express these operationally under a transaction cost approach, a somewhat different taxonomy from that of Dunning or Rugman is proposed to distinguish among two classes of hypotheses (1) Governance structures, and (2) Country-Specific characteristics. The implications of these two classes of hypotheses have been discussed in chapter 5. Eclecticism is not lost under this classification, instead it is emphasized. As explained in chapter 5, governance structure refers to organisational framework within which the integrity of a transaction is decided. Markets and hierarchies are two of the main alternatives. Much of the concern of extant studies has been with issues of the latter kind, only empirical issues of the former kind are addressed in this study.

Governance structure hypotheses encompass both conceptual and transactional attributes of traditional ownership-specific and internalization advantages under an expanded eclectic framework (see Dunning, 1988). Implicit in governance structure hypotheses are propositions that create an awareness of or establish the crucial role of corporate management in entry mode choices. The importance of managerial attributes to corporate investment has been recognised in a number of studies in accounting and finance. However, a significant aspect of corporate investment decisions in which managerial attitudes have been grossly ignored concerns foreign market entry mode choices. The incorporation of these under governance structures may be a useful corrective.

Hypotheses about country-specific characteristics both recognize and stress the importance of host country's economic-related and noneconomic factors in foreign investment decisions . Whereas natural economic features of a country conform to the traditional role of location-related factors in explaining inward foreign investment, noneconomic factors emphasize the effect of unnatural host country circumstances (such as political environment, intra-nation events of the host country, or inter-nation conflict and cooperation, etc.) on foreign investment decisions.

A transaction cost analysis of new forms of international investment under governance structures and locational influences is predicated upon the general hypothesis, known as "the obsolescence of FDI hypothesis" (Oman, 1984, p.26). Operationalizing this turns critically on the question posed by Anderson and Gatignon, (1986) namely: "What is the best entry mode for a given setting?" Surely, if FDI has been found inefficient in certain operational respects, as implied by the obsolescence hypothesis, it is because of the early unremitting emphasis on FDI as the only governance structure. It then raises the question about 'sanctity' of a firm's monopolistic advantages in transaction cost terms. It also raises the issue of tradeoffs between ownership-specific and internalization factors on which FDI propositions are predicated and compelling forces of the environment of operations. Such tradeoffs are difficult to evaluate and little understood because entry modes differ greatly in their mix of purposes, advantages and drawbacks (ibid).

Surveys on how firms make entry mode decisions indicate that few companies make a conscious, systematic analysis of the costs and benefits of the options (see Robinson, 1978). Despite the spate of literature on international business, the literature has been silent on how managers should weigh tradeoffs in order to make an optimum choice of entry mode that minimizes risks or maximizes returns on foreign investment (for a similar argument, see, Anderson and Gatignon, 1986). This apparent silence may be partly due to the systematic attempt by institutional economists in presenting the efficiency features of the firm as a datum. While recognizing that the criterion for organizing transactions is cost minimization, neoclassical reference to the firm has been one of production functions. Teece (1984) makes the point very strongly thus: "With little exaggeration, we can assert that, until very recently, economics lacked a theory of the firm. To be sure, textbooks contain chapter headings labelled 'the theory of the firm', but on closer examination one finds a theory of production masquerading as a theory of the firm. Firms are typically represented as production functions, or, in some formulations, production sets."

The second reason why the literature is silent on how managers should weigh tradeoffs about optimum entry made choices is rooted in the background and orientation of the antecedent literatures of international business, of which micro-economic theory of firms and industrial organization literature are pre-eminent. The problem is that both literatures were not developed with the education or orientation of business managers in mind (ibid). Rather, both disciplines in general, and their formal economic theories in particular, are shaped by a concern with normative questions in public policy that are both removed from actualities of the world and different from the strategic manager's view of international business. In addition, Teece contends that economics as an empirical science has long been determinedly oblivious to the problems of predicting behaviour of the individual decision unit, instead has focused attention and developed specialized tools for the statistical analysis of patterns of behaviour of parameters (whole populations) of economic actors.

Finally, and perhaps most importantly, because equilibrium analysis plays such a vital role within received microtheory, and because strategic change is so often modeled as an equilibrium movement (i.e. from one condition to another), the role and analysis of entrepreneurship tends to be neglected by economists (Baumol, 1968; Teece, 1984; Casson, 1985). Yet, by definition, it is the entrepreneur who owns and/or controls productive activities; it is his task to carry out the direction of resources with efficiency (i.e. low cost or high returns). He is aided in this process by endogenous as well as exogenous factors. Internalization of transactions is governed by internal considerations, largely at the discretion of management (Casson, 1985, p.155). The dominant mode of theorizing in international business and investment tends to distance the discipline from management problems, with the exception of accounting and finance. Without questioning the legitimacy or importance of the concerns and objectives that have shaped mainstream theories, there may be reservations about whether the discipline of international business thus shaped makes a wholly constructive contribution to strategic management.

Strategic management issues in general, and in the international environment in particular, are centrally concerned with dynamics. Economic theory, on the other hand, deals mainly with equilibrium analyses, which are very often static. Although, recent theoretical formulations have tended to incorporate dynamic features (see for example, Anderson Gatignon, 1986; Dunning, 1988), however formal modelling apparatuses of this kind are either too complex for the lay manager to assimilate or are insufficiently microanalytic to capture all the phenomena of interest. Accordingly, only very simple problems can be dealt with economically. Many of the problems confronting general management are behavioural and qualitative, and are not amenable to precise quantification. Existing foreign investment theories suffer from inattention to these issues, for, according to Teece, "managers are as concerned with the journey as they are with the destination when industries and markets are being transformed." Therefore, the need for integrating a theory of entrepreneurship (incorporating human resouces management) in international business is of considerable importance to strategic management.

Transaction cost theory thus provides a framework for the unification of concepts and practices in international investment. It provides a basis which allows different success criteria and distinctive comparative strengths and limits of internal governance structures to be integrated alongside entrepreneurship, strategic management and environmental considerations. It is a dynamic concept which can be used to assess long-term strategic decisions, such as entry mode choices. The classical approaches to such assessments emphasize choosing from the feasible set of options that which offers the highest risk-adjusted return. But, the literature on foreign investment hardly addresses the issue directly. Instead, the issue is configured in terms of control each mode affords the firm (Anderson and Gatignon, 1986). For example, it is claimed that the issue of control is central to the growth of the MNE (Buckley and Casson, 1976; Rugman, 1981; Daniels and Radebaugh, 1986; Rugman, Lecraw and Booth, 1986) and of new forms of international investment (Buckley, 1985, 1989).

Dwelling on the issue of control - defined as the ability to influence systems, methods, and decisions - Anderson and Gatignon (1986) proposed four constructs that determine the optimal degree of control, from a transaction cost analysis, to wit: (1) transaction-specific assets: that is, investments (physical and human) that are specialized to one or few users or uses; (2) external uncertainty: implying the unpredictability of the firm's external operating environment; (3) internal uncertainty: indicating the firm's inability to determine its agents' performance by observing output measures; (4) free-riding potential: that is, agents' ability to receive benefits without bearing the associated costs.

Clearly, these constructs are couched in terms which permit analysis to be pursued under hierarchy. Hence the propositions which the author developed fall within the traditional notion of the firm as a superior control mechanism over alternative structures. However, instead of an analysis based on a control/cost dichotomy, the attempt here is to formulate and test hypotheses based on judgements of corporate management about the transactional limits of the firm (governance-related factors) and external environmental considerations (host country limiting factors).

STUDY HYPOTHESES

Governance-related factors include, but are not restricted to, the firm's expansion ethos or entrepreneurial drive, firm size, experience in foreign markets, possession of brand name, etc., and economies of scope and geographical diversification. A firm's expansion ethos and entrepreneurial drive can be regarded as its internalization advantages, and are made manifest in the firm's (i.e. management's) willingness to share ownership and control in return for access to local markets. Additionally, the desire to minimize country risks and obtain economies of scope and geographical diversification are pervasive aspects of internalization advantages of the firm. All of these are background influences on international entry. They may not be seen to directly relate to foreign market entry, but increase the basis and likelihood of exposure to international possibilities and pressures (Wiedersheim-Paul, Olson and Welch, 1978; Welch, 1990).

Firm size, experience of foreign markets and possession of brand name, trademarks, etc (or possession of large corporate customers, in the case of banks) are ownership-specific advantages of the firm. These have been used in several studies to predict the pattern and types of influences on the movement into international operations by MNEs. As Dunning (1988, p.48) aptly observes, strategically related characteristics of firms most likely to be associated with aggressive international behaviour global dimensions of business include: firms' long-term goals and perspectives, the nature of their core assets, their attitude to innovation and change, the range and segment of critical markets served, their attitude to risk and uncertainty, their operational flexibility, their organizational and cultural ethos, the entrepreneurial initiative of their management (chief decision-makers) and their willingness and capacity to accept contractual/cooperative cross-border alliances. A transaction cost analysis of entry mode decisions incorporating these factors suggests the development of hypotheses along the lines discussed below.

8.3.2.1 MANAGERIAL ASSESSMENT OF FIRM-SPECIFIC CHARACTERISTICS

H_1: The adoption of new forms by a firm in foreign market development is significantly influenced by managerial assessments of firm-specific characteristics.

This hypothesis implies that the mode of foreign transfer will be determined by corporate management dependent upon the nature of the resource transfer and the way they view the firm's characteristics. The literature recognizes these factors as ownership-specific advantages and internalization-incentive factors. In the context of Dunning's eclectic paradigm, both sets of factors must exist in a simultaneous complementarity with location-specific factors for multinationality to occur. Although, this configuration has served economic analysis of foreign direct investment well, the outright omission or suppression of process of entrepreneurship (Teece, 1984; Casson, 1985) makes its utility and importance to strategic management somewhat insufficient. Besides, ownership advantages are constructed in terms of firm characteristics often perceived as monopolistic.

The concept of entrepreneurship is a crucial aspect of decision making: it has long played a role in the growth and theory of economic development; and has also been at the heart of much of business strategy theories (Buckley, 1990). The notion that a firm can choose from a finite set of strategies (e.g. lost cost high-volume strategies versus high cost innovative-product strategies) implies that a firm's resources and capabilities are not ubiquitous. Specific strategies require particular investment decisions, organizational structures, and particular organizational cultures. Caves (1980) succinctly asserts that certain factors of production are "semi-permanently tied to the firm by recontracting costs and market imperfections". By far the most common theoretical approach is that which takes the firm and its ownership assets as given, ignoring the fact that the options open to a manager include attempts at some degree of innovative improvement in existing ways of doing things (i.e. accomplishing transactions).

The decision making process of international market entry can be relatively complex, as has been shown by research on exporting (see, Wiedersheim-Paul, Olson and Welch, 1978; Yaprak, 1985; Rosson and Reid, 1987) and a number of FDI studies. The role of management is central in this process. The function of management is to adjust to change; the faster the rate of change, the higher the demand on and for management (Buckley, 1989, p.27). Buckley also notes that the FDI is (or should be) a management intensive activity "because of the risks involved in the move and because of the necessity to collect and, crucially, to channel information in order to support effective decisions." Such decisions are influenced by factors which prospectively lead to a consideration of international markets in ways that differ from one country to another.

A transaction cost analysis of firm-specific characteristics requires an assessment of the factors likely to favour international possibilities via new forms. Ownership factors of firm size, experience of foreign markets and possession of brand name or trademarks may be important. The following internalization factors are also significant in the decision process: willingness to share ownership and control in return for access to local markets;

minimization of country risks; economies of scope and geographical diversification; and cost of establishing foreign wholly-owned outlets. These factors have been mentioned in the descriptive literature as likely to induce firms to adopt new forms (see, Oman, 1984). They can be perceived as catalysts for international expansion, on the one hand, and constraints, on the other. As catalysts, the larger the combination of firm size, experience of foreign markets and possession of product identity with internalization advantages, the greater the firm's bargaining power (Harrigan, 1985; Monye, 1989). Conversely, these factors can constrain entry mode options if their underlying assumptions or forces are violated. For example, in studying whether foreign divestment is the reverse of foreign direct investment under the eclectic theory, Boddewyn (1983), notes that the former requires only that one of the firm's advantages be absent, whereas the latter requires that the three conditions of ownership-specific, internalization and location-specific advantages be present simultaneously.

The transactional model of the firm, as originally formulated, suggests factors that discourage joint ownership and control. These have been explored in the first two parts of this study. However, certain features of the firm may alter this tenacity. The first of these is associated with the firm's organizational structure. The growing tolerance of new forms, for example, has been related to organizational structure of the parent MNE (Caves, 1985, p.87). Also firms having worldwide product divisions and a high degree of product diversification may welcome new forms (e.g. joint ventures). New forms of investment have been especially evident in the extractive industries where projects are visibly risky or involve a large minimum efficient scale of operation or both (Oman, 1984; Caves, 1985). For these kinds of projects, collaboration with other entities permits the foreign firm to acquire or secure interest in the project while simultaneously spreading the risk and financial burden that would be otherwise imposed.

Costly and/or risky ventures or those involving long period to maturity, such as petrochemicals, hydrocarbon and steel projects, often stretch the capacity of firms. Alternatively, the firm may lack some capacity or competence needed to make a foreign investment succeed. Lack of transactional capability to exploit perceived market opportunities is a size-related factor that can prospectively lead to strategic alliances with local entrepreneurs who could, for instance, provide operational infrastructure, local guarantees, information and general assistance in risk bearing. A firm that is diversifying in product as well as geographical markets may be faced with shortage or absence of organizational skills necessary to maximize perceived benefits. Domestic market saturation is another internalization factor which has been found to be an influence on international entry by U.S. franchisors (Hackett, 1976, p.69), U.S. exporters and licensors (Bilkey and Tesar, 1977), Australian exporters, licensors and franchisors (Welch 1983, 1985, 1989, 1990) and several other studies.

However, while material factors may be crucial, the main influence group in the internationalization process may be the decision maker/s. In all the studies of the role of managerial decision-making on international entry and expansion (Walker and Etzel, 1973; Reid, 1981; Welch, 1983, 1989; Rosson and Reid, 1987 and others), the average find was that the relative impact of the various catalysts appeared to depend heavily on how they were perceived by the key decision-maker/s in the companies. In some cases the decision-maker was the direct initiating factor in the international move, creating a strong internal drive. In others an important influence was the experience of the decision-makers, developed ex ante (Reid, 1981; Welch, 1983). Managerial influence can manifest in the type of follow-through accompanying any evoked (ie. passive) international interest, indicating the extent of managerial perception of the strengths and limits of the firm as well as the extent of managerial commitment to the international move.

In the light of the foregoing, it is hypothesized that: The adoption of new forms by a firm in foreign market development is signigicantly influenced by managerial assessment of firm-specific characteristics.

8.3.2.2 RELATIONSHIP BETWEEN FIRM GLOBAL STRATEGY AND CHOICE OF NEW FORMS

H_2: The adoption of new forms in the internationalization process is positively related to the firm's global strategies/objectives, *ceteris paribus*.

This hypothesis seeks to asses the significance of firms' global strategies and/or objectives on the outcome of entry mode choices. Closely linked to managerial assessment of the strengths and limits of internal organization (hypothesis 1) is a re-examination of the reason behind a firms's international move and global pursuits. Global strategies are those which recognize that competition is no longer confined to the domestic market, that information is limited and interdependence between firms is necessary. Firms become global for many reasons and need an approach appropriate to meet new challenges when changes occur (Porter, 1980; Porter and Rudden, 1982). Adaptation requires that a change is not only a possibility but must be recognized in both decision-making processes and operational terms. In both respects, firms must re-examine their assumptions concerning how competitive advantage can be gained by integrating the operations of diverse geographic location, using flexible, cooperative and international strategic alliances such as joint ventures (Harrigan, 1983, 1984; Beamish, 1985; Franko, 1989), exporting (Bilkey and Tesar, 1977; Cavusgil, 1984), licensing (Telesio, 1979; Contractor, 1981, 1982; Contractor and Sagafi-Nejad, 1981; Carstairs and Welch, 1982; Davidson and McFetridge, 1985), franchising (Walker and Etzel, 1973; Hackett, 1976; Welch, 1989, 1990) and subcontracting (Germidis, 1980), amongst others.

When a profit opportunity has been diagnosed, the firm generally seeks to maximize the profit it can appropriate from it. The major constraints on the firm are the actions and the reactions of rival and non-rival firms. Since this interaction exists under an ecology of continual international competition, risks and uncertainty, and information impactedness, an enforceable economic contract which imposes a cooperative solution on the system or involves a collective action (Williamson, 1975, p.73) may in these circumstances become an attractive option. Although these mechanisms are not without costs; indeed every mechanism has, but the costs and strains on managerial capacity under a contractual/cooperative framework may not be comparable with the high demand of internal coordination of a vertically related MNE. Besides, contractual/cooperative modes allow flexibility and adaptation to the flow of events without concern for internal power consequences prospective with internal expansion (ibid).

Structural attributes of new forms of investment and their efficiency consequences have been discussed in part 2 of this study. Applications of these global strategies involve assessing the principal objectives of firms vis-a-vis rival behaviour in the international marketplace. In this setting, strategically similar firms readily recognize their interdependence with one another, pursue similar goals, and react alike to disturbances; whereas, strategically dissimilar firms do not have these natural harmonies (Caves, 1982, p.109). Nevertheless, active rivalry in the market has diversified, naturally aided by imperfections and politically by forces of deregulation. The configuration of economic activities manifests in different ways in different markets: some are vertically integrated, some are not; they differ in how they compete in the market; some specialise in particular products or markets, some are conglomerately diversified; some advertise, others do not; some desire monopoly power, others prefer steady growth; some invest in R&D, others are free-riders. In all these scenarios, anecdotal evidence suggests that the structural forces determining the boundaries of behaviour in international markets may be closely linked to firms' motives or objectives.

Global motives of firms vary according to the above configuration of economic activities. In operational terms, they include: to achieve international diversification; to acquire reciprocal access to technology or to reduce the cost of acquiring technology; to maximize perceived market opportunities at low costs; to circumvent host country barriers or competitive barriers; to avoid home market saturation; to reduce risk and uncertainty (country and investment); to gain access to a regional market with some preferential market arrangements, etc.

Successful internationalization requires that an assessment of the firm's motives be made and correspondingly matched with its specific advantages. A firm's strategic mission determines its need to cooperate with others (Harrigan, 1984). Where product lives are short, cost implications are high and competition is keen, an analysis of corporate objectives and how these fit into firms' characteristics can help forge configurations which prospectively reduce transaction costs, enhance profitability, and position business units more advantageously. The foregoing suggests that: The adoption of new forms in the internationalization process is positively related to the firm's global strategies/objectives, *ceteris paribus*.

8.3.2.3 THE IMPACT OF FIRM SIZE ON NEW FIRMS OF INVESTMENT

H_3: The choice of new forms in the internationalization process is not significantly influenced by the size of the firm.

A number of studies (reviewed in Hood and Young, 1986) assert that the most important ownership advantage explaining foreign production is firm size (p.72). The interpretation is that the size variable incorporates all or most of the other ownership-specific advantages which cumulatively catalyze multinationality (Horst, 1972; Lall and Streeten, 1977; Dunning, 1977, 1979, 1988). The orientation and focus of the size factor in most of the studies was on FDI, suggesting that ownership-specific advantages arising from the size and complementarity of the firm's activities need to be internally controlled (via wholly-owned foreign subsidiary) to be effectively exploited (Dunning, 1988, p.176). The size factor has also been extended to international banking in which foreign branch banking is hypothesized to depend on the size of the parent bank (Cho, 1986; Nigh, Cho, and Krishnan, 1986).

The evidence from these studies reveals a close relationship between firm size and the propensity to invest abroad. The studies also suggest that foreign investment is almost completely the preserve of large MNEs. The implications are that small and medium-size firms (SMFs) are generally viewed as being unable to internationalize their activities through FDI because of their limited resource base - especially their financial, managerial and technological resources as well as inexperience of foreign markets. According to this school of thought, the growing acceptance, use and familiarity with NFI worldwide may gradually create an international institutional framework in which SMFs can convert their unique talents and firm-specific advantages (e.g. small-scale production technology) into capital which can be invested in a foreign market without having to supply all the other components that constitute the traditional FDI package (Oman, 1984, p.97).

Two implications of this hypothesis can be identified. One which has just been sketched contends that an important result of the proliferation of new forms is, or will be, an increasing multinationalization of SMFs, implying a lack of statistical significance among small, medium and large firms in the variables that depict non-hierarchical consideration and use of new forms.

A corollary implication, and one which is consistent with FDI studies, holds that the size of a firm is positively related to its level of involvement in foreign markets. Empirical FDI studies have found firm size, as proxied by its equity capital, to be a good representative variable among various ownership advantage factors (see, for example, Cho, 1986). The average finding of these studies is that large size firms display a preference for FDI and less propensity towards new forms. This implies a statistical significance between the three groups of firms in the factors that proxy use of NFIs. However, as Contractor and Lorange (1987) and others have documented, there is abundant evidence on the use on NFI by western MNEs, and these are ordinarily regarded as large, even though the evidence about firm size is unclear.

The clearest evidence about the high propensity to internationalize via new forms by large firms comes from Japanese MNEs, normally regarded in the west as *de novo* MNEs, or "unconventional MNEs" (Buckley,1988). The organizational modes of investment by these *de novo* MNEs seem to suggest a high propensity to use variants of cooperative alliances. For example, Kojima and Ozawa (1984, p.42) document Japanese trading companies' proclivity to form joint ventures with local partners or third-country interests. The trading companies' high propensity to organise joint ventures with local partners is coupled with an equally high propensity to accept minority ownership. Taken together, Japanese overseas manufacturing ventures involving minority equity participation (precisely, 1-29 per cent equity ownership) account for as much as 74.8 per cent, and this pattern is reported to apply equally to each of the nine largest trading companies (ibid). The willingness of Japanese MNEs (most of whom ranking among the top 20 largest MNEs worldwide) to adopt new forms in their internationalization process could be taken seriously by western MNEs who may be disturbed by the prospects of losing out if they insist on wholly-or majority-owned investment (see also, Oman, 1984, p.83).

The operationalization of firm size in this study is somewhat different. While assuming that firms, as in the above cited studies, possess the corporate capability (i.e. firm-specific advantages) necessary to successfully engage in international expansion, firms are identified and classified by size according to both the perceptions of corporate executives of the firms themselves and financial variables as well as the number of employees in these firms. Furthermore, since western MNEs (unlike their Japanese counterparts) perceive new forms as " a second best" (i.e."a defensive reaction") alternative (Ozawa, 1984), certain factors which may symbolize this defensive reaction strategy can be associated with new forms. Such factors as willingness to share ownership and control in return for access to local markets; concern about country risks, cost of establishing a foreign subsidiary; size of the parent company; experience in foreign markets, etc., have been variously mentioned in the literature as factors which prospectively give rise to the use of new forms. Thus, it is hypothesized in the null form that: The choice of new forms in the internationalization process is not significantly influenced by the size of the firm.

8.3.2.4. THE ROLE OF FOREIGN INVESTMENT POLICY SHIFTS

H_4: New forms of investment are more likely to prevail in firms with a 'dynamic foreign investment posture' than in firms with a 'static posture'.

It has been argued that although host government policies can be held largely responsible for triggering the move towards increased use of new forms, company strategies and behaviour are presumed to allow these policies to succeed in obtaining assent to, and conditioned the kinds of MNEs that accepted, minority positions or contractual/cooperative arrangements (Franko, 1989). The relationship between firms' global strategies and new forms was explored under hypothesis 2 above. The emphasis here is on the possibility that changes in functional strategies might induce firms to adopt new forms. In her editorial introduction to multinational corporate strategy, Harrigan, (1984) wondered how business unit strategies would be adjusted to sustain competitive advantage in international markets. In effect what changes must be made in functional strategies when firms operate in many nations?

Strategic management dictates that firms need to match their corporate capabilities to the ever-changing environment if they are to sustain competitive performance. In the analysis, not only are resource allocation issues involved (Tavis, 1981; Teece, 1984), but changes in international investment strategy become increasingly inevitable. The former is in the realm of capital budgeting and related matters of financial analysis. The hypothesis of interest is concerned with the latter, that is, changes in "strategic postures" (Franko, 1989) of firms. Recourse to this permits adaptations to environmental uncertainty to be accomplished by new forms, rather than by internal administrative processes involving greater anticipation of contingencies from the outset (Williamson, 1975, p.9).

An investment posture can be dynamic or static, in operational terms. Reference to the former allows strategic moves which direct a firm's critical resources toward perceived market opportunities in a changing environment to be made. 'Static posture', on the other hand, is a relatice term, determinable by a periodic time frame. The basic characteristics of the contemporary business environment include actual or potential risks and uncertainties; increased worldwide competition; increased regulatory constraints, governmental intervention or other distortion propensities; increasing cost cum reduced availability of resources; and decreased predictability of environmental parameters (e.g. inflation, exchange rate fluctuations, etc).

In this kind of atmosphere, how can a firm compete under a static investment posture? In the above kind of dynamic environment, changes in corporate investment outlook can be anticipated with greater frequency, say every other year. For analytical purposes, corporate investment postures that have not undergone any reviews within the last five years, assuming the company has been in existence that long or more, can be classified as static. It has been argued that the notion of firm-specific advantage is essentially a short-run phenomenon because it is only in the short run when endowments of proprietary knowledge are fixed; in the long run, the assets of the firm at a point in time are determined by the firm's investment policy (Buckley, 1989, p.11).

One statistic for gauging a firm's foreign investment posture is its overseas geographic concentration (see Hood and Young, 1986, p.35). Thus, given the firm's industry or product concentration as well as its geographic concentration of foreign investment, it would be expected to have a strong market position and high penetration within key industrial sectors in such markets. Therefore, such firms can afford to be static, implying a low frequency or no change at all in their foreign investment posture. The propensity to use new forms in this case is expected to be relatively low. However, this contradicts

Harrigan's (1985, p.124) hypothesis that concentrated setting will be more attractive for JVs because firms operating within oligopolies will focus on mutually desirable goals with greater ease. Conversely, firms whose current overseas activity is not geographically concentrated are expected to adopt dynamic postures and may frequently use new forms to exploit perceived economic and comparative advantages of multi-country operations. Exporting, licensing, franchising and joint ventures afford such firms efficiency mechanisms as well as contractual opportunity to cut their losses in the face of a highly variable and precarious environment. Thus it is suggested that new forms of investment will more likely prevail in firms with a dynamic foreign investment posture than in firms with a static posture.

8.3.2.5. THE ROLE OF HOST COUNTRY-SPECIFIC CHARACTERISTICS

H_5: The choice of new forms in foreign market development is significantly influenced by managerial perceptions of host country characteristics.

Host country-specific characteristics or advantages represent the third strand of the eclectic paradigm and is traditionally concerned with the 'where' of investment. In its original formation, the eclectic paradigm stated that the extent, form and pattern of international investment was determined by the configuration of three sets of advantages as perceived by firms (Dunning, 1988, p.42). In other words, the transactional power of the firm to determine the 'how', 'why', and 'where' of foreign investment depended on how corporate management perceived the firm's net ownership, internalization and location advantages. However, research has progressed along the lines of the incentives to internalize markets in which FDI is seen to supersede contractual/ cooperative modes. Forceful arguments with public policy implications are engaged to justify FDI. For example, it is claimed that without the incentive to internalize markets, vertical or horizontal integration would be a redundant engagement and transactions would be accomplished via autonomous means (Buckley and Casson, 1976; Rugman, 1981; Dunning, 1979, 1988). Equally, Dunning claims that the distinctiveness of the eclectic paradigm is the ability to explain internalization incentives (1988, p.33), implying a concern with one made of organization - wholly owned subsidiary.

As with other theories, the eclectic paradigm has been criticized on two grounds. First, it is couched in static terms, which makes it insufficiently microanalytic for the dynamics or the process of change of international investment (Vernon, 1985). Second, it insufficiently, if it does at all, allows for firm-specific behavioural differences. The attention of this hypothesis is on issues of the latter kind. Vernon's concern about the neglect of behavioural interaction is with respect to international oligopolists, rather than with foreign investors in general.

Country-specific factors or location-specific advantages have been couched in terms of a focus on the economics of a location. The formal economic theory of location is shaped by a concern with normative equilibrium analyses of spatially transferrable comparative advantage of one country over another. Applying this notion to multinational phenomenon forces the following argument: because transactional market failure is sometimes country-specific, it has locational implications; consequently, reference to MNE is intended to allow for the potentials of "internalizing exogenous spatial imperfections" (Rugman, 1981). However, from a strategic management point of view failure to recognize the strategic response of decision-makers to a set of economic and other variables, and the way the idiosyncratic behaviour of firms might influence and respond to international market failure, is the major pitfall of these schools of thought strategic nature and importance of country-specific factors as very crucial in influencing the level and pattern of international investment (see Teece, 1984; Dunning, 1988, p.46).

It is also recognized that while some attempts have been made to model strategic behaviour of firms towards their foreign operations (see, the summary in Robock and Simmonds, 1983; and Rugman, Lecraw and Booth, 1986), they have not generally been incorporated into the mainstream of international investment theory (Dunning, 1988, p.47), nor have they been investigated empirically. Clearly, whether or not a firm adopts FDI or NFI reflects not only its ability to do so, but on its managerial perceptions of the resulting costs and benefits. While there is general agreement about the main country characteristics that constitute advantages or disadvantages of particular locations, much less attention has been given to identifying the key attributes of firms - in particular those which might be operationally or strategically based - which may affect their response to particular market opportunities.

Strategically related characteristics of host countries most likely to be assessed as potentially leading to use of new forms include: host governments' inward investment policy (restricting fdi), size of host countries' markets, economic/political climate, fiscal/monetary policies, psychic distance (incorporating language, cultural, business, customs, etc. differences), level/size of markets, technological/managerial capacity (especially for banks), and level of infrastructural development. Whether or not a firm will establish in a country by means of new forms will depend on managerial assessment and the degree of importance attached to each or a combination of these factors. For example, if management views the volatile economic/ political conditions of a country high enough to pass over perceived market opportunities, the firm will not invest whether or not the host government operates an open door policy. This is the case with Lebanon and some African countries. On the other hand, if the firm's products are customized to a host/regional market, then the firm may service the market, using contractual or cooperative investment modes. Thus, managerial assessment of country-specific characteristics is crucial to the use of new forms or fdi, for that matter.

On the subject of managerial perceptions of host country characteristics, Adams (1980) believes that "for the most part, the concept of an impediment to investment is a relative one" (p.2). In effect, the perception of the degree of impediments presented, for example, by certain government policies, by structural economic problems, or by political uncertainty, will often vary significantly from one potential or actual investor to another. Underlying these variations are distinct subjective and objective appraisals of the investment climate, different perceptions of distinctive characteristics (cost and benefits) of the host country, and different perceptions of cash flow implications of investing in a particular country (i.e. expected rate of return on capital invested). On the basis of the foregoing, it can be hypothesized that: the choice of new forms in foreign market investment is significantly influenced by managerial perceptions of host country characteristics.

8.3.2.6 IMPACT OF COMPETITORS' BEHAVIOUR

H_6: Firm choice/use of new forms in the internationalization process is independent of competitors' mode of organising foreign transactions.

One of the often cited reasons why firms choose new forms of investment is the need to match the behaviour of rival firms (Williamson, 1975, p.217; Oman, 1984; Buckley and Casson, 1985; Harrigan, 1985). Conceptually, global competition can force a firm to develop defensive strategies. A major task in this process is the development of a profile of the likely strategic behaviour of rival firms and of their potential reaction to the firm's strategic moves. A commonly held judgement (in international business and economics) concludes that firms use new forms of investment reluctantly (in response to host government demands) and as a 'defensive-reaction' strategy (Oman, 1984, p.71; Ozawa, 1984). Professor Ozawa quickly dispelled this view with the Japanese experience in which competitive considerations make new forms structurally better adapted conduits of corporate resource transfers than "the old form" (fdi).

The primary object of developing a global competitive strategy is to place a firm in a position where it can survive and prosper in the international marketplace relative to its rivals. In this process, the firm first develops a profile of competitors' behaviour; and then attempts to match its internal strength (firm-specific advantages) to competitors' strategic moves, industry specific conditions and its external environment (country specific factors). Porter (1980) identifies five factors which influence inter-firm competition; the rivalry among existing firms, the threat of potential or new entrants, power of supplier's, and the bargaining power of purchases. In an international environment, the bargaining power of the host government as well as that of the host country firms may constitute incremental types of competitive force. To a large extent, these factors may be seen as constituting both entry and exit barriers. Entry barriers to competition are economic impediments which, in relation to international entry process, may limit or hinder a firm's choice of entry mode. Transactional sources of economic impediments of six different kinds are suggested (ibid).

First, the existence of scale economies forces new entrants to establish large scale operations if they must be competitive, in transaction-cost terms. For example, the notion of scale barriers can exist in exchange relations which require potential entrants to demonstrate competitiveness by acquiring a degree of monopsonistic power similar to that enjoyed by incumbent rivals. Potential rivals are also prone to strong resistance from existing firms, to the extent that they may not realise scale economies because they are unable to capture a sufficiently large share of the market. The second transactional entry barrier stems from product differentiation. This requires potential entrants to eschew product loyalties and brand names to carve a niche in the international marketplace. Clearly this entails high R&D expenditure in product development and advertisement. Capital requirements which may be necessary to break into new grounds (geographical and product markets) are the third source of entry barrier.

The fourth, called switching costs, are the contractual costs of shifting from one supplier to another or upsetting the long term relationship between existing firms and their suppliers. Where the market in question is one for which economies of scale are large in relation to the size of the new entrant or one for which small-numbers exchange relations exist, the impediment to entry is apt to be severe for the firm. This may apply mainly to small and medium size firms. Fifth, access to distribution channels poses an entry problem. New entry into a mature industry or a market with well established marketing channels is impeded by the lack of knowhow, by the difficulty of upsetting established customer relationship, and by the absence of related performance history (including capital market credit references) which can be assessed by factor suppliers.

The sixth source of entry barrier springs from government regulations. In relation to foreign investment, host government imposed distortions (eg. tariff and nontariff barriers, sectoral restrictions on FDI, etc.) may progressively impede the allocative efficiency of existing firms, but more actively weaken entry mode options of would-be-entrants. These factors interact with other competitive forces to pose limitations on firms' behaviour generally in the marketplace, and mode of entry, in particular.

Active international rivalry in conjunction with 'foreign positioning' (Rugman, Lecraw and Booth, 1986, p.345) may force firms to maintain operational presence in a particular product or geographic market, despite declining market opportunities. These are termed exit barriers and can arise from six sources.

The first exit barrier to international investment lies in the nature of the firm's assets, notably idiosyncratic assets (Williamson, 1979). The attributes of idiosyncratic investments for which exit impediments are posed are transaction-specificity, nonmarketability, specialized usage and users, and nonrecurrent usage. Transaction-asset specificity of three kinds are critical: site (or geographic) specificity, as when successive operations are located cheek by jowl by reason of transaction-cost economy; physical asset specificity, as where specialized capital assets are required for production, as commonly found in large, capital-intensive firms in the petroleum (exploration, drilling and refinery), steel, or heavy-engineering industries; and human asset specificity that arises from specialized knowledge or that acquired by learning, induction or by reason of employment. The reason idiosyncratic assets are critical and constitute exit barriers is that, once an investment has been made, parties to the exchange (buyer and seller) are effectively 'locked into' bilateral exchange relation for a considerable length of time thereafter. Pulling out therefore might create transactional diseconomies, at least to the unwilling party who may then seek compensatory remedies.

The second source of exit barriers relates to the fixed costs of abandonment or termination. These costs are related to specificity, discussed above. Investments or exchange relations that are unspecialized among users or parties to the exchange pose few hazards, since the afflicted parties in these circumstances can readily turn to alternative sources without difficulty. However, for specialized transactions and for certain overseas operations, not only are nonmarketability problems posed, but labour settlements (including pension payments) complicated by low productivity and low abandonment value have important cost-bearing consequences.

Third, strategic costs of abandoning a market may inhibit divestment because otherwise the firm may lose foreign market positioning. In order to match rival firms in the fight for global or regional market share, it may be necessary for the firm to retain the operation with slow market growth simply for strategic reason (i.e. to defend its interests and preempt rival entry). Such transactions impose strategic costs which inevitably act as exit barriers.

Information barriers, the fourth source of exit impediments, can prevent or, at least, make it difficult for management to obtain accurate data to assess performance and exercise balanced judgement to exit. Exit decisions are made complex when impactedness combining with opportunism is in active interaction with uncertainty and small numbers exchange relations. The fifth source of exit barrier is both psychodynamic and intangible. Reference to managers' emotions is intended to capture or emphasize management's influence, pride and personal interest in a given project, and reluctance to quit from it.

Finally, public policy considerations may work to impose exit barriers for certain types of projects. Just as entry barriers arouse government and public concern, if they are deemed anticompetitive or are seen to have efficiency-debilitating properties, so can certain types of project abandonment cause public concern, if social and political issues are thereby raised (e.g. unemployment and regional imbalance).

At least, each source of entry and exit barriers bears some relationship to organizational patterns of operation. Existing firms have some advantage over would-be entrants. If entry barriers work to severely limit the capacity of firms to enter into the marketplace, exit barriers impose competition of a different kind, requiring firms already operating in the market to make special efforts to design exchange relations that have good continuity properties (Williamson, 1975). If the height of entry/exit barriers and the extent of foreign investment activity are highly correlated (see, Caves 1982, p.96), then the extent of foreign investment activity can be gauged by the entry mode behaviour of MNEs. If significant barriers to entry or exit surround a market, the modes best qualified to overcome them may be hypothesized to be variants of new forms. In order to verify this, it is hypothesized that: Firm choice/use of new forms in the internationalization process is independent of competitors' mode of organizing foreign transactions.

8.3.2.7 RELATIONSHIP OF STAGE OF COUNTRY DEVELOPMENT

H_7: Firm choice of new forms in the internationalization process is independent of stage of host country development.

It has been claimed that the move to acceptance or use of new forms of investment is specifically a less developed country phenomenon (Franko, 1989). Much earlier Franko and other writers had documented instances of MNE acceptance of reduced equity position as a trade-off for preferential access to protected markets (1974, pp.325-26 and other sources cited therein). Oman (1984) has argued that new forms may be suited for projects located in LDCs. In short, the tenet of these claims is one of the contextual backgrounds of this study. The issue of the relationship of stage of development of countries to use of new forms of investment is central to renewed interests in foreign investment theories. It has public policy implications and has been addressed mainly in descriptive form, albeit supported by historical, macroeconomic data and anecdotal evidence. Notable exceptions are the single component studies, cited below. While providing evidence on the relationship of stage of development to joint venture creation rationales (Tomlinson, 1970; Gullander, 1976; Janger, 1980; Beamish, 1984, 1985) and on the relationship of development level of a country and joint venture instability and performance (Franko, 1971; Reynolds, 1979; Janger, 1980; Stuckey, 1983; Beamish, 1984, 1985), the authors were silent on the central issue.

The hypothesis has implications for the transactional ubiquity of traditional FDI. The general proposition, referred to as "the obsolescence-of-FDI hypothesis" (Oman, 1984, p.26), is concerned with the claim that, in the North-South context, traditional FDI was becoming obsolete and was being replaced or superseded by new forms of investment. This claim is traceable to a paper published over twenty years ago by Charles D. Hyson and Dale R. Weigel (1970), which spotlighted the controversy surrounding the role of FDI in the development process. By that time, both policy-making emphasis and research focus were on the positive contribution of FDI to national development. At the time FDI accounted for around 25 per cent of the total foreign capital obtained by developing countries (ibid). At the same time also, conflict between MNE and governments (host, home, and multilateral) was brewing. The inevitability of conflicts was more apparent as

MNEs were perceived as not only vehicles for the transfer of their national cultures and political and economic values, but more importantly as having sufficient power to overcome government restrictions on their *modus operandi.*

By mid 1970s interest in the affirmative contribution of FDI in the development process has come full circle and was increasingly questioned by national and international governments (see, for example, UN, 1973). Progressively many host countries, notably LDCs, became interested in "unbundling" the package of resources (capital, technology and management) normally supplied under FDI, perhaps as a macroeconomic means of minimizing foreign exchange costs of acquiring foreign technology, and as a potent political means of checking the infusion of foreign cultural and political values. Whether these have been achieved or not remains a moot issue.

It is in this historical context that the hypothesis of interest was contrived as a North (developed country) to South (developing country) phenomenon. Since then analytical enquiries have progressed along single components of new forms (such as licensing, franchising, joint ventures, etc.), taking as a datum the claim that these forms of investment are restricted to, or best suited for, developing countries. At the same time, there is literature evidence that the new forms are used frequently by large MNEs in the developed countries (see, for example, Janger, 1980; Harrigan, 1985; Contractor and Lorange, 1987). Current evidence among EEC firms shows that the Single European Market has spun a web of cross-border strategic alliances characteristic of new forms (see, for example, Hiltrop (1991) and Thompson and Knox (1991)).

The object of this hypothesis is to test empirically the proposition that new forms of investment are devised for LDC projects. Certain proxy factors of development level of countries which are thought to encourage the use of new forms include: economic/political climate of a country, level of industrial development, openness of host country towards foreign investment, presence of many foreign businesses etc. These factors represent one of two perspectives of national stage of development; that is, they represent features of a developed country or a developing country. How the factors differ between DCs and LDCs as rationales for using new forms is based on the assessment of corporate management. This approach is consistent with Beamish (1984, 1985), but here more proxy variables are utilised to capture many features of level of country development than Beamish's study Thus it is hypothesised that: Firm choice of new forms in the internationalization process is independent of stage of host country development.

8.3.2.8 MANAGERIAL PERCEPTIONS OF BENEFITS OF NEW FORMS

H_8: Firm choice of new forms is dependent upon their perceived net benefits by corporate management.

The proposition that a firm is a system of relationships whose existence is dependent on the entrepreneur's direction of resources (Buckley, 1989, p.154) has largely been suppressed in both the theory and empirical analyses of corporate investment (Teece, 1984). Yet, the transactions cost approach recognizes that markets (of which new forms are important constituents) and hierarchies are alternative organizational mechanisms for supporting transactions, and that the choice of the one or other ought to be made according to which is the more efficient way to support the transaction in question (Williamson, 1975; Teece, 1984). In order to investigate why it may be desirable to use new forms in foreign transactions, one must explore the nature of new forms (their processes) and examine the attributes of transactions they appertain to.

The transactional features of new forms underlying their net benefits can be summarized as follows: (1) New forms of international investment (NFIs) enable firms to diversify risks (country and investment). (2) NFIs can be used to avoid market disabling factors of opportunism, uncertainty, barriers to market entry and exit, etc. (3) NFIs are superior means of exploiting a firm's assets abroad or foreign market opportunities, with minimum resources and risks. (4) NFIs provide advantage of flexibility to adjust to changes in the international marketplace. (5) NFIs may be used as pre-emptive manoeuvres to gain access to promising markets and technologies. (6) NFIs are particularly suited for projects destined for developing countries.

In themselves, these features cannot provide the commitment or stimulus to internationalize. They are important catalysts for choice of new forms, but the stimulus must come from the decision-maker's perception that the company can utilise these benefits (see, for example, Welch, 1990). The transactional features of NFIs create a clear perception of the international possibilities in them. The neoclassical assumption is that transactions will be organized by markets unless market exchange results in contractual incompleteness or difficulties, and hence transaction costs. Essentially, the presumption is that economic activity is best organized via markets because the bureaucratic distortions associated with internal exchange are thereby prospectively attenuated (Coase, 1937; Williamson, 1975; Teece, 1984). Additional advantages of markets over firms may include the following.

First, markets are informationally economical and efficient with respect to price adjustments. This is the economic principle governing the efficient markets hypothesis. Second, production cost advantages may be realized through markets. For instance, where the firm's internal needs are insufficient to exhaust scale economics, these can be more fully realized by buying instead. Furthermore, markets can aggregate uncorrelated demands, thereby achieving intertemporal efficiencies (ibid). This is readily found in exporting. The transactional properties of export houses, confirming houses and buying houses stem from their capacity to intermediate between manufactures and importers. They attempt to correlate and coordinate the demands of a large number of small buyers, who otherwise lack the monopsonistic power required to negotiate directly with manufacturers. Fourth, subcontracting or joint ventures can mitigate the diseconomies of scope and transactional difficulties (e.g. small-numbers relations) which attend ownership and exchange arrangements of indivisibilities of both physical capital and informational types. Finally, market modes can be used as pre-emptive manoeuvres to gain access to promising markets and technologies, without committing huge resources.

These features fit well into the "defensive reaction hypothesis" (Oman, 1984). Other issues related to this hypothesis are: the role of host government policy; and the importance of international managers' perceptions of a given country's 'investment climate', regardless of how subjective those perceptions may be (p.72). As with Oman's defensive reaction hypothesis, the proposition under investigation seeks to highlight the fact that the success of host government policies in attracting foreign firms via new forms may depend on the latter's willingness and ability to accommodate rather than simply pull out, or refuse to exploit perceived profit opportunities.

The notion of managerial perceptions of net benefits and their impact on choice of entry mode is a relative one. The perception of net benefits presented for example by diversification motive, by smoothing of cash flow and risk reduction, or by efficiency argument, will often vary significantly from one firm to another. One firm's benefit may be another's disincentive or, at least may be perceived so. Underlying the variations are distinct subjective and objective appraisals of the host environment, behaviour of rival firms, internal strengths and limitations, and strategic reasons for considering alternative modes of entry. How variations in perceptions will affect choice of new forms in the internationalization process is the subject of empirical investigation. In the light of the foregoing it may be hypothesized that: Firm choice of new forms is dependent upon their perceived net benefits by corporate management.

CHAPTER NINE

RESEARCH METHODOLOGY AND STATISTICAL PROCEDURES

CONTENTS

CHAPTER 9
RESEARCH METHODOLOGY
DATA COLLECTION AND QUESTIONNAIRE ADMINISTRATION

9.1 INTRODUCTION

The primary goal of survey research is data collection in which information is obtained directly from individual persons who are selected so as to provide a basis for making inferences about some larger population. In obtaining this information, two principal instrumentation methods, involving direct or indirect approach in each case, are generally employed. These are Questionnaire and Interview. Questionnaires can be administered by mail or self. Alternatively, information can be obtained through face-to-face or telephone interviews. Each of these four approaches has its merits and drawbacks.

MAIL QUESTIONNAIRE

Also called postal surveys, this particular method is the cheapest form of investigation. Provided an up-to-date mailing list of the sample respondents is available, mail questionnaires enhance the prospects of reaching certain groups of people who might not otherwise be reached by telephone or be disposed to grant personal interviews. Interviewer bias can potentially be reduced through mail questionnaires, provided the questions are clearly worded and framed in simple terms. The main drawbacks are: (1) They tend to be slow in revealing results; and (2) the response rate is usually very low and this may invalidate or skew the significance of the subsequent analysis.

SELF-ADMINISTERED QUESTIONNAIRE

From a research point of view, this method has two implications. First, if administered by the researcher it can facilitate information collection, if the appropriate respondent is reached, because thereby the researcher can stimulate the latter's interest to the aim of the research. Second, by meeting the respondents personally, the researcher can use "one stone to kill two birds" (i.e. use of the occasion to solicit for subsequent interviews). This is bound to yield greater interview schedule than would be obtained through mail request. The major drawback of this method is the high travelling expenses of self-administration. It is most useful if the researcher is within the locale of the respondents or if the respondents are within one locale. For example, since London is the headquarters of most UK-based banks, self-administration of questionnaires may prove cost effective in these circumstances.

PERSONAL INTERVIEWS

These offer the researcher the flexibility to modify the questions according to the interviewee response, enabling a more in-depth collection of information. In many cases, the researcher's data bank can be augmented with brochures and other material information about the firm which otherwise might not be obtained. However, if the interviewer strays from a structured set of questions, then elements of bias may creep in from either the respondent or the interviewer. Personal interviews are both expensive and a comparatively slow process of collecting data.

TELEPHONE SURVEYS

This method is easy to administer, fast in eliciting information and relatively inexpensive. As a sole source of information, it may yield insufficient information, except if the number of questions is very small. Imagine asking twenty questions or more (as most academic researches involve) over the telephone! As a support to any of the above methods, telephone survey permits the researcher to clarify questions that are not clearly understood; they also provide follow-up opportunities which can add to the improvement of both the quantity and quality of information obtained. However, it may tend to alienate potential respondents because of inconvenience at particular times. In any event, it is a very popular approach in industrial market research.

In general, the greater the combination of survey instruments used in a research, the greater the prospects of increasing and/or improving the quantity and quality of data. A survey should provide five types of information about respondents: facts, perceptions, opinions, attitudes, and behavioural reports (Manheim and Rich, 1986, p.105). In the design and administration of questionnaires for this study, these factors were uppermost. For this study, all of the above methods were adopted. The questionnaires were administered and interviews conducted with a view to evoking responses that a) were indicative of firm behaviour over a range of variables affecting or likely to affect the use of new forms of investment (NFIs) as entry modes, b) reflected firm-specific and country-specific factors, c) covered a broad spectrum of industrial sectors and activities as well as national orientations, and above all, d) reflected respondents' opinions and beliefs. Additionally, a careful consideration was made on the scope and context of the behavioural variables of significance to ensure that questions adequately sampled their full range and depth.

The development of the questionnaire ensured that each variable of interest was unambiguously defined, and that a variety of questions were developed as potential stimulants of response, especially in variable areas of strategic concern.

9.2 CRITERIA FOR QUESTIONNAIRE DEVELOPMENT

The sample consists of firms (Banks and Companies) with overseas operations, drawn from a large number of countries. These countries include developed as well as less developed countries and cover various geographical regions of the world. A study of this kind which involves firms drawn from different parts of the world can create both semantic and interpretational problems. The problems become complicated if the questions seek to elicit information of a strategic nature, such as questions concerning foreign investment and their deterministic features, or if the questionnaire is lengthy.

Experience, coupled with discussions with many executives, reveals a reluctance to spend company time to fill a lengthy questionnaire nor are executives prepared to divulge information other than those publicly available, e.g. annual reports. In at least 11 instances, the chief executives showed me a pile of questionnaires they had received in the last two months. Most of these were about 8 - 10 pages long, and one senior bank manager said emphatically: "there was no way I could make time to answer an eight-page questionnaire". One feedback from my pilot study was the curtailment of the questionnaire to very essential informational aspects. In order to achieve this, a number of criteria were set as a guide to questionnaire development. The decisions were informed by the researcher's experience (both in previous researches and as a company executive) and are consistent with the criteria of question formulation of Kerlinger (1970, pp.467-478) and Churchill Jr., (1987).

One criterion was to reduce technical terms to the bare minimum, Thus, where the question related to organisational mode of foreign investment or "new forms" by specification, respondents were rather asked to identify (by ticking) from a pool of common business patterns which one/s best described their companies' route of entry into a foreign market. While not claiming to be a standout procedure, the objective was to reduce any ambiguities in the research questionnaires.

Another criterion in the questionnaire development was to adopt the market survey approach, by keeping the questionnaire short, precise and manageable. The snag with this approach is that where the information desired is of a technical nature, precision may disallow or at least reduce a more in-depth gathering of information. However, by isolating and structuring questionnaires in short sections, and adopting criterion (1) above, the problem may be overcome. In developing the research questionnaire, each variable area of interest was defined, and a variety of questions, designed to produce multi-item measures to avoid bias commonly associated with single-item measures, were conceived as potential stimulants of response indicating behaviour in that area (see Mannheim and Rich, 1986, p.112; Questionnaire Design Technical Manual, No. 5, 1972).

The next criterion was organizational. Based on the pretest of the questionnaires, structured adjustments had to be made both in the content and scope of the questions asked. Also, questions varied slightly between banks and companies. For instance, questions on organizational modes of entry differ between the two groups of organizations; and within each group, questions had to be structured according to whether the bank or company was U.K. owned or foreign owned. Furthermore, brevity was achieved by asking less demanding questions in the early section of the questionnaire, such as those concerning firm characteristics which can be gleaned from their annual reports.

The fourth criterion was to ask questions germane to the research problem and objective. In this process, it is recognized that no set of questions can fully capture the phenomena of interest just as no sample can claim to capture all the characteristics of a population. Here, a number of measures were adopted. First, validity (internal and external) was pursued by avoiding leading questions that suggest directional answers, thus introducing bias (see Mannheim and Rich, 1986, p.83). Second, question wording was crucial in that if questions are asked in ways that encourage respondents to give one rather than another answer, the data will reflect the real world less than they will reflect the choices made in question construction. The literature provides some general guidelines, namely, using items that have been successfully used in prior research; using contingency questions to find out; using questioning formats that ask respondents to state the degree to which they agree or disagree with series of statements selected to reflect different attitudes about the subject matter (ibid, p.111; Robinson and Shaver, 1973).

The last and most important decision criterion, designed to reduce semantic and interpretational problems, was to include foreign companies with operational presence in the U.K., rather those operating outside the U.K. It is reasonable to assume that a foreign firm from a non-English speaking country operating in the U.K., will possess English language capability. The same goes for a U.K. firm operating in a non-English speaking country. In general, it may be assumed that a firm operating in a foreign country will possess some managerial competence in that country's national/official language. These five criteria improved data collection for the research.

9.3 QUESTIONNAIRE ADMINISTRATION

With these decision criteria, a two-phase exploratory study was conducted during the middle half of 1990. The first phase involved a questionnaire study covering 66 companies and 31 banks. The second phase involved interviews with 26 corporate executives; 12 bank executives and 14 company executives, most of whom were senior managers. Tables 9.1 and 9.2 present the summary and analysis of the response of the sample firms, respectively.

The study sample comprised:

1. U.K. Companies
2. Foreign Companies, drawn from 6 countries (Table 9.4)
3. U.K. Banks, and
4. Foreign Banks, drawn from 15 countries (Table 9.6).

The study covers 26 industrial sectors, ranging from banks through engineering and manufacturing to music and entertainment industry (Table 9.8).

Table 9.1 Summary of Questionnaire Administration

Nature of Firm	Number of Questionnaires	Number Returned	Useable Lot	Percentage Return
U.K. Companies	100	55	47	55.0
Foreign Companies	50	24	19	48.0
U.K. Banks	21	11	10	52.4
Foreign Banks	50	23	21	46.0
TOTAL	221	113	97	51.1

A total population of 221 firms was identified for the purposes of the study (Table 9.1). The Times 100: 1988-1989 Statistics of leading companies in Britain and Overseas and World Banking 1986 (which was the latest edition) formed the sampling frames. The study is limited to UK-based firms (banks and companies) and foreign-based firms. For the purposes of this study, the term 'firm' is used generically to refer to banks and companies collectively. Where a reference is intended for banks or companies, they will be used specifically. Also in this study, 'UK based firms' are defined as banks and companies with overseas investment operations (generally conceptualised as MNEs) having their registered head offices in the U.K. Similarly, foreign firms refer to banks and companies operating in the U.K. with registered head offices outwith the U.K.

Three criteria for inclusion in the sample were set for all firms, regardless of nationality. (1) The firms will have been involved in international operations for at least five years, where by international operation is meant one of the two criteria following. (2) At least 5 percent of the firm's (parent's) global investment is accounted for by foreign investment operations, or (3) at least 5 percent of the group turnover (or operating income for banks) is controlled by foreign investment earnings. These criteria have been used in other studies involving MNEs (See, for example, Demirag, 1988, 1990). Before administering the questionnaires, pretests were conducted by administering the survey to a small sample of respondents similar to those in the larger sample. Pretesting a survey instrument is viewed "as important to successful survey research as a test drive is to buying a good used car" (Mannheim and Rich, 1986, p.119). The pretests served to: develop different versions of the instrument, verify their utility, and refine the final output. The questionnaires were sent to the chief executives of 221 firms as detailed in Table 9.2. In order to increase the geographic representativeness/response, extra follow-up mail effort and telephone calls were undertaken.

Table 9.2 Analysis of the Response of the Sample Firms

	No. of Questions sent	Ineligible Firms	Total Eligible Firms
UK Companies	100	8	92
Foreign Companies	50	5	45
UK Banks	21	1	20
Foreign Banks	50	2	48
Total	221	16	205

ELIGIBLE FIRMS	Positive Response		Negative/Non Useable Response		No Response	
UK Companies	47	(51.1%)	6	(6.5%)	39	(42.4%)
Foreign Companies	19	(42.2%)	4	(8.9%)	22	(48.9%)
UK Banks	10	(50.0%)	2	(10.0%)	8	(40.0%)
Foreign Banks	21	(43.8%)	4	(8.3%)	23	(52.7%)
Overall	97	(47.3%)	16	(7.8%)	108	(52.7%)

TOTAL RESPONSES TO TOTAL POSSIBLE RESPONSES

UK Companies	55.0%
Foreign Companies	48.0%
UK Banks	52.4%
Foreign Banks	46.0%
Overall	51.1%

NO RESPONSES TO TOTAL POSSIBLE RESPONSES

UK Companies	45.0%
Foreign Companies	52.0%
UK Banks	47.6%
Foreign Banks	54.0%
Overall	48.9%

Ineligible Firms include return-to-sender mails, firms which have been acquired, out of business, unable to respond due to lack of time or were mistakenly identified as having overseas operations.

Negative/Non-Usable Responses represent firms which replied to the questionnaire but did not answer some of the core questions for reasons of confidentiality or inadequate knowledge.

Such follow-up attempts proved very useful because it turned out that about 10% of the initial questionnaires had been wrongly post-coded, or the firms had changed addresses, had been acquired, or had misplaced the questionnaire. The telephone calls were also used as a basis for establishing contacts for prospective interviews. Some of the interviews were informally established through this process.

9.4 QUESTIONNAIRE DATA RELIABILITY

Returned questionnaires were examined for completion, errors and omissions. Follow-up phone calls and letters saved such questionnaire that otherwise would have been discarded. The rates of positive response were 55.0%, 48.0%, 52.4%, and 46% for UK companies, Foreign companies, UK Banks, and Foreign banks, respectively. The overall rate of response (usable and unusable lots) was 51.1% (See, Table 9.2).

9.5 NON-RESPONSE BIAS

The overall response rate of 51.1% compares favourably with most studies. However, the presence of non-response may suggest that the viewpoint of non-responding firms was significantly different from that of respondents and this may affect the validity of the research. Non-respondents indicated why they did not participate in the survey. The average main reasons were 'company policy' and 'lack of time'. These reasons are consistent with the interview discussions, personal experience and other researchers' findings (See, for example, Pike, 1988). While non-response bias may pose a problem in a mail survey, the extent to which the bias may affect the validity of inference drawn from the sample was investigated. In order to detect any bias due to non-response, Oppenheim (1966, p.34) suggested that if late returns of questionnaires were assumed to represent non-respondents, then it would be possible to detect if non-response bias was present in a sample. The test for non-response bias is done by comparing one or more variables of interest between respondents and non-respondents (proxied by earlier and later returns). Here, two relevant variables of the sample firms were inspected using the Chi-square tests: the scope of international operations (proxied by Foreign Investment and Foreign Earnings ratios) and industry groups. These variables and test were also used by Demirag (1990), though in a different research context involving MNEs.

An alternative statistical test is the Mann-Whitney U test. In each case the Chi-Square tests showed that there was no indication of significant differences between respondents and non-respondents (Tables 9.3.1 and 9.3.2). Regardless of the statistical test applied, the Oppenheim methodology can only capture non-response bias that can be portrayed by the average responses. It does not capture non-response bias created by a non-symmetrical distribution of the respondents (Wallace, 1987). To capture such potential non-response bias, especially given the wide demography of the respondents, the demographic data of the late respondents and those of the respondents whose responses were not subjected to further analysis because of inadequate completion were compared with demographic data of 'valid' respondents. No statistically significant difference was found between the two groups, suggesting a lack of non-response bias.

Table 9.3.1 A Test of Indifference between Respondents and Non-Respondents in Scope of International Activities.

	Respondents		Non-Respondents			Valid Total
	Freq	%	Freq	%	No	%
UK Companies (n = 100)	47	88.7	6	11.3	53	46.9
Foreign Companies (n = 50)	19	82.6	4	17.4	23	20.4
UK Banks (n = 21)	10	83.3	2	16.7	12	10.6
Foreign Banks (n = 50)	21	84.0	4	16.0	25	22.1
	97	85.8	16	14.2	113	100.0

Chi-Square	D.F	Significance	Min.E.F.	Cells with E.F. < 5
0.667544	3	.87957	1.7	3

Table 9.3.2 A Test of Non-Response bias in the demographic data of Respondents and Non-Respondents.

	Respondents		Non-Respondents			Valid Total
	Freq	%	Freq	%	No	%
UK Companies	55	55.0	45	45.0	100	45.3
Foreign Companies	24	48.0	26	52.0	50	22.6
UK Banks	11	52.4	10	47.6	21	9.5
Foreign Banks	23	46.0	27	54.0	50	22.6
	113	51.1	108	48.9	221	100.0

Chi-Square	D.F	Significance	Min.E.F.	Cells with E.F. < 5
1.3718734	3	.71241	10.3	None

The basic criterion for the choice of respondents was their capability to provide the needed information on the basis of their participation in decision-making as chief executives or heads of international divisions. Consequently, the target respondent in each case was the Chief Executive or his nominee. The purpose of the personal interviews was to clarify and explore in more depth the implications of the results obtained from the postal survey. The selection of MNEs interviewed was based on: (a) the industry groups; (b) the size of parent firm; (c) the scope of international activities; (d) the nationality of the firms; and (e) the answers to key questions in the questionnaire. An overall attempt was made to interview firms of different nationalities, covering a wide spectrum of industries. Altogether interviews with 26 bank and company executives were conducted, as follows:-

4 UK Banks' executives - the most junior of whom was Senior Manager-International Operations.

12 UK Companies' executives, the most junior of whom was Manager Corporate Affairs.

5 Foreign Banks' executives - the most junior of whom were in charge of their UK branches/offices.

5 Foreign Companies' executives - the most junior of whom was Public Relations Manager.

With respect to possible cultural differences and their impact on responses of the 97 executive respondents, drawn from 16 countries, while these cannot be ruled out, Hofstede (1980) has observed that managerial values are a lot similar in these circumstances. In particular, at the macro level, it is claimed that managerial culture exhibits similarities to some degree (Cooper, 1979, p.10). Finally, the foreign firms' answers to certain questions were aggregated because most countries in the sample were represented by 1 company or bank, and as such could not be taken as representative of national trends (See, Tables 9.4 and 9.6).

9.6 ANALYSIS OF DATA AND STATISTICAL TECHNIQUES

The questionnaire for each sample group was divided into 5 sections, in a sequential order in order to enhance data entry since most of the questions were the same across the

4 groups. Data coding and analysis were carried out on the SPSS/PC+ - the DOS version of the Statistical Package for Social Sciences, which can be operated on any PC with hard drive. Appendix 4 shows the SPSS/PC+ data entry. The analysis was performed in a progressive order as follows:-

1. Analysis of Part 1 of the questionnaire in order to obtain a picture of the characteristics of the respondents and their degree of representativeness of the populations surveyed;
2. Analysis of Part 2 of the questionnaire to give a picture of respondents' scope of international operations and to determine the impact of changes.
3. Analysis based on Part 3 of the questionnaire to: (a) establish the pattern and frequency of respondents' use of new forms as initial entry mode choices, and (b) determine the importance of items in a contractual package and the significance of control features, if any, for companies in the survey.
4. Analysis based on Part 4 of the questionnaire to establish the extent to which firm-specific factors combine with entrepreneurs' perceptions and country-specific characteristics to provide fuller explanation of the divergent forms of foreign investment, and
5. Analysis based on Part 5 of the questionnaire to: (a) determine respondents' perceptions of the net benefits of new forms; (b) confirm or refute the hypothesis that the new forms are best suited for use in LDCs; and (c) to gauge respondents' opinions as to whether the new forms will gain or lose popularity and their reasons.

Respondents were asked to use a frame of reference for judging each item of information. They were further asked to indicate the degree of significance or importance they attached to series of statements selected to reflect different attitudes about relevant items of information. As Mannheim and Rich (1986, p.111) observe, this approach has several advantages over the use of simple statements. First, in an exploratory study of this kind, this approach provides a simple means of securing measures of the intensity of respondents' opinions. Second, it helps ensure that all respondents will be using the same frame of reference in answering, and it thereby increases the validity and reliability of measures. Furthermore, statements about various topics can be interspersed in a set so that respondents are not cued about the purpose of a line of questioning. Finally, series of statements are easily used in constructing complex measures of attitudes and perceptions called *scales* or *indices* (ibid, pp.140-149). In the questionnaire, Likert-type scales were used to assess respondents' perceptions and attitudes, with scores ranging from 1 to 5, except in certain cases involving an assessment of motivational factors and influence of locational and firm-specific factors where the range was higher. The ordinal scales were transformed into metric for computational purposes, by scoring as 1 items which respondents perceived as very important/significant to 5 (or higher number as the case may be) for items perceived as least important or very insignificant. In the SPSS/PC+ coding, Q1, Q2, Q3 and Q4 designate Foreign bank, UK bank, UK company and Foreign company, respectively (Appendix 4). For each, labels and variables are defined sequentially according to the numbering of the questionnaire.

9.6.1 DESCRIPTION OF STATISTICAL TECHNIQUES

A variety of statistical methods were used to test the hypotheses developed in Chapter 11. Means and standard deviations were calculated for all corporate responses and these were ranked according to the mean scores, with mean scores tending towards 1 being superior in rank to those tending towards 5 (or higher). Thus, a mean score of 1.677 ranks higher than mean score of 1.833, and so on. The data collected lent themselves to nonparametric statistics. Nonparametric statistical test appropriate to assessing the significance of differences between the firms' responses in respect of each of the variables were carried out. A detailed description of the statistical tools employed in the study is presented as Appendix 5.

ANALYSIS OF RESEARCH FINDINGS: PART 1

9.7 CHARACTERISTICS OF FIRMS IN THE SURVEY

The study sample consists of 66 companies drawn from seven countries including the UK (Table 9.4), and 31 banks drawn from sixteen countries including the UK (Table 9.6). In both cases, UK represents a home country, on the one hand, and a host country, on the other hand. Tables 9.5 and 9.7 below respectively provide a summary of the individual characteristics of the sample companies and banks. The companies cover a wide range of industrial activities (25 in all), ranging from battery and cable manufacture through heavy engineering and hotel & catering services to recorded music & entertainment and textile manufacture. The details of industrial distribution of the companies (together with the banks) in the survey are summarized in Table 9.8. Altogether the survey covers 97 firms. Every effort was made to represent as many industrial sectors and national origins as possible.

9.7.1 NATIONALITY OF THE FIRMS

From Table 9.4, US based companies represent 42 per cent of foreign companies in the survey. Japanese and German companies follow in that order with 32 per cent and 11 per cent, respectively. Companies based in Belgium, France and the Netherlands make up the rest of the sample with 5 per cent representation each. Returned questionnaires from these companies were unusable but two of these were included in the interview schedule. Employment and financial statistics from some of the foreign companies, especially Japanese companies, relate to their UK operations only. However, the sampling frame from which these companies were drawn depict that their parents rank amongst the 1000 largest industrial companies in the world.

A similar analysis from Table 9.6 puts Japanese banks (19%) ahead of other foreign banks in the sample, followed by Danish, French and Italian banks with 11% each. Banks from other eleven countries make up the balance of 48 per cent. In all, UK firms dominate the sample groups, as might be expected, constituting 71 per cent of sample companies and 32 per cent of sample banks.

Table 9.4 Summary of Nationality of Companies in the Survey

Country of Origin	Frequency	Cumulative Frequency	Percent	Cumulative Percent
Belgium	1	1	1.5	1.5
France	1	2	1.5	3.0
Germany	2	4	3.1	6.1
Japan	6	10	9.1	15.2
The Netherlands	1	11	1.5	16.7
U.K.	47	58	71.2	87.9
U.S.A.	8	66	12.1	100.0

n = 66

9.7.2 ORGANIZATIONAL RESPONSE

A breakdown of the respondents (Table 9.9) shows that the majority (45.4 per cent) of the respondents were divisional managers. Included in this group are functional heads, namely, Accountancy (Finance), Marketing, Production, Company Secretary/Legal, Corporate Affairs, Development/ Planning, etc. As was evident from the personal interviews and telephone conversations, the divisional heads were delegated by the Chief executives who felt that they were most suited to respond to the research issues involved. Majority of the respondents in this category were Finance Directors or Chief Accountants, Marketing Directors or Head of Corporate Strategy. Next to divisional managers were Managing Directors or General Managers (34 per cent). Senior Managers or other managers with equivalent responsibilities constituted 16.5 per cent of the respondents. For the reason stated above, it was not surprising that Chief executives/chairmen were responsible for answering 4.1 per cent of the questionnaires.

Table 9.5 Summary of Characteristics of Companies in the Survey

Company	Main Activity	Country of Origin	Size of Company[a]		Scope of International Activities[a]			
			Employees	Group Turnover £m	No. of Overseas Outlets	FI/GTI %Range	FIE/GE %Range	Respondent
1	Marketing of Sensitized Materials	Germany	1,022	194	25	10-20%	10-20%	CA
2	Paper Packaging	UK	925	70	4	10-20	10-20	CE
3	Rubber/Plastics Manufacture	UK	5,000	250	12	> 30	> 30	CE
4	Brewing/Pub Retailing	UK	90,138	4,036	N/A	N/A	N/A	MM
5	Contract Services	UK	132,025	2,224	55	20-30	20-30	MKD
6	Manufacturing - Steel Drums	UK	2,603	194	11	> 30	> 30	FD
7	Building Materials	UK	20,818	1,283	19	> 30	> 30	GS
8	Industrial Gases, Health Care Products	UK	38,350	2,309	79	> 30	> 30	CPM
9	Building Materials Manufacture	UK	11,930	961	24	> 30	> 30	FD
10	Specialist Chemicals	UK	1,037	89	N/A	> 30	> 30	MM
11	Gas Production & Distribution	UK	79,000	7,983	52	5-10	5-10	MD
12	Manufacture of Polymeric Products	UK	8,500	589	30	10-20	> 30	C/CE
13	Electric Typewriters	Japan	168[+]	25[+]	53	20-30	20-30	MM
14	Copiers & Photo Equipment	Japan	1,938[+]	356[+]	90	20-30	10-20	MD
15	Textile Manufacturing	UK	63,598	1,904	53	> 30	> 30	GS
16	Battery Manufacturing	UK	12,176	345	34	20-30	10-20	MD
17	Distribution	USA	21,000	5,130	131	> 30	> 30	MD
18	Security Printers	UK	11,826	484	49	> 30%	> 30%	R&DM
19	Manufacturing	USA	56,000	9,080	211	> 30	> 30	MD
20	Packaging/Stationery Manufacture	UK	12,783	424	40	20-30	20-30	MD
21	Luxury Consumer & Writing Products	UK	1,799	194	12	> 30	> 30	MKD
22	Chemical Manufacture	USA	145,787	18,320	215	> 30	> 30	MD
23	Information Publisher	UK	13,000	800	4	10-20	20-30	MD
24	Motor Vehicle Manufacture	USA	47,900	7,895	53	> 30	> 30	MKD
25	Defence Systems Manufacture	UK	42,372	6,664	75	> 30	> 30	GS
26	Engineering	UK	36,737	2,686	65	> 30	> 30	CAM
27	Retailers of Electrical Goods, etc.	UK	18,474	1,755	3	> 30	> 30	FD
28	Fresh Fruit/Vegetable Supplies	UK	5,304	499	12	10-20	10-20	FD

Table 9.5 Summary of Characteristics of Companies in the Survey continued..

Company	Main Activity	Country of Origin	Size of Company[a]		Scope of International Activities[a]			
			Employees	Group Turnover £m	No. of Overseas Outlets	FI/GTI %Range	FIE/GE %Range	Respondent
29	Steel & Engineering Products	UK	10,000	550	35	< 10	5-10	C/CE
30	Packing & Printing Materials	UK	3,204	130	9	10-20	10-20	CS
31	Motor Vehicle Manufacture	Japan	371[+]	436[+]	84	20-30	> 30	MD
32	Chemicals & Paints Manufacture	Germany	2,547	434	33	20-30	20-30	MD
33	Chemicals	UK	133,800	13,171	450	> 30	> 30	CPM
34	Architectural Consultancy	UK	30	1	4	5-10	5-10	MD
35	Gold/Silver/Platinum Refiners	UK	7,179	1,431	28	> 30%	> 30%	CPM
36	Oil Exploration & Production	UK	454	263	59	> 30	20-30	FD
37	Retailing	UK	75,000	5,600	400	N/A	N/A	CPM
38	Building Materials	UK	11,041	638	17	> 30	> 30	R&DM
39	Publishing	UK	20,652	1,242	35	5-10	5-10	GS
40	Cameras	Japan	20,000	1,550	111	> 30	> 30	FD
41	Finance	UK	1,000	597	9	< 10	N/A	R&DM
42	Water Treatment Manufng & Engineering	UK	78,000	6,000	N/A	N/A	N/A	FD
43	Building Materials	UK	27,915	1,460	12	> 30	> 30	CS
44	Communications Systems, computers	Japan	45,200	15,760	462	20-30	> 30	MD
45	Information & Entertainment	UK	27,915	1,460	12	20-30	> 30	CAM
46	Oil	Belgium	23,600	7,450	63	20-30	20-30	CA
47	Wire & Cable Manufacture	UK	7,486	525	13	> 30	> 30	R&DM
48	Telecommunications & Electronics	UK	26,216	1,655	13	> 30	> 30	MD
49	Recorded Music & Entertainment	Netherlands	7,265	1,263	41	5-10	> 30	CS
50	Manufacturing	UK	2,771	172	9	10-20	> 30	R&DM
51	Property & Sea Ferry	UK	64,000	4,578	44	> 30	> 30	CAM
52	Manufacturing	USA	30,000	1,500	24	20-30	20-30	CS
53	Services	UK	140	600	14	> 30	5-10	MD
54	Food Manufacture	USA	31,700	3,670	12	10-20	20-30	CPM
55	Oil & Gas	UK/Netherlands	134,000	47,779	500	> 30	> 30	CAM
56	Food & Catering	UK	3,308	281	34	> 30	> 30	FD

Table 9.5 Summary of Characteristics of Companies in the Survey continued..

Company	Main Activity	Country of Origin	Size of Company[a] Employees	Group Turnover £m	Scope of International Activities[a] No. of Overseas	FI/GTI %Range	FIE/GE %Range	Respondent
57	Retail & Home Furnishing	UK	29,290	1,221	285	10-20	10-20	MM
58	Sugar Refiners	UK	18,000	3,360	50	> 30	> 30	CPM
59	Electrical & Electronic Equipment	Japan	48,000	19,318	481	> 30	20-30	MM
60	Oil Production & Marketing	France	41,200	10,290	243	> 30	> 30	MKD
61	Oil	USA	2,700	251	120	20-30	20-30	CAM
62	Paper & Coating Manufacture	UK	1,557	103	3	10-20	10-20	OD
63	Hotel & Catering	UK	92,900	2,470	8	20-30	20-30	GM
64	Packaging	USA	30,000	1,563	21	10-20	10-20	FD
65	Pharmaceuticals	UK	17,857	1,408	56	> 30	> 30	OD
66	Food & Hygienic Products	UK/Netherlands	296,000	14,102	480	> 30	> 30	MD

Table 9.5 Summary of Characteristics of Companies in the Survey continued..

[a] Figures relate to 1989
+ Figures are for UK operations only

Notation of Respondent's Position

C/CE	Chairman/Chief Executive
CA	Chief Accountant
MM	Marketing Manager
MKD	Marketing Director
FD	Financial Director
GS	Group Strategist (Analyst/Manager/Director)
CPM	Corporate Planning Manager
R&DM	Research & Development Manager
MD	Managing Director
GM	General Manager
OD	Operations Director
CAM	Corporate Affairs Manager
CS	Company Secretary

Table 9.6 Summary of Nationality of Banks in the Survey

Country of Origin	Frequency	Cumulative Frequency	Percent	Cumulative Percent
Australia	1	1	3.2	3.2
Austria	1	2	3.2	6.4
Belgium	1	3	3.2	9.6
Brazil	1	4	3.2	12.8
Cyprus/Greece	1	5	3.3	16.1
Denmark	2	7	6.5	22.6
France	2	9	6.5	29.1
Italy	2	11	6.5	35.6
Japan	4	15	12.9	48.5
Nigeria	1	16	3.2	51.7
Pakistan	1	17	3.2	54.9
Sweden	1	18	3.2	58.1
The Netherlands	1	19	3.2	61.3
Turkey	1	20	3.2	64.5
U.K.	10	30	32.3	96.8
U.S.A.	1	31	3.2	100.0

n = 31

Table 9.7 Summary of Characteristics of Banks in the Survey

Bank	Country of Origin	Bank Size Employees	Scope of International Activities Group Assets £m	FI/GTI % Range	FIE/GE % Range	Respondent
1	UK	116,400	127,616	> 30%	> 30%	SM
2	UK	114,000	125,000	> 30%	10-20%	SM
3	UK	110,000	116,000	10-20	10-20	SM,GS
4	UK	40,000	25,000	< 10	< 10	SM
5	UK	38,000	4,316	10-20	N/A	M
6	Netherlands	35,000	48,425	< 10	< 10	GM
7	USA	32,000	30,800	< 10	< 10	GM
8	UK	28,700	28,700	> 30	> 30	SM
9	Brazil	28,690	2,060	< 10	> 30	GM
10	Italy	26,000	1,046	20-30	20-30	GM
11	Pakistan	25,622	4,479	< 10	20-30	GM
12	UK	24,000	30,096	10-20	10-20	SM
13	Turkey	20,212	5,080	< 10	20-30	AM
14	Denmark	16,500	31,088	< 10	10-20	GM
15	Italy	16,362	39,961	10-20	10-20	GM
16	France	16,300	30,535	N/A	N/A	M
17	UK	15,200	N/A	< 10	< 10	SM
18	Austria	10,932	27,689	< 10	< 10	GM
19	Japan	10,256	26,079	N/A	N/A	AGM
20	Nigeria	8,500	26,600	> 30	> 30	AM
21	Australia	7,084	8,511	< 10	< 10	GM
22	France	7,000	26,395	< 10	20-30	AGM
23	Japan	7,000	N/A	< 10	< 10	M
24	Japan	6,173	5,825	< 10	< 10	GM
25	Sweden	3,800	9,000	< 10	< 10	GM
26	UK	3,200	9,427	> 30	> 30	SM
27	UK	2,500	N/A	> 30	10-20	GM
28	Greece/Cyprus	2,026	1,261	> 30	< 10	M
29	Japan	125+	N/A	> 30	20-30	GM
30	Belgium	43+	N/A	< 10	> 30	MD
31	Denmark	N/A	N/A	> 30	20-30	MD

+ Figure only for UK operations

Respondents

M	Manager
SM	Senior Manager
AGM	Assistant/Deputy General Manager
GM	General Manager
MD	Director/Managing Director

Table 9.8 Industrial Distribution of Firms in Sample

Firm Type	Frequency	Cumulative Frequency	Percent	Cumulative Percent
Banking and Finance	32	32	33.0	33.0
Battery & Cable Manufacture	2	34	2.1	35.1
Brewery & Pub Retailing	1	35	1.0	36.1
Bldng Materials & Allied Products	4	39	4.1	40.2
Chemicals & Paint Manufacture	5	44	5.2	45.4
Computers & Comms Systems	2	46	2.1	47.5
Contracts, Consultancy & Services	3	49	3.1	50.6
Copies & Photographic Equipment	2	51	2.1	52.7
Defence Systems Manufacture	1	52	1.0	53.7
Distribution & Haulage	1	53	1.0	54.7
Electrical & Electronic Products	4	57	4.1	58.8
Food & Agro Products Manufacture	5	62	5.2	64.0
Heavy Engineering & Manufacture	6	68	6.2	70.2
Hotel & Catering	2	70	2.1	72.3
Information and Publishing	2	72	2.1	74.4
Luxury Consumer Products	1	73	1.0	75.4
Metal Refiners	1	74	1.0	76.4
Motor Vehicle Manufacture	2	76	2.1	78.5
Oil & Gas Production & Marketing	6	82	6.2	84.7
Rubber & Plastics Manufacture	5	87	5.1	89.8
Pharmaceuticals	2	89	2.0	91.8
Polymeric Products Manufacture	1	90	1.0	92.8
Property & Transportation	1	91	1.0	93.8
Recorded Music & Entertainment	2	93	2.1	95.9
Retail & Home Furnishing	3	96	3.1	99.0
Textile Manufacture	1	97	1.0	100.0

n = 97

Table 9.9 Position of Respondents

Position	Frequency	Percent	Cumulative Percent
Chairman/Chief Executive	4	4.1	4.1
Managing Director/Gen. Manager	33	34.0	38.1
Divisional Head	44	45.4	83.5
Senior Manager/Manager	16	16.5	100.0

n = 97

9.7.3 SIZE OF FIRMS

The size of firms in the survey was gauged in two ways: financial and by employee.

A. FINANCIAL - COMPANY PERSPECTIVE

Table 9.10 presents the size of companies in the survey as measured by Turnover. The information is as of June 1989. The greater part of the companies (33.4%) have a turnover of between £1 million (No. 34 in Table 9.5) and £500 million. These are small companies that nevertheless have a number of foreign outlets and derive between 5 to 10 per cent of their annual turnover from foreign investment and also commit the same level to foreign operations. For example, that company with £1 million turnover is a UK architectural consultancy company that employs 30 people; has 4 overseas outlets; invests about 8 per cent of its total resources abroad; and derives 10 per cent of its total resources from abroad. Within this group however are mainly the subsidiaries of foreign based multinational companies (e.g. Japanese and German MNCs) that reported only their UK figures.

Just under 32 per cent of the companies have a turnover of between £500 million and £2 billion. About 12 per cent have a turnover of between £2 billion and £5 billion. These three groups put together only account for 22 per cent of the combined turnover of the companies in the survey. However, the list is dominated by 15 large companies (22.7 per cent) with a turnover in excess of £5 billion, in particular by 7 of the companies (10.6 per cent) whose latest revenue was in excess of £10 billion. These 10.6 per cent account for no less than 55.6 per cent of the combined revenue of the companies while the next 12.1 per cent account for 22.3 per cent (Table 9.10). Companies within the 10.6% category include conglomerates such as the major oil companies (Royal Dutch/Shell, BP), ICI, IBM, Japanese MNCs, etc (See Table 9.5 for details).

BANK PERSPECTIVE

Whereas companies speak of size in terms of turnover (among other indices), banks speak in terms of total assets. Table 9.11 presents the size of banks in the survey as measured by Total Assets. The majority of the banks (44%) have assets of between £10 billion and £40 billion. This group accounts for nearly 41% of the combined banks in the survey. However, the list is dominated by the large multinational banks (MNBs) (16%) whose latest total assets range between £40 billion and £130 billion. This group accounts for more than 52% of the combined assets of the banks, with average bank asset of over £104 billion. With a low asset size of £48.5 billion and a high of £127.6 billion, this group consists of the three largest UK clearing banks and one Dutch bank (with £48.3 billion assets). Small banks with assets of between £1 billion and £10 billion make up the balance of 40%, but their combined assets total only 6.5%.

Table 9.10 Summary Size of Sample Companies by Turnover (as of June 1989)

Turnover	Frequency	Percent	% of Combined Turnover	Average Company Turnover (£m)
Under £100m	4	6.1	0.1	46.3
101-500	18	27.3	2.1	289.4
501-1,000	8	12.1	2.1	657.5
1,001-2,000	13	19.7	7.7	1,479.6
2,001-5,000	8	12.1	10.1	3,166.6
5,001-10,000	8	12.1	22.3	6,975.3
over 10,000m	7	10.6	55.6	19,820.0
	n = 66	100.0	100.0	-

Combined Turnover £249,765 million

Table 9.11 Summary Size of Sample Banks by Total Assets (as of June 1989)

Total Assets	Frequency	Percent	Valid Percent	% of Combined Assets	Average Bank Asset (£m)
£1,000m - £4,999m	5	16.1	20.0	1.7	2,632.4
5,000 - 9,999	5	16.1	20.0	4.8	7,568.6
10,000 -39,999	11	35.5	44.0	40.8	29,358.5
40,000-130,000	4	12.9	16.0	52.7	104,260.3
Don't know/Not Available	6	19.4	Missing	-	-
	n = 31	100.0	100.0	100.0	-

Valid Cases 25 Missing Cases 6
Combined Total Assets £790,989 million

B. SIZE OF FIRMS BY EMPLOYEES

The size of the firms in the sample vary widely also in terms of the number of staff employed. Table 9.12 presents a comparative view of the range and percentage of employees across the four groups in the sample. Surprisingly, UK companies by far employ the highest number (48.5%) of staff worldwide relative to other employer groups in the survey. They are followed, as would be expected, by foreign banks and foreign companies, in that order. These account respectively for 21.6% and 19.6% of the total number of people employed worldwide by the firms in the survey. 91 per cent of the firms are largely labour-intensive. Even highly technological manufacturing companies in the survey (i.e. ICI, IBM, Shell, etc) employ over 130,000 people worldwide. The least employer among the companies in the survey is that UK architectural consultant with 30 people. On interview, the managing director of the company revealed that the company subcontracts its overseas operations to local firms and does not regard these as its employees despite the long standing contractual relations with them. In effect, the company secures overseas architectural contracts and subcontracts to local firms under the UK company's control. The highest employer-company in the survey was a UK/Netherlands manufacturer of food & hygienic products with 296,000 employees worldwide as of June 1989 (No. 66 in Table 9.5). For banks, the least and highest reported employers were respectively a Cypriot bank with 2,026 employees worldwide (No. 28 in Table 9.7) and a UK bank with 116,400 employees (No.1 in Table 9.7).

Table 9.12 Summary Size of Sample Firms by Employee (as of June 1989)

Range of Employees	UK Companies Frequency	Percent	Foreign Companies Frequency	Percent	UK Banks Frequency	Percent	Foreign Banks Frequency	Percent	Valid Total Frequency	Percent
1- 999	4	4.1	3	3.1	-	-	2	2.1	9	9.3
1,000- 4,999	8	8.3	4	4.1	2	2.1	2	2.0	16	16.5
5,000- 9,999	5	5.2	1	1.0	-	-	5	5.1	11	11.3
10,000- 49,999	19	19.6	8	8.3	5	5.1	12	12.4	44	45.4
50,000-100,000	7	7.2	1	1.0	-	-	-	-	8	8.2
Over 100,000	4	4.1	2	2.1	3	3.1	-	-	9	8.3
Total/Percent	47	48.5	19	19.6	10	10.3	21	21.6	97	100.0

9.7.4 SCOPE OF INTERNATIONAL INVOLVEMENT

The degree of firms' internationalization was measured in three ways: (1) Foreign investment as a percentage of Total Consolidated Annual Investment (Table 9.13); (2) Foreign investment earnings as a percentage of Total Consolidated Annual Turnover (Table 9.14); and (3) Geographical concentration of overseas activities (Table 9.15). A fourth measure applied to companies only is the number of foreign outlets (Table 9.16). This could not be calculated for banks because of inadequate information.

Tables 9.13 and 9.14 are classified according to whether the firms are small (5%-20%), medium (20%-30%) or large (over 30%). Large banks (54.2%) and medium size companies (44.0%) display a higher propensity towards foreign investment than the other sizes of firms. Small and medium sized banks and large companies depict the most cautious exposure to foreign investment. The apparent caution of small and medium size banks may be attributable to size factor, deregulation and competition. The pattern is somewhat in terms of foreign investment earnings (Table 9.14). Small size banks and large companies appear to display a greater degree of internationalization (with 51.5% and 54.5%) than the other categories, followed by medium size banks (29%)and small companies (27.3%). That trend may be consistent with a cautious investment approach in which firms tend to invest or operate in markets with maximum return/risk.

Table 9.13 Categorization of Firms' Degree of Internationalization (Foreign Investment as Percentage of Total Group Annual Investment)

	BANKS		COMPANIES	
Degree of Internationalization	**MNBs**	**Percent**	**MNCs**	**Percent**
Small (5% to < 20%)	7	22.6	22	33.3
Medium (20% - 30%)	7	22.6	29	44.0
Large (Over 30%)	17	54.8	15	22.7
n =	31	100.0	66	100.0

N = 97

Table 9.14 Categorization of Firms' Degree of Internationalization (Foreign Investment Earnings as Percentage of Total Consolidated Annual Turnover)

Degree of Internationalization	BANKS MNBs	Percent	COMPANIES MNCs	Percent
Small (5% to < 20%)	16	51.6	18	27.3
Medium (20% - 30%)	7	29.0	12	18.2
Large (Over 30%)	6	19.4	36	54.5
n =	31	100.0		100.0

Table 9.15 Overseas Geographic Concentration of Sample Firms

Geographic Area	U.K. Banks n = 10 Percent	Foreign Banks n = 21 Percent	U.K. Companies n = 47 Percent	Foreign Companies n = 19 Percent
Western Europe	33	67	58	42
North America	67	5	34	27
Latin America	*	5	*	*
Far East (incl Japan)	*	14	2	26
Middle East	*	*	2	*
Africa	*	4	2	*
Asia	*	5	2	5
	100.0	100.0	100.0	100.0

* Respondents did not provide data for these areas. On telephone follow-up, they indicated that they did not consider their operations in these areas as bulky, as the question demanded, or of great significance in their global activities. Some said they were divesting in these areas because of hostile government policies, political and economic uncertainty, or simply as part of their global rationalization exercises.

Table 9.16 Scope of Internationalization (Number of Overseas Outlets by Sample Companies)

No. of Overseas Outlets	Frequency	Percent
Under 50	37	56.1
50-100	13	19.7
100-200	6	9.1
200-300	4	6.0
Over 300	66	100.0

Clearly the level of internationalization, as depicted by the number of foreign outlets, is high. 37 Companies have between 4 to just under 50 overseas establishments. In fact, but for the architectural consultancy company with 4 outlets, the rest have at least 8 overseas operations. 6 Companies have over 300 (See Table 9.5).

The geographic concentration of overseas operations (Table 9.15) indicates that UK banks tend to concentrate their overseas activities in North America (67%). In contrast, their foreign counterparts seem to operate predominantly in Western Europe (67%). The position is fairly different with companies, where both UK and Foreign companies maintain greater concentration in Western Europe, with 58% and 42% respectively. Outside Western Europe and North America, the Far East (defined to include Japan) has the next largest concentration of foreign operations, although UK banks appeared not to have any significant presence in the region. Middle East and Latin America seem to be least favourable host regions to the sample foreign firms.

9.8 DETAILS OF INTERNATIONAL ENTRY MODES

In terms of initial entry mode patterns, Tables 9.17, 9.18 and 9.19 respectively provide evidence on the preference of UK companies, foreign companies and banks (UK and foreign). Table 9.17 highlights initial entry mode choices of UK companies by geographic location. Equity Joint Venture (EJV) mode emerges as the dominant pattern both in geographic regions and in total usage. The slight exceptions are in North America and Australia where mergers and acquisitions and wholly/majority-owned subsidiaries are respectively the preferred modes. Licensing appears surprisingly a very low entry mode among UK companies, considering that licensing has historically been associated with technology transfer. The reasons may have to do with the observations of Hood and Young (1986, p.8) that: licensing can potentially inhibit the longer term development of a market, as commonly licensees do not perform up to expectations; and licensing is often associated with contracts for technical and managerial assistance. Of the total 254 modes of entry into the 8 geographical regions, Wholly Owned Subsidiary comes second to EJV with 19.7%, followed closely by mergers and acquisitions with 15.7%. EJV was also the most preferred choice of initial entry into the UK by foreign companies in the sample, followed by mergers and acquisition (Table 9.18).

Table 9.17 Overseas Ownership Patterns of 254 Affiliates of 47 UK MNCs as of June 1990.

Location	WOS	M&A	EJV	NEJV	Licencing	Franchising	Sales Office/ Agency	Management Production Contracts	Greenfield	Valid Total
W. Europe	11 23.4%	9 19.2%	21 44.7%	5 10.6%	-	1 2.1%	-	-	-	47 100.0%
North America	10 21.3%	18 38.3%	17 36.2%	-	1 2.1%	1 2.1%	-	-	-	47 100.0%
Far East (inc. Japan)	4 12.9%	3 9.7%	16 51.6%	2 6.5%	1 3.2%	1 3.2%	3 9.7%	1 3.2%	-	31 100.0%
Australia	15 37.5%	9 22.5%	10 25.0%	-	1 2.5%	-	2 5.0%	2 5.0%	1 2.5%	40 100.0%
Asia (inc. Japan)	2 8.7%	-	14 60.9%	1 4.4%	-	1 4.3%	2 8.7%	3 13.0%		23 100.0%
Middle East	3 12.5%	-	6 25.0%	3 12.5%	-	2 8.3%	4 16.7%	6 25.0%	-	24 100.0%
Eastern Europe	- 10.0%	1 30.0%	3 20.0%	2	-	-	2 20.0%	2 20.0%	-	10 100.0%
Africa	5 15.6%	-	14 43.8%	3 9.4%	-	-	6 18.7%	4 12.5%	-	32 100.0%
TOTAL	50 19.7%	40 15.7%	101 39.8%	16 6.3%	3 1.2%	6 2.3%	19 7.5%	18 7.1%	1 0.4%	254 100.0%

- = Data not available.
WOS = Wholly/Majority-Owned Subsidiary
EJV = Equity Joint Venture
M&A = Mergers & Acquisition
NEJV = Non-Equity Joint Venture

Table 9.18 Initial U.K. Entry Mode Choices by Sample Foreign Companies.

N.F.I. Entry Mode	Frequency	Percent	Cumulative Percent
Equity J.V.	12	63.2	63.2
Acquisition & Merger	6	31.6	94.8
Assembly/Sub-contracting	1	5.2	100.0

n = 19

9.8.1 INITIAL UK ENTRY MODE BY FOREIGN COMPANIES

Equity joint venture appeared to be the most popular mode of entry into the UK by the foreign companies in the sample (Table 9.18). About 63% of them indicated that they first entered into UK markets through EJVs. Acquisition and Merger was the next most popular method, with 31.6% of the firms venturing into the UK first time by it.

9.8.2 ESTABLISHMENT MODES OF INTERNATIONAL BANKING

For banks, branch network remains the most popular mode of establishing abroad (32.3%). Table 9.19 below shows branch banking, representative office, subsidiary banking and joint venture banking, in that order, as the preferred organizational modes of international banking. However, strict national regulations on branch banking means that, although banks would naturally show a preference for it, the frequency of its use on a global scale might be low. On the other hand, organizational modes promising less foreign control might have favour with many host governments. As Table 9.20 below illustrates, correspondent and representative offices are the most frequent organizational modes used by banks (both UK and Foreign alike), although the trend is in reverse order of frequency with foreign banks. Foreign affiliates/associates, joint venture banking and merchant banking services are widely used, in that order. It is still early days for overseas cash lines, despite their domestic popularity.

Table 9.19 Establishment Modes of International Banking: Initial Entry Mode Choices of Sample Banks

Entry Mode	Frequency	Percent	Cumulative Percent
Subsidiary banking	5	16.1	16.1
Branch banking	10	32.3	48.4
Representative Office	7	22.6	71.0
Correspondent Office	2	6.4	77.4
Joint Venture Banking	4	12.9	90.3
Mergers & Acquisition	2	6.5	96.8
Merchant Banking	1	3.2	100.0

n = 31

Table 9.20 Utilization Frequency of Establishment Modes (U.K. Banks and Foreign Banks).

ORGANIZATIONAL MODE	UK BANKS (n=10) PERCENT	FOREIGN BANKS (n=21) PERCENT
Foreign Affiliates/Associates	80.0	54.5
Representative Offices/Agencies	80.0	90.9
Correspondent Offices	90.0	77.3
Joint Venture Banking Arrangements	70.0	50.0
International Merchant Banking Services	70.0	40.9
Overseas Cash Line Services	40.0	9.1

9.9 SIGNIFICANCE OF SPECIFIC CLAUSES IN CONTRACTUAL ARRANGEMENTS

Specific and general terms are important features of contractual arrangements (discussed in Chapter 6). These clauses are crucial both in determining the bargaining power of the parties and in setting the operational boundaries and performance requirements of the parties in contractual terms. They also provide the basis for deciding royalty payments. Table 9.21 lists nine factors identified from the literature as likely to determine the outcome of international contractual arrangements. Because contractual arrangements are particularly used by companies, the question was restricted to companies.

Table 9.21 Importance of Specific Tie-in Clauses in Contractual Agreements.

Tie-Clause	% of Companies Citing Particular Clause as being Significant	Total Number of Companies Giving a Response
Machinery and equipment supply	80	45
Technical assistance in production	86	49
Technical assistance in plan design and construction	81	48
Technical assistance in procuring/supplying inputs & components	75	48
Technical assistance in marketing and management	63	46
Personnel training	62	47
Right for utilization of patents, trademarks, etc.	60	48
Right for utilization of design	32	47
Right to the use of advertising materials	9	45

Note: Replies were to the question: How significant is each of the following factors in contractual agreements (eg. licensing, turnkey arrangements, etc?) The possible replies range from Very Significant (1) to Very Insignificant (5). In this table 'Very Significant' and 'Significant' replies were combined, and so were 'Very Insignificant' and 'Insignificant' replies

Table 9.21a Specified Length of Time in Technical Agreements.

SPECIFIED LENGTH OF TIME IN TECHNICAL AGREEMENTS

Years	Frequency	Cumulative Frequency	Percent	Cumulative Percent
Not less than 5 years	8	8	50.0	50.0
5-10 years	5	13	31.2	81.2
10-15 years	2	15	12.5	93.7
Not less than 20 years	1	16	6.3	100.0

The managers of the multinational companies were asked to identify the most significant items they would consider in contractual agreements. Of the firms replying to each question, 86 per cent stated that technical assistance in production was the most important item in a contractual agreement; 81 per cent regarded technical assistance in plant design and construction as significant; 80 per cent stated that machinery and equipment supply was significant for them; and 75% considered technical assistance in procuring/supplying inputs/components as significant in contractual agreements. These items are all concerned with firm-specific advantages in technology.

Essentially, these items are inextricably linked with patents, trademarks and know-how. In general, these items are linked to one another and in many cases form part of the MNC's package of resources in international licensing, franchising, turnkey contracts or subcontracting. These findings are consistent with those of earlier studies (see, for example, Telesio, 1979; Monye, 1989).

Given the importance of specific features of contractual agreements, respondents were asked if there was a specified length of time in their technical agreements. 75.8% (i.e. 50) of the sample companies answered NO, meaning that there is no specified length of time in such agreements. Of the 16 companies (i.e. 24.2%) that answered in the affirmative, 50% of these indicated that the duration of such agreements was at least 15 years; 31.2% for 5 to 10 years; and 12.5% for 10 to 15 years. For one company, the minimum acceptable length of time is 20 years (Table 9.21a). The findings underscore the strategic importance of new forms of international investment.

9.10 MOTIVATIONS FOR NEW FORMS OF INVESTMENT

Respondents were asked to identify and rank, in order of relative importance, a list of 9 motivations for adopting new forms, broadly defined in the questionnaire as non-equity forms of foreign investment (Table 9.22). These motivational statements were informed by literature review and have been postulated in the literature as reasons favouring the use of new forms. An assessment of respondents' views indicates that the foremost reason why companies adopt new forms is to achieve international diversification. 74% of sample UK companies (Table 9.22) regard international co-operative arrangements as a way by which international diversification can most easily be achieved.

'Host government FDI regulations' and 'high political risk in host country' follow closely in that order, with 67% and 63% of UK companies citing them as particularly important. Firm size, denoting managerial and financial capacity, was least important, suggesting that capital constraint and organizational skills are not decisive factors for UK companies contemplating going abroad.

Table 9.22 Average Occurrence of Reasons for Adopting New Forms of International Investment by UK Companies Abroad

Rank	Reason for adopting new forms	% of companies citing particular reason to be of significance	Total Number of responding companies
1	Achieve international diversification via cooperative arrangements with local partners	74	36
2	Host government regulations/pressure restricting inward foreign direct investment	67	35
3	High political risk in host country (eg. risks of expropriation)	63	34
4	Risk diversification (ie. reduction) through cost/risk sharing with local partner/s	52	35
6	Reciprocal exchanges of technology/ high costs of technology	49	30
8	Because competitors adopt non-equity contractual forms	27	29
9	Size of firm too small to finance, manage and/or market overseas operations	21	31
5	Products customized to host/regional market	51	37
7	Protect/support existing foreign business	36	31

Note: Chief Executives of sample firms were asked to tick and rank in order of strategic importance the following motivations for adopting new forms of international investment (defined broadly as non-equity/ cooperative/contractual modes of foreign market entry). (Answers were 1=Most Important, 9=Least Important).

Table 9.23 Average Occurrence of Reasons for entering into UK via New Forms of International Investment by Foreign Companies.

RANK	Reason for adopting new forms	% of Companies citing particular reason to be of importance
2	Achieve international diversification via cooperative arrangements with host country partners	84
9	Reciprocal access to technology/high cost of technology	41
10	Because competitors adopt non-equity/flexible forms of entry	37
4	Size of firm too small to finance, manage and/or market overseas operations	68
8	High cost of establishing a foreign subsidiary	44
3	Strong market competition	76
6	Entry into UK as a gateway to wider EEC markets	53
5	Products customized to UK/EEC markets	64
7	UK Governments investment policy	47
1	Global profitability and increased market share	89

A similar survey was carried out among foreign companies operating in the UK. The chief executives of foreign companies in the UK were asked to tick and rank in order of strategic importance the motivations for adopting new forms of investment, with special reference to their entry into the UK. 89% of the companies responding cited global profitability and increased market share as the foremost reason for adopting new forms. The second and third reasons are closely linked with the goal of global profitability, namely, 'achieve international diversification...' and 'strong market competition', respectively. Unlike their UK counterparts, foreign companies regard firm size as an important factor for using new forms (rank 9 versus rank 4). Because the UK market is more advanced and open than that of most developed and developing countries, the questions reflected that position. However, an overall assessment of the reasons for adapting new forms shows a great deal of similarity between UK companies (Table 9.22) and foreign companies (Table 9.23).

Table 9.24 Organizational Influences on Entry Mode Choices

RANK		No of Times Cited As Being Influential	Percent
1	Managing Director/Chief Executive	33	34.0
2	Corporate Strategy/Development	16	16.5
3	Operations	15	15.5
4	Finance Director/Chief Accountant	11	11.3
5	Marketing	9	9.3
6	Board of Directors	8	8.2
7	Corporate Affairs/Investor Relations	5	5.2
		n=97	100.0

9.11 ORGANIZATIONAL INFLUENCES ON ENTRY MODE CHOICES

Decision-making has been undoubtedly one of the topical issues in the field of management. There is equally little doubt that decision-making is one of the most crucial attributes of successful management, leading experts such as Drucker (1954), Simon (1957), etc., to consider it synonymous with management. Drucker has argued that the major obstacle to organizational growth is managers' inability to change their attitudes and behaviour according to the requirements of their organizations. Thus, the role of management in corporate investment decisions is non-controversial. Corporate management encapsulates what is regarded in strategic management as the 'entrepreneur' (Casson, 1982, 1985; Teece, 1984; Ansoff, 1986; Buckley, 1989). However, there has been controversy, or a difference of emphasis, over the precise role of corporate management in international investment decisions (Casson, 1985, p.172). Further, because of the emphasis on equilibrium analysis within received theory, the role of corporate management tends to be downplayed, if not outright suppressed (Teece, 1984).

In order to investigate the strategic role of corporate management in the internationalization process, respondents were asked to identify and rank the influence of various organizational incumbents on their firm's entry mode choices. Table 9.24 gives the average rating for each member of corporate management. Clearly, the firm's chief executive or managing director, as the case may be, represents the most influential organizational agent in the international move. 34% of the sample firms ranked the chief executive highest. It is not however a surprising result in that the chief executive, who in all probability is also a member of his firm's board of directors, is the principal decision maker in the organization. His effectiveness lies in matching the potential capacity of the organization to meet environmental demands. Potential capacity, in turn, refers to the optimal match of the chief executive's decision styles, task demands and organizational climate (Driver and Rowe, 1979).

The chief executive, as the name implies, is *primus interpares*, that is 'first among equals'. To this end, 16.5% of the respondents cited corporate strategy/development unit of their firms as the next organizational influence in their internationalization process. Following this department closely are the operations department and the finance department, in that order, with 15.5% and 11.3% of the respondents citing them as potentially influential in entry mode choices. This order will appear to be both logical and pragmatic from a strategic point of view. There is little doubt that before any final decision is made on pattern of accomplishing foreign investments, these divisional managers will have put together a dossier for the chief executive, perhaps for onward presentation to the board of directors, specifying the strategic contribution and impact of suggested patterns on their units. The head of finance, for example, will have to develop the cash flow implications of licensing abroad, subcontracting, joint venture arrangements or direct investment for that matter.

The relative insignificance of the board of directors or corporate affairs department may not, for practical purposes, be surprising. In particular, non-executive board members tend to rely on the rationality of their executive counterparts who may be the authors of a proposed mode of entry. In the words of Lenz and Lyles (1989), "many board members, despite good intentions, have an inadequate understanding of both current strategy and broad issues affecting strategic success." To the besieged board of directors, therefore, the appearance of certainty conveyed by its chief executive supported by divisional heads is alluring. Executives can then present to board members an entry mode choice that has the trappings of profitability and shareholder wealth maximization. The findings here are consistent with those of Reid (1981) and Welch (1983, 1990). The authors found the influence of decision-makers to be very significant in the internationalization of Australian franchisors.

CHAPTER TEN

STATISTICAL ANALYSIS OF RESEARCH FINDINGS

CONTENT

CHAPTER TEN
STATISTICAL ANALYSIS OF RESEARCH FINDINGS

10.1 MANAGERIAL ASSESSMENT OF FIRM-SPECIFIC CHARACTERISTICS AND USE OF NEW FORMS

The purpose of this chapter is to test the hypotheses developed in Chapter Nine, using the statistical techniques described in Appendix 5. The analyses of findings are pursued in the order of the hypotheses.

> H_1: The adoption of new forms by a firm in foreign market development is significantly influenced by managerial assessments of firm-specific characteristics.

This hypothesis seeks to explore the extent to which the perceived importance of firm-specific characteristics determines the outcome of entry mode decisions. Certain factors have been identified in the literature as firm-specific advantages or characteristics. These are essentially in the form of ownership and internalization advantages (Dunning, 1977, 1979, 1981, 1988; Rugman, 1979, 1980, 1982). A firm's ownership advantages in relation to international move include: (1) its size (denoting corporate capability); (2)experience of foreign markets; and (3) possession of brand name, trademarks, etc. Similarly, its internalization advantages may manifest in: (1) its willingness to share ownership and control in return for access to local markets; (2) minimization of country risks; and (3) economies of scope and geographical diversification. Much of the empirical analyses focus on these factors as dependent variables. The emphasis of this hypothesis is on how they are perceived by decision-makers and how differences in perception may affect the outcome of organizational choice of foreign market entry mode.

Cooper (1979) has argued that many of the serious problems confronting industrial and public service organizations centre on 'people aspect of company life.' O'Toole (1979) characterizes the problem as that of 'differences in firm cultures.' Precisely, he argues that: as no two managers are alike no two corporations are identical: they differ by industry, product line, technology, size, age, nature of ownership, geographic location, and so forth (ibid, p.17). Firms also differ in more subtle structural aspects, an understanding of which can lead to a better understanding of organizational behaviour and the overall performance of the firm.

A transactional cost analysis integrating entrepreneurship first requires a recognition that: in neoclassical economics the manager is responsible for deciding upon and implementing the production plan; in institutional economics he is also responsible for choosing institutional arrangements and thereby determining the boundaries of the firm (Casson, 1985). It also requires that differences in firm cultures exist and that situations and environments can change in a way that a once-appropriate culture might become dysfunctional to the long-term survival of an organization (O'Toole, 1979, p.19). Received foreign investment theories have ignored these firm cultural differences, and in the process have suppressed the role of the entrepreneurship in foreign investment decisions - a point duly recognized by Professors Buckley, Casson and Dunning (the Reading School). One way to operationalize the foregoing is to restate the static economic models of systems in ways which permit dynamic features of the firm to be recognized and investigated. The hypothesis of interest offers a means of determining the extent to which perceived differences in 'firm cultures' affect entry mode decisions.

Five levels of perception were applied in assessing the significance of certain firm-specific advantages (as identified above). The assessments were made on inter-firm sample level, that is, UK companies versus Foreign companies, and UK banks versus Foreign banks. Corporate managers were asked to assess the significance of the identified firm characteristics in their firms' choice of mode of entry into a foreign market. Tables 10.1.1 and 10.1.3 show the results for companies and banks, respectively. For company executives, size was perceived to be the most important ownership advantage, with foreign companies attaching more importance to it than their UK counterparts (mean score 1.368 versus mean score 1.769). 'Experience of foreign markets' and 'willingness to share ownership and control in return for access to local markets' were perceived to be significant, in that order, by UK companies (mean score 1.854 each). UK companies also perceived 'minimization of country risks' as the fourth significant (internalization) factor affecting the choice of entry mode. On the other hand, their foreign counterparts perceived the significance of these factors somewhat differently, ranking them 3, 4, 2, respectively. Not only that, they were more sensitive to their importance as entry mode determinants, as shown in their respective mean scores and standard deviations, than their UK counterparts. Ownership advantages that derive from property rights (e.g. brand names and trade marks) are least important to U.K. companies as are advantages of common governance (e.g. economies of scope) least important to foreign companies.

These observations do not tell much about the effect of the observed differences in mean scores on entry mode choices. Suppose we assume in the research question that the observed differences in the mean scores of firm-specific advantages (FSAs) for the two sample groups (UK companies and Foreign companies) are merely a function of sampling error and that these two groups of samples are really drawn from populations that have the same mean. If this were true, the implication would be that differences in managerial assessments of FSAs do not affect discrimination entry mode choices. Thus,we have:

H_0: $\mu_K = \mu_F$

where K = UK company variable

F = Foreign company variable.

Table 10.1.1 Questionnaire Responses by Managers, Concerning the Significance of Firm-Specific Advantages (FSAs) in the Choice of Mode of Entry into a Foreign Market (Scale: 1=Very Significant to 5=Very Insignificant).

	Firm Specific Advantages	U.K. n = 47 Rank	Mean	Standard Deviation	FOREIGN n = 19 Rank	Mean	Standard Deviation
O	Size of company	1	1.769	0.872	1	1.368	0.496
O	Experience of foreign markets	2	1.854	0.478	3	1.579	0.507
I	Willingness to share ownership and control in return for access to local markets	3	1.854	0.882	4	1.684	0.582
I	Minimization of country risks	4	1.952	0.795	2	1.474	0.513
I	Economies of scope and geographical diversification	5	2.093	0.684	6	2.000	0.471
O	Possession of brand name, trade marks etc.	6	2.390	0.945	5	1.842	0.688

O = Ownership-specific advantage
I = Internalization-Incentive advantage

Table 10.1.2 Significant Differences in Mean Scores of FSAs as Entry Mode Determinants: UK Vs Foreign Companies.

			Pooled Variance Estimate		Separate Variance Estimate	
FSAs	**F-Value**	**Signif**	**t-statistic**	**Signif.**	**t-statistic**	**Signif.**
Minimization of country risks.	2.40	0.048	2.40	0.019	2.82	0.007*
Possession of brand name, trade marks etc.	1.89	0.148	2.26	0.028	2.54	0.015*
Experience in foreign markets.	1.13	0.725	2.03	0.047	1.99	0.055**
Size of company.	3.10	0.012	1.86	0.069	2.23	0.030*
Willingness to share ownership and control in return for access to local markets.	2.29	0.061	0.76	0.449	0.88	0.381
Economies of scope and geographical diversification.	2.10	0.090	0.54	0.592	0.62	0.539

* $p < 0.05$ ** $p < 0.10$

The alternative hypothesis is that the two groups are really samples from populations with different mean scores and the disparity between the observed sample means reflects the difference in their population values. This suggests that the different perceptions or assessments (as evidenced by their mean scores and rankings) indeed do produce a difference in entry mode choices. Symbolically, that is

H_1:μ_K is not equal to μ_F

To test the hypothesis, a series of t-tests was carried out. Two observations are noteworthy here. First, the statistical hypotheses are stated in terms of population parameters not statistics. This is because the decision to be made really involves what is true about the population/s, companies in general, not just about the two samples observed in this experiment. Second, the alternative hypothesis above does not specify whether μ_K is greater or less than μ_F. It just states that the population means for each variable (FSAs) are different. This implies that the statistical test should be sensitive to differences in either direction, $\mu_K > \mu_F$ and $\mu_K < \mu_F$, requiring a non-directional or two-tailed test. A summary of the test of the hypothesis is presented in Table 13.1.2. These procedures have been discussed in Appendix 5 and as explained, the SPSS prints two variance estimates: pooled or separate. The use of one or the other depends on whether equality of variance can be assumed. Norusis (1986, p.208) advises the use of the SEPARATE VARIANCE ESTIMATE whenever the researcher suspects that the variances are heterogenous, as might be expected in a behavioural science research.

The fundamental assumptions of using the t-test are fully met. First, the two sample variances (UK companies and Foreign companies, or banks as the case may be) are <u>independent</u> and sampling is <u>random</u>. Second, the population distributions of the two groups are <u>normal</u> or the samples are large (McCall, 1970).

As shown in Table 10.1.2, apart from experience in foreign market whose F-value is large (1.13) with the probability of .725, the probability levels of the other factors justify using the separate variance estimate. 3 of the 6 firm-specific factors were found statistically significant at less than 5% level, with another significant at less than the 10% level. These are: minimization of country risks (.007), possession of brand name, etc (.015), size of company (.030), and experience in foreign markets (.055).

The observed significance level in each case is the probability that the sample companies could show a difference at least as large as the ones observed in the managers' perceptions, if the population means are really equal. This result leads to a rejection of the null hypothesis of no difference between means. It implies that the observed difference between the mean scores is too remote to have probably occurred by sampling error alone and that the magnitude of difference in managerial perceptions does determine entry mode choice. However, the evidence from two FSAs, namely willingness to share ownership and control, and economies of scope and geographical diversification leads to an acceptance of the null hypothesis of no difference between mean values. No statistically significant differences between the mean values of comparative measures were found. Thus, the relationship between managerial perceptional entry mode choice is only in respect of the above four factors.

EVIDENCE FROM BANKS

The sample banks agree almost on the same level in their perceptions of the importance of certain Bank-specific advantages (BSAs) (Table 10.1.3). Possession of large international corporate customers is perceived as the most important BSA. While UK banks are more sensitive to minimization of country risks (rank 2 versus rank 4), foreign banks seem to attach greater importance to experience in foreign banking/market. With this exception all the other factors are evenly perceived by both groups.

Table 13.1.3 Questionnaire Responses by Managers, Concerning the Significance of Bank-Specific Advantages (BSAs) in the Choice of Mode of Entry into a Foreign Market (Scale: 1=Very Significant to 5=Very Insignificant).

		U.K. n = 10			FOREIGN n = 21		
Bank Specific Advantages (BSAs)		**Rank**	**Mean**	**Standard Deviation**	**Rank**	**Mean**	**Standard Deviation**
O	Possession of large international corporate customers.	1	2.000	0.500	1	1.842	0.834
I	Minimization of country risks.	2	2.000	1.225	4	2.105	0.875
O	Size of bank.	3	2.111	1.167	3	2.000	0.816
O	Experience in foreign banking.	4	2.200	0.789	2	2.000	0.745
I	Cost of establishing a foreign subsidiary/ branch.	5	2.333	0.500	5	2.158	0.898
I	Economies of scope and geographical diversification.	6	2.556	0.726	6	2.278	0.752
I	Willingness to share ownership and control in return for access to local markets.	7	2.556	1.509	7	2.632	0.955

O = Ownership-specific advantage
I = Internalization advantage

Similar t-tests were carried out to determine the effect of the observed indifference on mean scores on entry mode choices. The null hypothesis is the same as that tested for companies above. In other words, how likely is it to see a difference of the magnitude indicated by each dyad of mean scores if, in fact, there is no difference in managerial perceptions between the sample groups in the population? The result of this test (Table 10.1.4) indicates that the difference between the mean values of comparative measures is not statistically significant at the 5% level.

Table 10.1.4 Significant Differences in Mean Scores of BSAs as Entry Mode Determinants: UK Vs Foreign Banks

	F-Value	Pooled Variance Estimate Signif	t-statistic	Separate Variance Estimate Signif.	t-statistic	Signif.
Economics of scope and geographical diversification	1.07	0.970	-0.91	0.369	-0.93	0.368
Experience in foreign banking	1.12	0.796	-0.67	0.506	-0.66	0.517
Cost of establishing a foreign subsidiary	3.23	0.095	-0.54	0.591	-0.66	0.514
Possession of large international corporate customers	2.78	0.143	-0.52	0.606	-0.62	0.540
Size of bank	2.04	0.199	-0.29	0.772	-0.26	0.801
Minimization of country risks	1.96	0.225	0.26	0.796	0.23	0.821
Willingness to share ownership and control in return for access to local markets	2.50	0.102	0.16	0.872	0.14	0.892

Looking at the separate (or even pooled) variance t-test (Table 10.1.4 above), the smallest observed significance level associated with a t-value of -0.93 is .37. This implies that 37% of the time a difference of at least this magnitude would occur when the two population means are equal. There appears not to be much reason to believe that the means differ in the population. Casual observation of Table 10.1.3 tends to support this, as the mean scores and the rankings of the bank-specific advantages are somewhat evenly matched among the two groups. This finding however partly contradicts, and partly corroborates, the company evidence (Table 10.1.2). In contradicting it, the result suggests that in respect of banks there is no relationship between managerial perceptions of BSAs and entry mode choices. The company evidence corroborates the bank own only in respect of: willingness to share ownership and control in return for access to local markets, and economies of scope and geographical diversification.

To the extent that managerial perceptions differ between the groups, that is, the scores in one group are higher than those in the others, the several averages will be unequal. The mean values are not likely to be precisely equal but, under a null hypothesis of identical population distributions, will differ because of sampling error. The general rationale is that if the sample groups are distributed in the same way and with the same central tendency, then the averages of the ranks for the four sample groups should be approximately equal, implying no differences in perceptions and even if they occur, do not affect discrimination entry mode choices because such differences would have been due to sampling error. It is hypothesised that there is no difference between the perception score of UK banks, Foreign banks, UK companies and Foreign companies.

In order to verify whether the population distribution from which the samples were drawn are identical and whether the differences in perception of firm-specific advantages are due to sampling error, in which case may not affect entry mode choices, the Kruskal-Wallis test for K samples was carried out. The result of this test, presented in Table 10.1.5, indicates that the difference between the mean values of the following comparative measures is statistically significant at the specified percentage levels:

1. Willingness to share ownership and control, at .1% level.
2. Minimization of country risks, at 10% level.
3. Cost of establishing a foreign subsidiary, at .1% level.
4. Size of firm, at 10% level.
5. Experience in foreign markets, at 10% level.
6. Competitors' pattern of entry, at 5% level.

While providing evidence to reject the null hypothesis at the various significance levels, the analysis suggests that the probability that such a difference between means relative to the variability of such differences could occur merely as a function of sampling errors is so small in the above six variables that it is likely that the dyad means are from samples drawn from two different populations. The implication is that differential managerial assessments (at least with respect to these six factors) produce differences in entry mode decisions likely to lead to choice of new forms.

Interview sessions with respondents seem to corroborate this evidence. When interviewees were asked how managerial perceptions had influenced the choice of one mode or another, or, in fact, how such perceptions had influenced movement into international markets, the impression gained from both UK and Foreign managers (banks and companies) is that the various catalysts (listed in the above tables and others that have been used to explain FDI) appeared to depend heavily on how they were perceived by the chief executives of the various firms. One chief executive of a UK company put it bluntly: "I don't care what attractions a particular market has, if I think that the overall interests of my company might not be best served operating in that country, I'll not."

Another executive said that the type of follow-through which any international interests and enquiries might generate from his company varied considerably according to his perceptions and commitment to international move. The average impression gained from the interviews was the same, that is: while economic circumstances of the firm may induce it to invest abroad and/or adopt one particular mode or another, the decision-maker's influence is crucial to the choice and such influence is informed largely by the decision-maker's assessment or perception of the strategic nature of firm-specific advantages.

These findings support earlier studies (Walker and Etzel, 1973; Reid, 1981; Rosson and Reid, 1987; Welch, 1983, 1990) on the influence of the decision-maker on international entry. These findings also corroborate both the neoclassical and institutional economics roles of the manager (Casson, 1985) in which he is responsible for deciding upon and choosing the technique for implementing the foreign production plan, on the one hand, and responsible also for choosing institutional arrangements for accomplishing international transactions, on the other hand.

Table 10.1.5 Kruskal-Wallis One-way Analysis of Variance Test of Significance of Differences in the Importance of FSAs to Entry Mode Choices.

Independent Variable	UK Banks n = 10 Mean	SD	Foreign Banks n = 21 Mean	SD	UK Companies n = 47 Mean	SD	Foreign Companies n = 19 Mean	SD	Kruskal-Wallis @	Chi-Square Probability @
Willingness to share ownership and control.	2.56	1.51	2.63	.96	1.85	.88	1.68	.58	11.6477	.0087*
Minimization of country risks.	2.00	1.22	2.11	.88	1.95	.79	1.47	.51	6.5635	.872***
Cost of establishing a foreign subsidiary.	2.33	.50	2.16	.90	1.85	.48	1.58	.51	12.0327	.0073*
Size of firm	2.11	1.17	2.00	.82	1.77	.87	1.37	.50	7.4868	.0579***
Experience in foreign markets	2.20	.79	2.00	.75	2.39	.95	1.84	.69	6.4493	.0917***
Possession of corporate customers/brand name, etc.	2.00	.50	1.84	.83	2.09	.68	2.00	.47	2.7987	.4237
Economics of scope and geographic diversification	2.56	.73	2.28	.75	1.67	.58	N/A	N/A	5.8903	.1171
Competitors' pattern	3.40	.84	1.50	.71	2.13	1.46	1.73	.59	4.3463	.0371**

@ Corrected for Ties
* Significant at.1 percent
** Significant at 5 percent
*** Significant at 10 percent

10.2 THE FIRM GLOBAL STRATEGY DIMENSION

H_2: The adoption of new forms in the internationalization process is positively related to the firm's global strategies/objectives, ceteris paribus.

The object of this hypothesis is to assess the significance of firms' global objectives or strategies on the outcome of international entry mode choices. Put differently, to what extent does firm strategy and competitive position relative to industry rivals influence corporate acceptance/use of new forms. Franko (1989) addressed a similar question under the "Wells effect" or the propensity of smaller, lower-market share firms within an industry to utilize proportionately more non-FDI modes than industry leaders. Firms become global for a variety of reasons, including those identified in Table 10.2.1. The extent to which these reasons become important and induce international entry varies from one enterprise to another. As Kotter and Schlesinger (1989) have observed, the strategic options available to managers can be usefully thought of as existing on a continuum, the significance/adoption of one or a combination thereof depends on situational factors (the firm's internal and external forces).

A related question with which this hypothesis is concerned is: To what extent are new forms of investment characteristic of particular industries, but not of others? The former are characterized as "dominant", industry leaders with oligopolistic global strategies. Their risk-profile matching behaviour in a sector would push follower firms to adopt "flexible" ownership policies and strategic profiles in attempts to match leader firms' geographical scope (Vernon, 1974; Vernon and Wells, 1976; Knickerbocker, 1973).

Follower companies are deemed to lack the technological, financial or managerial capabilities necessary to fully take on foreign and host country rivals, and particularly host country and investment risks and challenges via wholly-owned subsidiaries (Franko, 1989). The schematic image is that Shell will endeavour to follow Exxon, Jaguar will try to follow and Ford Motors, Pepsi Cola will follow Coca Cola, Compaq computers will follow IBM, and Wimpy will follow McDonald's, but whereas McDonald's refused contractual/co-operative arrangements and Coca Cola avoided them, Wimpy and Pepsi Cola would accept them in a bid to 'catch-up.'

Table 10.2.1 Questionnaire Responses by Managers, Concerning Motivations for New Forms: Evidence from UK and Foreign Companies.

	U.K. n = 47			FOREIGN n = 21		
Motivation	**Rank**	**Mean**	**Standard Deviation**	**Rank**	**Mean**	**Standard Deviation**
Achieve international diversification via international co-operative arrangements.	1	1.833	1.699	1	1.677	0.970
Host government regulations (restricting fdi to selected sectors only, and requiring local equity participation in the rest).	2	2.588	1.811	2	2.000	1.374
High political risk in host country.	3	3.030	1.425	3	4.684	1.565
Risk diversification through cost/risk sharing with local partner/s.	4	4.206	1.122	6	5.000	2.108
Reciprocal exchanges of technology/high costs of technology.	5	4.552	1.292	8	7.059	2.015
Protect/support existing foreign business.	6	5.967	1.921	7	6.111	2.272
Products customised to host/ regional market.	7	5.971	2.203	5	4.786	2.007
Because competitions adopt flexible forms of foreign investment.	8	7.000	1.336	9	7.474	1.307
Size of firm too small to finance, manage or market overseas operations.	9	7.677	2.286	4	4.714	0.756

Range 1-9 1 = Most Important 9 = Least Important

The use or acceptance of new forms in general, and of any mode in particular, has *inter alia* industry-sector dimensions. More importantly, it has serious and often overlooked company strategy dimension (ibid). It has been said that the essence of strategy formulation is coping with competition (Porter, 1979). Franko uses this company strategy dimension to argue that in oligopolistic competitive industries in particular, it is firm strategic differences and not 'cultural differences' which may explain the more frequent use of new forms by Japanese, French, Italian and German firms than their U.S., U.K., Swiss and Dutch counterparts (1976). Following Franko's (1989) specific (i.e. minority joint venture) proposition, it can more generally be proposed that firm acceptance or use of new forms varies inversely with identifiable corporate competitive postures and strategies with respect to industry rivals.

Franko and other writers have used the Wells effect to hypothesize a relationship between MNE strategy and the propensity to accept or use new forms of investment. Presumably, significant differences in the incidence of new forms should be related to differences in global strategies or diversification strategies. Differential frequency analyses (Tables 9.22 and 9.23) have provided evidence which appear to support the notion that firms go international for a variety of reasons. Using measures of central tendency and dispersion, the characteristics of the frequency distributions are made more precise for analysis. For example, both the degree or level of importance and comparative sensitivity of each factor are portrayed using the mean and standard deviation.

Table 10.2.1 indicates that the most important motivational factor was the desire for international diversification with minimum resource/risk commitment. While multinationals may be keen to diversify, they show a cautious approach by collaborating with local partners. Foreign companies in aggregate exhibit this propensity more (mean score 1.677) than the UK companies (mean score 1.833). Also, Foreign companies are significantly more sensitive to the capacity to finance/manage overseas operations (rank 4 mean score 4.714) than their UK counterparts (rank 9 mean score 7.677). UK managers, in contrast, perceive risk diversification through local participation as a stronger incentive than do their foreign counterparts (rank 4 mean score 4.206 versus rank 6 mean score 5.000). Differences in ranking and sensitivity in the other strategic factors are shown in the table.

To test whether differences in global strategies have any effect on entry mode choices, the Mann-Whitney U test was carried out. The logic of this test centres on the idea that if the rankings of one sample group differ greatly from the rankings of the second sample group, then it can be concluded that there is a difference in central locations of the populations (Groebner and Shannon, 1985, p.632). In this case, the test statistic is not only sensitive to differences between the mean scores but also sensitive to both the central tendency of the scores and their distribution. Because the strategic policy of the firm incorporates an assessment of a totality of factors which potentially shape the 'mission' of the firm (Rugman, et al, 1986, p.325), the null hypothesis is thus stated in more general terms: differences in firms global strategies have no effect on entry mode choices.

Table 10.2.2 Mann-Whitney U Test of the Significance of Differences in Motivations For Use of New Forms Between UK and Foreign Companies.

Global strategy/objective favouring new forms	Number of Cases	Mann-Whitney U Test Z-Statistics	Significance
Achieve international diversification	66	1.7860	.0142***
Host government regulations restricting fdi	66	24.2596	.0000*
High political risk in host country	66	28.6151	.0000*
Risk diversification through cost/risk sharing	66	10.5220	.0022**
Size of firm too small to embark on overseas operations alone (as measured by Turnover)	66	4.3764	.0064**
(as measured by Employees)	66	3.1811	.0203***

* Significant at .01 per cent
** Significant at .10 per cent
*** Significant at 1 per cent

Table 10.2.1 shows that the average responses of UK companies are generally lower for most of the nine global strategies. This is exhibited in the ranking, though the ranking is unchanged for the first three strategic factors. This difference is significant for the following strategic factors (Table 10.2.2):

(1) Achieve international diversifications;

(2) Host government regulations restricting fdi;

(3) Avoid high political risk in host country;

(4) Risk diversification through cooperative arrangements with local partners; and

(5) Firm size (as measured by both turnover and employees).

The implication for the hypothesized relationship is that these factors may be seen to increase the basis and likelihood of international possibilities via new forms. The five factors are linked to one another and may be expressed differently by different firms, but their importance lies in their contribution to the analysis of foreign investment decisions, especially when information is restricted and interdependence between firms is recognized (Buckley, 1990, p.19). Differences in motivational values between individual firms reflect different preferences, abilities, endowments of wealth, entry mode choices, etc. Differences in the average values of parameters between microeconomic units reflect differences in both individual and corporate attitudes, economic structures, diversification strategies and international entry patterns. As Teece (1984), Buckley and Casson (1985) and others have observed, differences in market requirements, firm capabilities, and transactional relationships allow for differentiation amongst global strategies. Firms wishing to enter into potentially unstable but profitable foreign markets are likely to be more aware of the risks and uncertainty of heavy commitment of corporate resources than firms whose major concern may be to match competitors' action or to overcome mobility barriers. The evidence of three large companies in the survey supports the view that successful internationalization requires an assessment of the firm's motives and that these be correspondingly matched with its corporate ability. This is consistent with Harrigan's (1984) findings that firms' strategic missions determine their international entry pattern, and more specifically their need to utilize cooperative and contractual modes.

13.3 RELATIONSHIP BETWEEN FIRM SIZE AND USE OF NEW FORMS

H_3: The choice of new forms in the internationalization process is not significantly influenced by the size of the firm.

A widely held notion is that large firms will, ceteris paribus, prefer foreign direct investment to new forms due to their monopolistic power in ownership advantages. Firm size in itself is an ownership advantage which has been used extensively as a proxy for financial, managerial and technical capabilities. A corollary of this is that new forms will be a phenomenon of small and medium-size firms (SMFs). New forms, such as franchising, have often been perceived as a source of capital for small business expansion. For example, Oxenfeldt and Thompson (1969) argue that franchising systems are created because franchisors 'have too little capital to create a wholly owned chain.' Oxenfeldt and Kelly (1969) and Hunt (1973) have specifically argued that small companies with 'limited access' to capital markets use modes characteristic of new forms to expand. Other authors who subscribe to the view that new forms are a phenomenon of SMFs include Ozanne and Hunt (1971), Caves and Murphy (1976).

Large industry "majors" or "insiders" (Franko, 1989) with significant shares of world markets have resources and experience that lead them to see few, if any tangible, benefits from taking on local joint venture partners in foreign operations. Industry giants like ICI, IBM, Shell, ITT, Coca Cola, McDonald's, etc. therefore have little or no motivation to use new forms or, more specifically, to enter JVs with host country partners. In contrast, small and medium size firms, regarded as "second-tier", "outsider" firms (ibid.) might both attempt to gain world market share by displaying (1) a willingness to share ownership and control in return for access to local markets, (2) a high propensity to minimize country risks and cost of establishing a foreign subsidiary, (3) a desire for economies of scope and geographical diversification; and (4) a tendency towards managerial, financial and technological gains from local participation and cooperation.

This presumption of dominant firm behaviour was characterized as the "Wells effect" (see Stopford and Wells, 1971, especially pp. 138-141). Under this concept it has been asserted that some, if not all, "non-dominant" firms in particular industries show a high propensity to place special emphasis on the use of joint ventures (and other non-direct investment modes) in their international competitive strategies (Mascarenhas, 1986). Under both the "Wells effect" and the "oligopolistic market behaviour" (Knickerbocker, 1973) hypotheses, "non-dominant" firms are seen as small and medium size firms that lack the corporate prowess (in terms of financial, managerial, marketing, and technological capability) to engage in international competition.

However, casual observation indicates that in contrast to the traditional notion, new forms of investment are not limited to SMFs. There are many large MNEs that use variants of new forms. Such large MNEs as McDonald's, ITT Sears, Coca Cola, etc., internationalize by both direct investment and new forms (See Brickley, Dark and Weisbach (1991). In addition, it was reported that other large MNEs such as IBM, 3M, Deere and Co., Eastman Kodak, and Monsanto were considering possibilities of using variants of new forms of investment (The Wall Street Journal, December 30, 1988).

An agency-theory explanation of why firms use new forms suggests that they are not limited to SMFs with restricted access to capital markets (Brickley, Dark and Weisbach, 1991). Besides, finance theory indicates that in the absence of offsetting considerations (e.g. incentive effects), risk sharing will be preferable to equity ownership(Rubin, 1987).

In order to determine whether there is a relationship between the size of the firm and use of NFIs, two procedures were adopted. First, respondents were asked to indicate whether the size of their firm had any significant influence on the use of new forms. 38.6 per cent of UK companies responding and 68.4 per cent of Foreign companies admitted that the size of their companies has an influence on their choice of entry modes (Table 13.3.1) On the other hand, 61.4 per cent and 31.6 per cent of UK and Foreign companies respectively indicated that size was not influential. Altogether 47.6 per cent of the responding companies (i.e. 30 companies) aver that size is influential to their choice of new forms, while 52.4 per cent (or 33 companies) indicate otherwise.

Siegel (1954, p.104) states that when the data of research consist of frequencies in discrete categories, the X^2 test may be used to determine the significance of differences between two independent groups, which in this case are UK and Foreign companies.

Table 10.3.1 Questionnaire Responses by Managers, Concerning the Impact of Firm Size on the Choice of New Forms: Company Evidence. (Possible Replies: Influential, Uninfluential).

	Influential		Uninfluential		Valid Total	
	Freq.	Valid Percent	Freq.	Valid Percent	Freq.	Percent
UK Companies	17	38.6	27	61.4	44	69.8
Foreign Companies	13	68.4	6	31.6	19	30.2
	30	47.6	33	52.4	63	100.0

Chi-Square	C	D.F.	Significance	Min E.F.	Cells with E.F. < 5
3.60095	.23252	1	.0577	9.048	None
4.71952	.26399	1	.0298	(Before Yates Correction)	

The hypothesis under test is that there is no relationship between firm size and the choice of new forms in their internationalization process. Based on respondents' answers, a frequency table of influence was constructed in the form of a '2 x 2' contingency table. The underlying assumptions are: (1) The two groups of companies are independent; (2) the individual companies in each group were randomly and independently selected; (3) each observation qualified for one and only one category; and (4) the samples are large such that no expected frequency is less than 5 (ibid.). The results of the chi-square test are shown in Table 10.3.1. The SPSS prints two versions of the chi-square statistic. The standard version, labelled BEFORE YATES CORRECTION, equals 4.720. The observed significance level is .030, leading to a rejection of the hypothesized difference.

The Yates' correction is an adjustment to a 2 X 2 contingency table, designed to improve the estimate of the observed significance level. It incorporates a correction for continuity which markedly improves the approximation of the X^2 distribution. Based on the Yates' correction, the computed value leads to an acceptance of the hypothesis at the .05 level. In order to determine the strength of the relationship between firm size and use of new forms, a correlation coefficient is calculated. The nonparametric counterpart of the Pearson product-moment correlation coefficient r is the CONTINGENCY COEFFICIENT C (Siegel, 1954, p.196; Norusis, 1986, p.275). The C is a measure of the extent of association or relation between two sets of attributes. This measure is always between 0 and 1, where 0 denotes no relationship and 1, a perfect relationship. From Table 10.3.1, the value of C before or after Yates' correction is a function of the number of categories, thus for a 2 x 2 table (as Table 10.3.1), the upper limit of C is .707 (Siegel, 1954, p.201). Therefore, on a scale of 0 to .707, the strength of the association between firm size and choice of new forms of investment is .373. Thus we could conclude that firm size and choice of new forms are somehow related in the population of which UK and Foreign companies are samples (by a margin of 37.3%).

The second procedure involves categorizing firms into small, medium and large sizes, using the criteria of both turnover (or assets in the case of banks), and number of employees. These were examined separately as to their reliance on selected NFI-adoption rationales. Termed 'new forms of investment - adoption rationales', these are "defensive reaction" rather than "strategic initiative" reasons for employing the mechanism of new forms. They are also perceived as "second best" alternative reasons for adopting new forms (Oman, 1984, 1986; Ozawa, 1984). Differences between the mean ranks of the selected rationales were tested using the Kruskal-Wallis one-way analysis of variance (Tables 10.3.2, 10.3.3, 10.3.4 and 10.3.5) for Foreign companies, U.K. companies, Foreign banks and U.K. banks, respectively. The aim is to determine whether there are differences in the choice of new forms (i.e. differences in mean perceptions of NFI-adoption rationales) when the size of the firm is small, medium, and large. In general, it is hypothesized that the average perceptions of the NFI-adoption rationales will be the same among small, medium, and large firms. The results of the tests follow *seriatim*.

Table 10.3.2 Kruskal-Wallis One-Way Analysis of Variance Tests of the Relationship of NFI-Adoption Rationales to Firm Size: Foreign Companies' Evidence

	Mean Rank by Firm Size		
NFI-Adoption Rationale	**Small n = 5**	**Medium n = 5**	**Large n = 5**
Willingness to share ownership and control.	3	15	5
Minimization of country risks.	4	8	13
Cost of establishing a foreign subsidiary.	12	9	1
Size of parent company.	7	6	10
Experience in foreign markets.	2	14	11
ΣR_i =	28	52	40

$H = 2.88$ $\quad X^2_{2, 0.10} = 4.61$

EVIDENCE FROM FOREIGN COMPANIES

Small size foreign companies were found to be more sensitive to willingness to share ownership and control, minimization of country risks, and experience in foreign markets than their medium and large counterparts (see Table 10.3.2). Medium and Large firms appeared less sensitive on both these two factors and experience in foreign markets. Anecdotal evidence suggests that small firms are keen to expand their markets abroad.

With a lot of competition from medium and large firms in the domestic market, it would be surprising if they displayed an unwillingness to collaborate with local partners. Their willingness to share ownership and control would reflect in minimization of host country risks as well as compensate for lack of experience in foreign markets.

Large foreign companies, while not minding sharing ownership and control and less concerned with experience in foreign markets, were found to be more sensitive to cost of establishing foreign subsidiaries as well as to experience in foreign markets. These are internalization-incentive advantages in their internationalization process. Considering the nationalities of the foreign companies in the sample (Table 9.4), it is hardly surprising that the above characterizations are evident. Since the observed value of 2.88 is less than the critical value of 4.61 at the .10 level, the hypothesis of equal perceptions among the three sizes of companies is accepted. The data indicate lack or absence of significant differences in the mean perceptions of NFI-adoption rationales among small, medium, and large foreign companies.

Table 13.3.3 Kruskal-Wallis One-Way Analysis of Variance Tests of the Relationship of NFI-Adoption Rationales to Firm Size: UK Companies' Evidence

	Mean Rank by Firm Size		
NFI-Adoption Rationale	**Small n = 5**	**Medium n = 5**	**Large n = 5**
Willingness to share ownership and control	2	7	15
Minimization of country risks	14	4	12
Cost of establishing a foreign subsidiary	10	5	8
Size of company	6	1	13
Experience in foreign banking and markets	11	9	3
$\Sigma R_i =$	43	26	51

H = 720.9 $\quad X^2_{2\,,\,0.005} = 10.60$

EVIDENCE FROM UK COMPANIES

Similar tests were carried out among small, medium and large UK companies (see Table 10.3.3). The evidence is somewhat disaggregated. Similar to small foreign companies, UK small companies were found to be more willing to share ownership and control, but surprisingly, less concerned about the cost of establishing a foreign subsidiary, country risks and lack of experience in foreign markets. Again, anecdotal evidence supported by the interviews with small company executives seems to confirm this conservative and cautious approach.

UK medium-size companies, while willing to share ownership and control and to diversify were more concerned about their size, risks and cost of establishing a foreign subsidiary. This propensity is evident in the geographic concentration of U.K. companies (see Table 9.15) - that is, mainly in relatively stable geographic zones - Western Europe and North America. Large UK companies were found to be more sensitive about their experience in foreign markets and less concerned about the other factors. Differences in the perception of the three groups with respect to the factors were tested using the Kruskal-Wallis one-way analysis of variance. The observed value of 720.9 exceeds the critical value at .005 level, suggesting therefore a rejection of the hypothesis of a relationship between firm size and use of new forms. The data indicate significant differences in the rank perceptions of NFI-adoption rationales among small, medium, and large UK companies.

EVIDENCE FROM FOREIGN BANKS

The evidence of similar tests with respect to foreign banks is presented in Table 10.3.4. Medium size foreign banks were found to show a greater sensitivity towards the first four factors in the table than their small and large counterparts. On the other hand, they were less worried about their foreign experience, possesion of large corporate customers, and economies of scope. This would tend to be the case naturally since foreign banks, especially Japanese ones, are supported by large holding companies (*the sogo shosha*). Since many of the foreign small banks operating in the U.K. are not wholly branch networks, or at least did not initially establish through this process, it is not surprising that the sample group did not display much sensitivity towards cost of foreign branch, their size or experience in foreign branching. However, the evidence of a willingness to enter into collaborative ventures was surprisingly not too strong, mean score 8.70, even though they showed a high propensity towards economies of scope and geographical diversification. Large foreign banks were found to be most unwilling to share ownership and control. That also reflects on their low sensitivity to country risks. Partly due to the sad experience in sovereign loan losses, especially European and American banks, and partly due to the size and nationalities of the sample banks, high cost of establishing foreign branches coupled with the possession of large international corporate customers, accurately mirrors the perspectives expressed at the interviews.

The observed value of 9.801 exceeds the critical value of 9.21 at the .01 level, leading to a rejection of the hypothesis. The data indicate significant differences in the mean perceptions of NFI-adoption rationales among small, medium, and large foreign banks.

Table 10.3.4 Kruskal-Wallis One-Way Analysis of Variance Tests of the Relationship of NFI-Adoption Rationales to Firm Size: Foreign Banks' Evidence.

	Mean Rank by Firm Size		
NFI-Adoption Rationale	**Small n = 7**	**Medium n = 7**	**Large n = 7**
Willingness to share ownership and control	5	1	19
Minimization of country risks	6	3	16
Cost of establishing a foreign branch	17	6	10
Size of bank	20	4	9
Experience in foreign banking and markets	13	14	10
Possession of large international corporate customers	12	18	8
Economies of scope and geographical diversification	2	21	14
$\Sigma R_i =$	75	67	86

$H = 9.801 \qquad X^2_{2,\ 0.01} = 9.21$

EVIDENCE FROM UK BANKS

The evidence from UK banks is somewhat different from their foreign counterparts. UK medium-size banks show a high propensity to share ownership and control because they want to benefit from economies of scope and geographical diversification. They are equally concerned about their size and cost of establishing a foreign branch, for the same reasons given above, but less worried by country risks and foreign experience apparantly because, they are predominantly located in relatively stable European and North American continents. Large-size UK banks are not as much sensitive to their size, possession of large international corporate customers, and economies of scope as they are about country risks and cost of establishing a foreign branch network. Consequently, on the one hand, and surprisingly, on the other, they showed the greatest willingness to share ownership and control. Equally surprising was the fact that sample U.K. small banks were less willing to share ownership and control, and less sensitive to their size, but more worried about their experience in foreign banking/markets and country risks.

Table 10.3.5 Kruskal-Wallis One-Way Analysis of Variance Tests of the Relationship of NFI-Adoption Rationales to Firm Size: UK Banks' Evidence

	Mean Rank by Firm Size		Kruskal-
NFI-Adoption Rationale	**Small** **n = 7**	**Medium** **n = 7**	**Large** **n = 7**
Willingness to share ownership and control	21	9.5	3
Minimization of country risks	7.5	17	7.5
Cost of establishing a foreign subsidiary	13.5	13.5	4.5
Size of bank	18	6	9.5
Experience in foreign banking and markets	4.5	19.5	13.5
Possession of large international corporate customers	13.5	1.5	13.5
Economies of scope and geographical diversification	13.5	1.5	19.5
$\Sigma R_j =$	91.5	68.5	71.0

@ Corrected for Ties H = 1.2297 $X^2_{2\ ,\ 0.10} = 4.605$

Differences in the rank scores of the three groups with respect to each of the factors were also tested using the Kruskal-Wallis one-way analysis of variance. The correction factor for the ties in the scores has been incorporated in the Kruskal-Wallis H equation. The null hypothesis test is a X^2 test with 2 degrees of freedom. Since H = 1.23 is less than the critical value of 4.61, the null hypothesis is therefore accepted. This leads to a conclusion that the average perceptions of NFI-adoption rationales among small, medium, and large UK banks are the same. The correction for ties has little effect on the result.

The average result of no significant effect of firm size on foreign investment for the latter sample group tends to support earlier studies. In their study of the determinants of foreign investment by UK advertising agencies, Terpstra and Yu (1988) tested the hypothesis that "the size of an advertising agency should have a positive impact on its foreign investment." Their analysis contradicted this hypothesis, thus blurring the impact of firm size on advertising agencies' foreign investment. Similarly, Brickley, Dark and Weisbach (1991) found that new forms of investment (exemplified by franchising) are not simply tools for small and medium size firms, rather large MNEs use them as well. In a much earlier study, Stopford (1972) noted that the use of joint ventures and minority equity in foreign manufacturing operations by US MNEs appeared to be an inverse function of a firm's relative size in its industry.

Using the "Wells effect" by which large, "dominant" and "industry leaders" are regarded as having a lower propensity to use new forms of investment than their smaller, "non-dominant" rivals, Franko (1989) tested the correlation between company size and "minority joint venture propensities". Within a two industry population (tyres and autos and trucks) and study samples of US firms versus non-US firms, Franko found first, an inverse relationship between company size and minority joint ventures (MJV) use and second, the inverse relationship was much stronger among US firms taken alone. Thus, he concluded that the "Wells effect" "appears somewhat weak and nonlinear (not that there is any a priori reason to expect a linear relationship)." Franko also found a high incidence of MJV avoidance by smaller (relative to large, dominant industry leaders) segment-dominating firms, many of whom were European or Japanese MNEs. His findings are supported by the results of this study. The impression gained from interviewing three Japanese corporate executive (two companies and one bank) was that there appeared to be a sustained attempt by Japanese MNEs to adopt foreign investment approaches that are structurally and operationally different from those of their Western counterparts, especially the US MNEs, including a high propensity to use new forms.

10.4 THE IMPACT OF FOREIGN INVESTMENT POLICY SHIFTS

> H_4: New forms of investment are more likely to prevail in firms with a 'dynamic' foreign investment posture than in firms with a 'static' posture.

As a corollary to hypothesis 2 above and the "Wells effect," it could be argued on the basis of the "experience-effect logic" associated with the Boston Consulting Group (1972) that firms concerned about risks and uncertainties, increasing global competition, rising costs/reduced availability of corporate resources and environmental distortion propensities (in particular host governments') are more likely to adopt a flexible strategic investment approach than firms that adopt a relatively stable approach. The latter may be associated with industries experiencing a relatively stable growth, high share of world markets with high financial returns and little, if any, managerial and financial constraints. These features may frequently be associated with large, dominant and industry-leader firms, eg. IBM for the computer industry, Coca Cola for the soft drink industry, ICI for the health care industry, Exxon and Shell for the oil industry, and Nissan Motors and Ford Motors for the motor industry. In a word, these companies are conglomerates or industry giants and may be said to have a lower propensity to frequent changes in investment policy and, therefore, less likely to accept new forms than their rival followers.

On the other hand, firms that show greater concern for the above investment hazards may be more disposed to utilize new forms than the conglomerates or industry leaders. Through experience (or inexperience) these firms may be prone to lower market share, lower financial returns and, perhaps due to cash flow, managerial and financial constraints than the leader firms. Under these circumstances, these firms may be inclined to frequently change their investment policies as a strategic reaction posture, in attempts to both follow industry leaders' oligopolistic, risk-profile matching behaviour and achieve growth and financial performance. Accordingly, this group of firms may likely show higher propensity towards adopting 'flexible' ownership policies and entry mode patterns.

Presumably differences between these two firm groups can be examined to determine whether 'dynamic strategy profile' firms do more frequently use, or are more likely to use, new forms than 'static strategy profile' firms.

In order to examine whether a classification of the above kind might be helpful in interpreting firm strategic profile, two statistical procedures were applied: frequency analysis and X^2 test. Table 10.4.1 presents a cross-classification of UK and foreign firms in terms of the catalysts for change in foreign investment profile. Respondents were asked to identify the factors they considered likely to induce changes in, or stagnate, their international investment behaviour.

Table 10.4.1 Catalysts for Change in Foreign Investment Posture

	UK FIRMS		FOREIGN FIRMS	
	Banks	**Companies**	**Banks**	**Companies**
Factors mentioned by Respondents*	**n = 10**	**n = 47**	**n = 21**	**n = 19**
	%	%	%	%
Shift in corporate policy/strategy	60	66	45	32
Global Competition	40	29	31	23
Host Country's inward investment policy	-	5	-	24
Host Government's outward investment policy	-	-	-	21
	100.0	100.0	100.0	100.0

* In some cases respondents stressed more than one factor

As would be expected, more than one factor might be responsible for a corporate change in foreign investment profile. For example, operational activities of rival firms in a particular geographic or product market can force a shift in the company's investment policy/strategy with respect to that geographic region or product market or even its global approach. The predominant factor responsible for a change in firms' foreign investment profile is shift in corporate policy/strategy. Of course, if there is a shift in a firm's investment policy this may in all probability filter through the firm's foreign investment strategy to the effect that a particular product or market area may be abandoned or expanded. This factor appears to induce a change in investment profile more for UK companies and banks than their foreign counterparts, with UK banks exhibiting the greatest sensitivity to it. Foreign banks tended to be more affected by the factor than their company counterparts.

Another important catalyst cited by respondents is global competition. Again UK firms on the average appear more likely to be affected than their foreign counterparts. Also, foreign banks exhibit greater sensitivity to the factor than companies (both UK and foreign). It is rather surprising that host country's political/economic climate is not considered an important agent of change in foreign investment policy. Perhaps, this may be attributed to the nationality of the sample firms. Many of them have bulk of their overseas activities in Western Europe and North America (see Table 9.15), and, as such, are not exposed to the vangaries of their host countries as much as might be the case were they mainly located in LDCs.

Some respondents had other reasons than the above for changing foreign investment posture. For example, a major UK gas company was forced to alter its domestic and international investment policy and strategy following the government's privatization and relaxation of the government's control. Another, a major confectionery company, was forced to change its global diversification approach by the economic recession in general and, depression in the UK confectionery in particular, couped with global competition.

In addition to identifying the factors that induce changes in foreign investment posture, respondents were asked first, to indicate the overseas geographic concentration of their economic activities (Table 9.15) and second, whether this position had changed in the last five years. Hood and Young (1986, p. 35) had argued that a firm's foreign investment posture could be gauged by its overseas geographic or product concentration. Thus, given its geographic concentration, a firm would be expected to exhibit some of the characteristics of the market leader sketched above, i.e. strong market position and high penetration within host country's industrial sectors. Such firms would be expected to make little or no change in their strategic posture in such markets. Conversely, firms whose overseas activity is not concentrated and have had to make changes in the last five years may be characterized as displaying a dynamic investment posture.

Table 10.4.2 presents a crosstabulation of dynamic and static postures among sample banks and companies. 77.4 percent of sample banks have not altered their foreign investment posture in the last five years as against 30.3 percent of companies that adopt a similar posture. In all, it would appear that banks and companies tend to move in inverse direction with respect to foreign investment postures (see Table 10.4.2). A test of the relationship between foreign investment posture and the likelihood of adopting new forms is analogous to testing whether or not there is a difference between the two groups (firms with 'dynamic postures' versus firms with 'static postures') in the choice of new forms of investment. The hypothesis of study is that firms which adopted 'dynamic postures' would more frequently accept new forms of investment. The null hypothesis therefore is that there is no difference between firms with 'dynamic postures' and firms with 'static postures'.

Table 10.4.2 **Questionnaire Responses by Managers, Concerning Whether their Firms Maintain a 'Dynamic' or 'Static' Foreign Investment Posture: a X^2 Test of the Relationship between Foreign Investment Posture and the Choice of New Forms**

	DYNAMIC Freq.	Percent	STATIC Freq.	Percent	TOTAL Freq.	Percent
Banks	7	22.6	24	77.4	31	32.0
Companies	46	69.7	20	30.3	66	68.0
	53	54.6	44	45.4	97	100.0

Chi-Square	D.F	Significance	MIN E.F.	Cells with E.F. < 5
17.0394	1	.0000	14	None
14.2940	1	.0000	(Before Yates Correction)	

Since the observed significance level is too small, the null hypothesis that there is no difference between firms with 'dynamic postures' and firms with 'static postures' is rejected. As the study hypothesis (the alternative hypothesis) predicts the direction of the difference between the two groups, the region of rejection is one-tailed. The conclusion therefore is that firms which adopt dynamic foreign investment postures are more likely to accept new forms than do firms with static foreign postures. Franko (1989) found a similar result in his analysis of use of minority and 50-50 JVs. Using the 'Wells effect' he found that the 'strategic posture' of 'segment specialists' tended to disfavour the use of new forms (i.e. joint ventures) as part of an oligopolistic 'catch-up' or 'geographical-matching' strategy. The most plausible explanation for this result is that the 'dynamic strategic posture' allows firms to avoid head-on competition with industry leaders by using several options to diversify their markets. Also, as globalization of markets intensifies so will international expansion and competition in the international arena accelerate and so will the use of new forms intensify (see also Terpstra and Yu, 1988). Thus, although certain economic and non-economic factors can be largely held responsible for triggering the move towards the use of new forms, the kind of strategic posture adopted and behaviour both allowed these factors to succeed in inducing firm reaction to use of new forms, and conditioned the kinds of MNEs that accepted them in the internationalization process. Franko(1989) reached a similar conclusion in his study.

10.5 SIGNIFICANCE OF HOST COUNTRY-SPECIFIC CHARACTERISTICS

H_5: The choice of new forms in foreign market development is significantly influenced by managerial perceptions of host country characteristics.

The importance of location-specific advantages has been examined extensively in the literature. Locational advantages combine in simultaneous proportion with ownership and internalization advantages to constitute the eclectic theory. Several host country characteristics were isolated and respondents were asked to indicate in order of strategic importance the influence of these factors on their firms' decision to enter into foreign markets through the mechanism of new forms.

Table 10.5.1 presents the individual sample and cross-sectional results of the respondents' perceptions. The cross-sectional mean indicates that the size of host country's markets is the most important locational factor (overall mean score 1.567). Following this is the host country's inward investment policy/regulation (mean score 1.659). Psychic distance - representing language, cultural, business, customs, etc. - does not appear to be an important locational factor across the 4 sample groups (mean score 2.595). Within - group analysis shows that size of host country's markets is the most important locational factor favouring the use of new forms for both U.K. and Foreign companies, with the latter attaching greater importance to it than the former. With respect to host government inward investment policy, UK banks appear to be much more sensitive to it than other sample groups.

Banks were isolated and studied separately for significant differences in the importance of each of the locational factors (Table 10.5.2). The same procedure was applied to companies (Table 10.5.3). The t-tests showed, in the case of banks, two locational factors to be statistically significant at the 5% level. These are: the host government's inward investment policy, and the level of inter-bank market. No significant relationship was found between U.K. and foreign banks in respect of the importance of the other factors. This suggests that apart from host government's regulations and level of inter-bank market, there may be no significant difference in the importance of the other locational variables in determining the use of non-branch network in foreign market development.

Table 10.5.1 Questionnaire Responses by Managers, Concerning the Significance of Host Country-Specific Advantages (CSAs) in the Choice of New Forms of Investment (Scale: 1=Very significant to 5=Very Insignificant)

		UK Banks		Foreign Banks		UK Companies		Foreign Companies		Cross-Sectional	
@		n = 10		n = 21		n = 47		n = 19		n = 97	
Rank	Locational Factor	Mean	SD	Mean	SD	Mean	SD	Mean	SD	Mean	SD
2	Host Governments inward investment policy	1.333	0.500	1.947	0.780	1.674	0.837	1.684	0.478	1.659	0.218
1	Size of host country's markets	2.111	0.928	1.700	0.571	1.405	0.798	1.053	0.229	1.567	0.389
3	Economic/political climate	1.889	0.333	2.000	0.775	1.829	0.442	1.737	0.806	1.864	0.095
7	Fiscal/monetary policies	2.667	0.866	2.191	0.402	2.073	0.685	2.316	0.671	2.312	0.222
8	Psychic distance	2.778	0.441	2.450	0.759	2.429	0.801	2.722	0.669	2.595	0.157
5	Level of inter-bank market	2.333	-.500	1.750	0.786	*	*	*	*	2.042	0.292
4	Technological & Managerial Capacity	1.889	0.601	2.000	0.649	*	*	*	*	1.945	0.056
6	Infrastructural development in host country	*	*	*	*	2.214	0.470	2.000	0.594	2.107	0.107

* Questions were either not relevant to the group or were not properly answered.

@ Cross-Sectional Rank

The evidence from companies is similar (see Table 10.5.3). Apart from size of host country's market (significant at the 1% level), no statistically significant differences were found in the importance of other locational factors in determining the use of new forms.

Table 10.5.2 Significant Differences in Mean Scores of CSAs as Entry Mode Determinants: U.K. Vs Foreign Banks

	No. of cases	F-Value	2-Tail Probability	Pooled Variance Estimate t-value	2-Tail probability	Separate Variance Estimate t-value	2-Tail prob.
Host government's inward investment policy	28	4.65	0.032	1.62	0.118	2.06	0.050*
Size of host country's market	29	2.64	0.079	-1.47	0.153	-1.23	0.245
Economic/political climate	30	5.40	0.020	0.41	0.684	0.55	0.587
Fiscal/monetary policies	30	4.63	0.005	-2.08	0.047*	-1.58	0.147
Psychic distance	29	2.96	0.119	-1.20	0.241	-1.46	0.157
Level of inter-bank market	29	2.47	0.191	-2.04	0.052	-2.41	0.024*
Technological & Managerial capacity	29	1.17	0.867	0.44	0.666	0.45	0.659

* Significant at 5% level

Table 10.5.3 Significant Differences in Mean Scores of CSAs as Entry Mode Determinants: U.K. Vs Foreign Companies

	No. of cases	F-Value	2-Tail Probability	Pooled Variance Estimate t-value	2-Tail probability	Separate Variance Estimate t-value	2-Tail prob.
Host government's inward investment policies	62	3.07	0.012	-0.05	0.962	-0.06	0.954
Size of host country's market	61	12.10	0.000	1.88	0.065	2.63	0.011*
Economic/political climate in host country	60	3.33	0.002	0.57	0.568	0.47	0.644
Fiscal/monetary policies	60	1.04	0.959	-1.28	0.204	-1.29	0.204
Psychic distance	60	1.43	0.428	-1.36	0.178	-1.47	0.151
Infrastructural development in host country	60	1.60	0.221	1.49	0.141	1.36	0.186

* Significant at 1% level

In order to verify the significance of differences in managerial perceptions of the importance of certain host country factors in influencing the use of new forms, the Kruskal-Wallis one-way analysis of variance test was carried out. Table 13.5.4 presents the summary of the results of this test. In this summary presentation it is considered redundant repeating the mean values of each host country variable since these are shown in Table 10.5.1. Three host country-specific variables imported into the analysis from related set of questions to the respondents are: (1) products customized to host/regional market, (2) level of economic development, and (3) general phenomenon of LDCs. These three factors were brought in to permit the use of the Kruskal-Wallis test, in place of the factors ranked 4, 5 and 6 in Table 10.5.1.

Table 10.5.4 Kruskal-Wallis One-Way Analysis of Variance Test of Significance of Differences in the Importance of CSAs to use of New Forms Among the Four Sample Groups

Host Country Characteristics	Kruskal-Wallis Z-Value	Probability	X^2-Value	Significance
Host government's inward investment policy	24.2596	.0000	35.1000	.0000*
Size of host country's markets	2.1660	.1411	4.3400	.2265
Economic/political climate in host country	.9091	.3404	6.7400	.0806***
Psychic distance	2.3484	.1254	4.6700	.3226
Products customized to host/ regional market	2.6460	.1038	7.8516	.0016**
Level of economic development	1.3644	.2428	2.3000	.5122
General phenomenon in LDCs	1.6568	.6466	31.5900	.3459

* Significant at .01 per cent
** Significant at .10 per cent
*** Significant at 1 per cent

The result of the Kruskal-Wallis test indicates the difference to be statistically significant for the following three comparative country-specific factors:

1. Host government's inward investment policy, at .01%
2. Economic/political climate in host country, at 1%
3. Products customized to host/regional market, at .10%

However, this difference was not statistically significant for the following four country-specific variables:

1. Size of host country's markets
2. Psychic distance
3. Level of economic development
4. LDC phenomenon.

These findings seem to suggest an increasing importance of the former factors and a decreasing importance of the latter factors in foreign investment decisions over time. In the 1960s and up to mid 1970s, MNEs were less concerned with host government policy, economic/political climate or host/regional market customization. The reason could presumably have colonial attributes as well as historical trends. On the former dimension, imagine a British firm wishing to establish in any of the colonial territories in the 1950s up to the late 1960s. The firm did not have to worry about any of these factors because they were not at issue and consequently were not important considerations for foreign investment. However, inward investment policy shifts during the 1970s were the product of the economic and political tenor of the times and the growing nationalism of many countries. This period witnessed unprecedented rise of wealthy oil nation states. Economic power was to be matched by political power, resulting in restrictive inward foreign investment policies. Consequently, contemporary corporate investment decisions had to address issues that were of little or no consequence in the past. This view was shared by the chief executive of one UK company. He said his company had to choose between closing its operations in Saudi Arabia and entering into minority joint ventures with local partners in 1974. Obviously, his company had to choose the latter, but he also said that while at the time it was like "swallowing a bitter pill", over the years, however, the cash flow implications and wider business opportunities this avenue has generated has encouraged his company to adopt cooperative forms as a "first best alternative".

The literature on country characteristics and the empirical findings in manufacturing FDI suggests a positive relationship between manufacturing FDI and some of the above factors, e.g. psychic distance (see, for example, Dunning, 1981, 1988). However, the impact of the second set of factors (found to be statistically insignificant) on firms' foreign investment is not so clear. Empirical findings in international banking tend to suggest that geographic proximity (which is captured within psychic distance) has a minor impact on banks' foreign investment (Ball and Tschoegl, 1982; Choi, Tschoegl and Yu, 1986). Other researchers' findings on the significance of locational factors on foreign investment seem to corroborate the findings of this study (see, for example, Davidson and McFetridge, 1985; Terpstra and Yu, 1988; Franko, 1989).

10.6 THE IMPACT OF COMPETITORS' MODES OF ENTRY

H_6: Firm choice/use of new forms in the internationalization process is independent of competitors' mode of organising foreign transactions.

This hypothesis seeks to offer evidence on the irrelevance (or relevance) of competitors' international behaviour (i.e. international entry mode) on a firm's choice of new forms. One of the often cited reasons why firms choose new forms of investment is the need to match rivals' behaviour (Williamson, 1975, p. 217; Oman, 1984; Buckley and Casson, 1985; Harrigan, 1985). Global competition forces firms to develop defensive strategies. A major task in this process is the development of a profile of the likely strategies rival firms and their potential reaction to the firm's strategic moves. In effect, the essence of competitor analysis (Rugman, et al., 1986, p. 333) is to examine the impact of competitors' current and emergent strategies, capabilities and general industry conditions. In the analysis competitive structures of two kinds are discernible: entry and exit.

The propensity to use new forms is in part due to a desire of the host government to reduce foreign ownership and control but is also facilitated by the willingness of MNEs to compromise on total ownership (Buckley and Casson, 1985, p. 56). This, according to the authors, is often the result of competitive pressure. Thus, new forms of investment offer entry into markets which would otherwise be foreclosed to foreign MNEs in general or particular MNEs (e.g. of particular countries or trading circumstances). Of interest here is foreclosure of competitive kind, that is, entry barrier erected by existing oligopolistic competitive structure. In these circumstances, new forms of investment may offer entry prospects and may be preferable (Buckley and Davies, 1980; Oman, 1984).

While competitive structure of entry barriers works to severely limit the capacity of firms to enter into certain markets, competitive structure of exit barriers makes it difficult for existing firms to pull out. They are required to maintain exchange relations of good continuity properties. In this setting, some form of contractual/cooperative arrangements or minority equity participation may be seen as providing firms a leeway to both maintain operational presence in the market and limit its level of resource commitment. In both competitive structures, the pattern of competitors' behaviour can be influential to a firm's actions or reactions. In particular, competitors' entry modes may be significant, whether in terms of the follow-the-leader behaviour hypothesis (Knickerbocker, 1973) or as a defensive reaction strategy hypothesis (Oman, 1984).

To test both hypotheses, it is stated in the null form that firm choice/use of new forms is independent of competitors' mode of organizing foreign transaction. In operationalizing the hypothesis, respondents were asked to indicate whether their rivals' mode of entry had an influence on their firms' international entry modes choices. Tables 10.6.1 and 10.6.2 present the results and chi-square tests for companies and banks, respectively. 38.3% of UK companies and 21.1% of Foreign companies said that their competitors' modes of entry had a significant influence on their entry mode choices (Table 10.6.1). On the other hand, 61.7% and 78.9% of UK and Foreign companies respectively indicated that their competitors' entry mode patterns had no influence on their use of new forms.

On the basis of the crosstabulation, Chi-Square test was carried out between the Influential group and Uninfluential group in order to determine the significance of differences between the two groups. The test reveals that it is likely that the observed value might have arisen under H_0, that is, the observed probability is greater than X^2 critical value. The data do not therefore permit us to reject the null hypothesis that choice of entry mode is independent of competitors' entry patterns. Thus, on the basis of this evidence, it will appear that competitors' mode of international entry has no significant impact on the use of new forms of investment.

Table 10.6.1 Questionnaire Responses by Managers, Concerning the Influence of Competitors' Entry Mode Patterns on the Choice of New Forms: Company Evidence (Possible Replies: Influential; Uninfluential)

	Influential		Uninfluential		Valid Total	
	Freq.	Valid Percent	Freq.	Valid Percent	Freq.	Percent
UK Companies	18	38.3	29	61.7	47	71.2
Foreign Companies	4	21.1	15	78.9	19	28.8
	22	33.3	44	66.7	66	100.0

Chi-Square	C	D.F.	Significance	Min E.F.	Cells with E.F. < 5
1.11786	.129	1	.2904	6.333	None
4.71952	.163	1	.1784	(Before Yates Correction)	

Table 10.6.2 Questionnaire Responses by Managers, Concerning the Influence of Competitors' Organizational Entry Modes on the Organizational Pattern of International Banking: Evidence From Sample Banks (Possible Replies: Influential; Uninfluential)

	Influential		Uninfluential		Valid Total	
	Freq.	Valid Percent	Freq.	Valid Percent	Freq.	Percent
UK Banks	4	40	6	60	10	34.5
Foreign Banks	12	63.2	7	36.8	19	65.5
	16	55.2	13	44.8	29	100.0

Chi-Square	C	D.F.	Significance	Min E.F.	Cells with E.F. < 5
1.77778	.240	1	.1674	4.5	1
1.38808	.214	1	.2568	(Before Yates Correction)	

The result of a similar test on the sample banks is presented in Table 10.6.2. The findings are similar in one respect and different in the other. As with UK companies, 40% of the sample UK banks indicated that competitors' international entry modes had a significant influence on their entry mode choices. 60% of these said they did not have any influence. On the other hand, a significantly high percentage (63.2%) of Foreign banks (in comparison with 21.1% of Foreign companies) indicated that they were influenced by their competitors' entry patterns. Only 36.8% (as opposed to 78.9% of the sample foreign companies) appeared not to be influenced by competitors' behaviour.

The X^2 test was used to determine the significance of this difference between the influenced and uninfluenced bank groups. As with the sample companies, this difference was not statistically significant at the 5% level, suggesting therefore that banks' use of non-branch international banking modes is invariant to competitors' organizational pattern. Before the Yates correction for continuity, the observed significance level tells us that 25.7% (or 16.7% after correction) of the time a difference of at least the one observed between the two groups would occur in the population.

Although on the basis of the above tests, the null hypothesis is not rejected, it does not mean an absence of a relationship between competitors' entry mode behaviour and a firm's use of new forms. In order to know whether the two variables are related or to know the degree of their relation, a correlation coefficient is calculated. (For a discussion of this, see 10.3 above). The contingency coefficient C measures the extent of association or relation between two sets of attributes for 2 x 2 tables, the maximum value of C is .707. From Tables 10.6.1 and 10.6.2, the values of C are .163 and .214, respectively. Transforming these on a scale of 0 to .707 becomes .231 and .303, respectively. Thus, we could fail to reject the null hypothesis at the 5% level of significance, and conclude that competitors' entry mode behaviour and firm choice of new forms are not related in the population consisting of the four sample groups. In other words, C = .231 or C = .303 is not significantly different from zero.

While not providing a conclusive evidence, the findings here offer a weak (if not contradicting) evidence for the oligopolistic reaction hypothesis. The findings also contradict such US-based studies, as those of Perlmutter and Heenan (1986) and Terpstra and Yu (1988). Earlier Levitt (1983) had observed a trend towards globalization of markets caused by inter-firm competition, among other factors. Perlmutter and Heenan saw the development of joint ventures as a dynamic competitive reaction to this globalization of markets. Together Terpstra and Yu hypothesized that these two factors have a profound impact on internationalization activities of US advertising agencies. There is hardly any doubt about this! However, they argue in the process that globalization of markets and the need to follow clients bring about internationalization in which joint ventures (and other non-FDI modes, by implication) will be the outcome of intense competition and oligopolistic reaction. Although methodological differences are significant for interpretation of results, the empirical results of hypothesis 6 do not provide support for both their hypothesized relationship and the defensive reaction strategy hypothesis. In other words, while competitor analysis is important and while new forms may be responsive strategies to rivals' organizational patterns, the evidence is yet inconclusive. The strength of the methodology adopted here is in the fact that it is predicated on the practitioners' views, even though it is 45% of sample banks as against 67% of sample companies that are unaffected by competitors' mode of entry.

10.7 RELATIONSHIP OF STAGE OF DEVELOPMENT

H_7: Firm choice of new forms in the internationalization process is independent of stage of host country development.

An important objective of this study is to determine whether or not the use/acceptance of new forms of investment is a characteristic phenomenon of less-developed countries. Both the antecedent literature (Weigel and Hyson, 1970; Casson, 1979; Germidis, 1981; Oman, 1980, 1984) and subsequent literature references and related studies (Beamish, 1984, 1985; Buckley, 1985; Franko, 1987, 1989; and others) have unequivocally regarded the growth of, and trend towards, new forms of international investment' as a normative desirability of LDCs. The unremitting reference to their usage in the North-South context has gone unchallenged, even though they are found to be frequently used by Fortune 500 companies in the developed countries (Janger, 1980; Harrigan, 1985). Some writers such as Contractor and Lorange (1987) have shown that the use of new forms by US MNEs outnumbers that of wholly owned subsidiaries by a ratio of 4 to 1.

Despite the evidence, public policy emphasis (e.g. OECD and UNO) and literature discussions (e.g. Buckley and Davies, 1979; Casson, 1979) have had overtones of assertions of historical trend towards, as well as national preference for, new forms in LDCs. The argument is that in these countries the new forms are seen as a possible means of replacing hostile relationships between them and foreign (especially Western) MNEs with contractual, cooperative or reduced equity arrangements based on mutual trust and commitment (Franko, 1989). This hypothesis attempts to provide an empirical evidence on whether the move towards new forms of international investment is confined only to LDCs. To the extent that they were associated with LDCs, or to the extent that there was a move towards new forms of investment in LDCs, could their usage be said to have been prompted by LDC factors or were MNEs demonstrating a new, voluntary acceptance of these forms? Alternatively, was MNE acceptance of new forms related to host country policy quid pro quos (e.g. trade and other barriers to competition) that would assure the financial "success" of such ventures while isolating them from competition with, or integration into other parts of, MNE systems? (Franko, 1989).

The search for evidence to support or refute the above hypothesis and hence attempt to answer the above question is pursued through three statistical procedures. First, the relationship of stage of development to choice of new forms is examined through measures of central tendency and dispersion (Tables 10.7.1 and 10.7.2). Second, the extent of agreement or disagreement to the proposition that new forms are confined only to LDCs (i.e. LDC phenomenon) is presented and tested in Table 10.7.3. Finally, the significance of the relationship of stage of development to use of new forms is examined. (Tables 10.7.4 and 10.7.5).

Tables 10.7.1 and 10.7.2 illustrate how new forms are employed for different reasons in developed and developing countries by sample companies and banks, respectively. A number of proxy factors were isolated to estimate cumulatively a country's stage of development. These are factors which have been used in similar studies (see for example, Tomlinson, 1970; Balasubramanyan, 1973; Furnish, 1976; Gullander, 1976; Beamish, 1984, 1985; Davidson and McFetridge, 1985; Franko, 1989; and for banking, see Yannopoulos, 1983; Cho, 1983, 1985; Nigh, Cho and Krishnan, 1986).

COMPANY EVIDENCE (Table 10.7.1)

The size of host country's markets and economic/political situation in host country were the most important reasons for using new forms in developed and developing countries, respectively. For the sample companies, new forms were used in developed countries not as the result of government suasion or legislation, rather on account of host market's size. Two reasons may account for this market size effect. First, in the absence of restrictions on direct investment, the choice between internal and external transacting mechanisms can be hypothesized to depend primarily on the expected present value of cash flows from current and future international investments. The higher the expected value, ceteris paribus, the more likely that the firm will choose the direct investment option (Davidson and McFetridge, 1985). However, since many of the fixed costs of internalization tend to be independent of market size, the chances are that smaller markets will exhibit higher rates of new forms of investment (e.g. licensing). Second, since most developed countries operate more open market economies than LDCs, competition is more likely to prevail in the former than in the latter market. Competition is sustained under large numbers exchange relations (Williamson, 1975). When combined with market size and sophistication, it may induce firms, particularly small and medium size ones, to adopt inter-firm and market transfer mechanisms (see, Davidson and McFetridge, 1985).

Economic/political situation in LDCs is a major factor leading foreign firms to use new forms. These countries are generally associated with policies that restrict the use of wholly-owned foreign subsidiaries (see, Franko, 1989). Thus, the use of new forms will be seen as a way of 'appeasing' host governments but also of appropriating maximum rents by offering companies a mix of earnings (see, Contractor, 1985). Janger (1980) and Beamish (1985) observed a similar result, noting that MNEs formed joint ventures in LDCs for a variety of government-related reasons. Apart from the differentials in market size (rank 1 versus rank 3) and economic/political situation in host country (rank 3 versus rank 1), the evaluation of the factors that propel several of the companies surveyed appears to be symmetrically ranked in both developed and developing countries (Table 10.7.1), although the sensitivity of the factors is on the average greater in the latter than in the former. This suggests that the reasons for using new forms in LDCs may not necessarily have economic origin. On the contrary, the transactional reasons for employing new forms in DCs may be rooted in economics.

BANK EVIDENCE (Table 10.7.2)

The relationship of stage of country development to international banking networks is presented in Table 10.7.2. Location advantages accrue by reason of differences in location-specific endowments between countries. These advantages are not bank-specific by themselves, but their joint effects with ownership-specific advantages and internalization advantages are bank-specific, under the eclectic paradigm, and differ among multinational banks (MNBs). Major sources of location-specific advantages can generally be found in these areas (Cf. Cho, 1986): different banking/financial environments, different economic/political situations, presence of banks of different nationalities, differential levels of foreign investment, and effective interest rate differentials.

Table 10.7.1 Relationship of Stage of Development to Choice of New Forms: Company Evidence (n=66).

Proxy Factors of Stage of Development	DC Rank	Mean	S.D.	LDC Rank	Mean	S.D.
Size of host country's markets	1	1.405	0.798	3	1.737	0.816
Openness towards foreign investment	2	1.674	0.837	2	1.684	0.478
Economic/political situation in host country	3	1.829	0.442	1	1.053	0.229
Level of industrial development	4	2.214	0.470	4	2.000	0.594
Tax Rate Differential (between home & host countries)	5	2.312	0.222	5	2.316	0.671
Psychic distance (socio-cultural dissimilarities, etc.)	6	2.595	0.157	6	2.722	0.669

Table 10.7.2 Relationship of Stage of Development to Choice of Entry Modes: Bank Evidence (n=31).

Proxy Factors of Stage of Development	DC Rank	Mean	S.D.	LDC Rank	Mean	S.D.
Existence of major corporate clients in host country	1	1.889	0.333	1	1.700	0.571
Host country as a major/important financial centre	2	2.000	0.500	2	1.750	0.786
Economic/political situation in host country	3	2.111	0.928	5	3.667	0.816
Presence of other banks in host country	4	2.333	0.500	3	1.947	0.780
Level of foreign investment (including home country's)	5	2.600	1.265	4	2.000	0.775
Interest Rate Differential (between home and host countries)	6	3.333	3.536	6	4.667	1.966

The reasons that compel sample banks to internationalize (via non-branch banking networks) are shown to be somewhat similar in both DCs and LDCs. For the banks in the survey, the foremost reason for establishing overseas operations, whether in DCs or LDCs, is the existence of major corporate clients in the host country. Next in equal ranking in both country scenarios is the host country general banking environment. While the first factor has ownership-specific origin, the latter is a location-specific advantage.

It is surprising to find economic/political situation in a developed country being of moderate concern, but not surprising that it is of little concern in LDC banking. The impression gained from interviewing bank executives was that the opening of new markets in Eastern Europe offered opportunities for wider geographic expansion, but banks still remained sceptical about the economic/political situations in these countries. Even within the European Free Trade Area (EFTA), the lack of harmonization of social and economic policies, as would be required by the EEC, and the political neutrality of some member countries such as Austria, Sweden, and Switzerland are sources of political and economic concern for international branch banking. Hence, rather than attempting to set up new operations, several European banks have tried to enter new markets by means of acquisition. For specific examples, see Hiltrop (1991). In addition to acquisition mechanism, Hiltrop observes that a number of banks have responded to 1992 Single European market by forming international strategic alliances as well as acquiring minority interests in rival banks.

The fact that economic/political situation in LDCs received little concern for foreign MNBs was probed further through interviews with bank executives. In the words of the head of the international division of a major UK bank, "my bank, and I know it's the same for other major international banks, has yet to grapple with the financial problem of third world debt." When asked to reconcile this with the possession of large corporate clientele, the executive said that his bank "operates through a number of strategic mechanisms that are considered less risky than wholly owned foreign branches." A senior manager in the international division of a major Scottish bank described what he called "back-to-back strategy" as an international economic symbiosis by which a bank establishes strategic relations with banks of different nationalities, the main purpose being to provide services to their overseas customers on inter-bank reciprocal basis. In other words, if a UK bank's major customer was setting up operations in Nigeria, for example, a 'back-to-back' strategy allows the UK bank to 'domesticate' the customer's services and offer them as a package through a reciprocal arrangement with a major Nigerian bank or other foreign bank based in Nigeria, with offices in the U.K.

10.7.1 DEPENDENCY BETWEEN NEW FORMS AND LDCs

Overall, there is evidence that firms operate in developed and less-developed countries for various reasons, but the findings here (Tables 10.7.1 and 10.7.2) indicate that these reasons may not be radically different and specific for the acclaimed dependency between the use of new forms of investment and LDCs. The similarity between the findings here and those of earlier studies (cited at the beginning of the section) ends in the following way. Whereas they accept as a datum that the new forms are phenomena of LDCs, apparently because the central focus of their studies was on LDCs (e.g. Beamish, 1984, 1985; Cho, 1986; Franko, 1989), the argument here is broadened to include a proposition that its use is not confined to LDCs.

In order to determine whether the use of new forms of investment is confined or restricted to LDCs, sample respondents were asked if they agreed with or disagreed with this proposition. Table 10.7.3 presents the findings. Altogether, about 71% of the 97 respondents disagreed with the proposition, 13% agreed with it, and just over 15% were either neutral or did not know. An individual firm breakdown of those disagreeing reveals this order: 84.2% Foreign companies, 70.2% UK companies, 70% UK banks, and 61.9% Foreign banks. In fact, of the 19 foreign companies in the sample, none agreed with the proposition, instead 3 indicated that they were not sure.

Table 10.7.3 Questionnaire Responses by Managers, Concerning the Notion that the use of New Forms is a Phenomenon of LDCs. (Possible Answers: Agree, Disagree, Neutral/Don't Know).

	Agree		Disagree		Neutral/DK		Valid Total	
	Freq.	%	Freq.	%	Freq.	%	No	%
UK Banks (n = 10)	2	20.0	7	70.0	1	10.0	10	10.9
Foreign Banks (n = 21)	2	9.5	13	61.9	6	28.6	21	21.6
UK Companies (n = 47)	9	19.1	33	70.2	5	10.6	47	48.5
Foreign Companies (n = 19)	0	0.0	16	84.2	3	15.8	19	19.6
Total	13	13.4	69	71.1	15	15.5	97	100.0

	Chi-Square	C	D.F.	Significance	Min E.F.	Cells with E.F. < 5
(a)	1.4339	0.124	2	.50	4.4	1
(b)	2.6828	0.168	3	.30	3.0	1

(a) x^2-Value, when banks combined versus companies combined, in a 3 x 2 contingency table

(b) x^2-Value, when Neutral responses are merged with Agree Vs. Disagree, resulting in a 4 x 2 contingency table

Siegel (1956, p.178) suggests that when k is larger than 2 (and df> 1), then X^2 test may be used if fewer than 20 per cent of the cells have an expected frequency (E.F.) of less than 5 and if a cell has an E.F. of less than 1. If these requirements are not met by the data in the form in which they were originally collected, the researcher can combine adjacent rows and/or columns without distorting the data in order to increase the E.F. in the various cells (see also, Hinkle et al. 1979, p.348). This combination was achieved on two levels: (1) merging banks against a merger of companies, and (2) merging neutral responses with agreement versus disagreement (Table 10.7.3 above). Each of these combinations resulted in a failure to reject the hypothesis. Thus, there is a good evidence to reject the contention that the use of new forms is a phenomenon of LDCs. The maximum contingency coefficient is .205 (on a scale of 0 to .816), implying a weak (low) association between new forms and less developed countries.

Finally, the Wilcoxon's Matched-Pairs test was also applied to determine whether the stage of host coutry development has any effect on the use of new forms. The Wilcoxon test is regarded as the most useful test where behavioural data are involved, in particular if both the relative magnitude and the direction of differences are considered (See, Siegel, 1956, p.75). Tables 10.7.4 and 10.7.5 present the results of this test for companies and banks, respectively. Based on this test, 5 out of 8 proxy factors of stage of development were found to be statistically significant at the indicated levels. These are:

1. Economic/political situation in host country, at 10% level. (Table 10.7.4)
2. Level of industrial development, at 5% level. (Table 10.7.4)
3. Openness of host country towards foreign investment, at 5% level. (Table 10.7.4)
4. Major corporate customers in host country, at 5% level (Table 10.7.5)
5. Size of foreign investment in host country, at 5% level (10.7.5).

These lead to a rejection of the hypothesis at the 5% level, although the significance level for economic/political situation was weak at 10%. This result seems to imply that these country characteristics have a significant impact on the choice of new forms in servicing a country. In particular, while the host country's economic/political situation, openness towards foreign investment, and level of industrial development are significant company net locational advantages for the use of new forms, for multinational banks, such advantages are derived from possession of major corporate customers and level of foreign investment. Clearly these net locational effects are found to be favourable for firms' profitability. The results of this test also indicate that the size of host country's market is not enough to induce companies to use new forms, ceteris paribus, just as the presence of other banks in the host country and the locational advantages of being a major financial centre are not sufficient reasons for non-branch banking networks. These results are consistent with the findings of Contractor (1984).

Table 10.7.4 Relationship of Stage of Development to Choice of New Forms: Summary of the Results of Wilcoxon's Paired Tests: DCs Vs LDCs: Company Evidence.

Proxy Factors of Stage of Development	Mean Rank of DC Measure	Mean Rank of LDC Measure	Wilcoxon's Paired Test Z-Statistics	No of Cases	Prob.
Economic/political situation in host country	1.829	1.053	-1.8043	12	.0712**
Size of host country's market	1.405	1.737	-1.2136	7	.2249
Level of industrial development	2.214	2.000	-2.1974	26	.0280**
Openness of host country towards foreign investment	1.674	1.684	-2.8166	19	.0049*

* Significant at less than .5% ** Significant at less than 5%

Table 10.7.5 Relationship of Stage of Development to Choice of Entry Modes: Summary of the Results of Wilcoxon's Paired Tests: DCs Vs LDCs: Bank Evidence.

Proxy Factors of Stage of Development	Mean Rank of DC Measure	Mean Rank of LDC Measure	Wilcoxon's Paired Test Z-Statistics	No of Cases	Prob.
Presence of other banks in host country	2.333	4.667	- .629	6	.5294
Major corporate customers in host country	1.889	1.700	-3.2194	22	.0013*
Level of foreign investment (including home country's)	2.600	2.000	-3.0859	14	.0020*
Host country as a major/ important financial centre	2.000	1.750	- .7803	26	.4352

* Significant at less than .5%

10.8 SIGNIFICANCE OF PERCEIVED BENEFITS OF NEW FORMS

H_8: Firm choice of new forms of international investment is dependent upon their percieved net benefits by corporate management.

The proposition that markets and hierarchies are properly regarded as alternative governance structures to which transactions are assigned in discriminating (mainly transaction cost economizing) ways (Williamson, 1975, 1981b) has long been recognized in institutional economics, but has received relatively little attention in international business. Furthermore, that a firm is a system of relationships whose existence is dependent on the entrepreneur's direction of resources (Buckley, 1989, p.154) has been largely suppressed in both the theory and empirical analyses of corporate investment (see also, Teece, 1984). The fact is that it is the corporate manager or entrepreneur who ensures that the assignment of transactions to alternative governance structures is made in a discriminating way. He is guided in this process by his assessment of the costs and benefits of alternative governance structures, given the combined effects of net ownership-specific, internalization and location-specific advantages.

Thus, it can be hypothesized that whether a given set of transactions will be executed within the firm or across firms (i.e. markets) is dependent on managerial perception/assessment of the net benefits (or costs) of using one mode rather than the other. This means that given the circumstances limiting inter-country transactions (explored in hypotheses 1 to 7) in general, corporate choice to internationalize via the mechanism of new forms will be greatly determined by managerial assessment of the net benefits of using the new forms. This assessment may be behavioural and/or may be informed by an analysis of the risk-adjusted net present values of the income stream extracted from a country under each alternative governance structure. The approach adopted here is that of Telesio's (1979) qualitative assessment of the costs and benefits of technology licensing.

Table 10.8.1 Questionnaire Responses by Managers, Concerning Net Benefits of New Forms of Investment (Scale: 1=Strongly Agree; 2=Agree; 3=Neutral; 4=Disagree; 5=Strongly Disagree).

		UK BANKS n = 10		FOREIGN BANKS n = 21		UK COMPANIES n = 47		FOREIGN COMPANIES n = 19		CROSS-SECTIONAL	
RANK*	PERCEIVED BENEFITS	MEAN	SD	MEAN	SD	MEAN	SD	MEAN	SD	MEAN	SD
2	Diversify risks (country and investment) risks	2.400	1.265	2.810	.814	2.256	.581	2.000	.000	2.367	.293
4	Avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	3.300	.823	2.905	.768	2.500	.707	2.211	.419	2.729	.412
5	Superior means of exploiting a firm's assets abroad and foreign market opportunities, with minimum resources and risks	2.800	1.135	3.429	.746	2.628	.900	2.368	.895	2.806	.391
3	Flexibility to adjust to changes in both the host economy and the international market	2.700	1.059	3.048	1.071	2.628	.757	2.316	.478	2.673	.260
1	Pre-emptive manoeuvres to gain access to promising markets and technologies	2.500	1.080	2.143	.573	2.000	.724	1.842	.501	2.121	.243
6	A less-developed country phenomenon	3.600	1.350	3.571	.746	3.476	.862	3.842	.375	3.622	.135
	VALID CASES	10		21		43		19		93	

* Refers to Cross Sectional ranking

A variety of factors, which constitute both costs and benefits, serve to catalyse the use of new forms. A cross-sectional assessment of the factors (Table 10.8.1) indicates that the use of new forms as pre-emptive manoeuvres to gain access to promising markets and technologies is perceived as significantly more important than any other factor (with an overall mean score 2.121). While Foreign banks, U.K. companies, and Foreign companies perceive the use of new forms to diversify risks as next important benefit, U.K. banks view it as slightly more important than as pre-emptive manoeuvres (mean score 2.400 versus 2.5). Again, there is an overall agreement that the use of new forms is not restricted to LDCs.

An intrafirm analysis of the scores of the benefits gives the impression of differential managerial sensitivity towards each factor. Before testing the significance of the individual factors, it is helpful to examine whether there is a difference in the scores of the populations from which the samples were drawn. If for assessment purposes, it is hypothesized that there is no difference is managerial perceptions of the benefits of new forms, then it is possible to test this claim between independent sample groups, i.e. UK companies versus Foreign companies, and UK banks versus Foreign banks. If each pair of population distributions have the same form, the observed difference implies that the scores are higher or lower in one sample group than in another. The Mann-Whitney U test is chosen for this assessment because of its sensitivity to both the central tendency of the scores and the distribution of scores (Hinkle, Wiersma and Jurs, 1979, p. 355).

Tables 10.8.2 and 10.8.3 present the results of the Mann-Whitney U test for companies and banks, respectively. The result of the tests in both the sample companies and banks lead to an acceptance of the null hypothesis of no difference in perception between UK and Foreign companies. The only exception is the diversification use of new forms among UK and Foreign companies (Table 10.8.2). This was significant at 5% level, implying that managers do differ their perception of the risk diversification benefit of new forms. This difference is even apparent from Table 10.8.1. Whereas there appeared to be virtual unanimity among sample foreign companies in the diversification use of new forms (zero standard deviation), opinion differs somewhat among UK companies in the survey (standard deviation 0.581).

Obviously, the mean perception scores are not likely to be precisely equal, but may differ because of sampling error. The results of the Mann-Whitney U tests tend to buttress an organizational behaviour study which found that executives in large US corporations significantly share common cultural similarities with their counterparts in Western Europe (O'Toole, 1979). The fact that the four sample groups share a common perception of the benefits of new forms does not imply that the latter are normally chosen on these bases.

Table 10.8.2 Mann-Whitney U-Test of the Significance of Differences in Managerial Perceptions of Net Benefits of New Forms: UK Vs Foreign Companies.

	Mean Value By Type of Firm UK n = 47	Foreign n = 19	Number of firms	Mann-Whitney Z-Statistic	Signif.
Diversify both country and investment risks	2.256	2.000	62	-1.9651	.0494*
Avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	2.500	2.210	61	-1.5922	.1113
Means of exploiting a firm's assets abroad and foreign market opportunities with minimum resources and risks.	2.630	2.370	62	- .8947	.3709
Flexibility to adjust to changes in both the host economy and the international market	2.630	2.320	62	-1.5588	.1192
Pre-emptive manoeuvres to gain access to promising markets and technologies	2.000	1.820	62	- .6748	.4998
Best suited for less-developed countries	3.480	3.840	61	-1.4647	.1430

* Significant at 5% level

Table 10.8.3 Mann Whitney U-Test of the Significance of Differences in Managerial Perceptions of Net Benefits of Non-Branch Banking: UK Vs Foreign Banks

	Mean Rank By Type of Firm UK n = 10	Foreign n = 21	Number of firms	Mann-Whitney Z-Statistic	Signif.
Diversify both country and investment risks	2.40	2.81	31	-1.3708	.1704
Avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	3.30	2.91	31	-1.3028	.1927
Means of exploiting a firm's assets abroad and foreign market opportunities with minimum resources and risks.	2.80	3.43	31	-1.4588	.1446
Flexibility to adjust to changes in both the host economy and the international market	2.70	3.05	31	- .8222	.4110
Pre-emptive manoeuvres to gain access to promising markets and technologies	2.50	3.57	31	-1.1157	.2645
LDC phenomenon (i.e. best suited for LDC projects)	3.60	3.57	31	- .4311	.6664

In order to test that the choice of new forms is related to managerial perception of net benefits, the Kruskal-Wallis one-way analysis of the variance test was applied. In this test, the theoretical frame of reference (i.e. the null hypothesis) is that the choice of new forms is not related to perceived benefits. Put differently, the theoretical null hypothesis is that firm choice of new forms of investment is not dependent upon managerial perception of their net benefits.

Table 10.8.4 presents the results of the Kruskal-Wallis test. The analysis is significant (at the specified percentage levels) on all the benefit factors but one, namely their use as pre-emptive manoeuvres to gain access to promising markets and technologies. Thus, on the basis of these data, the perceived entry mode benefits will, ceteris paribus, induce firms to choose new forms in their internationalization process. In essence, firms will use the new forms:

1. To diversify country and/or investment risks;
2. To avoid market disabling factors of human and environmental kinds e.g. opportunism, uncertainty, entry/exit barriers, etc.,
3. As superior means of exploiting a firm's assets abroad and foreign market opportunities, with minimum resources and risks;

4. As a flexible means of adjusting to changes in the host country; and
5. To enter less-developed country markets that pose a combination of high political/economic risks and profitable market opportunities, or for marketing and service operations (e.g.professional service firms such as Accountants, Investment brokers, architects, etc).

Overall, if firms assessed the benefits of entry mode alternatives before starting foreign operations, the likelihood of costly failure and disappointments could be reduced.

10.9 SUMMARY OF THE RESULTS

Over a decade ago, Professors Yoram Wind and Howard Perlmutter (1977) noted that choosing the most appropriate entry and development strategy was a frontier issue for the international firm. A year later, Professor Richard Robinson observed that few firms actually made a conscious, deliberate cost/benefit analysis of the entry mode options. Up till today, entry mode choice remains one of the critical, but also one of the most difficult decisions in the internationalization process. Apparently, firms (mostly American MNEs) were and still are inflexible about the preeminent role of 'wholesale' ownership and control of foreign operations. Furthermore, assigning transactions between firms and markets in discriminating ways has only been recently acknowledged as the central task of corporate management.

The purpose of this study was to examine these issues by integrating entrepreneurship and the dynamics of foreign investment (the eclectic paradigm) under a transaction cost analytical framework. This required that the role of corporate management be made central to the analysis of foreign investment decisions. This in turn requires that management be aware of, and incorporate into entry mode equations, the circumstances limiting or favouring intrafirm (as well as interfirm) transactions (i.e. ownership-specific and internalization advantages), host country characteristics, and the net benefits of using alternative governance structures in any given foreign investment operation.

Table 10.8.4 Kruskal-Wallis One-Way Analysis of Variance Test of Significance of Differences in the Relationship of Perceived Net Benefits and Choice of New Forms.

Factor	UK Banks n = 10 Mean	SD	Foreign Banks n = 21 Mean	SD	UK Companies n = 47 Mean	SD	Foreign Companies n = 19 Mean	SD	Kruskal Wallis @	Chi-Square Probability @
Diversify risks	2.400	1.265	2.810	0.814	2.256	0.581	2.000	0.000	0.0016	0.0001*
Avoid market disabling factors of opportunism, etc.	3.300	0.823	2.905	0.768	2.500	0.707	2.211	0.419	0.0008	0.0102***
Superior means of exploiting a firm's assets abroad and foreign market opportunities, with minimum resources and risks.	2.800	1.135	3.429	0.746	2.628	0.900	2.368	0.895	0.0027	0.0306***
Flexibility to adjust changes in markets	2.700	1.059	3.048	1.071	2.628	0.757	2.316	0.478	0.0972	0.0750****
Pre-emptive manoeuvres to gain access to promising markets and technologies	2.500	1.080	2.143	0.573	2.000	0.724	1.842	0.501	0.1734	0.1220
An LDC phenomenon	3.600	1.350	3.571	0.746	3.476	0.862	3.842	0.375	0.5254	0.0016**

@ Corrected for Ties
* Significant at 0.01 per cent level
** Significant at 0.1 per cent level
*** Significant at < 5 per cent level
**** Significant at < 10 per cent level

Hypotheses concerning the transaction cost nature of these issues, the impact of managerial perceptions of their strategic importance to entry mode choices, and the relationship between the stage of country development and corporate choice of entry modes were tested using data gathered from a questionnaire survey of corporate executives from 47 UK MNCs, 19 Foreign MNCs (drawn from 6 developed countries), 10 UK multinational banks (MNBs) and 21 Foreign MNBs (drawn from 15 countries, including 3 LDCs). This was supported by interviews with executives of 12 UK MNCs, 5 Foreign MNCs, 4 UK MNBs and 5 Foreign MNBs.

A review of FDI studies and single component studies of new forms of foreign investment (e.g. licensing, franchising, joint ventures, etc) reveals unremitting references to a number of factors as explanatory variables of foreign investment. Table 10.9.1 presents these variables. These have never before been all brought to bear in a single empirical study. The variables accord with Dunning's eclectic framework, as indicated in the Table. The specified significance levels indicate the explanatory power of the variables, in statistical terms. From the discussion of the significance levels in several statistics books, it can be inferred that there is no rigid or hard-and-fast approach to the setting of significance levels. It is for heuristic reasons instead that significance levels are emphasized; such an exposition seems the best method of clarifying the role which the information contained in the sampling distribution plays in the decision-making procedure (Siegel, 1954, p. 8; see also, Norusis, 1986, p. 226).

Table 10.9.2 presents the relationship of these variables in explaining new forms of investment. Altogether 10 of the 17 variables are found to be significant explanatory variables of foreign investment. The findings suggest that these factors play important roles, albeit in varying degrees, in foreign investment decisions. They derive from firms' ownership-specific advantages, internalization-incentive advantages, and location-specific advantages (see Table 10.9.1). Ownership-specific advantages of the following kinds were found to be significant in explaining foreign investment. These are firm size (as measured by turnover, assets or employees), ability to customize products to host/regional market, and experience of foreign markets. The last two factors and firm size as measured by turnover were found statistically significant at 0.10%, while size as measured by employees or assets (for banks) was significant at 1%. Firm size denotes corporate capability, that is, financial, managerial and technical capability. In this study, the impact of firm size is tested in two ways (using the three criteria). First, it was established by Chi-square tests that firm size and choice of new forms were related for the sample UK and Foreign companies. Second, each sample group was categorized into small, medium and large sizes, and were examined separately as to the reliance on selected NFI-adoption rationales. These have been described as "defensive reaction" or "second best" alternative reasons for adopting new forms of investment (Oman, 1984, 1986; Ozawa, 1984). The statistical evidence from the four sample groups is not clear-cut; different sample groups manifest different relationships with selected NFI-adoption rationales (Tables 10.3.2 - 10.3.5). None of the NFI-adoption rationales was consistently significant across the four sample groups. But a cross-sectional analysis of the impact of firm size on the choice of new forms (Table 10.9.2) shows that it is significantly related to choice of from, regardless of the size criterion employed in the analysis.

However, the evidence from sample small and medium-size firms is not in accord with Franko's (1989) finding that "smaller companies hungry for market share often competed for governments' favours by offering minority ventures as a way of accomplishing their own objectives of entry into an international oligopolistic industry". There is certainly evidence of the willingness to share ownership and control by SMFs, particularly by foreign firms more than UK firms, but not of the kind seen under the "Wells effect." Perhaps, the apparent 'inertia' may have something to do with the traditional conservative attitude of the British. More importantly, however, is that on the average, large firms appeared to have a higher propensity to use new forms, which by implication means a greater willingness to share ownership and control, than SMFs. This may be due to the confidence they (the large firms) have in their ownership-specific advantages which allow for greater bargaining power and manoeuvrability - as one Japanese company executive called it, "switch-over power" - over the SMFs. The Japanese and European companies' executives interviewed underscored the importance of the flexible entry mode approaches to their corporate global existence. The marketing director of a large US MNE indicated that his group would be quite willing to collaborate with local partners once the market was there. For many large firms, the adoption of flexible entry mode enabled them to gain greater control subsequently because the inadequacy of the local partner would be so apparent that control would almost certainly default to the large foreign MNE partner.

Table 10.9.1 Some Determining Factors of Foreign Investment

Nature of Advantage	Explanatory Variable	Significant up to 5% level @	Insignificant beyond 10% level @
O	Size of Firm:		
	Measured by Turnover (for companies)	X	
	Measured by Assets (for banks)	X	
	Measured by Employees (all)	X	
I	To achieve international diversification	X	
L	Host government's policy/regulation on FDI	X	
L	High political risk in host country	X	
I	Willingness to share ownership and control	X	
I	Minimization of country and investment risks	X	
L	Political/economic climate in host country	X	
L	Psychic distance		X
I	Pre-emptive manoeuvres	X	
L	Less-developed country phenomenon		X
O/I	Products customized to host/regional market	X	
I	Economies of scope and scale		X
O	Experience of foreign markets	X	
L	Levels of economic development		X
L	Size of host market		X

@ = Depends on sample size. Here, n = 97

O = Ownership-specific advantage
I = Internalization-Incentive advantage
L = Location-specific advantage

It must be stressed that while firm size may be important in entry mode choices, it must be balanced against other firm-specific characteristics. For example, the desire to achieve international diversification, willingness to share ownership and control, desire to minimize risks, and extent to which pre-emptive measures are required are internalization-incentive advantages. All these were found to be particular strategies of firms in overseas operations and were significant in choosing new forms among the sample firms.

Table 10.9.2 New Forms of Foreign Investment: Analysis of Explanatory Variables.

	Kruskal-Wallis Z-Value	Probability	Chi-Square X^2-Value	Probability
Size of Firm (as measured by Turnover)	4.3764	.2236	22.1695	.0064**
Size of Firm (as measured by no. of employees)	3.1811	.3645	19.6316	.0203***
Size of Bank (as measured by Assets)	6.2888	.0984	20.2100	.0632***
Achieve international diversification	1.7860	.1814	17.5517	.0142***
Host government's policy/ regulation on FDI	24.2596	.0000	35.1000	.0000*
High political risk in host country	28.6151	.0000	45.0393	.0000*
Willingness to share control	10.5220	.0146	30.7300	.0022**
Minimization of country risks	5.5835	.1337	15.6600	.0741***
Political/Economic climate in host country	.9091	.3404	6.7400	.0806***
Psychic distance	2.3484	.1254	4.6700	.3226
Pre-emptive manoeuvres	5.4360	.1425	19.6000	.0750***
An LDC phenomenon	1.6568	.6466	31.5900	.3459
Products customized to host/ regional market	2.6460	.1038	7.8516	.0016**
Economies of scope	1.8659	.6007	12.6490	.3950
Experience in foreign markets	8.4383	.0378	23.2200	.0057**
Level of economic development	1.3644	.2428	2.3000	.5122
Size of host market	2.1660	.1411	4.3400	.2265

* Significant at .01 percent
** Significant at .10 percent
*** Significant at 1 percent

While firm-specific characteristics provide firms opportunities to evaluate their strengths and weaknesses in relation to a given overseas operation, host country-specific characteristics offer a complementary platform for assessing the optimum mode of entry into a particular country. Because most location advantages accrue by reason of differences in location-specific endowments between countries, they are not firm-specific by themselves. Rather, it is the combined effects of these with ownership-specific advantages and internalization-incentive advantages that generate firm-specificity and differences among multinationals. Of the seven location-specific characteristics commonly found in foreign investment studies and tested in this study, only three were found to have significant explanatory impact on new forms of investment across the four sample groups (Table 10.9.2). These are: the host government policy/regulation on FDI, high political risk in host country, and political/economic climate in host country. The last two are closely related. Together with national policies towards inward foreign direct investment, they act as strong determinants for choosing new forms of investment.

Host country-specific policies and environmental constraints on foreign investment vary considerably in form, intent and impact on firms. In general, host government's inward FDI policy and high political risk were found to be highly significant at .01% while political/economic climate was significant at 1%. These results are consistent with Davidson and McFetridge's (1985) hypothesis of greater reliance on external mechanisms in host countries with policies that restrict the use of internal transfer mechanisms. Of course, the greater foreign firms perceive the distortion propensities of host or potential host governments, the more likely resources, insofar as they will be transferred at all, will be transferred via contractual or cooperative rather than the internalized mode (see also, Dunning, 1988, p. 182). As Davidson and McFetridge observe, governments can oblige an inward investment transaction to be conducted in a manner that is inconsistent with preplanned entry mode. Such dramatic changes will doubtlessly involve costs on the part of the foreign firm. It will be interesting to know cost implications of such sudden policy changes. Do they lead to project abandonment? What structural costs and organizational changes are posed? These questions are a matter for further research. Although host government policies may be held largely responsible for triggering the shift towards increased use of new forms, it has been observed that firm strategies and behaviour are instrumental in allowing these policies to succeed in obtaining MNE assent to minority (as well as contractual and cooperative) positions, and conditioned the kinds of MNEs that accepted them (Franko, 1989).

Such other host country-specific factors as psychic distance, LDC phenomenon, level of economic development, and size of host market were not statistically significant across the sample groups. However, when the stage of development is emphasized as the independent variable, in which case the choice of form depends on the stage of national development (i.e. DC versus LDC), then the level of economic development is found to be significant. Either way, the size of host market was not found significant. This result is in accord with that of Davidson and McFetridge (1985). Although their emphasis was on internal transfer, the authors found no relationship between market size and sophistication of the host country and technology transfer via the internalized route. A plausible reason for the lack of relationship between level of economic development and entry mode choice, apart from methodological problem, may be the stage of development of countries in the sample. Contrary to Contractor (1981) and Dunning (1988, p. 185), as countries develop, the propensity of their governments to increasingly interfere with the market system will reduce. In other words, such countries will not frequently be seen to intervene in private transfer of resources; they will leave market forces to 'sort' these out and will only be concerned if the transactions have strategic or public policy implications (e.g. defence contracts, etc.).

These findings suggest that the use of new forms is not a phenomenon of LDCs and that while country-specific characteristics and microeconomic factors are important in entry mode decisions, the actual choice of mode rests with corporate management. The literature has largely ignored this fact either because the critical role of strategic management is taken for granted in this regard or it is deemed inconsequential to the analysis of foreign investment. Yet, both in neoclassical economics and institutional economics, the central role of management is emphasized. These two dimensions have been instrumental antecedents of foreign investment research, but researchers, with the exception of Professors Buckley and Casson, have tended to downplay the role of entrepreneurship, if not outright suppressed (Teece, 1984). The correspondence between corporate management and foreign investment is emphasized all through the study.

The impression gained from interviewing corporate executives suggests that it really does not matter what the microeconomic factors may be or what locational advantages exist, the decision-maker's influence is the ultimate decider of whether or not an overseas operation will be carried out and, if so, what modality it should take. Lack of strength to prove or show very clear domination of one or two factors as determinants of new forms of investment suggests the following: (1) the interplay of a variety of factors in determining the choice of new forms or any transactional mode; (2) the factors are situationally specific, that is, the set of factors that determine the choice of mode in one investment period/country may change in the next period or country; and (3) the dynamic nature of the factors as well as changes in corporate behaviour over a period of time.

Finally, it has been mooted that new forms of foreign investment may lose their popularity (see, for example, Franko, 1989). Franko's position is captured in the following exposition. "A move toward increased acceptance of minority ownership position by MNEs has thus occurred in a few of the LDCs that have insisted on it. Quite apart from whether the minority JV form is "new" form ... is it good, bad or indifferent from a host country's point of view?" The overemphasis on the notion that new forms are designed for LDCs has blurred research judgement that although host government policies may oblige firms to use non-FDI modes, firm strategies/objectives and behaviour are actually instrumental to the success of such policies. Firms need to approach foreign markets from diverse routes and need to maintain a flexible operational mode while seeking to secure optimum economic rents.

In consideration of the foregoing, respondents were asked what they thought the future of the new forms of investment would be. Possible replies were: Will be Popular, Will be Unpopular, and Neutral/Don't know. Of the possible 97 respondents, 93 (almost 96%) replied to the question. Of the respondents, 70% of UK banks, 31.6% of Foreign banks, 57.8% of UK companies and 89.5% of Foreign companies felt that the use of new forms will become popular in future. The composition of respondents who thought that its use in the future will diminish is as follows: 10% of UK banks, 26.3% of Foreign banks, 24.4% UK companies and 10.5% of Foreign companies. The remainder in each case represents those who were unsure or preferred to be neutral (Table 13.9.3).

A test of the difference between "popular" and "unpopular" respondents among the sample groups was performed using the Chi-square test. The null hypothesis is that there is no difference between "popular" and "unpopular" respondents regarding the future of new forms. In other words, in the population, the choice of new forms is independent of differences in managerial perception of their future popularity or unpopularity. Applying the notations of Table 10.9.3 as advised by Siegel (1956, p. 178) and Hinkle, Wiersma and Jurs (1979, p. 348), the null hypothesis of no difference is rejected at the 5% level.

Table 10.9.3 Questionnaire Responses by Managers, Concerning the Future Use of New Forms of Investment (Possible Replies: Will be Popular; Will be Unpopular; Neutral/Don't Know).

	Popular		Unpopular		Neutral/DK		Valid Total	
	Freq.	%	Freq.	%	Freq.	%	No	%
UK Banks (n = 10)	7	70.0	1	10.0	2	20.0	10	10.8
Foreign Banks (n = 21)	6	31.6	5	26.3	8	42.1	19	20.4
UK Companies (n = 47)	26	57.8	11	24.4	8	17.8	45	48.4
Foreign Companies (n = 19)	17	89.5	2	10.5	0	0	19	20.4
Total	56	60.2	19	20.4	18	19.4	93	100.0

% respondents 95.9%

	Chi-Square	D.F.	Significance	Min E.F.	Cells with S.F. < 5
(a)	6.704	2	.05	5.6	None
(b)	13.801	3	.01	4.0	1

(a) x^2-Value: when banks combined versus companies combined, in a 3 x 2 table
(b) x^2-Value: when Neutral frequencies are combined with Popular versus unpopular, in a 2 x 2 contingency table

In effect, the data support the contention that the propensity to use new forms in the future may depend on the "brightness" or "bleakness" of their future. If they are perceived to have a bright future (i.e. to be of popular use), the more likely that firms will tend to use them more frequently. On the other hand, if firms perceive their future to be bleak (i.e. unpopular), the tendency to use them will diminish.

As has been observed above, such managerial perceptions will generally be informed by a combined assessment of firm-specific characteristics and receiving country-specific characteristics. There is little doubt that the new forms of investment have come to be accepted as complementary to and, in some cases as, substitutes for foreign direct investment. The objective of the study was not to investigate the FDI obsolescence claim because the focus of the research was not on developing countries. However, while the study has provided some evidence that the use of new forms is not an LDC phenomenon, anecdotal evidence points to a renewed interest in the use of FDI in LDCs.

CHAPTER ELEVEN

CONCLUSIONS AND SUGGESTIONS FOR FURTHER RESEARCH

CHAPTER ELEVEN

CONCLUSIONS AND SUGGESTIONS FOR FURTHER RESEARCH

11.1 SUMMARY OF FINDINGS

This study tests a model of foreign private investment that identifies a mix of minority equity positions, contractual and cooperative arrangements, known as "new forms of international investments." It brings together several strands of past research on various aspects of new forms and tests empirically several claims that have been made in the literature about their operational utility. One of such claims is that the use of new forms is a particular phenomenon of LDCs. The other is that they are largely suited for small and medium-size firms deemed to lack monopolistic advantages required to countervail international (including indigenous) competition and 'size power' to establish the 'first best' alternative (i.e. wholly owned subsidiary). This study also integrates the economic theory of entrepreneurship with the eclectic paradigm under a transaction cost framework. The centrality of corporate management in the internationalization process is expressed through an examination of the significance of managerial perceptions of ownership-specific, internalization-incentive and country-specific factors in entry mode choices. This approach is novel in the entry mode literature, and so also is the application of the notion of new forms to the banking enterprise.

The examination of these issues follows a progressive order of the theoretical and empirical evidence on the phenomena of interest. In the literature review section of the study (Part 1), received microtheories of foreign investment were reviewed with a view to assessing their applicability to explaining new forms. Theories of new forms of investment can be viewed as extensions of FDI theories: they may be derived from relaxing some of the restrictive assumptions of orthodox theories. The three-part overview surveys the theoretical literature relevant to the modern understanding of the determinants of international investment.

In doing so, it emphasizes theories of the MNE based on (1) the market imperfections paradigm, the product life cycle hypothesis, the oligopolistic reaction hypothesis incorporating the behavioural motives notion, and the currency area phenomenon; (2) the international diversification hypothesis, the appropriability theory, the internalization theorem, and the eclectic paradigm; and (3) an analysis of the Japanese model of foreign investment, found to be both conceptually and operationally different from western style.

The review of the literature gives rise to generalizations of the following kinds. First, the theories are based on one mode of multinationalization, FDI, involving the establishment of wholly or majority-owned foreign subsidiary (or foreign bank branch, in the case of banking enterprise). Apparently, modes of foreign investment other than the hierarchical mode sat awkwardly within the neo-classical framework of transaction cost economy based on internal organisation. Second, among the received candidates - and there are many of them - for general theory of foreign investment and of the multinational enterprise, Dunning's eclectic theory is found to possess more explanatory powers than the other contending theories. However, this approach is still deficient in some respects. First, in its original formulation, it did not envisage changing international investment strategies and, as such, lacked the power to explain non-FDI modes of investment. Second, how the three elements are configured over time is unclear and leaves a classification system that lacks dynamic content. Third, the relationship between ownership-specific advantages and internalization appears logically redundant. Finally, the relationship between the three factors and foreign investment decisions is completely ignored.

Rugman's claim that internalization represents a general theory of foreign investment and of the MNE suffers from inattention to generalities. That the raison d'etre for firm existence is to internationalize transactions is questionable. If every economic transaction is exectued via hierarchy, then, not only will the size preserving tendency of the firm be violated but also its efficiency properties will, on the margin, decline. Additionally, the role of country-specific characteristics is suppressed under the internalization theory.

The Japanese model, on the other hand, is found to reflect the attributes of new forms of investment. A review of the trading companies' overseas investment activities reveals several features which are distinct from those shown by traditional "old" form of foreign direct investment. These include: (1) a high incident of minority ownership; (2) a high propensity to form joint ventures with indigenous firms; (3) a significant involvement in turnkey projects, equipment leasing, and active promotion of technology transfer of labour-intensive, standardised products; (4) an active use of direct overseas loans; (5) the propensity to invest in their own commercial activities; and (6) the prevalance of group-controlled investment.

The study of alernative strategies to foreign investment appropriately starts with a taxonomic identification of their forms. Chapters 5, 6, and 7, constitute part two of the study. The object of the part is simply to provide a synthesis of the identity of the alternative strategies, in terms of their dimensions, characteristics and strategic importance as foreign market entry modes.

Chapter 5 discusses the dynamic structure of entry mode determinants and the influence of corporate development strategies. It is noted here that the dynamics of the international environment force changes both in the direction and method by which economic activities are organized. Descriptions of foreign investment strategies assume a wide spectrum of entry patterns, ranging from export modes through variants of contractual and cooperative modes to wholly-owned subsidiaries. Exporting, the first part of the review, has been a historical means of opening up new markets. It offers opportunities for circumventing domestic market constraints and is a strategic means of increasing global turnover and profit. Exporting is often generalised as the least risky means of internationalization or the 'toe-in-the-water' in international business. Contrary to popular belief, exporting is not a simplistic form of foreign involvement; it is a specialised field which demands firm commitment, in terms of both resources and efforts.

Licensing and franchising are also reviewed as international market development and investment strategies. Although licensing and franchising are closely linked, they present relatively different organizational features. International licensing offers licensors the opportunity to exploit their know-how in foreign markets by granting rights to local licensees. The rights are generally associated with the manufacture and marketing of the licensor's product in the licensee's home or regional market. A licensing exchange can be outward, inward or reciprocal. International licensing decisions are complex: theoretical explanations of its motivations integrate contributions from economics, stages of development hypothesis and business strategy approach. These frameworks suggest circumstances under which licensing will be a transactionally superior mode of international market development to FDI. The strategic context of international license is seen as one in which markets and hierarchies combine with eclectic insights to explain the corporate motives for adopting this mode.

Franchising is a distinct type of license agreement. A franchise agreement provides a wider package of services than licensing. In general, the package incorporates the use of trademark and know-how, input and component supplies, support service, and a continuing direct relationship between franchisor and franchisee. Two types of franchise are distinguishable: the product and trade name franchise, and business format or full business sytem franchising. The latter type is more comprehensive and is the model that is populary used in an international context. The internationalization process of franchising follows many paths: some direct and some indirect. The adoption of any route is shown to depend on the interaction of three kinds of influence: change agents, pre-establishment stimuli and firm-specific characteristics. Also, managerial expansion ethos are shown to be important along with other decision-maker driven factors in determining international entry.

Five types of contractual arrangements commonly used in combination are found to manifest different characteristics. These are management contracts, turnkey contracts, international subcontracting, production-sharing contracts and risk-service contracts. Management contracts bring about the expertise of the foreign firm in general or specialised functional areas. This expertise confers operational control on the foreign contractor in the performance of the contract or crucial phases of it. The use of management contracts in servicing foreign markets connotes a willingness of MNEs to assume managerial role rather than equity interest. This transactional posture allows the MNE to establish in markets that are increasingly inhospitable to FDI or those traditionally closed to foreign investors. The motives for management contracts vary, including offensive or initiative strategy, capital constraint, risk reduction, market penetration and investment protection. As well as for profitability reasons, management contracts could be the only mode of involvement acceptable to some host governments.

Turnkey contracts involve a significant deployment of the firm's resources. Under the arrangement, the MNE has responsibility for setting up a complete production facility for eventual transfer to the host country owner. Turnkey projects represent idiosyncratic investments, involving expenditure of transaction-specific kinds in human and physical capital. Variants of turnkey contracts include product-in-hand contracts or sub-assembly contracts and market-in-hand contracts. Under these modified arrangements, the MNE's responsibility extends beyond ordinary turnkey to include training of local personnel who will take over the operation of the plant after the 'key has been turned.' In the latter version, the MNE additionally takes responsibility under the contract for the sale of the project's output. A feature common to all forms of turnkey arrangements is their size, in terms of both scale or complexity of operations and the amount of resources.

International subcontracting, also known as contract manufacturing, relates to the production of components or the assembly of finished products. Such contracts are primarily used for projects domiciled in developing and eastern bloc countries. The growth of international sub-contracting is closely related to the tariff regulations in developed countries and proliferation of free trade or export processing zones in developing countries. This mode of international entry can be viewed as arising from economic-dominant process in which the MNE's motivation is predicated upon the need to economise on production and transaction costs as well as on the desire to sustain a flexible production system. International subcontracting may also be induced by host government's distortion propensities and/or firm concern over risk considerations.

Production-sharing contracts are primarily found in oil and extractive industries. Such projects entail huge resource commitment and involve the host government or a state-owned company as a joint partner. Specific features of the agreement include pre-determined production percentage share, pre-determined share of the physical output, and length of time required to recoup pre-production costs and to hand over contract rights to the state company. Production-sharing contracts provide a host country opportunities for attracting foreign investment without losing ownership and control of its resources. The size and complexity of such projects coupled with their longevity contributes significantly to multiplicity of benefits flow which, in conjunction with the host government's partnership, potentially reduces both investment and country risks.

Risk-service contracts are similar to production-sharing contracts. Both are used primarily in the petroleum and extractive industries. The crucial investment distinction between the two is that under risk-service contracts, the MNE's share of output is paid in cash rather than in physical output, although the agreement may permit an exchange for equivalent amount of output determined at international market prices. Another important feature of risk-service contracts is that the burden of risk rests solely on the MNE, who also provides the investment capital for exploration and production. The compensation package comprises capital reimbursement, interest on the capital and a pre-determined percentage of risk fee out of production revenues.

The chapter concludes by summarising the role of joint ventures (JVs) in the strategy of international investment. JVs can be perceived as being next to wholly owned subsidiaries in the ladder of foreign investment, in terms of ownership and control. JVs have distinct characteristics and present a distinct set of advantages as an alternative mode of international investment from those considered in previous chapters. Yet, however, their operational dynamics frequently involve contractual modes such as management contracts or licensing. JVs may be equity based or non-equity based. The factors underlining the growth of IJVs range from cost and risk considerations through international competition to host government impositions. JVs offer opportunities for macroeconomic development, including new technologies, personnel training and transfer of tradesecrets and know-how, and access to international markets. Above all, they provide firms and host countries with resources for which there may be no equally efficient and available substitutes, especially for high risk and capital intensive projects.

Finally the configuration of a JV model requires an assessment of the external environment as well as an examination of firm-specific characteristics. The model should incorporate features which anticipate circumstances under which the JV reconfiguration may be necessary. It should also provide for adaptations to monitor performance and stability as well as contingency mechanisms for equitable disposition of the JV in the event of a dissolution.

Chapter 7 concludes this part of the study with a review of the strategic forms of international banking. This study is about alternative strategies of international investment. International banking is within its scope and is shown historically to be a logical extension of international business. International banking is not amenable to any precise definition. However, foreign branch banking is shown to be the FDI counterpart of foreign subsidiary of MNBs. From a technical viewpoint, banks have a wide range of organizational forms of servicing foreign markets. Within the purview of 'new forms of international banking', three categories of organizational modes are distinguished: cooperative arrangements, joint venture or consortium banking, and merchant banking and associated services.

Part three is the empirical and concluding part of the study. It is made up of four chapters (chapters 8 to 11). Chapter 8 discusses the research design and research hypotheses. It also presents a statement of the purpose of the research, discusses the need for the research and develops the study hypotheses.

The hypotheses of study are developed around eight propositions:

(1) managerial assessment of firm-specific characteristics and use of new forms of international investment (NFI).

(2) Firm global strategy dimension.

(3) Relationship between firm size and use of NFI.

(4) The impact of foreign investment policy shifts.

(5) Significance of host country-specific characteristics.

(6) The impact of competitors' entry mode behaviour.

(7) Relationship of stage of country development to use of NFI, and, in particular, the dependency between LDCs and NFI.

(8) The significance of perceived net benefits of NFI to entry mode choice.

Chapter 9 is concerned with the research methodology and statistical procedures. The chapter discusses the approaches adopted for field research and presents the preliminary analyses of the research findings. This is the descriptive phase and is divided into eleven sections, covering the questionnaire administration and data reliability, description of statistical techniques, characteristics of firms (companies and banks) in the survey and preliminary findings based on the fieldwork. The initial results of the study relate, inter alia, to details of international entry modes, including initial U.K. entry modes by foreign companies and establishment modes of international banking, significance of specific clauses in contractual arrangements (for MNEs); motivations for new forms of investment, and organizational influences on entry mode choices.

Chapter 10 presents the second, and main, part of the research findings. Essentially, the chapter is analytical and is concerned with an in-depth statistical analyses of the research findings. The analyses are based seriatim on the eight study hypotheses, postulated in chapter 8. For each hypothesis test, a comparison of the results is made against relevant previous or tangential research findings.

Hypotheses concerning the transaction cost nature of the eight issues, the impact of managerial perceptions of their stratetic importance to alternative entry mode choices, and the relationship between the stage of country development and corporate use of new forms are tested using data gathered from a questionnaire survey of corporate executives from 47 U.K. MNCs, 19 Foreign MNCs (drawn from six developed countries), 10 U.K. MNBs and 21 Foreign MNBs (drawn from 12 developed and 3 developing countries). Altogether the sample consists of 97 firms. The questionnaire survey is supported by interviews with 26 corporate executives drawn from 12 U.K. MNCs, 5 Foreign MNCs, 5 U.K. MNBs and 5 Foreign MNBs. Due to insufficient country coverage, firms drawn from outside the UK are aggregated as 'Foreign Companies' and 'Foreign Banks' for statistical analyses. In the analyses the role of corporate management is made central to foreign investment decisions. A review of FDI studies and single component studies of new forms of international investment (e.g. licensing, franchising, joint ventures, etc.) reveals a frequent reference to a number of explanatory variables. These variables are derived from Dunning's eclectic paradigm.

Different statistical techniques are applied in testing the hypotheses. The principal findings are summarized hereunder.

1. As a general rule, the central role of management in entry mode decisions, and, in particular, in firm assent to minority positions or contractual/cooperative forms is observable among MNEs and MNBs (see 10.1).
2. The study provides evidence on the relationship between corporate strategy and acceptance of new forms of investment (see 10.2). Firms become global for

many reaons, and need an approach appropriate to meet new or potential challenges in the international marketplace. Diversification motive hypothesis implies that firms go international in pursuit of global expansion. The oligopolistic reaction hypothesis suggests that firms become global as part of an oligopolistic "catch-up" or "geographical-matching" strategy. In short, strategy in international business is influenced by many considerations. Both the environment of operation and government-induced changes influence the strategic options open to the MNEs. Since not all MNEs can respond efficiently to these environmental parameters, this study provides strong evidence that those that seek to maintain competitive edge over rival or host country firms tend to use variants of new forms as part of market-matching or oligopolistic reaction strategy.

3. There appears to be no systematic relationship between firm size and the use of non-FDI modes among the sample firms. While there is some evidence, based on respondents' views, about the influence of firm size on the choice of new forms, there appears to be little evidence for the proposition that firms accepting minority or non-FDI positions are predominantly small and medium-size (see 10.3). The widely-held view is that smaller companies hungry for market share often competed for governments' favours by displaying a high propensity for new forms as a way of accomplishing their own objectives of entry into an international oligopolistic industry (Franko, 1989; see also, Oman 1984a, 1986). However, the cross-sectional evidence from the four sample groups contradicts the above proposition and is in accord with the findings of Franko who observed that "know-how diffusion and the breakdown of other barriers to entry ... obliged even industry "majors" to accept minority forms in the face of host country demands."

The lack of general, systematic relationship between firm size and use of new forms may be attributed to two reasons. One is the way of constructing the size variable and the other is the post-classification smallness of the sample size, particularly the sample banks. The first reason is not peculiar to this study; most researchers have attributed the inconsistent evidence of firm size to the way in which the size variable is constructed (see for example, Dunning, 1988, ch.6; Terpstra and Yu, 1988). For this study, methodological problems of the kinds experienced by these authors only arise from the "NFI-adoption rationales" rather than one of a statisical kind. On the other hand, the impact of firm size as perceived by the respondents themselves may likely be less subjective and hence less likely to bias downward the impact of firm size for the large firms in the sample than the above studies. This is the stance adopted in this study.

The second reason for the unsystematic result of the impact of firm size relates to the size of the firms after reclassifying them according to respondent managers' perceptions. Especially in the case of U.K. banks, this approach yielded 2 small-sized banks, 3 medium-sized banks and 5 large banks. With such small samples, the quality of "unbiasedness" cannot be protected by the statistics so produced.

4. Changes in firm foreign investment strategy are geared towards responding to changes in the environment of operations. Such firm policy shifts are necessary to take advantage of emerging opportunities in the market place, such as the need to accept a reduced equity position or accept cooperative/contractual arrangements in return for a preferential access to a protected market. Firms contemplating entry into Japan or other protected markets tend to alter their foreign investment policies to suit host government inward investment requirements.

"Strategic postures" as used in this study classify firms not by size or by "specialty niche/segment domination" as employed by Franko (1989), but according to the recurrence of shifts in corporate investment behaviour (see 10.4). Firms classified as pursuing a "dynamic strategic posture" were those that frequently altered their foreign investment posture in the last five years in relation to their geographic concentration. The converse represents "static strategic posture." Unlike Franko's classifications which were made subjectively by him, the classifications in this study are made by corporate managers of the responding firms on the basis of industry characterizations. Firms with highly diversified product lines and/or those with diversified geographic operations tend to adopt "flexible" or "dynamic strategic postures". These firms may favour using new forms either as a means of obtaining incremental returns from products which are gradually phased out of the corporate product portfolio (ibid.) or as a means of adjusting to "geographical-matching requirement of high-performing but protected markets. A number of researchers have described the process by which oligopolistic, risk-profile matching behaviour in a sector, would propel 'follower companies' to adopt flexible ownership policies in attempts to match 'leader companies' geographical scope (Knickerbocker, 1973; Vernon, 1974; Vernon and Wells, 1976). The reason is that the follower companies, generally seen as small or medium size firms (SMFs) are presumed to lack the technological, financial and managerial capabilities required to fully compete with rival industry leaders as well as with LDC risks and challenges, via wholly or majority-owned subsidiaries.

5. While firm-specific characteristics provide firms opportunities to evaluate their strengths and weaknesses in relation to a given overseas operation, host country-specific characteristics offer a complementary platform for assessing the optimum mode of entry into a particular country. Host country-specific policies and environmental constraints on foreign investment vary considerably in form, intent and impact on firms. In general, host governments' inward FDI policies, high political risk and political/economic climate bear significant relationship with the use of non-FDI modes (see 10.5) . The findings here are consistent with Davidson and McFetridge's(1985) hypothesis of firm reliance on new forms (defined generally in their study as market mechanisms) in host countries with policies that restrict the use of internal transfer mechanisms.

Managerial perceptions of the nature and importance of host country characteristics and their impact on the diversification strategy of the firm are significant in entry mode choices. Thus, the greater foreign firms perceive the distortion propensities of potential host countries, the more likely resources, insofar as they would be transfered at all, will be transfered via new forms rather than via hierarchy. The evidence of this study appears to show little or no support for the impact of the following host country-specific factors on the use of new forms (see 10.5): psychic distance, LDC phenomenon, level of economic development, and size of host market. But, when the stage of country development is emphasized as a dichotomous independent variable (i.e. DC versus

LDC), then the level of economic development is found to be significant in the use of new forms (see 10.7). Either way however, the size of host country's market does not appear to be significant. Thus, in support of the findings of earlier studies of Davidson and McFetridge (1985), Terpstra and Yu (1988), and contradictory to the findings of Contractor (1981) and Dunning (1988, ch.6), there appears to be little or no relationship between market size and sophistication of the host country, on the one hand, and mode of entry into the market, on the other. Psychic distance is used to capture such features as cultural, social or geographic proximity. On the evidence of this study, it can be hypothesised that psychic distance has no significant impact on entry mode choice. Terpstra and Yu (supra) reached a similar conclusion in their study, although an earlier study by Davidson and McFetridge (supra) found support for the impact of psychic distance (i.e. geographic proximity) and the probability of internal transfer.

6. One interpretation of the defensive reaction hypothesis or oligopolistic reaction hypothesis is that the move by multinational firms towards greater use of new forms of investment is an essentially defensive reaction, as these firms seek to match competitor behaviour, or as part of an oligopolistic "catch-up" or market-matching strategy. In particular, the "Wells effect" presumes a higher propensity of smaller, lower market-share firms within an industry to utilize the non-FDI modes than do industry leaders (i.e. large multinationals). These hypotheses are not supported by the findings here (see 10.6). A simple way of determining whether rival firms' entry mode behaviour influences corporate assent to minority or non-FDI position is to pose the question directly to business executives in the "corridors of power." A large proportion of the executives indicated that competitors' entry mode behaviour had no influence on their use of new forms as opposed to those who answered in the affirmitive (see Tables 10.6.1 and 10.6.2). Thus, contrary to the initial concern, there appears to be little evidence for the defensive reaction hypothesis, oligopolistic reaction hypothesis or the Wells effect, implying that the trend towards the use of new forms is independent of rival firms' mode of international entry or choice of form. Perhaps, one reason why firms' entry mode choices are unaffected by rivals' entry mode behaviour may be firms' greater concern with host government policies and their

own strategic posture than with competitors' behaviour per se. Another may be what can be termed the 'fashion of the investment climate or period' as well as the dynamic nature of the factors that determine choice of form. Entry mode patterns are as dynamic as the environmental parameters that determine them. Therefore, what may be fashionable in one period or country may not obtain in another.

7. One primary concern of this study is to provide empirical evidence to support or refute the widely held notion that the use of new forms is a particular phenomenon of LDCs. In other words, is the move towards the use of new forms of international investment related to the stage of country development? To determine the relationship of stage of development to NFI-usage rationales, a number of macro- economic variables identified as proxy factors of host country characteristics are used to gauge situations in which the use of non-FDI modes will differ between developed and developing countries (Tables 10.7.1 and 10.7.2). In the tests, certain host country factors are found to be significant in the choice of entry modes between DCs and LDCs among the sample firms. These include, economic/political situation in host country, level of foreign investment in host country, level of industrial development and openness (or restriction) of host country towards foreign investment (Table 10.7.4 and 10.7.5). These factors provide rationales for adopting new forms. As countries develop the propensity for their governments to interefere with the market system will reduce, *ceteris paribus.* Thus, high distortion propensities juxtaposing "profitable investment opportunities are likely to lead to the use of new forms. This finding is however contradictory to an original hypothesis which states that, as countries develop, the propensity for them to rely proportionately less on internalized mode and proportionately more on externalized mode will increase (see Contractor, 1981; Dunning, 1988, p.185).

There seems to be a lack of general systematic relationship between the stage of development and the use of new forms in the sample firms. The findings suggest that the use of new forms may not be a particular or a general phenomenon of LDCs and that while country-specific characterists and micro-economic factors are important in entry mode decisions the actual choice of mode rests with corporate management. In this connection managers of the sample firms were asked if, in their opinion and experience, the use of new forms is a general phenomenon of LDCs. Majority of the respondents disagreed with the proposition. Sample foreign companies, in particular, showed a complete disagreement with the hypothesis (Table 10.7.3). Notwithstanding this finding, there is little doubt that MNE acceptance of new forms is related to host country policies as the earlier evidence suggests. As the literature also suggests, such policies could have been prompted by government insistence on increased local ownership and participation. This in itself is not a bad policy: it is a way of protecting indigenous skills which every national government is obliged to do, developed or developing.

Beyond this however, the observed shifts in LDC policies during the 1970s were the product of the economic and political tenor of the times. First, the period (1973-1975) witnessed series of United Nations hearings on the role of transnational corporations in third world development(see Franko, 1989). Second, this period saw unprecedented increases in the wealth of many oil producing LDCs. By the mid 1970s the combination of these two factors could be seen as highly contributory to the increased bargaining powers of many LDCs. For countries like Iran, Libya, etc. their "hatred" for American government literally spilled over to American allies such that western MNEs were perceived as instruments of 'American imperialism' or 'anti-Moslem.' These are subterraneous factors which were largely responsible for the apparent hostility towards foreign MNEs. In short, the unremitting reference to the notion that new forms are designed for LDCs has blurred research judgment that while host government policies may oblige firms to use non-FDI modes, firm strategies/ objectives and behaviour are actually instrumental to the success of such policies.

8. This study attempts to emphasize the correspondence between entrepreneurship and foreign investment decisions. The literature has largely ignored this fact. The impression gained from interviewing the corporate executives suggests that the decision-makers' influences and perceptions are very crucial to whether or not an

overseas operation will be embarked upon and, if so, what modality it should take (see also, Welch, 1990). Usually, the decision-maker is guided by his assessment of the firm's corporate capability (i.e. its ownership-specific advantages), its internalization-incentive considerations, host country-specific characteristics and cost/benefit analysis of using alternative governance structures. All these considerations are incorporated in the analysis of new forms of investment.

Accordingly, it is hypothesized that firm use of the new forms is significantly related to their perceived net benefits. In the cross-sectional questionnaire, the managers of multinational banks and companies were asked questions relating to their perceptions of the benefits obtained or likely to be obtained from using non-equity modes of foreign investment. They were asked, for each of six factors (including the five below), to state the extent of their agreement or disagreement with 'a certain factor' (Table 10.8.1). A statistical analysis of the managers' responses offers evidence that perceived net benefits of new forms (and for that matter, direct investment) can function as a seed bed for relevant impulses and prepare the foundation for an international move (Tables 10.8.2 and 10.8.3). Through variants of new forms of international investment, a multinational firm can (1) diversify both country and investment risks; (2) avoid market disabling factors of opportunism, uncertainty, barriers to entry or exit, etc., (3) exploit both its advantages abroad and foreign market opportunties, with minimum resources and risk; (4) secure flexibility to adjust to changes in the host economy as well as in the international market; and (5) invest in promising LDC markets, without committing large resources or with minimum risks and uncertainties. Its use as a pre-emptive manoeuvre is not supported by the statistical tests. As with licensing studies (Telesio, 1979), exporting studies (Reid, 1981; Welch, 1983) and franchising studies (Welch, 1990; Brickley, Dark and Weisbach, 1991), the relative impact of the catalysts of non-FDI modes appear to depend heavily on how they are perceived by corporate management acoss the sample firms.

11.2 CONCLUSIONS FROM THE STUDY

Analyses of the research findings suggest several conclusions which primarily reflect the objective of the study. The objectives in turn capture most of the literature concerns about the transactional efficiency of new forms of investment. These concerns relate to issues of four general kinds. First, are the new forms ofinvestment substitutes for, or complements, of foreign direct investment? Second, is FDI becoming obsolescent in the changing global investment environment? Third, what is the role of the economic theory of entrepreneurship in foreign investment decisions and, in particular, in entry mode choices? Finally, are the new forms of investment confined to LDCs?

11.2.1 NEW FORMS AS A SUBSTITUTE FOR FDI

The option of minority-equity and non-FDI modes as a means of entering into and establishing in a foreign market instead of making a full investment has been recognized in the literatures of international business, international economics and international financial management. But the transactional properties of new forms have received little systematic attention in these literatures. Alternative investment strategies provide firms (as investors) and host nations (as recipients) opportunities to build satisfactory institutional forms for reconciling their competing interests. On the inter-firm level, they provide institutional mechanisms for reducing the cost and risk of foreign investment. A foreign investment must be both profitable for the multinational firm and effective for the host country's objectives. In these circumstances, new forms present opportunities to reconcile the firm's global objectives with environmental considerations in ways which may not be practicable or acceptable under FDI mode.

The evidence of the study also suggests that the new forms present opportunties for multinational firms to penetrate markets and countries foreclosed to foreign MNEs via direct involvement. The findings of the study lead to a suggestion that in certain circumstances, the new forms are transactionally more expedient than the direct investment mode. In particular, the empirical analyses here suggest five main reasons why sample multinational firms prefer new forms to foreign direct investment. These are, in order of importance:

1. When the objective is to achieve international diversification with minimum commitment of corporate resources.
2. When host government's regulation/pressure restricts inward direct investment.
3. When a promising host market is potentially strewn with high political risk, in particular risk of expropriation.
4. Risk and costs diversification, improving their sensitivity to host country conditions and thereby penetrating awkward market segments.
5. Customizing products to a host country without commiting huge resources, especially if such investments are non-recurrent or if host country policies do not permit direct investment.

These findings correspond with the conclusions of earlier studies (Contractor and Sagafi-Nejad, 1981; Contractor, 1981b, 1984, 1985). Although the study did not investigate a direct comparison of returns which Contractor found to disfavour the direct investment mode, the evidence of perceived benefits of new forms, coupled with the impression gained from interviewing the managers, suggests that a mix of entry mode choices is an increasingly acceptable corporate strategy. This finding corresponds with that of Wright(1981). The establishment of wholly owned foreign subsidiaries (or foreign branch banks) can no longer be seen as a primary organizational concern in the internationalization process of firms, even the very large ones. Firms are increasingly favouring international cooperative arrangements alongside other options. Notwithstanding the evidence, any categorical statement suggesting that the new forms are a substitute for direct investment will be presumptuous. Rather, one would state that under certain circumstances, as outlined above, the new forms may be more efficient governance structures than FDI, and hence preferable under those circumstances.

11.2.2. NEW FORMS AS A COMPLEMENT OF FDI

The empirical findings here suggest that the strategy choice of new forms made by sample multinational firms is largely influenced by host government policies in active conjuction with firm-specific factors. The choice of appropriate foreign investment strategy is at the core of international business. Therefore, alternative investment strategies must be evaluated in terms of their economizing properties or income generating potentials. Even in awkward host country circumstances, a strategy of new forms can be linked with at least three types of income or compensation mix:

1. Joint participation in project returns,
2. Royalty or technical fees, and
3. A mark-up or a margin on component/input supplies to the project.

There is also a potential advantage of transfer pricing. Transfer pricing has conventionally been associated with internal (intracorporate) transfer pricing. However, as Arpan and Radebaugh (1985 p.257) have observed, transfer pricing can be both intracorporate and intercorporate. The former refers to sales among subsidiaries or divisions of a single incorporated entity, and the latter refers to sales among different corporate entities associated in global pursuits and objectives. In an international context, intercorporate transfer pricing refers to "any transfer made within the global corporate family" (ibid.). Mere anecdotal evidence suggests the plausibility of intercorporate transfers via the mechanism of new forms. Because the notion of transfer pricing connotes manipulative pricing tendency and/or a means of accomplishing other unsavoury deeds (e.g. tax avoidance) deemed offensive to public policy, the corporate executives interviewed were unwilling to discuss the issue. Accordingly, the study did not investigate the possibility of using new forms to accomplish transfer pricing.

Regardless of host government policies however, the above income channels may provide stability of earnings which direct investment alone may not yield. Because these types of income are linked to turnover rather than profit, they are less volatile than dividends which are payable only if and when profits are realized and declared. In this sense, the income channels of new forms may smooth out cash flow and reduce risk. Second, economic stabilization policies (e.g. balance of payments problems) may force a host government into freezing dividends, but may release foreign exchange for necessary components imports, royalties and other payments called for under international contracts (ibid.). Finally, sales of the product to third country importers through the foreign firm would be encouraged by the host government, thereby enabling the firm to earn profits thereon. A combination of these factors enhances potentials of new forms as viable complements to FDI, in reducing risk and taxes, and stabilizing earnings, which FDI alone may not fulfil.

11.2.3. THE OBSOLESCENCE OF FDI HYPOTHESIS

From the findings of this research it is difficult to surmise that FDI is becoming obsolescent. What is though clear from the evidence of sample firms is the perception of growing popularity of new forms of international investment. The majority of the international managers indicated that new forms would become even more popular in international business in the future, for the reasons stated in the preceeding two sections (see Table 10.9.3). If by increased popularity is implied declining importance of FDI, then the results of this study point to the fact that the use of hierarchy is increasingly coming under scrutiny both at the firm and national levels.

The results also lend credence to the fact that the choice of strategy - markets and hierarchy - made by sample multinational firms is influenced by firm-specific factors (ownership and internalization-incentive factors) as well as host country-specific factors. Given that national controls are, and will continue to be a fact of economic life (Hood and Young, 1986 p.366), and the fact that these controls are by no means confined to developing nations, as the results of this study and those of Contractor (1981) and Thompson and Knox (1991) suggest, then it is possible to view the growing popularity of new forms by the multinational firms in the survey as reflecting Dunning's (1981) and Baranson's (1981) hypothesis that international resource transmission will, over time, move towards greater "dis-internalization."

There is nothing to suggest that international transactions may likely receive less host governmental scrutiny in the future. Besides, even large multinational firms (e.g. IBM and Germany's Deutsche Bank or French Credit Lyonnais) are willingly entering into strategic cooperative alliances or assuming minority-equity positions in Europe and elsewhere (See, Hiltrop, 1991; Thompson and Knox, 1991). All these signify the fact that the hitherto undue reliance on FDI mode of internationalization may be waning. Notwithstanding this observation, because host country policies and environmental constraints on foreign investment vary considerably in form, intent and impact on multinational firms, it is difficult to make simple generalizations of the kinds suggested by the FDI-obsolescence hypothesis or the substitution of FDI by new forms.

11.2.4. ENTREPRENEURSHIP AND THE DYNAMICS OF FOREIGN INVESTMENT

The review of the literature reveals that received microtheories of foreign investment have concentrated largely on equilibrium analyses of the firm and the hierarchical mode of economic transactions. In both respects, not only are the economizing attributes of alternative governance structures insufficiently recognized, if not ignored, but, more importantly, the role of entrepreneurship is grossly suppressed. Although this 'neglect' has been acknowledged by some authors (e.g. Teece, 1984; Casson, 1985; Buckley, 1989), the economic theory of entrepreneurship has as yet not been subjected to any systematic investigation.

This study has attempted to bridge the gap by integrating entrepreneurship and the eclectic paradigm). In this process, the role of corporate management is acknowledged and made central to the analysis of foreign investment decisions. By juxtaposing this with an understanding of the circumstances limiting or favouring intrafirm (as well as interfirm) transactions, it is possible to develop an economic theory of foreign investment which offers insights into international business behaviour.

While firm-specific characteristics provide firms opportunities to evaluate their strengths and weaknesses in relation to a given overseas investment operation, and while host country-specific factors offer a complementary platform for assessing the optimum mode of entry into a particular country, it is the contention of the study that the assignment of transactions between hierarchies and markets (of which new forms are the principal constituents) in discriminating ways ought to be seen as the central task of corporate management. The congruency between the owner-entrepreneur or the manager-entrepreneur (Casson, 1985) and foreign investment is explicable from two strands of economics: neoclassical economics and institutional economics.

In both traditions the centrality of corporate management is made conspicuous. The manager is deemed to be responsible for deciding upon and implementing operational strategies as well as making the choice of institutional arrangements, thereby "determining the boundaries of the firm" (ibid.). In relation to foreign investment, decisions have to be made about resource content, the type, how to transfer corporate know-how, to which country and in what form to establish the foreign entry. Decisions of this kind cannot be satisfactorily addressed under conditions of static equilibrium nor can they be fully explored by separating entrepreneurship from control of the firm. The evidence of this study tends to suggest that while country characteristics and microeconomic factors are important in determining the pattern of foreign entry, the actual choice of mode rests with corporate management. In the study, the relative impact of these factors appeared to depend heavily on how they were perceived by corporate management, thus confirming the findings of earlier studies (e.g. Reid, 1981; Welch, 1983, 1990) on the importance of management in the internationalization process.

11.2.5. CORRESPONDENCE WITH LDCs

The frequent association of new forms with LDCs has created an aura of correspondence of their usage with developing countries. Yet, there is abundant evidence pointing to their growth among developed countries. The argument that the move to acceptance of minority-equity and/or non-equity forms is due primarily to LDC policies (Franko, 1989) may have been exaggerated because, as Contractor (1981) has already pointed out, these policies are in no way confined to developing countries. Several developed countries (including European countries, U.S.A., Canada and Japan) are found to have policies and regulations that are similar in spirit to those of LDCs (ibid.). Even with the evolvement of the Single European Market, there is evidence of entry barriers and protective attitudes displayed by several European countries against firms of fellow community member nations (See, Thompson and Knox, 1991).

There is little doubt that host country policies are active factors in the internationalization process. Whereas host governments employ various regulations and incentives to achieve the twin goals of sovereignty and increased net benefits from the operations of multinational firms within their borders, the latter, in response, adopt a variety of strategies to circumvent such regulations or to optimize the incentives. In both "camps", a foreign investment must be seen to profit the foreign firm on the one hand, and effective for the realization of the host country's socio-economic objectives, on the other hand. Thus, new forms of international investment should be seen in a broader perspective as a set of transactional mechanisms for reconciling the firm's global objectives with environmental concerns in ways perceptibly different from hierarchies. The behaviour of many LDC governments in the 1970s should be seen in the context of international political strains and the economic fortunes of the time. Clearly, there was an identifiable move towards a greater acceptance of minority positions by western multinational firms, especially those from the U.S. and its 'allies,' but as Franko (1989) observed, this move did not appear to have a continuous "trend" rather it occurred "quite suddenly" during the period 1973 - 1975. Moreover, the sudden shift was observed in few LDCs (e.g. Iran, Mexico, Brazil, India and the Phillipines) (ibid.).

The political tenor of the 1970s was a seed bed for relevant impulses in the international relations between some LDCs, such as Iran, Libya, some Central and South American countries (e.g. Brazil, Mexico, Nicaragua, Phillipines) and the U.S.A. The conflictive inter-nation political relations generated both increased nationalism and spillover effect on the 'allies' of both sides, with western MNEs left as the proverbial grass that suffers when two elephants fight. In reality some of the host government reactions were not without foundation. For instance, some U.S. FDI activities were reported to be instruments of the U.S. government policy (Behrman, 1971). In addition, it has been observed that one result of the U.S. government's use of the multinational corporation as an instrument of power projection is the host government's increased hostility against U.S. firms (Nigh, 1985). Furthermore, U.S. investors realized that their foreign subsidiaries were often the most visible U.S. institutions in the host country and, as such, targets for anti-U.S. feelings (LaPalombara and Blank, 1977). Generalizations of this kind contribute to a host country's perception of a linkage between the interest of foreign governments and their national direct investors. Thus, as inter-nation relations degenerate, foreign investors view the desirability of investing via the direct route as being prospectively dangerous. If complete divestment was not contemplated or feasible in the circumstances, the transactional expediency of alternative governance structures would become apparent ex post.

The economic dimension witnessed an unprecedented increase in the wealth of many oil producing and exporting LDCs. The governments of these countries pursued policies aimed at matching political independence with economic sovereignty. Included in this category are Nigeria, India, Malaysia, Korea and Peru. The feeling of these governments in the 1970s was that unlimited access to inward foreign investment might create adverse effects on the domestic economy, such as the control of domestic industry by foreign firms, which could lead to insecurity or vulnerability in times of external shock prospective with massive withdrawals and potentially weaken fabrics of the economy.

Thus, rather than a developing country-specific phenomenon, it can be postulated in general that as inter-nation or intra-nation conflict increases (that is, as the number and/or intensity of conflictive inter-nation or intra-nation events increases), the host country's hostility towards related foreign investors tends to be high. Conversely, as inter-nation cooperation increases the more likely foreign investment will be spurred, *ceteris paribus*. In either scenario, firms operating via new forms are likely to experience greater continuity with, and support from, their host country partners, especially where the operation has been based upon mutual forebearance, trust and consummate cooperation.

In conclusion, the findings of this study do not lend a strong support to the hypothesis that the new forms of investment are phenomena of LDCs. The results however lend credence to the proposition that although host government policies may be largely responsible to corporate move towards increased use of new forms, firm strategies and managerial perceptions are ultimately instrumental in allowing the policies to succeed in evoking firm assent to use of new forms.

11.3. POLICY IMPLICATIONS

Studies of new forms of international investment have become important not only for firms but also for governments. The historical role of and research focus on FDI have tended to blur the significance of emerging changes in corporate foreign investment strategies. Yet, such changes have come about as a result of environmental pressures: host and home governments, market forces, and internal pressures. All of these are variables in the complex equation that determines the choice of form. Such a choice can be seen as part of the firm's wealth-maximizing process in which the central role of corporate management is decisive.

Management choice of form would tend to be influenced by their perceptions of the significance of the above pressures. In particular, it is argued that while the inducement factors of ownership-specific, internalization-incentive and country-specific advantages are important, they must be seen as static configurations in the dynamic equation of foreign investment decisions. In essence, the enabling force is corporate management. The policy implications of the argument are of three kinds. First, there is a possibility that the undue emphasis on hierarchical modes, in transactional terms, may be designed to hide the microeconomic utility of alternative modes of economic organization. Discussions of alternative governance structures are geared towards highlighting these. On the basis of this empirical investigation, new forms can be seen to have economic consequences for both the firm and recipient country. An assessment of their implications for ownership and control as well as for relationship with host governments may be especially important. This is considered as the macroeconomic utility of new forms. The third implication relates to multilateral governments such as the OECD and UNO, concerned about the behaviour of multinational firms and their relationships with host governments.

11.3.1 MICROECONOMIC UTILITY OF NEW FORMS OF INVESTMENT

The organisational failures framework, encompassing market imperfections, has been used to justify the shifting of economic transactions out of a market into a firm. A symmetrical analysis warrants a converse argument, that is, a presumption of internal organisation failure for transactions that are so unshifted (market-mediated). This is one way of looking at the microeconomic utility of new forms. However, recognition that alternative modes of economic organisation give rise to differing exchange relations which are highly valued requires that organizational effectiveness be viewed more broadly than the usual efficiency argument would dictate. Thus, modes of organisation which would have superior productivity consequences but would raise a range of socio-political issues if implemented within the firm, may be modified or rejected in favour of "next best" alternatives. A firm's foreign investment pursuit is tailored towards making profit as a market seeker, resource seeker or efficiency seeker. As a market seeker, the firm wishes to sell in the host country's domestic market; as a resource seeker, the firm wishes to establish in a country that offers the desired resources; and as an efficiency seeker, the firm wishes to economize on production costs of labour. In all of these, the firm is transfering resources of some sort at a cost and seeks to minimise the cost. The flexibility to shift from one objective setting to another or to combine objective settings without upsetting host country's macroeconomic goals is a criterion of success in a foreign market. Given the unrelenting degree of host governments' control, a careful 'match' between the foreign firm's entry mode behaviour and local desires and aspirations is therefore essential.

The conventional basis for this decision is profitability. The arguments that firms will often prefer FDI to variants of new forms were tenable up to the mid 1970s; such arguments are hardly tenable in the contemporary investment environment. The arguments of control desire by the MNE, appropriability of returns, market imperfections, lack of an institutionalized market for knowledge, etc. are constantly projected as the raison d'etre of FDI. However, such arguments are not only inconsistent with the realities of the business world but also are self-limiting. If all overseas transactions are executed by internal organization, then holding organization form constant, a point will be reached where the distinctive powers of hierarchy will be impaired and transactional diseconomies incurred as firm size and degree of vertical integration are progressively extended. At this point the qualitative implications of the FDI pre-eminence are not only upset but those of new forms appropriately recognized.

Another tentative policy implication that can be drawn on the basis of this study is that the whole concept of firm-specific advantages must be questioned (See also, Buckley, 1983). However, the ground for questioning here is somewhat different from Buckley's. He challenges it on the ground that the concept is artificially attenuated at the point where the firm first enters a foreign market, or at least where it has the potential to do so. Thus, firm-specific advantage reflects this cut-off point in the dynamic process, suggesting a short-run notion when endowments of such advantages are fixed.

Here, however, the notion of firm-specific advantages is questioned from the perspective of the economic theory of entrepreneurship. The emphasis throughout this study is that assigning transactions between hierarchies and markets in discriminating ways is a central task of corporate management. In doing so, management is presumed to be aware of the limits of firm-specific advantages and host country characteristics. In addition, management is presumed to have assessed the net benefits (or net costs) of using alternative governance structures in a given foreign market. In simple terms, corporate management is responsible for deciding upon foreign investment, for choosing institutional arrangements for implementing it and for determining the boundaries of the firm. The entrepreneur is engaged in purposeful pursuit of steering the firm into global profitability. As the firm experiences competition in the process, it is the task of the entrepreneur to discover and arbitrate profit opportunities. Yet, the crucial role of entrepreneurship is neglected both by policy statements and instruments.

To this end, a more detailed and constructive policy debate is necessary. Such a debate will help in understanding the true determinants of foreign investment and thus add dynamism to the theory construction. The firm behaviour may no longer be viewed in abstract terms but in the context of the key decision-makers. Finally, policy towards international technology transfers should be formulated on the basis of mutual forebearance, trust and consummate cooperation between foreign multinational firm and the host country partner/s. Such a policy should be based on the following premises: (1) the transfer must be seen to profit both parties, in terms of their objectives; (2) both the multinational firm and the host governments must build satisfactory institutional arrangements capable of reconciling the competing interests with minimum friction; and (3) both parties must acknowledge and explore the transactional properties of alternative governance structures. The combination of these factors may improve the bargaining power of the firm and the host country.

11.3.2 MACROECONOMIC UTILITY OF NEW FORMS: HOST COUNTRY IMPLICATIONS

The findings of this study suggest a relationship between host country policies and mode of entry. Such policies are not confined to developing nations, contrary to some studies (e.g. Franko, 1989). One implication of this study is that if governments want to restrict the inflow of foreign direct investment, the inflow of new forms will increase unless also restricted. New forms in their ramifications can, to a large extent, be a substitute for FDI in attracting foreign investments. Given host governments' resistance to foreign control of local resources on the one hand, and the contribution of inward foreign investment to macroeconomic development, on the other hand, further restrictions on new forms will be counterproductive. Developing countries, in general, and those that lack the technological and/or managerial skills to harness their resources, in particular, cannot afford to be too casual with the policy of creating disincentives to multinational firms willing to compromise on total ownership. Besides, sectoral restrictions may be compromised where active collaboration with local partners prospectively yields access to improved technology as well as to international market.

In any event, host governments should not be deluded into thinking that economic control is necessarily achieved via new forms. Some variants of new forms such as turnkey contracts, production-sharing and risk-service contracts or management contracts warrant a great deal of foreign responsibility and control. Without commensurate control, foreign firms may be reluctant to commit huge resources entailed by such projects. Incentive mechanisms such as reduced tariffs or taxes, etc. will both assuage foreign investors and encourage them to behave cooperatively in a joint-profit maximizing way. Above all, government policy makers should be realistic to the kind of foreign investment and investors they can attract through new forms. For example, it would be easy to convince a foreign hotel chain to enter into management contracts over a state-sponsored hotel enterprise, but it would be difficult to expect the same mode of organization for technology-intensive projects, such as petrochemical, pharmaceutical or motor assembly plants, since the level or size of resource commitment is relatively high and risky.

One of the concerns of foreign multinationals is high political risk, especially in developing nations. It is important that foreign multinationals engaged in their normal business activities are not held hostage to strains in political relations betweeen the host nation and their home government. It is within the host country's own sphere of control and policy to provide a stable operational environment or, at least, a safe departure of foreign multinationals in times of such inter-nation political antagonism. Not only would the host country be building a congenial atmosphere to work in, but would be sustaining its relations with the international business community which may even attenuate the effect of potential deterioration in political relations.

11.3.3 IMPLICATIONS FOR HOME GOVERNMENTS

The results of this study provide evidence to encourage home governments in their policies towards outflow of foreign investment. Most governments already have export promotion programmes. Such incentive programmes and policies should be widened to include cooperative/contractual forms of investment. In other words, foreign investment promotion programmes designed to inform existing or potential investors, especially small and medium sized firms, of the opportunties and challenges of contractual and cooperative modes would improve investors' understanding of the benefits of alternative modes of accomplishing foreign transactions.

A country's competitive position in the international marketplace is greatly enhanced the more its home firms are able to match rival firms' behaviour, using a wide variety of operational patterns compatible with host countries' economic goals. Japan is a classic country example, where the government actively encourages foreign investment outflow via the new forms. Firms should be encouraged to invest abroad even if on the so-called "defensive reaction" basis, as otherwise they would lose their foreign markets to rival firms from other countries.

Banks should be encouraged to provide better organizational forms of sustaining economic transactions abroad. Many businesses depend to a large extent on their bankers' advice and services. A critical analysis of many banks' posture, in terms of their undue concern over foreign risks with a less symmetrical concern over corresponding returns, leads to a conclusion of their lack of interest and/or organizational skill in foreign transactions. Most commercial banks show a higher propensity to finance mortgages than to fund commercial transactions. This feeling was echoed by some of the respondent company executives who noted that lack of proper banking advice and support was stifling their competitive position in the international arena. Perhaps, home governments' insurance guarantee schemes, similar to export credit guarantees, would help cushion the excessive concern of banks over foreign transactions and assist businesses wishing to exploit the perceived foreign market opportunities.

11.3.4 IMPLICATIONS FOR MULTILATERAL GOVERNMENTS

The evidence of this study seems to challenge the proposition that the incidence of new forms of international investment is a particular phenomenon of developing countries. The overriding reason for associating new forms with LDCs is the latter's policies. Yet, such policies have been shown to prevail in the developed countries as well. Although in the study certain LDC characteristics, such as high political risk and political/economic climate, appeared to have a significant relationship with the propensity to use new forms, however, in general, host country inward FDI policy was found to be an important causative factor in firm assent to non-FDI modes. Since it is in the interest of every country to regulate the direction and flow of inward foreign investment and since no country is likely to permit such flows uncontrolled, policy statements should address the effect of alternative modes of economic organization on the economic welfare of home and host countries. It is important that firms' entry mode choices be reconciled with host country's socio-economic goals.

A more detailed and constructive policy debate is necessary to consider the ramifications of alternative modes of foreign investment. Alternative governance structures should be seen not in terms of correspondence with developing countries' policies, but more broadly as mechanisms for reconciling firms' global objectives with environmental considerations. In policy-making areas, it is essential to keep in perspective the crucial role of corporate management and its relationship to organizational modes of entry. The analysis of the impact of entrepreneurial behaviour in the growth and spacial distribution of multinational firms, as attempted here, raises important policy issues for the future of foreign investment in general, and of new forms, in particular. Furthermore, attempts by multilateral bodies, such as the UNCTC and OECD, at making policies should recognize the fundamental relationships between managerial behaviour and choice of governance structure. Finally, the constant association of new forms with LDCs should make way to a policy debate which recognizes that firms need to approach foreign markets from diverse routes and need to maintain a flexible operational mode while seeking to secure optimum position in such markets.

11.4. SUGGESTIONS FOR FURTHER RESEARCH

Further composite research on new forms of international investment would be a useful addition to the paucity of empirical investigation of the phenomena of interest. Avenues for such research include (1) using sample firms drawn from wider geographic areas than those of this study; (2) refining the statistical procedures presented in this study; (3) replicating the hypothesized relationships and statistical techniques adopted here, using different contextual settings e.g. firms established in North America, other European countries, etc., (4) replicating the study, using the same context with a view to corroborating or refuting the findings here; and (5) and undertaking industry-specific research, either on one-country or multi-country basis.

The attempt here is the first of its kind to extend the central notion of alternative governance structures to the banking industry. Without doubt there is a need for further research in this area. Applications of the phenomena to other service areas would be a useful addition to the scanty literature.

One of the exploratory attempts of this study is the incorporation of the economic theory of entrepreneurship into a transaction cost analysis of the eclectic paradigm. Such an effort is bound to have methodological shortcomings in a comparative literature sense. Further empirical investigation will provide such an evidence. Besides, it is highlighted here that the role of corporate management has been long suppressed in the foreign investment literature. Studies that seek to integrate the theory of entrepreneurship into the general theory of foreign investment will be appropriate attempts at recognizing the interdisciplinary nature of international business. Operationalizing the role of corporate management in such empirical investigations will both add dynamism to the theory and further evidence on its relationship in the internationalization process.

It is difficult to generalize on the evidence of single components of new forms that they are substitutes for, or complements of, foreign direct investment. This study, though in composite form, did not attempt to investigate the claim either, although on the basis of the tangential evidence, it can be said that under certain circumstances, variants of new forms can be transactionally superior to FDI, and, in some cases useful complements.

Further research in this area is called for. Related to this is the proposition that, in the North-South context, foreign direct investment is becoming obsolescent. An investigation of this kind was not contemplated here since the premise of the study was not confined to a North-South dichotomy. While such a generalization remains contentious, it leaves the corridor open for further research.

The review of the literature on new forms of investment reveals a dearth of publication in some components, e.g. turnkey contractual arrangement and its variants, management contract, and international subcontract/contract manufacturing. Literature focus has been on licensing and joint ventures, with relatively less attention to franchising and other modes. Studies on these little researched areas will be a useful contribution in the international investment literature.

In the area of market research, a study of the relationship between international diversification, risk reduction and new forms of investment will be an additional avenue of research. Specific questions of interest include: (1) Is the risk of profits of firms adopting new forms higher or lower than that of purely FDI-firms of similar characteristics (e.g. size)? (2) Are the rates of return and stability of earnings of the former type firms significantly higher or lower than those of the latter type firms? Related to these is the question concerning market perception of risk profiles of firms' international investment operations. A test of market valuation of firms adopting non-FDI modes of internationalization can be made by comparing the shares of such firms with those of FDI-firms.

Finally, are new forms specific or general phenomena of LDCs? This question is still unresolved. The evidence of this study does not appear to lend much credence to that proposition. Further studies are required to validate the notion that LDC policies are specifically instrumental to corporate assent to new forms of international investment. Such studies will add clarity to public policy views of the kinds held by the OECD.

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Appendix 1

ASGOW BUSINESS SCHOOL

Glasgow Business School, Department of Management Studies, University of Glasgow,
53-59 Southpark Avenue, Glasgow, G12 8LF, Scotland. U.K. Tel: 041-339 8855, Telex: 777070 UNIGLA, Fax: 041-330 56(

Our Ref: WH/KmcC

Direct Line: 041-332-2652
Direct Fax: 041-339-1695

Date as postmark

Dear Sir/Madam,

I am conducting a research under the auspices of Glasgow Business School, University of Glasgow. The focus of the research is on the alternative forms by which international business operations are conducted other than by foreign direct investment (which involves the establishment of wholly- or majority-owned foreign subsidiaries).

These alternative investment strategies refer to: (1) joint international business ventures in which foreign-held equity does not exceed 50%, and (2) international contractual arrangements under which foreign companies may contribute no equity capital, but which involve some degree of investment, control and returns. Examples include licensing and technical assistance contracts, franchising, turnkey contracts, leasing, management contracts, international sub-contracting, and production-sharing contracts.

The exploration seeks to address the following:

1. The identification of alternative (to foreign direct investment) organizational modes of foreign investment;
2. The determinants of foreign organizational networks;
3. The motivational factors that informed the choice of the present corporate modes and locational preferences;
4. The factors that foster incentives for use of minority equity participation, equity and non-equity joint ventures, and contractual arrangements such as licensing, turnkey, etc. as operational entry modes into overseas markets; and
5. The perception of costs and benefits of these entry modes.

The study is based on questionnaire administration to a representative sample of companies across industries, of which your company has been chosen. It is for this reason that I am writing to you. The success of this project depends entirely on the goodwill and co-operation of corporate executives like yourself. I would be very grateful if you could spare 10 minutes to complete and return to me the attached questionnaire. As you may appreciate, an exploratory study of this kind will rely on a lot of quality information, therefore, I would be most obliged to you if you could enclose with the questionnaire any brochures about your company which may assist me in my data collection.

I assure you that <u>absolute confidentiality and anonymity of any information provided</u> is guaranteed since results will be analysed in aggregate form with no reference to individual companies. Thank you immensely for taking time to complete the questionnaire and, if you wish, the result of the study will be made available to you.

I look forward to the pleasure of your prompt attention and return of the questionnaire.

Yours faithfully

Wilson Herbert

Appendix 2

SGOW BUSINESS SCHOOL

Glasgow Business School, Department of Management Studies, University of Glasgow,
53-59 Southpark Avenue, Glasgow, G12 8LF, Scotland. U.K. Tel: 041-339 8855, Telex: 777070 UNIGLA, Fax: 041-330 56c

Our Ref: WH/KmcC

Direct Line: 041-332-2652
Direct Fax: 041-339-1695

Date as postmark

Dear Sir/Madam,

I am conducting a research under the auspices of Glasgow Business School, University of Glasgow. The focus of the research is on the alternative forms by which international banking is conducted on a long term basis, other than by foreign direct investment (which involves the establishment of wholly- or majority-owned foreign subsidiaries or branches).

These alternative investment strategies refer to: (1) joint international ventures or partnerships in which foreign-held equity does not exceed 50%, and (2) international contractual arrangements under which foreign banks may contribute no equity capital, but which involve some degree of investment, control and returns. Examples include representative offices, agencies, correspondent relationships, affiliated/associated banking relationships, consortium banking arrangements, overseas cashline services and merchant banking services (incorporating international leasing etc).

The exploration seeks to address the following:

1. The identification of alternative (to foreign subsidiaries) organizational modes of foreign banking;
2. The determinants of foreign organizational networks;
3. The motivational factors that informed the choice of the present corporate modes and locational preferences;
4. The factors that foster incentives for use of minority equity participation, equity and non-equity joint ventures, and contractual arrangements such as representative offices, correspondents, etc., as operational entry modes into overseas markets; and
5. The perception of costs and benefits of these entry modes.

The study is based on questionnaire administration and personal interviews with a representative sample of banks. It is for this reason that I am writing to you. The success of this project depends entirely on the goodwill and co-operation of bank executives like yourself. I would be very grateful if you could complete and return to me the attached questionnaire. As you may appreciate, an exploratory study of this kind will rely on a lot of quality information, therefore, I would be most obliged to you if I could arrange an interview appointment, with yourself or your nominee to discuss these issues. The length of the interview will not exceed 30 minutes and will be at your convenience. I would appreciate any brochures about your bank which may assist me in my data collection.

I assure you that absolute confidentiality and anonymity of any information provided is guaranteed since results will be analysed in aggregate form with no reference to individual banks. Thank you immensely for taking time to complete the questionnaire and, if you wish, the result of the study will be made available to you.

I look forward to the pleasure of hearing from you as soon as possible.

Yours faithfully

Wilson Herbert

APPENDICES 3.1 - 3.4

QUESTIONNAIRES

This questionnaire is designed to cover the following four broad categories in four different sets:

1. UK companies (large and small) operating abroad.
2. Foreign companies operating in UK.
3. UK banks operating abroad
4. Foreign banks operating in UK.

New forms of International Investment are defined in broad terms to include all non-FDI organizational forms, excluding spot market and fade-out arrangements.

The questionnaire is divided, in each case, into five sections (1-5).

1. Corporate background information.
2. Scope of International Operations.
3. Modes of Entry into Foreign markets.
4. Determinants and Independent Variables.
5. Impact of NFI on corporate strategy.

Appendix 3.1

FOREIGN BANKS IN THE U.K.

1. BANK DETAILS

1.1 Name of Bank:____________________

1.2 Position of Respondent:____________________

1.3 Are you:

	Tick
a parent bank? (ie, with subsidiaries & branches)	
a subsidiary/branch bank?	______
a branch member?	______
a member of an international consortium?	______
a joint venture bank (with a UK bank)?	______
an affiliate of a UK bank?	______
other (please specify)	______

1.4 What is the nationality of your bank?____________________

1.5 Size of parent bank (please complete as per your 1989 Annual Report).

Group Turnover (£m)	Number of Employees
______	______

2. SCOPE OF INTERNATIONAL OPERATIONS

2.1 What percentage of your bank's total investment is accounted for by your UK operations?

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

2.2 How much of your global earnings is contributed by foreign investment earnings?

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

2.3 Is the bulk of your company's current overseas activity in:

1. West Europe (incl UK)? ______
2. North American (USA and Canada)? ______
3. Latin America? ______
4. Australia and New Zealand? ______
5. Far East (incl Japan, Hong Kong, China, etc)? ______
6. Asia (incl. India, Singapore, Pakistan, etc)? ______
7. Middle East (Israel, South Arabia, etc)? ______
8. Africa? ______
9. Eastern Block (incl. Soviet Union, Poland, etc)? ______
10. Other? (please specify) ______

2.4 Has the position in 2.3. above changed in the last 5 years? YES/NO

If Yes, could the reason be due to: (please tick as many as apply)

1. Shift in corporate policy/strategy? ______
2. Home government's outward investment policy? ______
3. Host government's inward investment policy? ______
4. Host country's political/economic situation? ______
5. Global competition? ______
6. Other (please specify)? ______

3. DETAILS OF MODES OF ENTRY INTO UK MARKET

3.1 Which of the following organizational forms best describes your bank's route of entry into UK?

Tick (one only)

1. Establishment of a subsidiary ______
2. Branch banking ______
3. Affiliation with UK bank(s) ______
4. Representative office ______
5. Correspondent banking arrangements ______
6. Banking partnership (eg, consortium or joint venture banking) ______
7. Through financing trade & investments (including merchant banking services) ______
8. Merger/Acquisition of a UK/foreign bank. ______
9. Other (please specify) ______

3.2 Other than foreign subsidiaries/branches, which of the following operational modes does your bank have as part of its international network? (Please tick as many as applicable).

1. Foreign Affiliates/Associates. ______
2. Overseas Agency/Representative Offices ______
3. Foreign Correspondents ______
4. Consortium/Joint Venture Arrangements. ______
5. International Merchant banking services. ______
6. Overseas Cash Line Services. ______
7. Other (please specify) ______

3.3 Would the choice of organizational form of entry have been different if you were to locate in a less developed country?

YES/NO?

Please explain the reason for your answer.______________________________
____
____

4. DETERMINANTS AND INDEPENDENT VARIABLES

4.1 Please rank in order of strategic importance the influence of the following factors in your bank's choice of UK (1 = most important 10 = least important.)

	LOCATION FACTOR	Tick
1.	Presence of other banks in the UK	( )
2.	Possession of major corporate customers in the UK	( )
3.	Size of UK markets (capital, product & factor markets)	( )
4.	Size of trade between your country and UK	( )
5.	London as a major international financial centre.	( )
6.	Strength of pounds sterling as a major world currency.	( )
7.	Your country's political/economic ties with UK.	( )
8.	Effective tax and interest rates differentials between your country and UK.	( )
9.	Socio-cultural similarities with your country	( )
10.	Other (please specify)	( )

4.2 How significant is each of the following characteristics to your bank's choice of mode of entry into a foreign market?

	Very Significant	Significant	Neutral	Insignificant	Very Insignificant
A. FIRM CHARACTERISTICS:					
1. Willingness to share ownership & control in return for access to local markets	1	2	3	4	5
2. Minimization of country risks	1	2	3	4	5
3. Cost of establishing a foreign subsidiary	1	2	3	4	5
4. Size of bank (denoting financial, managerial and technical capabilities)	1	2	3	4	5
5. Experience in foreign banking	1	2	3	4	5
7. Possession of large international corporate customers	1	2	3	4	5
8. Economics of scope & geographical diversification.	1	2	3	4	5
9. Other (please specify)	1	2	3	4	5
B. HOST COUNTRY-SPECIFIC CHARACTERISTICS					
1. Government's policy against foreign control	1	2	3	4	5
2. Level of inter-bank market	1	2	3	4	5
3. Size of your country's trade/investment in host country.	1	2	3	4	5
4. Fiscal and monetary policies.	1	2	3	4	5
5. Economic/Political climate	1	2	3	4	5
6. Technological and Managerial capacity	1	2	3	4	5
7. Psychic distance (language, cultural, business, customs, etc differences).	1	2	3	4	5
8. Other (please specify)	1	2	3	4	5

5. BENEFITS OF MINORITY-EQUITY (CO-OPERATIVE FORMS) OF FOREIGN BANKING.

5.1 Please state the extent of your agreement or disagreement with the following statements (Non-equity/co-operative forms of foreign banking are defined as listed in 3.2 above)

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1. Minority-equity/(co-operative) forms of international banking enable firms to diversify both country and investment risks	1	2	3	4	5
2. Minority-equity forms of international banking enable banks to avoid market disabling factors of opportunism uncertainty, entry barriers, etc.	1	2	3	4	5
3. Minority-equity/co-operative modes of entry into overseas markets are a superior means of exploiting a bank's assets abroad and foreign market opportunities, with minimum resources & risks.	1	2	3	4	5
4. Minority-equity modes offer banks the advantage of flexibility to adjust to changes in both the host economy and the international market.	1	2	3	4	5
5. Minority-equity entry modes may be used as pre-emptive manoeuvres to gain access to promising markets and technologies.	1	2	3	4	5
6. Minority-equity entry modes are a less-developed country phenomenon.	1	2	3	4	5

5.2 Finally, do you feel that minority-equity/co-operative forms of international banking will become popular or less popular as host governments become increasingly concerned about foreign control of banks and financial institutions?

Popular	Less Popular	Don't Know
______	________	________

Please explain the reason for your answer________________________________

____

____

Thank you for your help in completing this questionnaire. Please return it in the pre-paid envelope as soon as possible, to:

WILSON HERBERT, ESQ
GLASGOW BUSINESS SCHOOL
DEPT OF MANAGEMENT STUDIES
UNIVERSITY OF GLASGOW
GLASGOW G12 8LF
SCOTLAND

Appendix 3.2

U.K. BANKS OPERATING ABROAD

1. BANK DETAILS

1.1 Name of Bank:______________________________

1.2 Position of Respondent:______________________________

1.3 Are you:

	Tick
a parent bank? (ie, with subsidiaries & branches)	______
a subsidiary bank?	______
a branch bank?	______
a member of an international consortium?	______
a joint venture bank (with a UK bank)?	______
an affiliate of a UK bank?	______
other (please specify)	______

1.4 If parent bank, how many subsidiaries/branches have you in:

U.K?________________ elsewhere?________________

1.5 Size of parent bank (please complete as per your 1989 Annual Report).

Group Turnover (£m)	Number of Employees
____________	____________

2. SCOPE OF INTERNATIONAL OPERATIONS

2.1 What percentage of your group's total investment is accounted for by foreign investment?

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	____

2.2 How much of your group turnover is contributed by foreign investment earnings?

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	____

2.3 Is the bulk of your company's current overseas activity in:

1.	W. Europe (excl UK)?	______
2.	North America?	______
3.	Latin America?	______
4.	Australia and New Zealand?	______
5.	Far East (incl Japan, Hong Kong, China, etc)?	______
6.	Asia (incl. India, Pakistan, Singapore, etc)?	______
7.	Middle East (Israel, Saudi Arabia, etc)?	______
8.	Africa?	______
9.	Eastern Bloc (incl. Soviet Union, Poland, etc)?	______
10.	Other? (please specify)	______

2.4 Has the position in 2.3. above changed in the last 5 years? YES/NO

If Yes, could the reason be due to: (please tick as many as apply)

1. Shift in corporate policy/strategy? ______
2. Home government's outward investment policy? ______
3. Host government's inward investment policy? ______
4. Host country's political/economic situation? ______
5. Global competition? ______
6. Other (please specify)? ______

3. <u>DETAILS OF MODES OF ENTRY INTO FOREIGN MARKET</u>

3.1 Which of the following organizational forms best describes your bank's route of entry into foreign countries.

<u>Tick (one only)</u>

1. Establishment of a subsidiary ______
2. Branch banking ______
3. Affiliation with host country's bank(s) ______
4. Representative office ______
5. Correspondent banking arrangements ______
6. Banking partnership (eg, consortium or joint venture banking) ______
7. Through financing trade & investments (including merchant banking services) ______
8. Mergers and acquisitions. ______
9. Other (please specify) ______

3.2 Other than foreign subsidiaries/branches, which of the following operational modes does your bank have as part of its international network? (Please tick as many as applicable).

1. Foreign Affiliates/Associates. ______
2. Overseas Agency/Representative Offices ______
3. Foreign Correspondents ______
4. Consortium/Joint Venture Arrangements. ______
5. International Merchant banking services. ______
6. Overseas Cash Line Services. ______
7. Other (please specify) ______

4. <u>DETERMINANTS AND INDEPENDENT VARIABLES</u>

4.1 Please rank in order of strategic importance the influence of the following factors in your bank's decision to locate in either a developed (DC) or less developed country (LDC) (1= Most important, 13 = Least).

	<u>LOCATION FACTOR</u>	DC	LDC
1.	Presence of other banks (UK & other countries) in host country.	( )	( )
2.	Existence of major corporate customers in the host country.	( )	( )
3.	Economic/political situation in host country.	( )	( )
4.	Size of host country's banking markets.	( )	( )
5.	Interest rate differential between host country and UK.	( )	( )
6.	Tax rate differential between host country and UK.	( )	( )
7.	Level of industrial development in host country.	( )	( )

8.	Size of UK's investment in host country.	( )	( )
9.	Openness of host country towards foreign banks.	( )	( )
10.	Host country as a major/important financial centre.	( )	( )
11.	UK's political and economic ties with host country.	( )	( )
12.	Socio-cultural similarities with host country.	( )	( )
13.	Other (please specify).	( )	( )

4.2 How significant is each of the following characteristics to your bank's choice of mode of entry into a foreign market?

	Very Significant	Significant	Neutral	Insignificant	Very Insignificant
A. <u>FIRM CHARACTERISTICS</u>:					
1. Willingness to share ownership & control in return for access to local markets	1	2	3	4	5
2. Minimization of country risks	1	2	3	4	5
3. Cost of establishing a foreign subsidiary	1	2	3	4	5
4. Size of bank (denoting financial managerial & technical capabilities)	1	2	3	4	5
5. Experience in foreign banking	1	2	3	4	5
6. Possession of large international corporate customers	1	2	3	4	5
7. Economies of scope & geographical diversification.	1	2	3	4	5
8. Competitors' patterns of entry	1	2	3	4	5
9. Other (please specify)	1	2	3	4	5
B. <u>HOST COUNTRY CHARACTERISTICS</u>					
1. Government's policy against foreign control of banks.	1	2	3	4	5
2. Level of inter-bank market	1	2	3	4	5
3. Size of UK trade/investment in host country	1	2	3	4	5
4. Fiscal and monetary policies.	1	2	3	4	5
5. Economic/Political climate	1	2	3	4	5
6. Technological and Managerial capacity	1	2	3	4	5
7. Psychic distance (language, cultural, business, customs, etc differences).	1	2	3	4	5
8. Other (please specify)	1	2	3	4	5

5. BENEFITS OF MINORITY-EQUITY (CO-OPERATIVE FORMS) OF FOREIGN BANKING.

5.1 Please state the extent of your agreement or disagreement with the following statements (Non-equity/co-operative forms of foreign banking are defined as listed in 3.2 above)

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1. Minority-equity/co-operative forms of international banking, enable banks to diversify both country and investment risks.	1	2	3	4	5
2. Minority-equity/co-operative forms of international banking enable banks to avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	1	2	3	4	5
3. Minority-equity/co-operative forms of entry into overseas markets are a superior means of exploiting a bank's assets abroad and foreign market opportunities, with minimum resources and risks.	1	2	3	4	5
4. Minority-equity entry modes offer banks the advantage of flexibility to adjust to changes in both the host economy and the international market.	1	2	3	4	5
5. Minority-equity entry modes may be used as pre-emptive manoeuvres to gain access to promising markets and technologies.	1	2	3	4	5
6. Minority-equity entry modes are a less-developed country phenomenon.	1	2	3	4	5

5.2 Finally, do you feel that shared-equity/co-operative forms of international banking will become popular or less popular as host governments become increasingly concerned about foreign control of banks and financial institutions?

Popular	Less Popular	Don't Know
______	________	

Please explain reasons for your answers.________________________________

____

Thank you for your help in completing this questionnaire. Please return it in the pre-paid envelope, as soon as possible, to:

WILSON HERBERT, ESQ
GLASGOW BUSINESS SCHOOL
DEPT OF MANAGEMENT STUDIES
UNIVERSITY OF GLASGOW
GLASGOW G12 8LF
SCOTLAND

APPENDIX 3.3

UK COMPANIES ABROAD

1. COMPANY DETAILS

1.1 Name of company:________________________________

1.2 Position of Respondent:________________________________

1.3 Major industry classification (eg. manufacturing, oil, etc).__________

1.4 Please tick which of the following best describes your company:

1.	An independent company (ie. without parent or subsidiary)	______
2.	A parent company (ie. with subsidiaries)	______
3.	A subsidiary company	______
4.	An associate/affiliate of another company.	______
5.	A member of a Consortium.	______
6.	Other (please specify)	______

1.5 Size of Parent company (Please complete as per your 1989 Annual Report).

Group Turnover (£m)	Number of Employees
______________	______________

2. SCOPE OF INTERNATIONAL ACTIVITIES.

2.1 How many foreign branches/subsidiaries/affiliates, etc. do you have?_____

2.2 Is the bulk of your company's current overseas activity in:

1.	West Europe (excl UK)?	______
2.	North America (USA and Canada)?	______
3.	Latin America?	______
4.	Australia & New Zealand?	______
5.	Far East (incl Japan, Hong Kong, China, etc)?	______
6.	Asia (incl. India, Pakistan, Singapore, etc)?	______
7.	Middle East (Israel, Saudi Arabia, etc)?	______
8.	Africa?	______
9.	Eastern Bloc (incl. Soviet Union, Poland, etc)?	______
10.	Other (please specify)	______

2.3 Has the position in 2.2. above changed in the last 5 years? YES/NO
If Yes, could the reason be due to: (please tick as many as apply)

1. Shift in corporate policy/strategy? ______
2. Home government's outward investment policy? ______
3. Host government's inward investment policy? ______
4. Host country's political/economic situation? ______
5. Global competition? ______
6. Other (please specify)? ______

2.4 What percentage of your group's global investment is accounted for by foreign investment? (Please tick)

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

2.5 How much of your group turnover is contributed by foreign investment earnings? (Please tick)

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

3. DETAILS OF ENTRY MODES INTO FOREIGN MARKETS.

3.1 Which of the following operational modes do you regard as best describing the manner in which your company entered any of these country zones? (Tick one mode against each applicable area).

ENTRY MODE	W.Europe excl UK	USA/ Canada	Far East Incl Japan Korea	Australia & New Zealand	Asia incl. India, Pakistan etc.	Middle East	Eastern Bloc incl Russia	Africa
Non-Equity Joint Venture.								
Equity Joint Venture.								
Licensing.								
Franchising.								
Agency.								
Turnkey Contracts.								
International Leasing.								
Contract Management.								
Production Sharing Contracts.								
Acquisition & Merger								
Other (please specify)								

3.2 How significant is each of the following factors which may be included in contractual agreements (eg. licensing, Turnkey, etc)? Please circle.

CONTRACTUAL PACKAGE	Very Signif	Significant	Neutral	Insignificant	Very Insignficant
1. Machinery/Equipment supply	1	2	3	4	5
2. Technical assistance in production.	1	2	3	4	5
3. Technical assistance in plant design and construction.	1	2	3	4	5
4. Technical assistance in procuring/supplying inputs & components.	1	2	3	4	5
5. Technical assistance in marketing & management.	1	2	3	4	5
6. Personnel training.	1	2	3	4	5
7. Right for utilisation of patents/trademarks.	1	2	3	4	5
8. Right for utilisation of design, formula etc.	1	2	3	4	5
9. Right to the use of advertising materials.	1	2	3	4	5
10. Other (please specify)	1	2	3	4	5

3.3 Is there any specified length of time in such technical agreement. YES/NO
If yes, how long is it?______________ - years

4. DETERMINANTS AND INDEPENDENT VARIABLES

4.1 Please tick, and rank in order of relative importance, the following motivations for adopting non-equity forms of foreign investment. (1 = most important, 10 = least important).

MOTIVATIONAL STATEMENT		TICK RANK
i.	Achieve international diversification via international co-operative arrangements.	( )
ii.	Host government regulations (restricting foreign direct investment to selected sectors only, and requiring high local equity participation in the rest).	( )
iii.	High political risk in host country (eg. risks of expropriation)	( )
iv.	Risk diver[illegible] technology	( )
vi.	Because competitors adopt non-equity/contractual forms of investment.	( )
vii.	Size of firm too small to finance, manager or market overseas operations.	( )
viii.	Products customized to host/regional market.	( )
ix.	Protect/support existing foreing business.	( )
x.	Other (please specify)	( )

4.2 Does the size of your parent company have any influence on the choice of entry mode? YES/NO

If yes, what kind of influence does it have?____________________

____

4.3 Does the entry choice of your competitors influence your company's entry strategy? YES/NO

If yes, please explain the extent of the influence.____________________

____

4.4 How significant is each of the following in your company's choice of mode of entry into a foreign market? (Please circle)

	Very Significant	Significant	Neutral	Insignificant	Very Insignificant
A. FIRM CHARACTERISTICS:					
1. Willingness to share ownership & control in return for access to local markets	1	2	3	4	5
2. Minimization of country risks	1	2	3	4	5
3. Experience in foreign markets	1	2	3	4	5
4. Size of company (denoting financial, managerial and technical capabilities)	1	2	3	4	5
5. Possession of brand name, trade marks etc.	1	2	3	4	5
6. Economies of scope & geographical diversification.	1	2	3	4	5
7. Other (please specify)	1	2	3	4	5
B. HOST COUNTRY CHARACTERISTICS					
1. Level of ecnomic development	1	2	3	4	5
2. Size of host market	1	2	3	4	5
3. Government controls on inward direct investment	1	2	3	4	5
4. Fiscal and monetary policies.	1	2	3	4	5
5. Political/Economic climate in host country.	1	2	3	4	5
6. Psychic distance (language, cultural, business, customs etc. differences).	1	2	3	4	5
7. Transport & communication costs	1	2	3	4	5
8. Other (please specify)	1	2	3	4	5

5. BENEFITS OF NON-EQUITY (CONTRACTUAL FORMS) OF FOREIGN INVESTMENT.

5.1 Please state the extent of your agreement or disagreement with the following statements (Non-equity/contractual forms are defined as listed in 3.1 above)

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1. Non-equity (contractual) forms of international investment enable firms to diversify both country and investment risks	1	2	3	4	5
2. Non-equity forms of international investment enable firms to avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	1	2	3	4	5
3. Non-equity modes are a superior means of exploiting a firm's assets abroad and foreign market opportunities, with minimum resource & risks.	1	2	3	4	5
4. Non-equity modes offer firms the advantage of flexibility to adjust to changes in both the host economy and the international market.	1	2	3	4	5
5. Non-equity entry modes may be used as pre-emptive manoeuvres to gain access to promising markets and technologies.	1	2	3	4	5
6. Non-equity entry modes are a less-developed country phenomenon.	1	2	3	4	5

5.2 Finally, do you think that contractual/non-equity modes of entry into foreign markets would gain/lose popularity in future?

Gain Popularity	Lose Popularity	Don't Know
________	________	______

Please explain the reason for your answer:______________________________________

____

____

Thank you for your help in completing the questionnaire. Please return it in the pre-paid envelope, as soon as possible, to:

WILSON HERBERT, ESQ
GLASGOW BUSINESS SCHOOL
DEPARTMENT OF MANAGEMENT STUDIES
UNIVERSITY OF GLASGOW
53-59 SOUTHPARK AVENUE
GLASGOW
G12 8LF

Appendix 3.4

FOREIGN COMPANIES IN UK

1. COMPANY DETAILS

1.1 Name of company:________________________________

1.2 Position of Respondent:______________________________

1.3 Major industry classification (eg. manufacturing oil, etc).____

1.4 Please tick which of the following best describes your company:

1. An independent company (ie. without parent or subsidiary) ______
2. A parent company (ie. with subsidiaries) ______
3. A subsidiary company ______
4. An associate/affiliate of a British company. ______
5. A member of a Consortium. ______
6. Other (please specify) ______

1.5 What nationality is your company? (eg, French, Canadian, etc)__________

1.6 Size of company (please complete)

Group Turnover (£million)	Number of Employees
__________	__________

2. SCOPE OF INTERNATIONAL ACTIVITIES

2.1 How many associate companies do you have:
in the UK? __________
elsewhere? __________

2.2 Is the bulk of your company's current overseas activity in:
1. West Europe (excl UK)? ______
2. North America? ______
3. Latin America? ______
4. Australia & New Zealand? ______
5. Far East (incl Japan, Hong Kong, China, etc)? ______
6. Asia (incl. India, Pakistan, Singapore, etc)? ______
7. Middle East (Israel, Saudi Arabia, etc)? ______
8. Africa? ______
9. Eastern Bloc (incl. Soviet Union, Poland, etc)? ______
10. Other (please specify) ______

2.3 Has the position in 2.2. above changed in the last 5 years? YES/NO
If Yes, could the reason be due to: (please tick as many as apply)

1. Shift in corporate policy/strategy? ______
2. Home government's outward investment policy? ______
3. Host government's inward investment policy? ______
4. Host country's political/economic situation? ______
5. Global competition? ______
6. Other (please specify)? ______

2.4 What percentage of your group's global investment is accounted for by foreign investment? (Please tick)

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

2.5 How much of your group turnover is contributed by foreign investment earnings?

Less than 10%	Between 10 & 20%	Between 20 & 30%	Over 30%
______	______	______	______

3. DETAILS OF MODES OF ENTRY INTO THE UK.

3.1 Which of the following organizational forms best describes your company's route of entry into UK? (please tick)

Entry Mode Activity in the UK		Tick
1.	Equity Joint Venture with UK company	______
2.	Non-Equity Joint Venture with UK company	______
3.	Acquisition/Merger of UK-based company	______
4.	Licensing	______
5.	Franchising	______
6.	Agency	______
7.	Turnkey contracts	______
8.	Assembly/Sub-assembly plant operation	______
9.	Leasing	______
10.	Contract Management/subcontracting	______
11.	Production sharing	______
12.	Other (please specify)	______

3.2 Please rank the following factors in order of their influence on your company's decision to locate in UK (1=most influential, 9=least influential).

MOTIVATION FACTORS		Tick
1.	Presence of other companies in the UK, including your competitors.	( )
2.	London as a major international financial centre	( )
3.	Strength of pounds sterling as a major world currency	( )
4.	Your country's political ties with UK	( )
5.	Effective tax & interest rates differentials between your country and UK	( )
6.	Trade/economic relationship between your country and UK	( )
7.	Size of UK markets (capital, product and factor markets)	( )
8.	Geo-political and economic status of UK	( )
9.	Other (please specify)	( )

3.3 How significant is each of the following factors which may be included in contractual agreements?

CONTRACTUAL PACKAGE	Very Significant	Significant	Neutral	Insignificant	Very Insignificant
1. Machinery/Equipment supply	1	2	3	4	5
2. Technical assistance in production.	1	2	3	4	5
3. Technical assistance in plant design and construction.	1	2	3	4	5
4. Technical assistance in procuring/supplying inputs & components.	1	2	3	4	5
5. Technical assistance in marketing & management.	1	2	3	4	5
6. Personnel training.	1	2	3	4	5
7. Right for utilisation of patents/trademarks	1	2	3	4	5
8. Right for utilisation of design, formula etc.	1	2	3	4	5
9. Right to the use of advertising materials.	1	2	3	4	5
10. Other (please specify)	1	2	3	4	5

3.4 Is there any specified length of time in such technical agreement. YES/NO
If yes, how long is it?__________________ - years

4. DETERMINANTS AND INDEPENDENT VARIABLES

4.1 Please tick, and rank in order of relative importance, the following motivations for adopting non-equity forms of foreign investment (1 = most important, 10 = least important).

MOTIVATIONAL STATEMENT

	Motivational statement	Tick Rank
1.	Achieve international diversification via co-operative arrangements with local partners.	( )
2.	Reciprocal access to technology/high costs of technology.	( )
3.	Because other countries' multinationals adopt flexible forms of foreign investment.	( )
4.	Size of firm too small to finance foreign operations alone.	( )
5.	High cost of establishing a foreign subsidiary.	( )
6.	Strong market competition.	( )
7.	Entry into UK as a gateway to wider EEC markets.	( )
8.	Products customized to UK/EEC market.	( )
9.	Host Government's Policy.	( )
10.	Global profitability and increased market share.	( )

4.2 Did the entry choice of your competitors into the UK influence your company's entry strategy? YES/NO

If yes, please explain the extent of the influence.____________________

____

4.3 Does the size of your parent company have any influence on the choice of entry mode? YES/NO

If yes, what kind of influence does it have?____________________

____

4.4 How significant is each of the following in your company's choice of mode of entry into a foreign market? (Please circle)

	Very Significant	Significant	Neutral	Insignificant	Very Insignificant
A. FIRM CHARACTERISTICS:					
1. Willingness to share ownership & control in return for access to local markets	1	2	3	4	5
2. Minimization of country risks	1	2	3	4	5
3. Experience in foreign markets	1	2	3	4	5
4. Size of company (denoting financial, managerial and technical capabilities)	1	2	3	4	5
5. Possession of brand name, trade marks etc.	1	2	3	4	5
6. Economies of scope & geographical diversification.	1	2	3	4	5
7. Other (please specify)	1	2	3	4	5
B. HOST COUNTRY CHARACTERISTICS					
1. Level of economic development	1	2	3	4	5
2. Size of host market	1	2	3	4	5
3. Government controls on inward direct investment	1	2	3	4	5
4. Fiscal and monetary policies.	1	2	3	4	5
5. Political/Economic climate in host country.	1	2	3	4	5
6. Psychic distance (language, cultural, business, customs etc. differences.	1	2	3	4	5
7. Transport & communication costs	1	2	3	4	5
8. Other (please specify)	1	2	3	4	5

5. BENEFITS OF NON-EQUITY/(CONTRACTUAL FORMS) OF FOREIGN INVESTMENT.

5.1 Please state the extent of your agreement or disagreement with the following statements (Non-equity/contractual forms are defined as listed in 3.1 above)

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1. Non-equity (contractual) forms of investment enable firms to diversify both country and investment risks	1	2	3	4	5
2. Non-equity forms of international investment enable firms to avoid market disabling factors of opportunism, uncertainty, entry barriers, etc.	1	2	3	4	5
3. Non-equity modes are a superior means of exploiting a firm's assets abroad and foreign market opportunities, with minimum resources & risks.	1	2	3	4	5
4. Non-equity modes offer firms the advantage of flexibility to adjust to changes in both the host economy and the international market.	1	2	3	4	5
5. Non-equity entry modes may be used as pre-emptive manoeuvres to gain access to promising markets and technologies.	1	2	3	4	5
6. Non-equity entry modes are a less-developed country phenomenon.	1	2	3	4	5

5.2 Finally, do you think that the non-equity contractual modes of entry into foreign markets will become popular or less popular in future?

Popular	Less Popular	Don't Know
_____	_________	_________

Please explain the reason for your answer.______________________________________

____

____

Thank you for your help in completing this questionnaire. Please return it in the pre-paid envelope, as soon as possible, to:

WILSON HERBERT, ESQ
GLASGOW BUSINESS SCHOOL
DEPT OF MANAGEMENT STUDIES
UNIVERSITY OF GLASGOW
GLASGOW G12 8LF
SCOTLAND

APPENDICES 4.1 - 4.4

DATA CODING

WH1.SYS

Variable: V5 Label: A PARENT BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V6 Label: A SUBSIDIARY BRANCH BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V7 Label: A BRANCH MEMBER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V8 Label: A MEMBER OF AN INTERNATIONAL CONSORTIUM
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V9 Label: JOINT VENTURE BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V10 Label: AN AFFILIATE OF UK BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V11 Label: OTHER BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
.00 No 1.00 Yes

Variable: V12 Label: NATIONALITY OF BANK

No value labels   Type: Number   Width: 2   Dec: 0
Missing: * None *

Variable: V13   Label: GROUP TURNOVER

No value labels   Type: Number   Width: 10   Dec: 0
Missing: * None *

Variable: V14   Label: NUMBER OF EMPLOYEES

No value labels   Type: Number   Width: 7   Dec: 0
Missing: * None *

Variable: V15   Label: PERCENTAGE OF BANKS TOTAL INVESTMENT ACC
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Less than 10%   2.00   Between 10 & 20%
3.00   Between 20 & 30%   4.00   Over 30%

Variable: V16   Label: GLOBAL EARNINGS CONTRIBUTED BY FOREIGN I
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Less than 10%   2.00   Between 10 & 20%
3.00   Between 20 & 30%   4.00   Over 30%

Variable: V17   Label: BULK OF COMPANY'S CURRENT OVERSEAS ACTIV
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   West Europe   2.00   North America
3.00   Latin America   4.00   Australia and New Zealan
5.00   Far East   6.00   Asia
7.00   Middle East   8.00   Africa
9.00   Eastern Block   10.00   Other

Variable: V18   Label: POSITION CHANGED IN LAST 5 YEARS

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V19   Label: SHIFT IN CORPORATE POLICY/STRATEGY

```
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V20          Label: HOME GOVERNMENTS OUTWARD INVESTMENT
POLI
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V21           Label: HOST GOVERNMENTS INWARD INVESTMENT
POLIC
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V22            Label: HOST COUNTRY'S POLITICAL/ECONOMIC
SITUAT
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V23            Label: GLOBAL COMPETITION

   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V24            Label: OTHER REASON

   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V25          Label: ORGANIZATIONAL FORMS DESCRIBES YOUR
BANK
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No


 Variable: V26            Label: FOREIGN AFFILIATES/ASSOCIATES

   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                2.00   No
```

Variable: V27 Label: OVERSEAS AGENCY/REPRESENTATIVE OFFICES
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V28 Label: FOREIGN CORRESPONDENTS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V29 Label: CONSORTIUM/JOINT VENUE ARRANGEMENTS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V30 Label: INTERNATIONAL MERCHANT BANKING SERVICES
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V31 Label: OVERSEAS CASH LINE SERVICES

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V32 Label: OTHER OPERATION MODE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V33 Label: ORGANIZATIONAL FORM OF ENTRY HAVE BEEN D
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V34 Label: PRESENCE OF OTHER BANKS IN THE UK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Yes 2.00 No

Variable: V35 Label: POSSESSION OF MAJOR CORPORATE CUSTOMERS
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V36 Label: SIZE OF UK MARKETS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V37 Label: SIZE OF TRADE BETWEEN YOUR COUNTRY AND U
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V38 Label: LONDON IS A MAJOR INTERNATIONAL FINANCIA
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V39 Label: STRENGTHS OF POUNDS STERLING AS A MAJOR
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V40 Label: YOUR COUNTRY'S POLITICAL/ECONOMIC TIES W
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V41 Label: EFFECTIVE TAX AND INTEREST RATES DIFFERE
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V42 Label: SOCIO-CULTURAL SIMILARITIES WITH YOUR CO

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V43   Label: OTHER

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V44   Label: WILLINGNESS TO SHARE OWNERSHIP IN RETURN
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V45   Label: MINIMIZATION OF COUNTRY RISKS

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V46   Label: COST OF ESTABLISHING A FOREIGN SUBSIDIAR
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V47   Label: SIZE OF BANK

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V48 Label: EXPERIENCE IN FOREIGN BANKING

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V49 Label: POSSESSION OF LARGE INTERNATIONAL CORPOR

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V50 Label: ECONOMICS OF SCOPE AND GEOGRAPHICAL DIVE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V51 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V52 Label: GOVERNMENTS POLICY AGAINST FOREIGN CONTR

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V53 Label: LEVEL IN INTER-BANK MARKET

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V54 Label: SIZE OF YOUR COUNTRY'S TRADE/INVESTMENT
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V55 Label: FISCAL AND MONETARY POLICIES

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V56 Label: ECONOMIC/POLITICAL CLIMATE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V57 Label: TECHNOLOGICAL AND MANAGARIAL CAPACITY
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V58 Label: PSYCHIC DISTANCE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V59 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V60 Label: MINORITY EQUITY FORMS IN INTERNATIONAL B
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V61 Label: MINORITY FORMS INTERNATIONAL BANKING/BAN
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V62 Label: MINORITY/CO-OPERATIVE MODES INTO OVERSEA
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V63 Label: MINORITY ENTRY MODES OFFER BANKS THE ADV
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V64 Label: MINORITY ENTRY MODES USED AS PRE EMPTIVE
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V65 Label: MINORITY EQUITY ENTRY MODES LESS DEVELOP
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V66 Label: MINORITY EQUITY FORM OF INTER. BANK. WIL
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Popular 2.00 Less Popular

3.00 Don't Know

WH2.SYS

```
 Variable: V5               Label: A PARENT BANK

   Value labels follow       Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   YES                                  2.00   NO


 Variable: V6               Label: A SUBSIDIARY BANK

   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V7               Label: A BRANCH BANK

   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V8                  Label: A MEMBER OF AN INTERNATIONAL
CONSORTIUM
   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V9               Label: A JOINT VENTURE BANK

   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V10              Label: AN AFFILIATE OF A UK BANK

   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V11              Label: OTHER BANK

   No value labels            Type: Number   Width:  1   Dec: 0
Missing: * None *

 Variable: V12              Label: HOW MANY SUBSIDIARIES HAVE YOU IN
THE UK
   No value labels            Type: Number   Width:  4   Dec: 0
Missing: * None *

 Variable: V13                Label: SUBSIDIARIES/BRANCHES HAVE YOU
ELSEWHERE
   No value labels            Type: Number   Width:  4   Dec: 0
Missing: * None *

 Variable: V14              Label: GROUP TURNOVER

   No value labels            Type: Number   Width: 10   Dec: 0
Missing: * None *
```

Variable: V15 Label: NUMBER OF EMPLOYEES

No value labels Type: Number Width: 7 Dec: 0
Missing: * None *

Variable: V16 Label: PERCENTAGE OF GROUPS TOTAL
INVESTMENT AC
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Less than 10% 2.00 Between 10
& 20%
3.00 Between 20 & 30% 4.00 Over 30%

Variable: V17 Label: GROUP TURNOVER CONTRIBUTED BY
FOREIGN IN
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Less than 10% 2.00 Between 10
& 20%
3.00 Between 20 & 30% 4.00 Over 30%

Variable: V18 Label: BULK OF COMPANY'S CURRENT OVERSEAS
ACTIV
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V19 Label: POSITION CHANGED IN LAST 5 YEARS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V20 Label: SHIFT IN CORPORATE POLICY/STRATEGY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V21 Label: HOME GOVERNMENT'S OUTWARD
INVESTMENT POL
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V22 Label: HOST GOVERNMENT'S INWARD INVESTMENT
POLI

```
   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V23            Label: HOST COUNTRY'S POLITICAL/ECONOMIC
SITUAT
   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V24            Label: GLOBAL COMPETITION

   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V25            Label: OTHER

   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V26          Label: ORGANIZATIONAL FORMS DESCRIBES YOUR
BANK
   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V27            Label: FOREIGN AFFILIATES/ASSOCIATES

   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V28            Label: OVERSEAS AGENCY/REPRESENTATIVE

   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No


 Variable: V29            Label: FOREIGN CORRESPONDENTS

   Value labels follow    Type: Number   Width:   1    Dec:  0
Missing: * None *
       1.00    Yes                                2.00    No
```

```
 Variable: V30                Label: CONSORTIUM/JOINT VENTURE
ARRANGEMENTS
   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                             2.00   No

 Variable: V31           Label: INTERNATIONAL MERCHANT BANKING
SERVICES
   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                             2.00   No

 Variable: V32          Label: OVERSEAS CASH LINE SERVICES

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                             2.00   No

 Variable: V33          Label: OTHER

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                             2.00   No

 Variable: V34          Label: PRESENCE OF OTHER BANKS - DC

   Value labels follow    Type: Number   Width:  2   Dec: 0
Missing: * None *
       1.00   Most Important                 13.00   Least

 Variable: V35             Label: EXISTENCE OF MAJOR CORPORATE
CUSTOMERS I
   Value labels follow    Type: Number   Width:  2   Dec: 0
Missing: * None *
       1.00   Most Important                 13.00   Least

 Variable: V36           Label: ECONOMIC/POLITICAL SITUATION IN
HOST COU
   Value labels follow    Type: Number   Width:  2   Dec: 0
Missing: * None *
       1.00   Most Important                 13.00   Least

 Variable: V37           Label: SIZE OF HOST COUNTRY'S BANKING
MARKETS -
   Value labels follow    Type: Number   Width:  2   Dec: 0
Missing: * None *
       1.00   Most Important                 13.00   Least
```

Variable: V38   Label: INTEREST RATE DIFFERENTIAL BETWEEN HOST
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V39   Label: TAX RATE DIFFERENTIAL BETWEEN HOST COUNT
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V40   Label: LEVEL OF INDUSTRIAL DEVELOPMENT IN HOST
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V41   Label: PRESENCE OF OTHER BANKS - LDC

Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V42   Label: EXISTENCE OF MAJOR CORPORATE CUSTOMERS I
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V43   Label: ECONOMIC/POLITICAL SITUATION IN HOST COU
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V44   Label: SIZE OF HOST COUNTRY'S BANKING MARKETS -
Value labels follow   Type: Number   Width: 2   Dec: 0
Missing: * None *
1.00   Most Important   13.00   Least

Variable: V45   Label: INTEREST RATE DIFFERENTIAL BETWEEN HOST
Value labels follow   Type: Number   Width: 2   Dec: 0

Missing: * None *
1.00 Most Important 13.00 Least

Variable: V46 Label: TAX RATE DIFFERENTIAL BETWEEN HOST AND U
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V47 Label: LEVEL OF INDUSTRIAL DEVELOPMENT IN HOST
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V48 Label: SIZE OF UK'S INVESTMENT IN HOST COUNTRY
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V49 Label: OPENNESS OF HOST COUNTRY TOWARDS FOREIGN
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V50 Label: HOST COUNTRY OF MAJOR FINANCIAL CENTRE
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V51 Label: UK'S POLITICAL AND ECONOMIC TIES WITH HO
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V52 Label: SOCIO-CULTURAL SIMILARITIES WITH HOST CO
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V53 Label: OTHER

Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V54 Label: SIZE OF UK'S INVESTMENT IN HOST COUNTRY
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V55 Label: OPENNESS OF HOST COUNTRY TOWARDS FOREIGN
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V56 Label: HOST COUNTRY OF MAJOR FINANCIAL CENTRE
No value labels Type: Number Width: 2 Dec: 0
Missing: * None *

Variable: V57 Label: UK'S POLITICAL AND ECONOMIC TIES WITH HO
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V58 Label: SOCIO-CULTURAL SIMILARITIES WITH HOST CO
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V59 Label: OTHER

Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Most Important 13.00 Least

Variable: V60 Label: WILLINGNESS TO SHARE OWNERSHIP

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V61 Label: MINIMIZATION OF COUNTRY RISKS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V62 Label: COST OF ESTABLISHING A FOREIGN STUDENTS
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V63 Label: SIZE OF BANK

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V64 Label: EXPERIENCE IN FOREIGN BANKING

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V65 Label: POSSESION OF LARGE INTERNATIONAL CUSTOME
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V66 Label: ECONOMIES OF SCALE & GEOG.
DIVERSIFICATI
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V67 Label: COMPETITORS PATTERNS OF ENTRY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V68 Label: OTHER FIRM CHARACTERISTICS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V69 Label: GOVERNMENT'S POLICY AGAINST FOREIGN
CONT
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V70 Label: LEVEL OF INTER-BANK MARKET

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V71 Label: SIZE OF UKE TRADE/INVESTMENT IN HOST COU
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V72 Label: FISCAL AND MONETARY POLICIES

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V73 Label: ECONOMIC/POLITICAL CLIMATE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V74 Label: TECHNOLOGICAL AND MANAGERIAL CAPACITY
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V75 Label: PSYCHIC DISTANCE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V76 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V77 Label: MINORITY-EQUITY FORMS OF INTERNAT. BANKI
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V78 Label: MINORITY-EQUITY FORMS OF INTERNAT. BANKI
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V79 Label: MINORITY-EQUITY/CORPORATE MODES OF ENTRY
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V80 Label: MINORITY-EQUITY OFFER BANKS ADVANTAGE OF
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V81 Label: MINORITY-EQUITY USED AS PRE-EMPTIVE MANO
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V82 Label: MINORITY-EQUITY ENTRY MODES LESS DEVELOP
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V83 Label: MINORITY-EQUITY/INTERNAT. BANK. BECOME L
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Popular 2.00 Less Popular

3.00 Do Not Know

WH3.SYS

```
 Variable: V5              Label: AN INDEPENDANT COMPANY

   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V6              Label: A PARENT COMPANY

   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V7              Label: A SUBSIDIARY COMPANY

   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V8             Label: AN ASSOCIATE/AFFILIATE OF ANOTHER
COMPAN
   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V9              Label: A MEMBER OF A CONSORTIUM

   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V10             Label: OTHER

   Value labels follow     Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                                .00   No

 Variable: V11             Label: GROUP TURNOVER

   No value labels          Type: Number   Width: 10   Dec: 0
Missing: * None *

 Variable: V12             Label: NUMBER OF EMPLOYEES

   No value labels          Type: Number   Width:  7   Dec: 0
Missing: * None *
```

Variable: V13 Label: HOW MANY FOREIGN BRANCHES/SUBSIDIARIES E
No value labels Type: Number Width: 4 Dec: 0
Missing: * None *

Variable: V14 Label: WHAT IS THE BULK OF YOUR COMPANY'S CURRE
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *

1.00	West Europe	2.00	North America
3.00	Latin America	4.00	Australia/N Zel.
5.00	Far East	6.00	Asia
7.00	Middle	8.00	Africa
9.00	Eastern Bloc	10.00	Other

Variable: V15 Label: POSITION CHANGED IN LAST 5 YEARS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V16 Label: SHIFT IN CORPORATE POLICY/STRATEGY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V17 Label: HOME GOVERNMENT'S OUTWARD INVESTMENT POL
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V18 Label: HOST GOVERNMENT'S INWARD INVESTMENT POLI
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V19 Label: HOST COUNTRY'S POLITICAL/ECONOMIC SITUAT
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V20 Label: GLOBAL COMPETITION

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V21 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V22 Label: PERCENTAGE OF GROUPS GLOBAL INVESTMENT A
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Less than 10% 2.00 Between 10 & 20%
3.00 Between 20 & 30% 4.00 Over 30%

Variable: V23 Label: GROUP TURNOVER CONTRIBUTED BY FOREIGN IN
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Less than 10% 2.00 Between 10 & 20%
3.00 Between 20 & 30% 4.00 Over 30%

Variable: V24 Label: OPERATIONAL MODES FOR W. EUROPE EXCL. UK
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint
3.00 Licensing 4.00 Franchising
5.00 Agency 6.00 Turnkey Contracts
7.00 International Leas. 8.00 Contract Management
9.00 Prod/Share Contract 10.00 Aquis./Merger
11.00 Other

Variable: V25 Label: OPERATIONAL MODES FOR USA/CANADA

Value labels follow Type: Number Width: 2 Dec: 0

Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V26 Label: OPERATIONAL MODES FOR FAR EAST INCL
JAPA
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V27 Label: OPERATIONAL MODES FOR AUSTRALIA &
NEW ZE
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V28 Label: OPERATIONAL MODES FOR ASIA INCL.
INDIA,
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V29 Label: OPERATIONAL MODES FOR MIDDLE EAST

Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V30 Label: OPERATIONAL MODES FOR EASTERN BLOC
INCL.
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey
Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V31 Label: OPERATIONAL MODES FOR AFRICA

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Non Equity/Joint 2.00 Equity Joint

3.00 Licensing 4.00 Franchising

5.00 Agency 6.00 Turnkey

Contracts
7.00 International Leas. 8.00 Contract
Management
9.00 Prod/Share Contract 10.00 Aquis./Merger

11.00 Other

Variable: V32 Label: MACHINERY/EQUIPTMENT SUPPLY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V33 Label: TECHNICAL ASSISTANCE IN PRODUCTION

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V34 Label: TECHNICAL ASSISTANCE IN PLANT
DESIGN AND
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V35 Label: TECHNICAL ASSISTANCE IN
PROCURING/SUPPLY
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V36 Label: TECHNICAL ASSISTANCE IN MARKETING
& MANA

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V37   Label: PERSONNEL TRAINING

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V38   Label: RIGHT FOR UTILISATION OF PATENTS/TRADEMA
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V39   Label: RIGHT OF UTILISATION OF DESIGN, FORMULA
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V40   Label: RIGHT TO THE USE OF ADVERTISING MATERIAL
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V41   Label: OTHER

```
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Very Significant                     2.00   Significant

       3.00   Neutral                           4.00   Insignificant

       5.00   Very Insignificant


 Variable: V42            Label: SPECIFIED LENGTH OF TIME IN SUCH
TECHNIC
   Value labels follow    Type: Number   Width:   1   Dec:  0
Missing: * None *
       1.00   Yes                                    .00   No


 Variable: V43            Label: IF YES, HOW LONG

   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable: V44           Label: ACHEIVE INTERNAT. DIVERSIFICATION
VIA IN
   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable: V45            Label: HOST GOVERNMENT REGULATIONS

   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable: V46         Label: HIGH POLITICAL RISK IN HOST COUNTRY

   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable:  V47              Label:  RISK  DIVERSIFICATION  THROUGH
COST/RISK S
   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable:  V48                 Label:  RECIPROCAL  EXCHANGES  OF
TECHNOLOGY/HIGH
   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable:  V49                     Label:  COMPETITORS  ADOPT
NON-EQUITY/CONTRACTUAL
   No value labels          Type: Number   Width:   1   Dec:  0
Missing: * None *

 Variable: V50           Label: SIZE OF FIRM TOO SMALL TO FINANCE
```

No value labels Type: Number Width: 1 Dec: 0
Missing: * None *

Variable: V51 Label: PRODUCTS CUSTOMIZED TO HOST/REGIONAL MAR
No value labels Type: Number Width: 1 Dec: 0
Missing: * None *

Variable: V52 Label: PROTECT/SUPPORT EXISTING FOREING BUSINES
No value labels Type: Number Width: 1 Dec: 0
Missing: * None *

Variable: V53 Label: OTHER

No value labels Type: Number Width: 1 Dec: 0
Missing: * None *

Variable: V54 Label: SIZE OF PARENT COMPANY HAVE ANY INFLUENC
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V55 Label: ENTRY CHOICE OF COMPETITORS INFLUENCE CO
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes .00 No

Variable: V56 Label: WILLINGNESS TO SHARE OWNERSHIP AND CONTR
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V57 Label: MINIMIZATION OF COUNTRY RISKS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V58   Label: EXPERIENCE IN FOREIGN MARKETS

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *

1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V59   Label: SIZE OF THE COMPANY

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *

1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V60   Label: POSSESSION OF BRAND NAME, TRADEMARK ETC

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *

1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V61   Label: ECONOMICS OF SCOPE GEOGRAPHICAL DIVERSI

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *

1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V62   Label: OTHER

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *

1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V63 Label: LEVEL OF ECONOMIC DEVELOPEMENT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V64 Label: SIZE OF HOST MARKET

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V65 Label: GOVERNMENT CONTROLS ON INWARD INVESTMENT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V66 Label: FISCAL AND MONETARY POLOCIES

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V67 Label: POLITICAL/ECONOMIC CLIMATE IN HOST COUNT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V68 Label: PSYCHIC DISTANCE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V69 Label: TRANSPORT AND COMMUNICATION COSTS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V70 Label: OTHER CHARACTERISTICS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V71 Label: ENABLE COUNTRY TO DIVERSIFY RISKS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V72 Label: AVOID MARKET DISABLING FACTORS OF OPPORT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00 Strongly Agree 2.00 Agree

3.00 Neutral 4.00 Disagree

5.00 Strongly Disagree

Variable: V73 Label: A SUPERIOR MEANS OF EXPLOITING OPPURTUNI
Value labels follow Type: Number Width: 1 Dec: 0 Missing: * None *
1.00 Strongly Agree 2.00 Agree
3.00 Neutral 4.00 Disagree
5.00 Strongly Disagree

Variable: V74 Label: OFFERS ADVANTAGE OF FLEXIBILITY TO ADJUS
Value labels follow Type: Number Width: 1 Dec: 0 Missing: * None *
1.00 Strongly Agree 2.00 Agree
3.00 Neutral 4.00 Disagree
5.00 Strongly Disagree

Variable: V75 Label: MAY BE USED AS PRE-EMPTIVE MANOEVRES
Value labels follow Type: Number Width: 1 Dec: 0 Missing: * None *
1.00 Strongly Agree 2.00 Agree
3.00 Neutral 4.00 Disagree
5.00 Strongly Disagree

Variable: V76 Label: LESS DEVELOPED COUNTRY PHENOMENON
Value labels follow Type: Number Width: 1 Dec: 0 Missing: * None *
1.00 Strongly Agree 2.00 Agree
3.00 Neutral 4.00 Disagree
5.00 Strongly Disagree

Variable: V77 Label: GAIN OR LOSE POPULARITY IN THE FUTURE
Value labels follow Type: Number Width: 1 Dec: 0 Missing: * None *
1.00 Gain Popularity 2.00 Lose Popularity
3.00 Dont Know

Variable: V4   Label: INDUSTRY CLASSIFICATION

No value labels   Type: Number   Width: 2   Dec: 0

Missing: * None *

WH4.SYS

Variable: V5 Label: AN INDEPENDENT COMPANY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V6 Label: A PARENT COMPANY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V7 Label: A SUBSIDIARY COMPANY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V8 Label: AN ASSOCIATE/AFFILIATE OF A BRIT.
COMP.
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V9 Label: A MEMBER OF A CONSORTIUM

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V10 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V11 Label: NATIONALITY OF COMPANY

No value labels Type: Number Width: 2 Dec: 0
Missing: * None *

Variable: V12 Label: GROUP TURNOVER

No value labels Type: Number Width: 10 Dec: 0

Missing: * None *

Variable: V13 Label: NO. OF EMPLOYEES

No value labels Type: Number Width: 7 Dec: 0
Missing: * None *

Variable: V14 Label: ASSOCIATE COMPANIES IN UK

No value labels Type: Number Width: 4 Dec: 0
Missing: * None *

Variable: V15 Label: ASSOCIATE COMPANIES ELSEWHERE

No value labels Type: Number Width: 4 Dec: 0
Missing: * None *

Variable: V16 Label: BULK OF COMP. CURRENT OVERSEAS ACTIVITY
Value labels follow Type: Number Width: 2 Dec: 0
Missing: * None *

1.00	West Europe	2.00	North America
3.00	Latin America	4.00	Austral./New Z.
5.00	Far East	6.00	Asia
7.00	Middle East	8.00	Africa
9.00	Eastern Bloc	10.00	Other

Variable: V17 Label: POSITION CHANGED IN LAST FIVE YEARS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Yes	2.00	No

Variable: V18 Label: SHIFT IN CORPORATE POLICY/STRATEGY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Yes	2.00	No

Variable: V19 Label: HOME GOVT. OUTWARD INVEST. POLICY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Yes	2.00	No

Variable: V20 Label: HOST GOVT. INWARD INVEST. POLICY

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V21   Label: HOST COUNTRYS POLIT./ECON. SITUATION
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V22   Label: GLOBAL COMPETITION

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V23   Label: OTHER

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V24   Label: % OF GROUPS GLOBAL INVEST. ACCOUNTED FOR
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Less than 10%   2.00   Between 10 & 20%
3.00   Between 20 & 30%   4.00   Over 30%

Variable: V25   Label: TURNOVER CONTRIB. BY FOREIGN INVES. EARN
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Less than 10%   2.00   Between 10 & 20%
3.00   Between 20 & 30%   4.00   Over 30%

Variable: V26   Label: ORGAN. FORMS DESC. COMP. ROUTE OF ENTRY
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00   Yes   2.00   No

Variable: V27   Label: PRESENCE OF OTHER COMPANYS IN UK

```
   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V28             Label: LONDON MAJOR INTERNAT. FINANC.
CENTRE
   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V29               Label: POUNDS STERLING MAJOR WORLD
CURRENCY
   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V30            Label: COUNTRYS POLITICAL TIES WITH UK

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V31            Label: EFFECTIVE TAX AND INTEREST RATES

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V32            Label: TRADE/ECONOMIC RELATIONSHIPS

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V33            Label: SIZE OF UK MARKETS

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No


 Variable: V34           Label: GEO-POLITICAL AND ECONOMIC STATUS

   Value labels follow    Type: Number   Width:  1   Dec: 0
Missing: * None *
       1.00   Yes                               2.00   No
```

Variable: V35 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Yes 2.00 No

Variable: V36 Label: MACHIN./EQUIPT. SUPPLY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V37 Label: TECH. ASSISTANCE IN PRODUCTION

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V38 Label: TECH. ASSIS. IN PLANT DES. AND CONST.
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V39 Label: TECH. ASSIS. IN PROC./SUPP.INPUTS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V40 Label: TECH. ASSIS. IN MARKET. AND MANAGEMENT
Value labels follow Type: Number Width: 1 Dec: 0

Missing: * None *
1.00 Very Significant
2.00 Significant
3.00 Neutral
4.00 Insignificant
5.00 Very Insignificant

Variable: V41 Label: PERSONAL TRAINING

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant
2.00 Significant
3.00 Neutral
4.00 Insignificant
5.00 Very Insignificant

Variable: V42 Label: RIGHT FOR UTILISATION OF PATENTS
ETC
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant
2.00 Significant
3.00 Neutral
4.00 Insignificant
5.00 Very Insignificant

Variable: V43 Label: RIGHT FOR UTILISATION OF DESIGN

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant
2.00 Significant
3.00 Neutral
4.00 Insignificant
5.00 Very Insignificant

Variable: V44 Label: RIGHT TO THE USE OF ADVERT.
MATERIALS
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant
2.00 Significant
3.00 Neutral
4.00 Insignificant
5.00 Very Insignificant

Variable: V45 Label: OTHER

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Very Significant   2.00 Significant

3.00 Neutral   4.00 Insignificant

5.00 Very Insignificant

Variable: V46   Label: SPEC. LENGTH OF TIME IN SUCH AGREEMENT
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V47   Label: IF YES, HOW LONG

No value labels   Type: Number   Width: 1   Dec: 0
Missing: * None *

Variable: V48   Label: ACHEIVE INTERNAT. DIVERSIFICATION

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V49   Label: RECIPROCAL ACCESS TO TECHNOLOGY

Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V50   Label: MULTINAT. ADOPT FLEX. FORMS/FOR. INVEST.
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V51   Label: FIRM TOO SMALL TO FINANCE FOREIGN OPERAT
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

Variable: V52   Label: HIGH COST OF ESTABLISH. FOREIGN SUBSIDIA
Value labels follow   Type: Number   Width: 1   Dec: 0
Missing: * None *
1.00 Yes   2.00 No

```
 Variable: V53            Label: STRONG MARKET COMPETITION

   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V54              Label: ENTRY INTO UK CATEWAY TO EEC
MARKETS
   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V55              Label: PRODUCTS CUSTOMIZED TO UK/EEC
MARKETS
   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V56            Label: HOST GOVT. POLICY

   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V57           Label: GLOBAL PROFIT. AND INCREASED MARK.
SHARE
   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V58            Label: ENT. CHOICE/COMPET. INFLU. COMP.
ENT. ST
   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V59            Label: SIZE PAR. COMP. INFLU. CHOICE OF
ENT. MO
   Value labels follow    Type: Number   Width:   1    Dec: 0
Missing: * None *
       1.00   Yes                                2.00    No


 Variable: V60            Label: SHARE OWNERSHIP  CONTROL IN RET.
FOR ACC
   Value labels follow    Type: Number   Width:   1    Dec: 0
```

Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V61 Label: MINIMIZATION OF COUNTRY RISKS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V62 Label: EXPERIENCE IN FOREIGN MARKETS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V63 Label: SIZE OF COMPANY

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V64 Label: POSSESSION OF BRAND NAME, TRADE MARK ETC
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V65 Label: ECON. OF SCOPE & GEOGRAPH. DIVERSIFICATI

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V66 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V67 Label: LEVEL OF ECONOMIC DEVELOPMENT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V68 Label: SIZE OF HOST MARKET

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V69 Label: GOVT. CONTROLS ON INWARD DIRECT
INVESTME
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V70 Label: FISCAL AND MONETARY POLICIES

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V71 Label: POLITICAL/ECONOMIC CLIMATE IN HOST COUNT
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V72 Label: PSYCHIC DISTANCE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V73 Label: TRANSPORT AND COMMUNICATION COSTS

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V74 Label: OTHER

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *
1.00 Very Significant 2.00 Significant

3.00 Neutral 4.00 Insignificant

5.00 Very Insignificant

Variable: V75 Label: NON-EQUITY FORMS OF INVESTMENT

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V76 Label: NON-EQUITY FORMS OF INTERNATIONAL INVEST

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V77 Label: NON-EQUITY MODES ARE SUPER. MEANS OF EXP

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V78 Label: NON-EQUITY MODES OFFER FIRMS ADVANT. OF

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V79 Label: NON-EQUITY MODES USED AS PRE-EMPT. MANOE

Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V80 Label: NON-EQUITY ENTRY MODES/LESS DEVELOP. PHE
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Agree Strongly	2.00	Agree
3.00	Neutral	4.00	Disagree
5.00	Strongly Disagree		

Variable: V81 Label: NON-EQUITY CONTRACT. MODES ENTRY POP./LE
Value labels follow Type: Number Width: 1 Dec: 0
Missing: * None *

1.00	Popular	2.00	Less Popular
3.00	Do Not Know		

APPENDIX 5

DESCRIPTION OF STATISTICAL TECHNIQUES

FREQUENCY ANALYSIS

Data collected by original investigation are generally recorded in the form of raw scores. The fundamental method for tabular summarization of a set of data is the frequency distribution. It shows a tallying of the number of times each score value (or interval of score values) occurs in a group of scores. In a given sample, it presents a compact summary of the frequency of occurrence of a particular variable in a survey. Such a table quickly conveys much information about the data. Apart from its computational ease (although with statistical packages one need not bother about this), its main utility lies in the fact that all measures of central tendency and dispersion are based on frequency distribution.

MEASURES OF CENTRAL TENDENCY AND DISPERSION

Two types of statistics commonly used to describe the distribution of cases over the values of a single variable are the *measure of central tendency* and the *measure of dispersion.* The central tendency of a distribution is a typical or representative score. In other words, the measure of central tendency helps us to identify the most typical value, the one value or score that best represents the entire set of cases on that variable. More specific definitions of central tendency, each with its own set of characteristics and implications, include the **mean, median,** and **mode.** These three represent different levels of measurement. The median is the measure of central tendency for ordinal data, while the mode is the measure of central tendency for nominal variables. These two are not as powerful and informative as the mean. Interval data provide researchers with the most complete information of all, including categorization, rank, and distance. Interval values can be subjected to any arithmetic manipulation. The mean - being the measure that locates the central part of a distribution in terms of both the number of cases on either side of that point and their distance from it - possesses several properties that make it very useful and generally employed in "higher" statistical analyses.

The notion of central tendency is that the "typical" value or score represents the *tendencies* (general characteristics) within the population, but may not accurately reflect each individual case. For this reason, once we have identified such a typical score we must ask a follow-up question: How typical or representative is it? How good is this average score in summarizing the distribution of scores for all the scores on a given variable? This question is answered by using a second type of statistic, the *measure of dispersion*. The *Variance* with its derivative, the *standard deviation*, is the index that reflects the degree of variability in a group of scores. The measure of dispersion indicates whether the variation around the mean value identified is limited, in which case we can have confidence that the average is a meaningful one, or whether that variation is so great that the mean value is not really very representative of the population after all. The limitation of these statistics is that they describe the characteristics of individual variables, hence they are often called univariate statistics. However, most empirical surveys involve relationships between two (bivariate) or more (multivariate) variables, and these make further use of both the frequency analyses and the measures of central tendency.

MEASURES OF ASSOCIATION AND SIGNIFICANCE FOR NOMINAL VARIABLES

When the data of research consist of frequencies in discrete categories, the X^2 *(Chi-Square) test* is often used to determine the significance of differences between two or more independent groups. The level of measurement involved may be as weak as the nominal scale. Four assumptions underlie the X^2 test. First, the two or more (k) samples must be independent from one another. This usually implies that different and unrelated sets of subjects (sample groups) are selected. In this study, there are four independent sample groups. Second, the subjects within each group must be randomly and independently sampled. Third, each observation must belong to a discrete category, i.e. it must qualify for one and only one category in the classification scheme. Fourth, the sample size must be relatively large. The rule of thumb for sample size is that the Minimum Expected Frequency should not be less than 5. In general, the chi-square test should not be used if more than 20% of the cells have expected values less than 5 and if any of the expected values is less than 1 (Siegel, 1954; Norusis, 1986). However, Siegel also suggests a remedy when these conditions are violated.

Siegel suggests that when there are more than 2 sample groups (and thus the degree of freedom greater than 1), the X^2 test may be used if fewer than 20 per cent of the cells have an expected frequency of less than 1. If these requirements are not met by the data in their original form, the researcher must combine adjacent categories in order to increase the expected frequencies in the various cells (p.110). Only after this combination can the X^2 test be applied. With regard to the statistical power of the X^2 test, Siegel notes that when it is used "there is usually no clear alternative."

YATES' CORRECTION FOR CONTINUITY

The SPSS/PC$^+$ prints two versions of the chi-square statistic, below every crosstabulation. The standard version is the one labelled "*BEFORE YATES CORRECTION.*" The most common of all uses of the X^2 test is the test of whether an observed breakdown of frequencies in a table with two rows and two columns (known as "2 X 2" contingency table) could have occurred under the null hypothesis. For such a table, the approximation by the chi-square distribution will be markedly improved if it incorporates a correction for continuity (Siegel, 1954, p.64; Norusis, 1986, p.230). This is achieved by the Yates' Correction. In other words, the Yates' Correction for Continuity is an adjustment to a 2 X 2 contingency table, intended to make the approximation to the theoretical chi square distribution more precise and thus improve the estimate of the observed significance level. Although it is used in almost all Statistical textbooks, statisticians are not in agreement as to whether this correction is really necessary (McCall, 1970, p.289; Norusis, 1986, p.239). Since the SPSS automatically prints it, it is incorporated in the statistical analysis and interpreted accordingly as to its effect on the decision to reject or not to reject the hypothesis, of interst.

THE *t*-DISTRIBUTION

The t-distribution is very much like the normal distribution. It just shifts the area in the normal distribution to adjust for the uncertainty that surrounds the true values of the standard deviations (Norusis, 1986, p.200). A heuristic judgement is that when sample sizes are large, usually $n > 30$, the t-distribution looks very much like the normal distribution (ibid). Using the t-distribution enables us to test how often we would expect to see a difference between the means of two sample variables when there is no difference between the two groups in the population.

The output from the t-test procedure differs depending on whether in the population the two groups (in this case, UK companies versus Foreign companies or UK banks versus Foreign Banks) can be assumed to have the same variances or not. Norusis (1986, p.203) advises that the numbers in the columns labelled:

1 POOLED VARIANCE ESTIMATE be used if the researcher can assume that the two variances are equal;

2 SEPARATE VARIANCE ESTIMATE be used if such equality cannot be used; and

3 SEPARATE VARIANCE ESTIMATE be used if the probability of the F-value is small.

The SPSS prints next to the F-value the probability of seeing a difference at least as large as the one observed in the sample if the variances are equal in the population and if the distribution of the variable is normal. It should be noted that the F-test for equality of variances is quite sensitive to departures from normality, while the t-test is not (Siegel, 1954). Thus, if the data are not from normal populations, the observed significance level for the F statistic may not be reliable. But, if the observed significance level is large, then there is little to worry about the variances. As stated above, if the observed significance level for the F statistic is small, then it is advisable to use the t-test marked SEPARATE VARIANCE ESTIMATE.

In general, Norusis notes that it is a good idea to use the separate variance t-test whenever the researcher suspects that the variances are not equal. The t-statistic printed next is the standardized score for the variable, obtained computationally by dividing the difference between the two means by its standard error. The SPSS, of course, prints this value automatically. Because the hypothesized parameter for investigation is the difference between two population means, that is μ_1-μ_2=0; the corresponding statistic is the difference between two sample means; Just as the standard error for the mean is a function of the variability of the raw score, the standard error of the difference between mean scores is a function of the variability within each population. For the relation between F and t and the analysis of variance, See McCall (1970, pp.241-244).

ANALYSIS OF VARIANCE (ANOVA)

ANOVA is a statistical procedure which, as its name implies, is used to examine population variances to determine whether the population means are equal. Application of this technique requires that three assumptions be satisfied. (1) The samples must be independent random samples. (2) The samples must be selected from populations with normal distributions, and (3) The populations must have equal variances. In behavioural or social science studies, nonparametric analogues of the parametric analysis of variance have been found to be extremely useful without having to make the assumption of normality (Seigel, 1954; McCall, 1970). The most common approach to this kind of analysis is the *KRUSKAL-WALLIS ONE-WAY ANALYSIS OF VARIANCE BY RANKS.*

The *Kruskal-Wallis test* is described in many Statistics textbooks as an extremely useful test for deciding whether several independent samples are from different populations (Siegel, 1954, p.184; McCall, 1970, p.298; Matre and Gilbreath, 1980, p.470). It is the nonparametric counterpart of the One Way Analysis of Variance. Its purpose is to determine the probability that the means of the four groups of scores (i.e. UK banks, UK companies, Foreign banks and Foreign companies) deviate from one another merely by sampling error. According to Siegel (1954, p.194) and many statistics authors, the Kruskal-Wallis test seems to be the most efficient of the non-parametric tests for K (i.e. more than 2) independent samples. It has power-efficiency of $3/\pi=95.5$ per cent in comparison with the F test, the most powerful parametric test. Since sample values almost invariably differ somewhat, the question is whether the differences among the samples signify genuine population differences or whether they represent merely chance variations as might be expected among several random samples from the same population. The test requires that the level of measurement of the variable be at least ordinal. The Kruskal-Wallis test is an extension of the MANN-WHITNEY U test to more than two populations.

The *Mann-Whitney U test (or Mann-Whitney-Wilcoxon test*, as it is sometimes called) is one of the most powerful of the nonparametric tests, and it is a most useful alternative to the parametric $\underline{t}$ test when the latter's assumptions cannot be met or when the measurement in the research is weaker than interval scaling (Siegel, 1954, p.116).