

Transnational Corporations (TNCs)

1. TNCs & Global Shift
2. Significance of TNCs
3. Key Influences in TNC Location Decision-Making
4. Spatial Organization & Structure
5. The New World Economy
6. Competing for TNCs
7. Socioeconomic Impact of TNCs

Learning Outcomes

1. Characteristics of TNCs
2. Spatial organization & structure of TNCs
3. Command & control relationship between TNCs & host economy
4. Social & economic impact of TNCs in economies (FDI & influence)
5. Role of government in attracting investments

(1) TNCs & GLOBAL SHIFT

- ✓ **Global shift in NIDL in past 30 years: no more traditional division of labour (EMDCs industrial goods, ELDCs primary goods)**
- ✓ Outsourcing part of growing international structure of modern manufacturing & service enterprises
 - Manufacturing first to discern & exploit locational & operational advantages of multinational operation
- ✓ TNCs have become driving force behind economic globalization
- ✓ TNCs: **capitalist enterprises engaging in FDI & organizing production of goods & services in 1 < country**
- ✓ TNCs extending global reach as rules regulating trade & investment relaxed
 - FDI growth expands, source & destination of investments diversifies
- ✓ TNCs also involved in partnerships with other companies globally, increasingly important relations since competition is now global
- ✓ 65000 TNCs control 85000 foreign affiliates employing 54m workers
- ✓ TNC affiliates account for \$19tr in sales, 10% of world GP & 1/3 of world exports

(2) SIGNIFICANCE OF TNCs

- ✓ 3 basic characteristics:
 - Able to coordinate & control processes & transactions within production networks
 - Potential ability to take advantage of geographic differences in distribution of production factors
 - Potential geographical flexibility in switching resources & operations between locations
- ✓ Much of changing geography of global economy shaped by TNC through:
 - Decisions to invest in particular locations
 - Resulting flows (materials, parts, products, technology & expertise) between TNCs' dispersed operations

- ✓ TNCs are highly differentiated in operation, size, geographical extent
- ✓ TNCs reflect characteristics of home country environments
- ✓ Rise of TNCs results from EOS
 - Saturation in home markets reduce opportunities for expansion
 - As firm size increases, cost per unit output decreases
 - Outsourcing facilitated by transport developments

(3) KEY INFLUENCES IN TNC LOCATION DECISION-MAKING

- ✓ **Cost differentials**
 - Production costs VS efficiency & productivity of location
- ✓ **Asset seeking (skills & knowledge)**
 - Using ICT to utilize assets globally
- ✓ **Clustering**
 - Co-location with competitors, knowledge providers & suppliers
 - Access to source of tacit knowledge for competitive advantage
- ✓ **Immaterial EOS: global advertising & marketing of global brand**
- ✓ **Vertical integration** also explains development of large companies
 - Efficiency gains, improved QC & protection of IP
 - Forward (customer) and / or backward (supplier linkages) in production chain
- ✓ 'Follow the leader' effect: competitors follow footsteps of successful TNCs
- ✓ Service enterprises providing TNCs specialist knowledge & advice on overseas expansion have followed clients globally (e.g. accountancy, advertising, financial etc)

(4) SPATIAL ORGANISATION & STRUCTURE

- ✓ Different parts of TNC have different locational needs therefore develop distinctive spatial patterns (spatial hierarchical distribution)
 - Corporate & regional HQ
 - R&D
 - Production units / branch plants
- ✓ **TNCs actively exploit comparative advantage**, thus internationalizing plant-siting decision processes & increasing number of locationally separated operations
- ✓ TNCs produce in regions where costs of material, labour & other inputs are minimized
 - While maintaining operational control & declaring taxes where economic climate is more favorable
 - R&D, accounting & other corporate functions placed where economical and convenient

Corporate & Regional HQs

- ✓ Locus of **overall control**, responsible for all major strategic investment & disinvestment decisions
- ✓ Particular requirements:

- Strategic location on global transportation & communications network (to keep in contact with other parts of network)
- Access to high-quality services & skilled labour
- Global cities like London, NY & Tokyo

R&D Facilities

- ✓ TNCs drive to remain competitive & profitable globally → innovation of new products / processes & R&D spending
- ✓ With intensified pace & changing technology, R&D even more crucial
- ✓ **Home country bias in R&D**
 - Large supply of scientists, engineers & technicians
 - Proximity to universities & research institutions
 - Quality living for research staff (especially higher ranked)
 - E.g. San Francisco & San Diego, Denver-Boulder
 - Concentrate core of technological activities at home with international outposts & small foreign labs for adaptive R&D

Production Units / Branch Plants

- ✓ 90% of TNCs based in EMDCs (especially USA, France, Germany, UK & Japan), with branches in EMDCs & ELDCs
- ✓ Overseas branches in ELDCs
 - Production costs lower (wages, land, transport)
- ✓ Branches in EMDCs
 - Suitable workforce
 - Cheap land (in declining industrial areas)
 - Well-developed transportation
 - High unemployment (good labour supply)
 - Past economic problems (government will offer financial assistance through grants & tax rebates)
- ✓ Pattern varies greatly between industries
- ✓ **Host-market penetration**
 - Close to market to be sensitive to variations in customer demands & preferences & provide rapid after-sales service
 - E.g. Toyota introduced Lexus in 1989 to gain higher share in US domestic luxury car market
- ✓ **To jump over tariffs & import duties**
 - E.g. EU set up quota restrictions on Japanese cars to protect local car industries, Japanese firms build factories in EU (Toyota at Derby, Nissan at Sunderland UK) → cars considered made in Europe thus no quota restrictions
- ✓ **Product specialization** for global / regional market to serve large markets (e.g. EU, NAFTA)
- ✓ Transnational vertical integration: geographical specialization by process / semi-finished product (e.g. offshore assembly operations of US electronics firms in Mexico)
- ✓ **Firms in NICs have become TNCs** (especially in tiger economies of East Asia) and are extending into neighbours with cheaper labour (e.g. South Korea to China)

(5) THE NEW WORLD ECONOMY

- ✓ World economic geography increasingly tied together by large firms
- ✓ TNCs operate worldwide, **accounting for transfer of knowledge & specialized labour**
- ✓ Growth of TNCs beyond mere spatial expansion, but characterized by intensification of corporate control over global operations
- ✓ Between 20 - 25% of world production undertaken by TNCs
- ✓ Mid-1990s: 500 TNCs control 70% of world trade, 80% of world investment & 30% of global GDP
- ✓ Centralization of information & decision-making, decentralization of operations
- ✓ Increased international mobility of capital (more footloose)
- ✓ Centralization + Decentralization + Global structure = Flexible locations + Risk reduction
- ✓ Corporate strategy able to respond quickly to changes in world economy without destabilizing organization
- ✓ Main advantage: large scale of operation
 - Efficiency & reduce operational cost
 - Capital to establish large plants with lower unit costs (EOS) → higher profits → investment in R&D, marketing, advertising etc
- ✓ For host nation, TNCs are significant part of national economy so have little control over them

(6) COMPETING FOR TNCs

- ✓ Attracting TNCs not just through cash & loans
 - Workforce training
 - Property tax reduction
 - Subsidized costs of land & building
- ✓ Objective: **secure new jobs & benefit from general economic stimulus & employment growth that jobs generate** (injection)
- ✓ TNCs' role in promoting manufacturing development in ELDCs catalyst for further industrial development
- ✓ Governments set up special economic zones (SEZs) & free cities offering particular incentives
- ✓ Capital inflow help promote economic development
 - Multiplier effect on local industry & services
 - Employment opportunities & skill development, increasing spending power & aspirations of locals

(7) SOCIOECONOMIC IMPACT OF TNCs**Export-Processing Zones (EPZs)**

- ✓ Named Special Economic Zone (SEZ) in China & India, Free Economic Zone (FEZ) in South Korea
- ✓ Search by MNCs for cost-saving locations
 - Especially wage costs
 - Shift manufacturing, assembly & production from EMDCs

- ✓ EPZs important part of NIDL, by 2000 90+ countries have EPZs
- ✓ Decentralization of production processes
 - Profitable to shift standardized production to lower labour cost areas
 - EPZs also have favorable investment, trade, tax & labour conditions and concessions
- ✓ EPZs established in wide-range of environments, from border areas (e.g. Mexico) to undeveloped areas & next to large cities (e.g. China)
 - 40% of EPZs in 1990s in Asia-Pacific, generating 2/3 of employment
- ✓ EPZs represent easy path to begin industrialization in country
- ✓ (+) Short-term benefits: provide technology, capital & export markets
- ✓ (-) Long-term concerns:
 - Economic sustainability, where reliance on export processing perpetuate reliance on low-skilled, labour intensive economy
 - Labour standards & regulations (e.g. child labour, poor health conditions, that EMDCs & ELDCs do not wish to regulate)
 - Environmental regulation (e.g. industrial pollution by maquiladoras at US-Mexico border)
- ✓ (-) Danger of overdependence on TNCs since TNCs can stimulate & destabilize national economies (through disinvestment)
 - E.g. Wal-mart threatened to pull out of Bangladesh unless taxes are removed
 - E.g. Maxtor pulled out of Singapore, costing 700 jobs in Singapore
 - Absence of effective planning & negotiations between TNCs & government
 - **Short-term benefits of employment creation may not offset negative social effects**, especially when limited local participation, development of industry & improvement of skills

Decision-Making of TNCs

- ✓ Development of **global core** (HQs in EMDCs) & **global periphery** (production locations like Indonesia), where investment flows towards periphery and low-cost products flow towards core
- ✓ Characteristics of global / industrial periphery:
 - Unskilled labour
 - Low labour costs
 - Poorer working conditions
 - Creation of new local markets
- ✓ (+) Exposure to new technology improves skills & labour productivity and facilitates upgrading of industry into value-adding

Technological Impact of TNCs

(-) Extent of technology transfer

- ✓ TNCs possess & exploit technology and guard it jealously
- ✓ Terms of technology transfer by TNCs dictated by own interests
- ✓ Transfer know-how but not know-why (ideology)

- ✓ Most technology-creating activities done at home or other EMDCs
- ✓ Host governments must exert pressure to establish R&D in return for market access

(-) Appropriateness of technology transferred

- ✓ Do processes & products introduced match local conditions & needs?
- ✓ Extent to which TNCs adapt process technology for use in ELDCs
 - New technologies introduced tend to be capital-intensive, but ELDCs have low-skilled labour with limited capital
- ✓ Products within reach of only small elite
- ✓ Are technologies environmentally objectionable or unsafe?
- ✓ Some TNCs known to shift hazardous operations to ELDCs with less stringent standards (e.g. Enron)

(-) Cost of acquiring technology

- ✓ TNC may not want to license technology or may charge high prices
- ✓ Accept entire TNC package or nothing at all
- ✓ Producing the technology locally not feasible for ELDCs

(-) Employment & Labour Issues

- ✓ Does entry of TNCs create new jobs?
- ✓ What kinds of jobs are created?
 - Are they appropriate for skills & needs of labour force?
 - ELDCs: most jobs in TNC plants are production-related
 - EPZs: low-level production by young females
 - E.g. Thailand, skill level of labour force rising with labour training but little increasing involvement of specialist staff
- ✓ Do TNCs pay higher or lower wages than domestic firms?
- ✓ Do TNCs have acceptable labour relations?

(-) Overdependency

- ✓ TNCs' economic domination discourage local investment, damaging indigenous enterprise
- ✓ Host country loses control of own economy
- ✓ TNC operations affect local welfare & environment
 - E.g. Union Carbide in Bhopal, India (1984: poison gas leak killed 2500 & injured 200k, company closed without compensation)
- ✓ Are TNCs really placeless & borderless?
 - No! Still rooted in home countries / EMDCs
- ✓ Excessive foreign penetration should be avoided by host economies
- ✓ (+) Success story: East Asia
 - EPZs in South Korea, Taiwan important in early rapid industrial growth
 - Governments active & successful in promoting EPZs