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Multinational Corporations (MNCs) and Enterprises (MNEs)

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Abstract:

This article focuses on key characteristics of multinational companies (MNCs) in a global business environment. After the definition of the multinational company, the authors present an overview of the geographic origin of MNCs and trends concerning foreign direct investments (FDI). They analyze location strategies followed by MNCs and explain the growing importance of MNCs from emerging economies. Several theoretical perspectives contribute to a better understanding of MNCs: industrial organization theory, transaction cost theory, organizational capability theory, contingency theory, business network theory and institutionalization theory. A typology of different conceptualizations (heterarchical, transnational and meta-national companies) emphasizes their heterogeneous and changing character. Recent trends highlight the increasing fragmentation of the value-chain and the development of 'global factories'.

Key words:

Multinational corporations, multinational enterprises, multinational companies, location strategies, emerging multinationals.

DEFINITION

A multinational company (MNC) can be defined as an enterprise that engages in foreign direct investments (FDI) and which owns or, to a certain extent, controls value-added activities in several countries (Dunning and Lundan, 2008, p. 3). These activities generally take place within subsidiaries which can take the form of wholly owned subsidiaries (subsidiaries where the MNC owns the majority or the entire share capital), minority equity investments (companies where the MNC holds a minority equity share) or joint ventures (companies where the MNC shares its capital with another company). Multinational companies exist in a variety of forms, ranging from smaller companies that invest abroad to large groups that manage subsidiaries in an important number of countries. Today, the boundaries between an MNC and its environment have become loose (Mayrhofer, 2012). Foreign subsidiaries frequently cooperate with local companies and interact autonomously with other actors in their local business environment (suppliers, distributors, clients, government, etc.). MNCs are thus embedded in multiple networks which are likely to evolve over time according to the local environments where they operate (Hennart, 2009).

OVERVIEW

According to figures provided by UNCTAD (2011), there exist about 82,000 multinational companies in the world, which own 810,000 subsidiaries located in various countries. The ranking published by Global Fortune 500 (2011) shows that, among the 500 largest MNCs, 133 have their headquarters in the United States, 68 in Japan, 61 in China, 35 in France, 34 in Germany and 30 in the United Kingdom. It seems important to note that the recent period is marked by the growing weight of multinational companies from emerging countries, which have significantly increased their investments abroad (Ghemawat and Hout, 2008). In the past, the Global Fortune 500 ranking was dominated by MNCs from Triad nations (North America, Western Europe, Japan), and it is only in recent years that MNCs from emerging economies have gained strong positions on the global market. Table 1 indicates the 20 largest MNCs in the world. In 2010, the Wal-Mart group appears to be the first multinational company, followed by Royal Dutch Shell and Exxon Mobil.

Table 1: Classification of the world's largest multinational companies (according to their total sales in 2010)

Rank/Company	Country	Industry	Total sales (in billion US dollars)	Net income (in billion US dollars)
1. Wal-Mart	United States	Retail	421.8	16.4
2. Royal Dutch Shell	Netherlands	Petroleum	378.2	20.1
3. Exxon Mobil	United States	Petroleum	354.7	30.5
4. BP (British Petroleum)	United Kingdom	Petroleum	308.9	-3.7
5. Sinopec	China	Petroleum	273.4	7.6
6. China National Petroleum Corporation	China	Petroleum	240.2	14.4
7. State Grid Corporation	China	Power	226.3	4.6
8. Toyota Motor	Japan	Automobile	221.8	4.8
9. Japan Post Holdings	Japan	Services	204	4.9
10. Chevron	United States	Petroleum	196.3	19
11. Total	France	Petroleum	186.1	14
12. Conoco Phillips	United States	Petroleum	185	11.4
13. Volkswagen	Germany	Automobiles	168	9
14. Axa	France	Insurance	162.2	3.6
15. Fannie Mae	United States	Financial services	153.8	-14
16. General Electric	United States	Diversified	151.6	11.6
17. ING (Internationale Nederlanden Groep)	Netherlands	Financial services	147.1	3.7
18. Glencore International	Switzerland	Integrated commodities	145	1.3
19. Berkshire Hathaway	United States	Trader of bulk commodities	136.2	13
20. General Motors	United States	Automobiles	135.6	6.2

Source: Based on data provided by Fortune Global 500 (2011)

Over past few decades, foreign direct investments of MNCs were mainly located in their home region, and eventually in another region of the Triad (North America, Japan, Western Europe) (Rugman, 2005). Considering the increasing globalization of markets, MNCs tend to accelerate the internationalisation of their activities and to diversify the geographic location of subsidiaries. Figures provided by UNCTAD (2011) show that, during the year 2010, MNCs have created 19,547 subsidiaries. 14,142 subsidiaries are greenfield investments of which 47.8% are established in developed countries, and 5,405 subsidiaries result from mergers and acquisitions of which 67.3% have been conducted in developed countries. Available figures highlight the growing interest of MNCs for FDI in developing countries, namely in BRIC (Brazil, Russia, India, China) countries where MNCs establish 21.7% of their greenfield investments and 15.1% of their mergers and acquisitions.

REGIONAL VS. GLOBAL MULTINATIONALS

Location strategies of multinational companies have been widely studied in the international business literature. Rugman (2005) developed a classification of MNCs, which is based on two criteria: the geographic scope of firm-specific advantages and the geographic reach of locational advantages. Firm-specific advantages (for example, technological or marketing competences) are factors that allow building a competitive advantage. They can be exploited at the regional or the global level. For example, the regional scope of a firm-specific advantage can be linked to a European patent. Firm-specific advantages with a global scope need to become global standards or global brands, or they need to generate global integration benefits, thus allowing economies of scale and experience effects. Locational advantages concern exogenous factors that determine the regional or global locus of the company's competitive advantage. They can be based on elements such as natural resources, the legal system, infrastructure, workforce qualification or local demand. For example, at the regional level, locational advantages can be linked to national or regional government regulation; at the global level, they can result from the legal context determined by international organizations such us the World Trade Organization (WTO) or the International Monetary Fund (IMF).

According to their location strategy, multinational companies can be divided into four categories: (1) companies that possess firm-specific advantages with a regional focus and locational advantages with a global scope; (2) regional companies whose firm-specific and locational advantages have a regional reach; (3) global companies who can benefit from the global scope of firm-specific and locational advantages; (4) bi-regional companies whose firm-specific advantages have a global reach, but whose locational advantages are regional; they mainly operate in two geographic regions. The empirical study conducted by Rugman (2005) highlights that the majority of the world's 500 largest MNCs are regional or bi-regional groups, characterized by a strong presence in their home region. The regional focus of MNCs seems to remain important, but recent statistics show that an important number of companies have considerably accelerated the geographic diversification of their activities, namely in emerging countries. The growing internationalization of activities concerns production as well as research and development activities. Specialists forecast a further development of observed trends (UNCTAD, 2011).

EMERGING MULTINATIONALS

During several decades, the world economy has been dominated by multinational companies from Triad nations (Western Europe, North America, Japan) who located most of their activities in their home region and other developed countries. The recent period is marked by the growing importance of new multinational companies from emerging countries (for example, Geely, Lenovo, Tata Group), which also expand in international markets and aim to become global market leaders (Ghemawat and Hout, 2008). These new MNCs have developed different patters of internationalization, which challenge existing models of MNCs (Guillén and García-Canal, 2009). They have expanded rapidly into international markets by using mainly external growth in order to upgrade their capabilities and increase their global market reach. Their strong position on their home-market and their late internationalization allowed them to adapt to the current context of the global business environment. The model they adopt can be assimilated to the born-global firm which has emerged in developed countries. 'Born globals' are companies that attempt, from their creation, to construct competitive advantages by directly using or selling their products in different countries without using an incremental approach (Zucchella and Scabini, 2007). MNCs from Triad nations thus need to renew their strategies and organizational configurations to remain competitive. They increasingly use outsourcing strategies and network structures to meet the new challenges they face in the global business arena.

THEORETICAL PERSPECTIVES

Several theories contribute to a better understanding of the existence of multinational companies, their characteristics and their relationship with the environment. Forsgren (2008) put forward six theoretical perspectives: industrial organization theory, transaction cost theory, organizational capability theory, contingency theory, business network theory and institutionalization theory.

Industrial organization theory views the MNC as a company whose aim is to exploit a monopolistic advantage in foreign markets. The organizational configuration is mainly hierarchical, and the headquarters play a predominant role in the definition of corporate strategies and the management of business activities.

According to transaction cost theory, the MNC is a company that internalizes and coordinates market transactions across country borders, which are difficult to develop between independent firms. The creation of foreign subsidiaries responds to logics of global efficiency. The organizational configuration is hierarchical, and the headquarters seek to apply appropriate behavioural constraints to local subsidiaries.

The organizational capability theory, which is based on the resource based view (RBV), argues that the MNC needs to possess a competitive advantage. It should thus be able to create, transfer, combine and use unique capabilities in foreign markets. Capabilities are specific configurations of resources and competences that can be distributed throughout the group. They allow the MNC to build a competitive advantage. The major role of headquarters is to stimulate the creation of capabilities within the company.

Contingency theory highlights the capacity of the MNC to adapt to the complexity and to changes that take place in the environment. The MNC can exist in a long-term perspective if it develops the ability to adapt the organization and control systems to changes in the environment. The role of the headquarters is to analyze the environment and to shape the organizational structure according to different local contexts. The emphasis is put on values that are shared by the members of the organization.

According to business network theory, which is based on network theory and resource dependence theory, the MNC can be viewed as a network. This perspective highlights the importance of business networks (suppliers, distributors, customers, governments, etc.) developed by local subsidiaries, which can be considered as strategic resources. The power is dispersed throughout the company, and each unit of the group can thus influence strategic decisions through its local business network.

The institutionalization theory views the MNC as a political actor rather than as a business actor. The approach focuses on different institutional environments that the MNC needs to deal with, but also on the influence the company can have on these environments. Headquarters and subsidiaries need to manage political situations and conflicts in various institutional contexts, at both national and international levels.

TYPOLOGY

In the international business literature, different types of multinational companies have been conceptualized, which emphasizes their heterogeneous and changing character.

Hedlund (1986) considers the multinational company as a 'heterarchy', possessing several decision centres that need to be coordinated. The author emphasizes that the organizational configuration of the MNC influences strategic decisions and the interpretation of the environment. The heterarchical structure requires a strong integration of different units to preserve the unity of the organization, but also a certain disintegration of other activities to avoid a high degree of centralization.

Bartlett and Ghoshal (1989) introduce the 'transnational company', which allows going beyond the centralization/decentralization dialectic. The authors describe a system of internal differentiation which assigns different roles and responsibilities to foreign subsidiaries. Based on a strong interdependence between subsidiaries, this management system can increase learning capacities and improve the MNC's competitiveness on international markets.

Doz *et al.* (2001) develop the 'meta-national company', whose competitive advantage is built through the knowledge acquired by foreign subsidiaries. The authors consider that, in a knowledge economy, companies innovate thanks to their learning capacity in different parts of the world. The meta-national company has three key competences: it is the first to identify new knowledge developed in different parts of the world; it is able to innovate by using this knowledge before its competitors; it creates value through innovation by an efficient production and marketing process at the global level.

RECENT TRENDS

A survey of 500 companies in North America, Europe and Asia conducted at MIT (Massachusetts Institute of Technology) highlights the diversity of strategies conducted by multinational companies in a context of growing market globalization. The findings clearly indicate that global competition does not lead to a standardized model of economic organization, both at the level of companies and countries. They show that development pathways are numerous and that performance varies considerably, even within the same industries. The observation of business reality shows the increasing fragmentation of value-chains across the world. Information and communication technologies facilitate this modular organization which allows distributing business functions around the world. For instance, like in a "lego game", the modularization of production allows MNCs to use the same pieces in different ways to produce different forms, according to market trends (Berger, 2005).

Unlike in the past when business functions were predominantly coordinated within companies, today MNCs frequently decide to outsource functions to independent companies which are located in a variety of countries. The model of the "global factory" developed by Buckley and Ghauri (2004) contributes to a better understanding of the fragmentation of the value-chain. The authors observe that an increasing number of MNCs develop flexible production systems to respond to changes in customer expectations in different parts of the world. The global factory is organized around several key functions generally controlled by the headquarters: design, engineering, brand strategy and marketing. Some aspects associated with these central functions (e.g. research and development, design and engineering) may be subcontracted to other companies. The production function is frequently outsourced to external suppliers which produce different components of the products; their assembly may be carried out by the company or subcontracted. This system allows producing closely to final clients, reducing fixed costs and adapting products to expectations of local markets.

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