

Agarwal, Jamuna P.

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Intra-LDCs foreign direct investment: A comparative analysis of third world multinationals

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Working Paper No. 198

Intra-LDCs Foreign Direct Investment, A
Comparative Analysis of Third World Mul-
tinationals

by

,

Institut für Weltwirtschaft an der Universität Kiel

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Intra-LDCs Foreign Direct Investment, A Comparative Analysis

of Third World Multinationals

I. Introduction

Foreign direct investments (FDI) from developing market economy countries (LDCs) such as Argentina, Brazil, Hongkong, India, Singapore, South Korea and Taiwan in other LDCs are drawing considerable attention in discussions on the activities of multinational corporations. Some have welcomed them as agents of suitable technology for the host countries (Wells, 1981; Lall, 1982). Others hope that these investments will lead to improved investment climate in their home countries for FDI from developed countries (Heenan and Keegan, 1979). In this paper an attempt is made to analyse some of the important aspects of these investments in the light of experience on FDI from developed market economy countries (DCs) which have a much longer history. Of late some of the oil-surplus countries (e.g. Kuwait, Saudi Arabia or U.A.E.) have invested abroad significant amounts of capital. These investments are made, however, mostly through acquisition of equity or portfolio interests without any major active participation in the management of the enterprises concerned. Therefore they are not included in this analysis. A further limitation of the paper is that LDC multinationals constitute a relatively new field of research, and information available on them is very limited. Hence some of the generalisations in this paper have to be read with a due amount of caution.

II. Regional Pattern

Data on FDI from LDCs are scarce. Only a few of these countries like India publish figures on outflows of FDI and a few others

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such as Indonesia on inflows of FDI. Recently the UN Centre on Transnational Corporations has published some overall figures on the basis of balance-of-payments data. They indicate that FDI of developing countries constitute only a fraction of those from the developed countries, but they have been growing faster. During 1970-72 the total outflow of FDI from LDCs amounted to US\$ 43 Mill., i.e. 0.33 per cent of the outflow from DCs. In 1978-80 this ratio had risen to 1.64 per cent. For the ten year period from 1970 to 1980 the growth of FDI from LDCs was however more than two and a half times the growth of FDI from DCs (UN, 1983, p. 18 f.). In some host countries (Indonesia and Thailand) they already constitute as much as 20 to 25 per cent of total stock of FDI (table 1). In terms of the number of projects, their importance is even greater¹. In some countries (Nigeria and Ghana) selected industries (e.g. textiles) are already dominated by LDC investors (Busjeet, 1980).

Table 1 - Share of Intra-Developing Countries FCI in Total FDI in Selected Host Developing Countries, Percentages

Argentina	(1976)	1.73	Indonesia	(1976)	21.82
Brazil	(1979)	0.60	Mexico	(1978)	0.22
Chile	(1974-78)	0.95	Peru	(1978)	2.00
Colombia	(1978)	6.48	Philippines	(1976)	3.37
Ecuador	(1977)	6.40	Thailand	(1975)	24.86 ^a
Guatemala	(1976)	6.80	Venezuela	(1979)	0.78
Hongkong	(1976)	2.76 ^a			

^aThere is some error in the original source in Table III-49, probably in calculating the percentage shares. Therefore this share has been calculated on the basis of absolute figures in Tables III-41 and III-49 of the original source. In the case of Thailand the difference may arise also due to difference in base years.

Source: UN, 1978, p. 247 ff. - Compos, 1980 quoted in O'Brien and Monkiwicz, 1981, p. 48.

¹ By the end of the last decade 963 LDC firms had 1964 subsidiaries or branches in 125 host countries of which about 50 per cent were in the manufacturing sector. However, it would be wrong to consider all of these LDC firms as multinationals because many of them may not have a subsidiary or branch or joint venture in more than one foreign location. If a multinational is defined as a firm having manufacturing facilities in six or more foreign countries only 6 of the above LDC firms could be specified as such (Well, 1983, p. 2 ff.).

Table 2 - Selected Important Home and Host Countries of FDI in the Third World, Mill. US\$

Largest home countries ^a		Largest host countries ^a	
Argentina	(35)	Brazil	(42)
Brazil	(30)	Colombia	(36)
Hongkong	(753)	Ecuador	(33)
India	(22)	Hongkong	(54)
Korea (South)	(107)	Indonesia	(1388) ^b
Malaysia	(48)	Mexico	(21)
Mexico	(30)	Thailand	(44)
Philippines	(276)	Venezuela	(22)
Singapore	(131)		
Thailand	(30)		
Uruguay	(21)		
Venezuela	(42)		

^aFigures in brackets refer to total FDI in 1976 or one to two years earlier in or from neighbouring important developing countries. - ^bData for Indonesia refer to approved intended investments and are therefore not quite comparable with other countries.

Source: UN, 1978, p. 246 f.

The largest investors in Asia are Hongkong, South Korea, the Philippines and Singapore, and in Latin America Argentina, Brazil, Mexico and Venezuela. The largest host countries are Indonesia, Hongkong and Thailand in Asia and Brazil, Colombia and Ecuador in Latin America. Many of these countries are home as well as host countries of Third World multinationals (table 2).

One of the important characteristics of these multinationals is that they generally invest in their neighbouring countries with sizeable populations of their own ethnic and cultural background. For example nine tenths of Argentinian FDI in 1980 were concentrated in Latin America mainly in Brazil, Peru and Uruguay (O'Brien and Monkiewicz, 1981, p. 46) and of India in Asia and Kenya (IIC, 1981, p. 25 f.). More than four fifths of the affiliates of companies from

Singapore and more than half of those of Malaysian firms are in South and East Asia (UN, 1983, p. 34). Ethnic and cultural similarity is very often correlated with similarity of demand structures of home and host countries. Moreover, ethnic and cultural similarity tends to assure the investors of an elastic local supply of personnel which suits their taste and can be trained for managerial and technical jobs. This is more important for their long run planning than in short run when they tend to employ a relatively high proportion of expatriates from their home countries. Early expansion of DC multinationals was also characterised by a similar pattern.

Notwithstanding, the importance of this factor should not be overemphasised. A small minority population of Indians could for example attract Indian FDI as far as Nigeria but not further to Guyana where the Indian population is in majority. Investing in countries at very long distances and with quite different cultural, economic and political conditions involves higher information and management costs which are generally avoided by LDC multinationals. Their investments are on the whole confined to nearby regions, although there are exceptions to this pattern. Hongkong FDI in textiles have for example a wider geographical spread and in servicing activities FDI of all developing countries are widely distributed. A few Indian firms have opened hotels and restaurants in Australia, France, U.K. and the USA. Chinese restaurants are spread all over the world, though many of which may be locally owned. Banks from South Korea, India and other developing countries are - like those from the developed countries - following their trade by opening branches in their main partner countries. A larger part of the Korean FDI in the trading sector is spread over North America, Europe and Africa. Nonetheless, regional concentration of affiliates of LDC multinationals is very high, in any case higher than that of affiliates of DC multinationals.

III. Sectoral Structure

A great part of FDI from developing countries is concentrated in the manufacturing sector. Two out of every three Indian joint ventures are engaged in industrial activities. About 80 per cent of outward Taiwanese and inward Colombian FDI, are in the manufacturing sector (table 3)¹. Within this sector the investments are spread over a number of industries producing mostly - unlike the DC firms - products which are characterised by mature technologies, low price competition and absence of product differentiation (Busjeet, 1980). More than half of the Hongkong FDI seems however to be concentrated in textiles (Chen, 1981). In the case of India, textile investments occupy second place. The biggest share of her FDI goes to light engineering industries (FICCI, 1982). Intra Latin American FDI are preponderantly in food products (White, 1981). Thus LDC investments take place mostly in those industries which dominate the manufactured exports of investing countries supporting the hypothesis that trade is followed by FDI (Roemer, 1975).

FDI of developing countries in raw materials of host countries are relatively less important, though the situation differs from country to country. India has recently set up a joint venture in Senegal, which will enable India to import phosphoric acid from that country from 1984-85 onwards. Some firms from Hongkong and the Philippines have invested in Borneo to exploit the local supply of timber. Hongkong firms supply timber mainly to their home-based furniture industry whereas the Filipino timber investors in Borneo are world market oriented. In Argentina and South Korea the share of raw material-FDI is probably the highest among all the investing countries of the Third World (table 3). In the case of Argentina it is mainly in petroleum and most of the South

¹ This table has been prepared on the basis of heterogeneous data. Therefore the figures quoted for one country are not quite comparable with those for another country. Nonetheless, it is helpful in drawing some broad conclusions with regard to industrial distribution of FDI of developing countries in the absence of better data.

Table 3 - Sectoral Distribution of FDI of or in Selected Developing Countries^a, Percentages

	India 1982	South Korea 1978	Taiwan 1979	Argen- tina 1974	Ecuador 1974	Colom- bia 1974	Vene- zuela 1974
Manufacturing sector	65	17	78	49	33	81	46
Construction	5	13	...	8	17	6	10
Mining, Agri- culture and Forestry	...	26	8	38 ^c	12
Trading acti- vities	13	20	11	4	9	...	40
Others ^d	17	24	1 ^b	2	29	13	4

^aOutward FDI in the case of Argentina, India, South Korea and Taiwan. Inward FDI in the case of Ecuador, Colombia and Venezuela. - ^bIncludes construction. - ^cIncludes petroleum. - ^dShares do not add up to 100 due to rounding.

Source: FICCI 1982, Jo 1981, O'Brien and Monkivicz 1981, Ting 1981, White 1981.

Korean investments are in timbering in South East Asia. The Peruvian Cia Minera Buenaventura' has capital participations in some mining companies of other Latin American countries like Venezuela and Ecuador. Brazil has a joint venture in Colombia to ensure coal supply to her steel factory in the public sector. As host countries Indonesia in Asia, Ecuador and Venezuela in Latin America appear to have attracted relatively more FDI in their raw material sectors from other developing countries.

IV. Relevance of Eclectic Theory

The present theoretical discussion on FDI is dominated by the eclectic theory of international production according to which FDI are a function of ownership, internalisation and locational advantages. Ownership advantages refer to invisibles like proprietary technology, patented trade marks, control on market entry, etc., enabling the investor to outweigh the disadvantages of operating in a foreign environment. Further, these advantages should yield greater benefit to the investor through internalisation (i.e. FDI) than through their outright sale (licensing, technical service agreement or sale of turn-key projects, etc.) to third parties. Finally, the host country must offer some locational advantages (e.g. lower wage costs, cheaper energy or raw materials) over the home country of the investor to attract FDI (Dunning, 1981). In the absence of any of these three factors a firm will try to serve a foreign market through exports (of goods or invisibles) or refrain from that market.

This theory is deduced from the experience on FDI behaviour of those DC investors who have already become multinational producers and sellers of goods and services for a sufficiently long time to appear in front lines of international business. Most of the LDC multinationals are relatively very small and in their initial stages of the internationalisation process. Therefore the question arises whether the eclectic theory is applicable to the phenomenon of foreign investing by LDC firms. As the following discussion shows, the answer is in the affirmative in spite of many differences between these two kinds of foreign investors with regard to their ownership specific advantages, market behaviour and locational strategies.

According to the eclectic theory a firm must have at least one ownership-specific advantage over its competitors in a foreign country in order to invest there successfully. Such ownership-specific advantages of DC multinationals are in most of the cases attributable to their larger size whereas in the case of LDC firms to their smaller size. This hypothesis needs however further elaboration. But prior to this, it may be added that this basic difference between these two kinds of multinationals constitutes practically the origin of most of the arguments, such as suitability of managerial and technical know-how given in favour of FDI from one in another developing country.

The larger size of a firm enables it to undertake high R & D activities which enable it to have more patents, trade marks and such other ownership-specific advantages. Size is instrumental also in helping a firm to have a greater control on market entry. Therefore, size is found as the most important determinant of multinationality of firms in the USA (Vernon, 1971; Horst, 1972). LDC firms usually do not possess exclusive patented or unpatented know-how or internationally renowned trade-marks to have a competitive edge over local or foreign competitors in a host country. There are only a few companies like the Filipino brewer San Miguel, F & N of Singapore, Inca Kola of Peru or Perle's Confectionary of India who have been able to build an international brand image and take its advantage in promoting their FDI (Wells, 1983). But there are exceptions to the general pattern of FDI from developing countries. Ownership advantages of LDC investors generally stem from the scaling down of the technologies imported from developed countries and thus making them suitable for smaller markets of poorer countries. LDC firms are active in goods produced with mature and standardised techniques which they have not only learnt but also adapted to local climatic and social conditions. This gives them a competitive advantage over the original producers of these techniques. DC multi-

nationals are generally used to bigger markets and their managers do not find it profitable to work in countries with smaller markets. Managers from developing countries are on the contrary used to operating in their smaller home markets and they carry this advantage to their host countries. Moreover, they are prepared to work at lower salaries than the managers from developed countries. The optimum size of firms established by LDC multinationals is smaller and thus more suitable for the needs of the host developing countries with limited domestic markets. This does not apply to those cases where FDI are undertaken to supply export markets with elastic demand. Such intra-LDCs investments are however rare, although their exact share is not known. Textile firms from Hongkong have been active in this field for a long time. They established their export platforms first in Singapore and later spread over to Mauritius and the Philippines. Their competitive advantage over the local firms consists in having established business relations with customers especially in developed market economies (Wells, 1983).

The second postulate of eclectic theory of international production is that the exploitation of ownership-specific advantages through FDI should be more profitable for the owner of these advantages than through their direct or indirect sale. Capital goods which have been adapted to local conditions of the less industrialised countries can be easily exported and are in fact exported by them to other developing countries wherever local entrepreneurs are willing and able to establish production units with these capital goods. But the local entrepreneurship is not always forthcoming in the latter group of countries, or is not prepared to take the complete risk of a new enterprise in view of its lacking managerial know-how. This know-how which is available in the more industrialised developing countries is personified in the managers who are mostly employed in the firms of these countries. They cannot be imported into the other developing countries freely through market

channels. There are various reasons for this managerial immobility among the developing countries. Firstly, immigration laws of these countries are restrictive and quite often more than what they are in many developed countries. Secondly, business managers in the more industrialised developing countries are aware of the indigenisation in other developing countries. Therefore they are not willing to sacrifice their long term security of jobs in their home countries for short term gains in poorer developing countries¹. They are often prepared to take similar risks in developed countries where employment markets are more lucrative and large enough to offer sufficient chances for alternative jobs. But employment markets in developing countries are relatively small. Further, a manager returning to his home developing country from an even more underdeveloped country has to face poorer local job prospects than the one coming back with experience in a highly industrialised economy.

This kind of market failure is probably the most important reason for internalisation process of managerial know-how of firms from newly industrialising countries. Though it is not of their own creation, it helps them to promote their FDI instead of exports of their goods and services to lesser developed countries.

The third condition of eclectic theory is that the host country must possess one or more of locational advantages over the home country of a foreign investor. Otherwise he would prefer to serve the market of the host country through exports of his products. Locational advantage is, however, a relative concept. It may be directly related to the economy of the host country

¹ Business executives of public sector enterprises in more industrialised developing countries do go on deputation to lesser industrialised developing countries. This kind of export of managerial know-how is generally confined to public utility services where FDI are generally not allowed.

and be able to attract foreign investors to establish production facilities there. Or a locational advantage of a host country may be an indirect result of disadvantage(s) in the home country of an investor. The former may be called direct and the latter indirect advantage because it is a function of locational disadvantage(s) in the investing country.

The more popular of the direct advantages are: fiscal incentives, import protection, large or growing domestic market, natural resources and low-cost labour. A survey of FDI of developed countries into developing countries showed that it was doubtful whether fiscal incentives given by host countries had much effect on the inflow of these investments. Import protection was found to play a greater role especially if the domestic market was large. Investors are usually attracted by protected markets (Reuber et al., 1973). A survey of Indian joint ventures in Indonesia, Kenya, Malaysia, Nigeria and Singapore showed that though such locational advantages did positively influence the decisions of Indian investors, they could not be said to be of very great importance for this purpose (Chishti et al., 1977). As compared to fiscal incentives and import protection, market size has proved to be a more important variable at macro level in a number of studies on investment behavior of DC multinationals¹. This may apply to LDC multinationals too, though this could not be verified from the limited number of empirical studies available in this field. The availability of a cheaper labour force has proved to be an important determinant in the case of FDI from developed countries (Riedel, 1975; Donges, 1976, 1980; Agarwal, 1978; Juhl, 1979). But it is not such an important consideration as yet for the investors from the newly industrialising countries (Lecraw, 1977) because their unit labour costs in the host developing countries may not be significantly different from those in their home countries. Hongkong (Busjeet, 1980), Singapore and to some

¹ See for example Bandera and White (1968), Scaperlanda and Mauer (1969) and Schwartz (1976).

extent South Korea are now exceptions. Rapidly rising wages especially in the first two countries have encouraged some investors to look for cheaper locations in the neighbouring countries of Thailand, Malaysia, Indonesia and the Philippines.

Indirect locational advantages of a country arise for example from restrictions on monopolistic practices, environmental regulations or market saturation in home countries of investors. In a recent survey¹ about ten per cent of the parent companies of Indian joint ventures stated that the restrictions on their domestic expansion are an important ground for their decisions to multinationalise their businesses². In the USA the growth of bigger corporations is found to be constrained by anti-trust regulations. Therefore they find in FDI an alternative to further growth at home (Bergsten et al., 1978). It is known that environmental regulations in Japan and the USA have encouraged their firms to increase their offshore productive activities. In contrast to these disadvantages created by legal restrictions, home country disadvantages can arise also on economic grounds. For example, local firms in developing countries easily reach a market saturation point and exports to other countries may not fulfil their desire for enough growth due to protectionist policies of trade partners. Thus they may be encouraged to invest abroad. This suits sometimes also their need for geographical diversification of business activities. One of the motives for geographical diversification is to achieve a greater flexibility in the field of foreign exchange transactions. All developing countries impose restrictions on their firms in some way or other with regard to their receipts and payments in foreign exchange and by doing so they

¹ Agarwal and Chishti (forthcoming).

² In order to encourage medium scale firms restrictions were imposed in the 1970s in India on further expansion of its bigger domestic industrial companies. These restrictions were later relaxed to some extent.

are able to control some other activities indirectly. By internationalising their production these firms hope to increase their freedom from national exchange regulations at least in the long run. FDI provide generally better opportunities than portfolio investments for transferring funds internationally to avoid foreign exchange restrictions of both home and host countries.

V. Host Country Benefits

Appropriate technology

One of the commonly accepted characteristics of FDI of developed countries is that the technologies associated with these investments are capital intensive whereas the host developing countries need on account of their factor endowments labour intensive technologies. As a result, costs of production of goods produced by these imported technologies are higher than what they would have been if they were produced with labour intensive technologies. These costs are sometimes even higher than those in the home countries of foreign investors primarily because domestic markets of host developing countries are generally smaller than optimum size of the imported technologies. Therefore such goods are internationally not competitive¹ and in the domestic markets of host countries they can be sold only with the support of local import protection. This leads however to inefficiency of domestic resources, especially of capital which is scarce in developing countries. The technologies associated with the FDI of investing LDCs are claimed to be more labour intensive and therefore more appropriate for the host developing countries (Wells, 1983). Another important reason for

¹ Moreover, exports of such goods is subject to export restrictions imposed by parent firms. Such restrictions were more popular in the 1960s. Since then host countries have succeeded to some extent in avoiding export restrictions associated with technology import especially in the field of mature products.

their appropriateness is that their optimum size of production (Lall, 1982) is generally lower than that of technologies imported from highly industrialised countries. The main sources of these advantages are the following:

- Even if investing developing countries are not able to spend sizeable funds on R & D activities, they have succeeded in developing some production techniques and processes corresponding to their own factor proportions (Agarwal et al., 1975). These methods of production are very likely to suit other developing countries endowed with similar factors of production.
- Though most of the FDI from developing countries is in mature products incorporating technologies once imported from the developed countries, these technologies have undergone adjustments and adaption to local conditions in the original importing countries (O'Brien and Monkiewicz, 1981). This is more common in ancillary operations than in the main production processes. In many cases developing countries have succeeded in scaling down the main production processes to suit their market sizes. Such adapted technologies are naturally more appropriate for other host developing countries than the unadjusted original forms of these technologies. This is considered to be one of the important reasons for the profitability of LDC firms for example in the Philippines (Busjeet, 1980) where they are able to avoid idle capacity by adjusting to the available demand.
- Sometimes the investing LDC has not adjusted or changed an imported technology at all but the same technology is no more available from the original exporting developed country because it has gone over to more labour saving production processes in order to reduce the costs of production. When the older technology is imported from one into

another developing country, it is more appropriate for the latter in relation to its successive models available from a highly industrialised country.

A comparison of firms from developing and developed countries in Indonesia showed that on an average the former needed only about half of the capital per worker used by the latter during the period 1967-76 (Wells and Warren, 1979)¹. Lecraw's (1977) comparison of Thai firms with different origins showed that in each industry firms with partners from developing countries (India, Taiwan, Singapore and Malaysia) used considerably less capital per unit of output than those having their parents in highly industrialised countries or those which were purely locally owned. The fact that the subsidiaries of MNCs from the developed countries tend to use capital intensive technologies is well known. But the finding that this applies also to the local firms in Thailand is somewhat surprising. One explanation could be that the relative factor prices on the domestic market are distorted. But this should apply also to firms having foreign partners from LDCs. The fact that these joint ventures are using labour intensive technologies in spite of distorted factor prices indicates that local entrepreneurs are too eager to import the latest possible technologies from the developed countries which are capital intensive and this is facilitated by distorted relative prices on factor markets. Local firms import as much as 80 per cent of their machinery from the developed countries and only 4 per cent from developing countries. The higher optimum size of these capital goods leads to lower capacity utilisation in the local firms (Lecraw, 1977). Busjeet's (1980) comparison of LDC and DC firms in the Philippines and Mauritius confirmed that the former are more labour intensive, not only in those cases where the production was done primarily for local market but also in the case of export-oriented projects where competitive

¹ Comparisons at 2 and 3 digit levels also showed that capital-labour ratios of the LDC joint ventures were lower than those from industrialised countries in each industrial branch except in food products (Wells and Warren, 1979).

pressure is expected to force producers to opt for the most appropriate technologies.

Absorption of Local Resources

Firms having their parents in the developed countries are generally parts of integrated worldwide oriented big corporations with centralised sourcing and selling strategies. Therefore the absorption of local resources by these firms in developing countries is likely to depend less on domestic resource availability than on the strategic considerations of the parent firms and the local prices in relation to those of other sources accessible to parent firms. LDC firms in the host countries are generally not quite so integrated in sourcing and marketing strategies of parent companies. Therefore they are likely to absorb a relatively greater proportion of domestically available raw materials and capital goods. This is likely to be reinforced by the majority ownership of local partners in these ventures. Nearly all the foreign involvement of Indian firms in developing countries is through joint ventures in accordance with the declared policy of the Indian government. About two thirds of Latin American firms having foreign equity participation from developing countries of the same region are joint ventures¹. Similar results were yielded by a survey in Thailand. Whereas only about one fourth of the multinationals from developed countries held minority equity participation in Thailand, for developing countries this indicator was as high as 86 per cent (Lecraw, 1977)².

¹ White et al., 1977, quoted in O'Brien, 1980.

² FDI by DC multinationals are often undertaken to exploit proprietary rights of their technical know-how. Local equity participation endangers these rights at least in the long run. Therefore the proprietors of these rights resent having local capital partnerships. Investors from developing countries generally do not bring with them such invisible assets to their host countries. They are instead more interested in taking advantage of the local market experience of their partners in the host countries. However, in the light of experience in their home countries they may be also interested in avoiding confrontation with the host governments on the point of ownership by opting for minority participation (Lecraw, 1977). The Indian government does not generally allow its investors to have majority ownership abroad in keeping with its policy of discouraging majority foreign ownership of firms domiciled in India.

LDC firms in Thailand import only two fifths of their raw material requirements as compared to a three-fourth share of imports in the case of DC firms. Similarly local firms are also consuming more imported raw materials than LDC firms in Thailand (Lecraw, 1977). An Indian firm adopted its technology to suit the consumption of locally available quality of raw materials in Mauritius¹.

Local financing plays a bigger role in the case of FDI of developing countries than those of developed countries. However, reliable statistics are not available to support this hypothesis. An inference in its support is drawn from the fact that most of LDC joint ventures have local majority equity participation. LDCs facing foreign exchange shortage generally do not allow export of financial capital for FDI. In India for example cash transfers for this purpose were not at all permitted until 1978 and FDI took place by capitalising the value of exported capital goods and services such as managerial and licensing fees. Since then cash investments are permitted for those projects which are likely to stimulate exports of Indian machinery and equipment. However, the share of such cash remittances in India's FDI remains very low at about 10 per cent (IIC, 1981)². Statistical evidence for other countries is wanting. Whatever information is available, it indicates that most of the FDI of other developing countries also consists of the capitalised value of exported capital equipment and services (Ting and Schive, 1981). This is not very surprising when considered that host developing countries may not be found by investing firms as better resorts of capital security than their home countries.

¹ For more such examples see Wells (1983).

² This share will however increase in the next few years because some of the joint ventures now under implementation have been permitted to transfer relatively high amounts of cash for equity participations abroad. In all these cases the Indian government is one of the partners. One of them is Indo-Senegal joint venture to produce phosphatic fertilizers and phosphoric acid; the other two are banks in Nigeria and Sudan to be established in collaboration with the State Bank of India (IIC, 1983).

Local majority share in capital should normally lead to indigenous control of management. But LDC joint ventures tend to have a very high share of expatriate managerial and supervisory staff coming from their home countries. Unlike MNCs from developed countries, firms in home LDCs are generally controlled and managed by individuals or individual families. They tend to employ in their foreign firms their relatives or managers who have served them for a long time in order to secure a continuity of their managerial system and effective control. Busjeet (1980) found cases in the Philippines and Mauritius in which this was tolerated by the local partners, though they had majority ownership.

VI. Home Country Benefits

If it is assumed that the governments act in the interests of their people, they would expect from their investors abroad to receive in the long run net transfer of foreign exchange earnings. Firstly, they may come directly from export of goods and services generated by FDI as well as from remittances of dividends. Secondly, FDI are supposed to project a positive image of host country's technological and economic capability and thus improve the export chances in general. Thirdly, the distribution system created by the FDI in the host market may be used to promote other exports of the home country.

These policy objectives are quite obvious in the Indian case. Export promotion is a declared aim of government policy towards Indian joint ventures abroad which are promoted by means of tax incentives, import replenishment scheme, etc. (FICCI, 1982). As it is evident in table 4, this policy of the Indian government has been successful. Up to 1980 Indian joint ventures ignited an initial export of capital equipment worth 256 Mill. Rs. which were capitalised and had

Table 4 - Initial and Subsequent Effects of Joint Ventures on Indian Balance of Payments, 1970 - 1980^a (Mill. Rs.)

	Initial Capitalised Export of Goods to Joint Ventures	Subsequent Export of Goods to Joint Ventures	Inflow of repatriated Dividends	Inflow of other Repatriations	Total foreign exchange earnings	Percentages of			
						2 to 1	3 to 1	4 to 1	5 to 1
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Up to 1971	48.75	53.72	6.00	5.86	65.58	110.2	12.3	12.0	134.5
1972	12.77	13.28	1.84	1.32	16.44	104.0	14.4	10.3	128.7
1973	21.78	42.09	2.56	1.65	46.30	193.3	11.6	7.6	212.6
1974	23.86	73.57	3.25	2.29	79.11	308.3	13.6	9.6	331.6
1975	30.11	97.97	2.59	13.03	113.59	325.4	8.6	43.3	377.3
1976	34.25	104.49	3.92	13.62	122.03	305.1	11.4	39.8	356.3
1977	24.55	133.10	5.75	20.69	159.54	542.2	23.4	84.3	649.9
1978	17.28	144.00	7.43	23.95	175.38	833.3	43.0	138.6	1014.9
1979	28.77	218.65	18.59	49.26	286.50	760.0	64.6	171.2	995.8
1980 ^b	13.74	255.96	6.88	14.55	277.39	1862.9	50.1	105.9	2018.9
Total	255.86	1136.83	58.81	146.22	1341.86	444.8	23.0	57.1	524.5
of which:									
Joint ventures in operation	209.37	946.57	48.93	102.27	1097.77	452.1	23.4	48.8	524.3
Joint ventures abandoned	33.85	146.76	9.88	19.85	176.49	433.6	29.2	58.6	521.4
Joint ventures under implementation	12.64	43.50	-	24.10	67.60	344.1	-	190.7	534.8

^a Fiscal years April to March. - ^b Incomplete.

Source: IIC, 1981 and 1983.

no direct impact on balance of payments. The growth of additional exports of raw materials, intermediate goods and components generated by them up to 1972 was slow. Since then the ratio of these exports to initial exports of capital equipment has been growing. In 1978 to 1980 additional exports amounted on an average to ten times the initial export of capital equipment (Column 6 of table 4). In addition, foreign exchange earnings through dividend transfers (column 7) and other repatriations (fee for technical know-how, engineering services, management, consultancy, etc., column 8) have also gone up considerably during this period so that on a flow basis joint ventures in the last three years (1978/80) for which the data are available were yielding foreign exchange to India on an average as much as twelve times the initial capitalised value of exported machinery and equipment (column 9). On a cumulative basis for the period ending in March 1981, this crude¹ measure of balance-of-payments effect of Indian FDI results in a ratio of 1:5 (table 4). It is somewhat higher in the case of joint ventures still under implementation indicating that the total foreign exchange earnings in terms of per unit of investment are likely to increase when these joint ventures also start remitting dividends. Even those joint ventures which have been abandoned by Indian investors performed equally well on an average in terms of export earnings, dividends and other remittances. If the other components of FDI (viz., capitalisation of know how and preliminary expenses, etc., cash investment, Bonus shares) are also taken into account, total Indian investments in her joint ventures in operation at the end of August 1980 comes to 357 Mill. Rs. (IIC, 1981). On this basis the cumulative foreign exchange earnings of Indian joint ventures amounted in 1980 to more than

¹ For a comprehensive assessment of balance-of-payments effect of FDI, the value of exports displaced by them and some other variables will have to be taken into consideration, which has not been done here for want of readily available data. A more detailed analysis will be attempted in another forthcoming study devoted exclusively to India. However, some of the difficulties involved in estimating indirect effects of FDI on balance of payments of home countries cannot be overcome empirically. For a simple and useful discussion of the problem involved see Reddaway et al., 1967 and 1968.

300 per cent. In view of India's need for foreign exchange, her relatively recent start of industrialisation and limited international competitiveness of Indian goods, this is undoubtedly a remarkable performance. Moreover, a higher inward flow of foreign exchange may have been hindered insofar as Indian investors may be willing to build resources in foreign countries in order to seek greater international mobility of their capital than is allowed under existing foreign exchange rules in India.

Sufficient data for other investing LDCs are not available to analyse the effects of FDI on their balance of payments. Evidence from Thailand as a host country suggests that LDC investors cover a considerable part of their import demand with supplies from their home markets or other developing countries (Lecraw, 1977). Further, FDI from LDCs are mostly undertaken to supply the host markets or third countries (e.g., Hongkong textile investments in the Philippines to export to the USA or in Mauritius to meet the European demand). As a result, balance-of-payments effect of FDI is likely to be positive in investing LDCs in general unless the exports of capital equipment and associated goods triggered through FDI and the remittances of dividends, etc., are compensated by the displacement of exports made to host markets prior to investing there. It is very speculative to make generalisations on export displacement in the absence of any conclusive evidence. In the USA - the country with the largest stock of FDI - this question has proved to be very controversial, especially between the trade unions and the American investors abroad. The former believe that export displacement effect together with imports of the American MNCs from their foreign affiliates is higher than additional exports triggered by FDI, whereas the latter argue in the opposite direction. Literature on both macro and micro studies shows that the relation between FDI and trade is indeterminate. In their relatively recent study carried at macro level Bergsten et al. (1978) concluded "that a modest amount of foreign

investing is highly complementary to U.S. exporting but that higher levels of foreign investment have no strong or consistent impact on U.S. exports" (p. 95 f.). FDI of LDCs including India can be considered modest in the spirit of the above view.

VII. Conclusions

Compared with the FDI of developed countries the intra-LDCs investments are very small, though the correct magnitude of the latter is not known. LDC investors are active in mature products and rely on low price competition. DC multinationals prefer to invest in technology intensive and highly differentiated products dependent on sophisticated marketing efforts. Thus mostly there is not much scope for conflict or competition between the two in the host developing countries. The intra-LDCs investments are rather complementary to DC investments insofar as they raise the demand for capital goods and other inputs supplied by the parents of DC affiliates or for their own products in host countries by raising national income. LDC firms may also act as subcontractors to DC firms in the host developing countries. Moreover firms from poor and rich countries may cooperate to establish joint ventures in third countries. A number of such joint ventures have already been established (Wells, 1983).

The presence of LDC multinationals has increased the options of host LDCs to choose from a larger number of suppliers of investment and technology, especially in those industries which suit their factor endowments. This would strengthen their bargaining power and enable them to conclude better deals. Some LDC governments have shown preference for FDI from other developing countries on political grounds. In Syria, Iraq and Egypt FDI from other Arabian countries are given a preferential treatment to promote Islamic unity (Shihate, 1975). Sri Lanka's trade minister is quoted to have said that his country preferred investors from countries like Hongkong because in such

a case nobody could talk about a sell-out to imperialism (Heenan and Keegan, 1979). Intra-LDCs investments have however a disadvantage that LDC investors prefer local partners of the same ethnic and cultural background and to that extent they may disturb the balance between different racial and religious communities of host countries. Sometimes rivalry between people of different origins as in Sri Lanka is very strong and FDI favouring one particular community may add fuel to the fire. Relying only on LDC investors is not advisable also because they are not able to supply technology for many industries requiring a continuous flow of technological development¹.

LDC foreign investors are motivated, in addition to profits², by a number of factors whose relative importance for them varies from project to project. As in the case of DC investors the most popular motive of LDC investors is to maintain their existing markets and/or to gain new ones. When an export market is threatened by protectionist measures of an importing country, the exporter tries to maintain his sales in that country by launching local production. The history of import protection in the host LDCs is however often older than that of many LDC investors in these countries. Therefore what has happened more often is that the investors from newly industrialising countries after having achieved enough success on their home markets have tried to gain ground through FDI in the protected markets of other LDCs. Market maintenance argument applies more to DC investors because they were supplying the markets of host LDCs before these countries became independent and introduced pro-

¹ Even in those cases where parent firms from developing countries are able to make major technological contributions at the beginning of joint ventures, they may not be able to keep up with the technological progress due to lack of innovations in the home country. An early Argentinian multinational 'Siam di Tella' had to sell all its foreign subsidiaries. Somewhat contrary to this the Brazilian affiliate of Argentinian Alpargatas is now larger than its parent and probably not dependent on it for technological growth. Generalisation of Argentinian experience is however risky because of the stagnating domestic economy (O'Brien and Monkiewicz, 1981).

tectionist import barriers. Sometimes FDI are undertaken in a particular LDC to gain a preferential access to a third country market with which the host country has a preferential trade arrangement. For example, Hongkong textile firms have established joint ventures in Mauritius to supply the members of the European Economic Community.

The other important motives of intra-LDCs investments are directly related to economic and political policies of their home governments. In some cases (e.g. India) FDI are sought as an alternative to domestic growth which is restricted by laws meant to control monopolistic practices of big industrial companies. Joint ventures or subsidiaries are established in foreign countries also to seek greater freedom from restrictive foreign exchange regulations in home countries. Geographical distribution of assets through FDI is considered more useful for this purpose than through portfolio investments, which are moreover not permitted by most of the LDC governments.

Some of the joint ventures especially in the public sector are offsprings of bilateral economic negotiations between developing countries. Besides helping the partner countries, the investing governments hope to raise their exports of goods and services through direct investments. Host governments, on the other hand, expect from these investments appropriate technologies free from political strings because they have a feeling of negotiating on the basis of equality. Insofar as both the sides are able to realise their aims, intra-LDCs direct investments are going to increase South-South investment and trade which will strengthen economic cooperation among the LDCs in other fields also. The existing experience in this field is however not devoid of disturbances. The rate of unsuccessful joint ventures which are abandoned to those which continue to operate is high¹. Though the blame for this is to rest primarily on

¹ Among Indian joint ventures it was as high as 37 per cent up to March 1982 (IIC, 1983).

the managers especially those appointed by the parent firms, the host governments have also failed from time to time to implement conditions under which the foreign investments from LDCs as well as DCs were attracted. Therefore, the host government policies towards FDI have to be more consistent and stable over time if host countries are interested in a continuous flow of resources from abroad. The same policy would be useful in the home LDCs also if it is adopted towards DC investors. There is no doubt that in selected industries the newly industrialising countries also need sophisticated technologies available with the DC multinationals who would not be prepared to export them before they can count on reasonable investment conditions in these countries. The experience of these countries as investors in other LDCs is likely to help them in drawing the right conclusions for their own policies in this field.

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