ON THE ASCENT OF MULTINATIONALS FROM EMERGING ECONOMIES: INELUCTABLE CLASHES

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Abstract

The ongoing tendencies suggest the global marketplace is poised to become a level playing field: companies from all over the world will be able to sell their products and services on any national market, no matter how different or demanding. World production and trade will no longer be polarized and the large gaps existing today between DCMNEs and EEMNEs in terms of size, market power and efficiency will diminish. But although tendencies toward equalization are evident enough, how soon this will happen and how fierce the clash between the two groups of enterprises is going to be is still unclear.

Keywords*: emerging economies, cross-border differences, technological prowess, established multinationals*

JEL Classification: *F-2*

1. Introduction

Authors e.g. Hoskisson *at al.* (2000) defined emerging economies as countries that score a rapid pace of economic development, and whose governments pursue policies favoring economic liberalization and the adoption of a free-market system. Globalization has laid the foundation for firms in emerging economies to expand beyond their national boundaries. The development of multinationals from developed countries (hereinafter DCMs) has been propped up by sound driving forces (foreign markets penetration, economies of scale, acquisition of technologies, governmental policies etc.)

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Multinational companies from emerging economies (hereinafter EEMs) are likewise enjoying financial and institutional buttress domestically.

The contemporary development of multinational enterprises from emerging economies can be considered, from many points of view, a sui-generis phenomenon; its novelty notwithstanding, it does not deviate sensibly from mainstream theory predictions. On the other hand, the process has its idiosyncrasies; there are certain differences from the traditional pattern in respect of objectives, driving forces and means of fulfillment. The international expansion of firms from the developing world is going on unevenly. Firstly, empirically, one can easily notice that the global picture is polarized and contrasting: most of the new multinationals are concentrated in only a small number of home-countries. Secondly, the process is firm-, industry- and country-specific: often, firms originating in certain home-countries perform differently as compared to firms originating in other home-countries; in certain industries, the expansion process is going on faster than in others.

Here are some naturally-arising questions regarding the nature of EEMs' ascent: has their growth been a success story so far? Is their global expansion, for all its conspicuousness, also rewarding? Are they in a position to control industries that are really valuable in terms of market growth, value added, high returns etc. or, all they have accomplished was filling the vacuums left by western companies that are retreating from poorly lucrative domains? Statistics so far point to the second variant. Why are companies headquartered in Eastern Europe lagging behind? Companies in ex-communist countries seem to be lacking both robustness and determination that should enable them to accumulate market power on a global scale. Hypothetically, there are certain handicaps, including weak governmental support, that are keeping East-European players from increasing their participation overseas. This paper is intended to discuss the above issues and maybe shed some light on some of them.

2. The global marketplace, poised to become a level playing field

Two paramount trends are manifest in the contemporary global economy: on the one hand, many EEMs are striving to become truly global players despite their prevalent regional orientation; this implies equally succeeding on emerging and developed countries' markets. As shown above, when tackling western markets, EEMNEs are laying greater stress on nonprice competitiveness factors thus trying to overcome the traditional outlook, still prevailing among western consumers, about firms in developing countries offering cheap, low-grade goods. Performing on sophisticated western markets therefore requires building valuable, widely recognized brands and this is perhaps, one of the most difficult things for EEMs to achieve. Instead, said shortcomings are compensated by two important advantages the latter enjoy on emerging markets: a better knowledge of local conditions and more experience in low-cost manufacturing. "That allows them to develop products such as the Nano car made by Tata of India and the range of Haier domestic appliances sold to peasant families."[1]

On the other side, DCMs are also permanently adjusting their strategies in order to enhance their performances on emerging economies (especially the BRICs)' markets and, at the same time, preserve positions they are holding on their own. In the former case, they are facing a serious hindrance: to produce cheaper products without jeopardizing their brands. Should they offer on emerging markets the same types of products they sell at home, they'll be likely to lose the contest; products must be adjusted in order to meet the demand of legions of low-income customers. It is not only producers of consumer goods that are forced to adjust their production in order to meet the demand prevailing on low-income markets; suppliers of heavy equipment are facing the same problem. Siemens for instance, is considering redesigning its iron and steel making equipment, electricity generators and rail carriages, following the lead of Tata Motor that had created the first $2,000 car.[2]

3. Diverging trends are here to stay

How soon will happen and how fierce the clash between the two groups of enterprises is going to be depends on two questions: how far apart the two groups are at present, with respect to technological and managerial potential and how difficult overcoming cross-border differences really is for either group. At the first point, differences in potential are still highly visible: DCMs practically dominate the new, dynamic, knowledge-intensive industries, characterized by fast technological upgrading and innovation, ever shorter product-cycles, frequent changes in consumers' needs and more pronounced sensitivity to brands. Good examples in this respect are many

[1] *Financial Times* – "The flaw of banking on brand recognition", Jan. 21, 2010
[2] *Financial Times* – "The age of 'Innovation' dawns", June 15, 2010

Japanese companies, whose valuable global brands are based not on size or turnover but on technological prowess. Japan Steel Works for example, is the only company in the world that has the technology to forge solid-steel vessels (to contain radioactivity) required by nuclear reactors. In consumer electronics, although big Japanese electronics companies such as Panasonic, Sharp and Sony have been losing market share to rivals from China, South Korea and Taiwan, other smaller, less well known Japanese firms continue to dominate niches upon which the global technology industry depends. As concerns the speed of new product introduction, the best examples are the electronic handsets producers (Apple, Research in Motion, Dell, Samsung, Hewlett-Packard etc.), which are scrambling to grab a slice of the fledgling market for touch-screen tablet computers.[1] By contrast, EEMs are holding stronger positions in older-type labor or capital-intensive industries, requiring less frequent production renewal, lower share of R&D expenses in total costs and slower reactions to market signals. Examples of companies that fall under this category: Haier (China, household appliances), Galanz (China, microwave ovens), BenQ (Taiwan, consumer electronics), Bajaj Auto (India, motorcycles), Aspen Pharmacare (South Africa, generic antiretroviral drugs), Adcock Ingram (South Africa, drugs), Ambev (Brazil, beer and soft drinks), Femsa (Mexico, beer and soft drinks), Grupo Bimbo (Mexico, food), Gruma (Mexico, food), Pearl River Piano (China, pianos), Huawei (China, telecom equipment), Rongsheng Kelon (China, home appliances), Li&Fung (Hong Kong, consumer goods), Konka (China, electronics), TCL (China, tube-type television sets), Mengniu (China, dairy products), Yili (China, dairy products), Hisense Group (China, white goods), Geely Automobile (China, motor vehicles), Sadia (Brasil, frozen food).[2]

In brief, EEMs and DCMs seem to be quite far apart for the time being because they dominate different, all but non-overlapping industrial sectors. Moreover, empirical evidence points to the fact that the former tend to increase their presence in the very domains the latter are abandoning such as computer and related business and chemicals.

In chemicals for example, the number of DCMs ranked in UNCTAD's Top 100 decreased from seven in 1996 (Bayer AG, Hoechst AG, Du Pont, Rhone-Poulenc, BASF, Ferruzzi/Montedison, Dow Chemical's) with total foreign assets worth $136.2 bn. to three in 2006 (BASF, Dow Chemical's, L'air liquide groupe) with total foreign assets worth $78.1 bn. During the same interval, the number of EEMs grew from zero to two

[1] *The Economist* – "Japan's technology champions", Nov.15 2009; "Tablet computers: chasing King Apple", Sep.30th 2010

[2] Source: *Financial Times*

(Formosa Plastic Group of Taiwan and Sasol Limited of South Africa) with total foreign assets worth $22.4 bn. In computers and related business, the number of DCMs included in the same ranking decreased from one in 1996 (IBM) to zero in 2006, while the number of EEMs increased from zero in 1996 to eight in 2006 (Taiwan Semiconductor Manufacturing, Quanta Computer Inc. from Taiwan, Lenovo Group from China, Inventec Company from Taiwan, Qisda Corp. from Taiwan, Mitac International Corp. from Taiwan, Advanced Semiconductor Engineering from Taiwan, Datatec Limited from South Africa) with total foreign assets worth $21.7 bn.[1]

At the second point (surmounting cross-border differences), firms investing overseas, regardless of their home country development level will have to pursue far-reaching strategies that involve, among other things: building valuable global brands, conquering better positions on retail markets and streamlining international marketing channels. This is, probably, the hardest task for EEMs.

4. How close is the clash?

Whether and to what extent should advanced nations be worried about EEMs' steady growth is one of today's topical matters. The media abounds in rhetorical statements expressing worry about the danger that western companies be overthrown by contenders from emerging economies, especially the BRICS. "With such a rapid increase in cross-border activity, are Europe and North America ready for Chinese, Indian or Brazilian companies taking over their national champions?"[2] Even before the financial crunch began, many businessmen were worried that America was losing its lead in innovation to India and China. The Council on Competitiveness, an influential group of American company bosses, university presidents and labour leaders, issued a terse report on the matter on November 11th and demanded that Barack Obama "take bold action to recapture America's competitiveness" in his first 100 days in office. Craig Barrett, the chairman of Intel, the world's biggest chipmaker, has also made similar complaints of late.[3]

Are EEMs crowding out established multinationals from domains the latter had long dominated? In the light of what has been said up to this point,

[1] UNCTAD, *The World's Top 100 TNC and Top 100 TNCs from developing countries*, 1996-2006

[2] *Financial Times* – "Raids on western companies are more than a fad", Aug.10, 2005

[3] *The Economist* – "A gathering storm?", Nov.20th 2008

the answer is: hardly. On the contrary, there are facts that point to the opposite: it is newcomers who "need to be careful in going head-to-head with the old players" or otherwise they might wind up being crowded out themselves. The example of Ranbaxy, formerly India's largest pharmaceutical company, is illustrative. The firm got into trouble partly because its litigiousness cost it valuable collaborative opportunities with foreign pharma companies and, ironically, ultimately forced it into the arms of one of them.[1] Still, if EEMs are not in a position to win this contest at present, it does not mean they won't be able to succeed in the future. Assuming this as a probable fact (based on the current steady growth of EEMs), the question is: how soon will it happen?

Forecasts about emerging economies are trying to project either the future development of these countries as macroeconomic entities or the future of their firms. These two types of forecasts differ in respect of degree of uncertainty: forecasts based on macroeconomic indicators are, in their majority, quite positive about emerging economies (with the BRICS as flagships, of course) becoming dominating powers of the global economy around mid 21st C. Here is one example: "If things go right, in less than 40 years, the BRICs economies together could be larger than the G6 in US dollar terms. By 2025 they could account for over half the size of the G6. Currently they are worth less than 15 percent. Of the current G6, only the US and Japan may be among the six largest economies in US dollar terms in 2050". (Wilson & Purushothaman 2006, p.3) In contrast, viewpoints and forecasts about the future of firms from emerging markets are by far shakier. Ghemawat & Hout (2010) for example, declaim rhetorically: "What will the ranks of the world's leading multinational corporations look like 25-50 years from now? At one extreme, one might imagine companies from these and other emerging markets crowding out ones from advanced economies: what has been dubbed the decline of the west and the rise of the rest. At the other, one could conceive of the companies from emerging markets continuing to be confined to marginal positions, with a few exceptions of the sort that we are already starting to see. Which of these extremes is likely to prove closer to the mark?"

Foreseeing the future (either in the form of predictions such as Wilson & Purushothaman's, or simple rhetorical questions like Ghemawat & Hout's, quoted above) is challenging for researchers. Conceptually, two things are particularly important in forecasting: causality, to begin with, implies

[1] *Financial Times* – "China and India take on the multinationals", Feb. 12, 2009

identifying correlations that might exist between variables. In our particular case, a causal relationship might be easily intuited: between nations' economic development and firms' international expansion. Such a correlation (e.g. between the level of development and the amount of outward investment) has been highlighted by UNCTAD in a study that included 135 countries of the world.[1] This correlation is noticeable: the recent rapid development of the BRICs[2] for example, obviously has caused a rapid development of BRICs' multinationals. The second issue is related to trends; their nature must be accurately assessed because otherwise, the accuracy of forecasts will be affected.

5. Conclusions

How fierce the clash between old multinationals and the new ones emerging from the developing world is going to be is a matter of widespread concern today. Although the ascent of newly emerged multinationals from developing countries will most likely follow the path trodden by the old incumbents, there are visible divergent trends between the two groups: whereas DCMs keep controlling the knowledge and innovation intensive sectors, characterized by fast technological upgrading, ever shorter product-cycles and ever more exacting consumers, EEMs are holding stronger positions in older-type labor or capital-intensive industries, characterized by low R&D expenses in total costs, low innovative strength and poor future growth prospects. There are domains and geographical locations that are most intensely targeted by the EEMs; in these particular domains, the new players seem to be crowding out the old ones. Instead, certain domains and locations are still hardly accessible to the new comers, for various reasons. Still, in the domains where multinationals from emerging economies are advancing most rapidly, they are capable to catch up with or even outperform their western rivals in terms of size, market leverage, internationalization, competitiveness etc. However, since EEMs tend to increase their presence in the areas DCMs are abandoning, the two groups are in fact dominating different industrial sectors. This makes the clash seem rather remote.

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[1] UNCTAD – *World Investment Report*, 2006, p.144

[2] Acronym designating the group of four largest developing countries: Brazil, Russia, India, China.

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