Rethinking MNE-Emerging Market Relationships: Some Insights from East Asia

Mo Yamin and Pervez N. Ghauri

INTRODUCTION

It is generally agreed that over the past two decades or so, multinational enterprises (MNEs) have had the upper hand in less developed countries (LDCs) (Buckley and Ghauri 1999; Dunning and Narula 1999; Ghauri and Buckley 2002; Jenkins 1999; Narula and Dunning 2000). Over this period, the general trend has been for a steady change in the policy stance of LDCs away from control, structuring, and regulation of MNEs and toward the liberalization and facilitation of MNE operations in their economies. Governments were persuaded that the adoption of liberal and pro-MNE policies was generally beneficial to their economies. In any case, their bargaining power was generally weakening due partly to changes in the international policy environment, such as pressure from the World Trade Organization (WTO) toward increasing liberalization of world trade and investment, and partly to changes in MNE strategies toward greater cross-border integration and increasing emphasis on efficiency seeking investments.

Over the last several years, however, there has been a noticeable shift in the intellectual climate with respect to the appropriate policy stance in regard to LDCs vis-à-vis MNEs. This shift can be characterized as a retreat from at least the extreme forms of liberalization with their advocacy of a minimal state and is linked to a more general disenchantment with globalization and the emergence of a movement for a global civil society (Buckley and Ghauri 1999; Stiglitz 2002). In the specific context of LDCs, many scholars now reject the view that the economically valid or legitimate scope for government inter-
vention is limited to establishing macroeconomic stability. The assumption that market forces, once liberated from government controls, can automatically generate economic development is increasingly questioned. This questioning has gained ground as liberalization failed to deliver the expected economic performance in most emerging economies and, even more dramatically perhaps, in a number of transitional economies (notably the Russian Federation) that implemented liberalization/marketization policies most enthusiastically (Stiglitz 2002).

Narula and Dunning (2000, 115) capture the emerging consensus succinctly when they observe that “On its own, liberalisation—as with excessive protectionism—is insufficient as a driver of growth.” Also needed is a set of measures and policies that creates supporting institutions and stimulates a developmental orientation in market forces (Lall and Teubal 1998; Narula and Dunning 2000; Ocampo 2002; Perez-Aleman 2000; Stiglitz 2002; Yamin 1998).

This paper considers one particular manifestation of this change—the advocacy of a more active industrial policy, particularly in shaping MNE activities in emerging economies, than had hitherto seemed advisable. Our aim is to contribute to the critical perspectives on international business and the MNE (Forsgren 2002; Ghauri and Buckley 2002; Havila, Forsgren, and Hakansson 2002) and more specifically to highlight the changing views relating to the positive role that policy intervention can have in maximizing the developmental impact of the MNE. This paper explains that the change in the intellectual climate hinges specifically on two issues: first on a growing realization and emerging consensus that East Asian industrialization was a governed process (Wade 1990) and was not market led, and second on the stark contrast between rapid industrialization in East Asia and near economic stagnation in the bulk of LDCs where government had followed a liberalization approach.

THE DEBATE ON EAST ASIAN INDUSTRIALIZATION

Although the debate on the appropriate roles of national governments in economic development has a long history (see, e.g., Dunning 1997a), the current debate centers on opposing interpretations of the experience of East Asian tigers. These few countries are unique among LDCs in enjoying sustained and high rates of economic growth in the postwar period. For example, Korea had a lower gross domestic product (GDP) per capita than Ghana in 1960, but by 1990 its per capita GDP was seven times larger than Ghana’s (World Bank 1999, 12). Until the early 1990s the impressive performance of East Asian tigers was trumpeted as being the model of a market-driven economic system based on free trade and an open door policy toward foreign direct investment (FDI) (Lall 1997). This interpretation was strongly promoted by the World Bank in particular and became one of the pillars of the so-called Washington Consensus. So strong was the belief that the superior
performance of East Asia was a victory for the fundamental and universal truth of free market economics that those who challenged the consensus were dismissed as cranks (Gore 2000, 790).

The most detailed case for the Washington Consensus view on East Asian industrialization was elaborated in a study, appropriately titled *The East Asian Miracle*, by the World Bank (1993). This study articulated an accumulation explanation of East Asia’s performance (Lall and Teubal 1998, 1369). Accumulation theories stress the role of physical and human capital investment, while assimilation theories stress the centrality of learning in identifying, adapting, and operating imported technologies. The accumulation view sees a limited role for government. The government’s role is to concentrate on ensuring a stable macroeconomic environment and remove obstacles to the operations of factor and goods markets both domestically and internationally. The World Bank attributed East Asia’s growth performance to the correctness of macroeconomic fundamentals, which permitted sustained high rates of saving and investment, including investment in education and export promotion. Government intervention beyond sound macroeconomics is seen as harmful.

The World Bank study devoted relatively little space to FDI policies—only 2 out of 360 pages (World Bank 1993, 301–3). It stressed East Asia’s openness to foreign technologies but viewed this as just one facet of its openness to trade and investment. It did not comment in detail on specific policies, for example, in Taiwan and Korea, that tended to regulate MNE operations. However it specifically rejected the relevance of industrial policy (including those specifically targeting MNEs) that would promote certain industries or subsidize learning in technologically complex industries. It argued that industrial policies pursued in East Asia had been largely ineffective: industrial policies targeted to promote the development of specific knowledge and capital-intensive industries were not generally successful and imposed significant costs on the economy (World Bank 1993, 308–9). It viewed such policies as unnecessary, arguing that, as long as macroeconomic conditions are right for growth, industrial learning takes place automatically and rapidly with investment, particularly if growth is export oriented:

What then has contributed to [East Asia’s] apparently superior performance in adopting and mastering international best-practice technologies? We argue that the combination of competitive discipline and well functioning factor markets with a pro-export orientation—the export push strategy—employed by these economies was responsible for their superior productivity performance. (World Bank 1993, 261)

However, this interpretation was in fact strongly challenged and there is now general agreement that strong government intervention was a key aspect of the East Asian economic experience. In particular, the World Bank’s dismissal of industrial policy as a key explanation for East Asia’s performance has been severely criticized by a growing number of commentators. Scholars have
argued that the World Bank did not appreciate the degree to which macro-
economic policies in East Asia were deeply anchored in micro-institutions
that exhibit pervasive state intervention (Amsden 1989, 1994, 2001; Hobday
and others focusing more on the Latin American experience (see Perez-
Aleman [2000] for a recent example) are of the view that the World Bank
study ignores a crucial issue in economic development—the link between
technological learning and industrialization. Physical investment alone does
not ensure the development of capabilities needed to put the economy on a
dynamic growth path. In other words, learning by doing, albeit important, is
not on its own sufficient for economic development. Technological develop-
ment plays as vital a role in the industrial success of developing countries as
it does in developed countries. Even if developing countries are not on the
frontier of innovation, they need to develop new skills, knowledge, institu-
tions, and organizational capabilities to master the technologies they import
and to grow efficiently. In fact, even in developed economies a significant
proportion of the innovations involve large elements in imitation of technol-
yogy already developed in other countries. There is often no clear-cut distinc-
tion between innovation and imitation. As Bell and Pavitt (1997) have stressed,
"the argument that importing foreign technology and creating it locally are
alternative means of generating technical change does not reflect the experi-
ence of developed countries" (Bell and Pavitt 1997, 97).

The critics of the World Bank argue that it did not pay sufficient attention
to factors that specifically affect technological development. In particular, the
World Bank study ignored the large number of empirical studies of techno-
logical change both in developed and developing countries showing (for re-
view, see Bell and Pavitt 1997) that technological learning is an evolutionary
and incremental process always beset, to varying degrees, by market failure
in that it is subject to significant risk, uncertainty, and externalities. These
characteristics imply that, especially in the context of developing countries,
technological learning processes cannot be left to market forces alone.

This line of thinking has created coherent and convincing accounts of the
East Asian experience. Thus East Asian governments adopted a whole range
of not only functional policies (i.e., policies that promote all economic activ-
ities, such as investment in education and the infrastructure) but also selective
policies that promoted particular dynamic activities and industries. The basis
of such selectivity has been the degree of difficulty of the learning and knowl-
edge acquisition process and reflects the premise that market forces would
provide insufficient support for such activities. Reliance on market forces
tends to encourage development along the existing structure of comparative
advantage (typically promoting labor intensive activities). In East Asia, par-
ticularly in Korea, government policies used a set measure to encourage firms
to gain skills and knowledge beyond that immediately available within their
own economies and thus helped to create a new, more advanced structure of
competitive advantage. As Wade (1990) has argued, the East Asian experience is one where market forces are not ignored but were extensively governed to generate economic development.

Policies toward multinational companies in East Asia were firmly set within this broader strategic vision of the governed development process. East Asian governments in the original tiger economies—the first-tier Newly Industrialized Countries (NICs) (except Hong Kong)—followed strategies toward MNEs actively geared to stimulate technology and knowledge diffusion to the local economy (see Table 13.1).

The experience of mainland China, which has enjoyed a similar sustained rapid growth, is also worthy of mention in the present context. In mainland China, the government has followed a two-pronged policy with regard to multinational enterprises. According to a recent United Nations Conference on Trade and Development (UNCTAD) study (Gabriele 2001), the vast majority of FDI has been low-tech and carried out by expatriate Chinese and firms from the East Asian region. This was encouraged mainly to generate employment in traditional, labor intensive sectors of light manufacturing rather than for its capacity to generate technological spillover or learning. On the other hand, the government has focused efforts on upgrading China’s science and technology institutions and strongly promoting local research and development.

**Table 13.1**

<table>
<thead>
<tr>
<th></th>
<th>FDI Strategy</th>
<th>Raising Local Content</th>
<th>Raising Technological Effort</th>
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<tbody>
<tr>
<td>Hong Kong</td>
<td>None, leave to market forces</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>Singapore</td>
<td>Aggressive targeting and screening of MNCs</td>
<td>Promoting subcontracting for SMEs</td>
<td>MNCs targeted to increase R&amp;D</td>
</tr>
<tr>
<td>Taiwan</td>
<td>Screening FDI, entry discouraged where local firms strong. Local technological diffusion pushed.</td>
<td>Pressure for raising local content, technology diffusion and local subcontracting</td>
<td>Intense support for local R&amp;D and upgrading of SMEs. Government targeted and orchestrated high-tech development</td>
</tr>
<tr>
<td>Korea</td>
<td>FDI kept out unless necessary for technology access or exports, joint ventures and licensing encouraged</td>
<td>Stringent local content rules, creating support industries, protection of local suppliers and subcontracting promotion</td>
<td>Ambitious plans for R&amp;D in advanced industry, heavy investment in technology infrastructure. Targeting of strategic technologies</td>
</tr>
</tbody>
</table>

*Source: Based on Lall and Teubal (1998): 1377.*
development (R&D) in order to raise local technological capability and enhance its own bargaining power in the case of the (much smaller) FDI flows by firms from more advanced countries.

MNEs, LDCs, AND THE INTERNATIONAL DIVISION OF LABOR

Since the early 1980s most developing countries, with the exception of the Asian tigers, were persuaded to follow liberal trade and foreign investment policies to a significant degree. As Table 13.2 shows, over the last decade, many less developed countries adopted very permissive policies toward MNEs.

At the same time, as Table 13.3 suggests, although there has been a very large influx of MNEs into LDCs, these have typically resulted in extremely shallow levels and types of investment. The sharp disparity between the share of LDCs in inward FDI stocks/flows and their share of the number of foreign affiliates is indeed telling. Some disparity would of course be expected, as investment in less developed countries would tend to be more labor intensive and absorb lower amounts of FDI. However, the magnitude of the disparity is also due to a change in the structure of MNE activity in many LDCs away from a focus on local markets and toward their incorporation in the rationalized internal production networks that they control.

This pattern fits well into Dunning’s analysis of how globalization and greater mobility of firm-specific assets have influenced the pattern of MNE activities in LDCs (Dunning and Narula 1999; Narula and Dunning 2000).

Table 13.2: The Dominance of Pro-FDI Policies in Emerging and Developing Countries, 1991–2000

<table>
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</tr>
</thead>
<tbody>
<tr>
<td>Number of countries that introduced changes in their investment regimes</td>
<td>35</td>
<td>43</td>
<td>57</td>
<td>49</td>
<td>64</td>
<td>65</td>
<td>76</td>
<td>60</td>
<td>63</td>
<td>69</td>
</tr>
<tr>
<td>Number of regulatory changes</td>
<td>82</td>
<td>79</td>
<td>101</td>
<td>110</td>
<td>112</td>
<td>114</td>
<td>151</td>
<td>145</td>
<td>140</td>
<td>150</td>
</tr>
<tr>
<td>Of which: More favorable to FDI</td>
<td>80</td>
<td>79</td>
<td>101</td>
<td>108</td>
<td>106</td>
<td>98</td>
<td>135</td>
<td>136</td>
<td>131</td>
<td>147</td>
</tr>
<tr>
<td>Less favorable to FDI</td>
<td>2</td>
<td>0</td>
<td>1</td>
<td>2</td>
<td>6</td>
<td>16</td>
<td>16</td>
<td>9</td>
<td>9</td>
<td>3</td>
</tr>
</tbody>
</table>

Most underdeveloped countries can at best attract asset-exploiting investment, while the vast majority of asset-augmenting investment will be highly concentrated in the developed triad economies. Asset-exploiting FDI takes place when a company’s primary purpose is to generate economic rents through the use of firm-specific assets. Asset-augmenting FDI is motivated to gain new technological and other strategic assets and is mainly attracted to a relatively small number of regional clusters within the Organisation for Economic Cooperation and Development (OECD) countries, as these locations provide an ample supply of the required complementary resources such as high-level specialized skills, a sophisticated infrastructure, and advanced research centers and universities (Dunning 1997b). In the context of less developed countries, asset-exploiting FDI comprises the transfer of relatively low technology and low value activities to be combined with the main location-bound advantages of these countries—primarily cheap labor. In fact, the production of standardized manufacturing products is now increasingly organized through elaborate international production networks controlled by large multinational companies. This is a main reason for the rapid expansion of trade in manufacturing and it also helps to explain why manufacturing trade expansion has not produced the expected gains for LDCs. Thus, according to a recent *Trade and Development Report*,

International production networks promote a new pattern of trade in that goods travel across several locations before reaching final consumers, and the total value of trade recorded exceeds the value added by a considerable margin. Consequently, trade in such products can grow without a commensurate increase in their final consumption as production networks are extended across space. (UNCTAD 2002, 64)

As we have already noted, this has generated only shallow investments in LDCs, sometimes through the takeover and subsequent hallowing of domes-

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**Table 13.3**

<table>
<thead>
<tr>
<th>Area</th>
<th>Stock of FDI</th>
<th>FDI Flow</th>
<th>Foreign Affiliates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Developed Economies</td>
<td>67.7</td>
<td>73.5</td>
<td>13.7</td>
</tr>
<tr>
<td>Developing Economies</td>
<td>30.1</td>
<td>24.0</td>
<td>51.5</td>
</tr>
<tr>
<td>Central and Eastern Europe</td>
<td>2.2</td>
<td>2.5</td>
<td>34.8</td>
</tr>
</tbody>
</table>

*Source: UNCTAD (2000) and Ietto-Gillies (2001).*
tic enterprises and with relatively little linkages with local suppliers (UNCTAD 2001).

Almost 30 years ago, Hymer (1972) provided an analysis of the impact of MNEs on the structure of the world economy in terms of two basic laws of development, namely the Law of Uneven Economic Development and the Law of Increasing Firm Size. It suggested that while North Atlantic MNEs would dominate, a geographical division of labor and dependence relationship, with one side being superior and the other being subordinate, would emerge. This situation would lead to tensions and conflicts and to further uneven development.

Using the Chandler-Redlich (1961) scheme, Hymer (1972) suggested that MNEs would spread their day-to-day, manufacturing activities all over the globe, thus diffusing industrialization to developing countries and creating new centers of production. The other activities, coordination and communication, would stay closer to the head offices, which would be completely centralized. As a result, the best highly skilled and highly paid manpower would concentrate in the major cities of the U.S. and Europe, while lower-level skills and manpower would remain in other parts and cities of the world. Most new products would be developed in the major cities and, once accepted there, would travel to other countries. MNEs would thus be greatly interested in the markets of these less-developed countries. This system would automatically force developing countries not to develop skilled manpower above a certain level, as there would be no market for their skills. The local governments would not even be able to invest in their own infrastructure, communication, education, and health to achieve growth, as they would not be able to finance these investments. They would not be able to tax MNEs to acquire finance, due to the ability of these corporations to manipulate transfer prices or to move to low-tax countries, whereas the home countries of these MNEs would be able to tax these corporations as a whole, as well as through their highly paid manpower.

It is remarkable that Hymer’s (1972) projections appear to be strongly validated: the uneven development he predicated is indeed upon us and is fully reflected in the broad structure of the world economy and particularly in the global configuration of MNEs. His radical analysis of 30 years ago is now incorporated into the mainstream. We have already seen that mainstream analysis of multinational firms (e.g., Dunning 1997b) sees increasing divergence between a concentration of high value-added activities in advanced regions/clusters within advanced countries, while low value-added, assembly operations are increasingly footloose and dispersed to cheap labor locations. Robert Wade (2001), in trying to explain how globalization may have created greater international inequality, suggests the following as one of the deep causes:
tances. Think of Silicon Valley, a dense concentration of the very companies that are driving the world’s communication revolution. But also think of the clustering of the higher value added activities of the multinational corporations in their home countries within the OECD world, despite high congestion costs, while they may outsource the lower value added activities in less developed countries. (Wade 2001, 17)

With liberalization, multinational companies have increasingly become the arbiter of the evolving pattern of international trade and capital movements. This pattern incorporated many LDCs in the global networks of trade and investment controlled by MNEs, and consequently both trade and foreign investment inflow have increased significantly. However, the promised land of high rates of economic growth is increasingly regarded as a mirage (Amsden and Van der Hoeven 1996; Ocampo 2002; UNCTAD 2002).

THE END OF THE WASHINGTON CONSENSUS?

As already noted, the Washington Consensus was sold to LDCs as a policy approach that had produced impressive performances in East Asia. The contrast between the successes of East Asia (misleadingly portrayed as free market economies) and the failures of import substituting policies of the 1960s and 70s meant that most developing countries were keen to embrace liberal policies, hoping to emulate the growth performance of East Asia. The intellectual environment is becoming less favorable for the Washington Consensus, not only due to the reinterpretation of East Asia’s experience of industrialization, but also due to broader but still related developments. While the mantra of the Washington Consensus has been a dual emphasis on the liberalization of capital flows and macroeconomic stability, the Asian crisis revealed a contradiction between macroeconomic stability on the one hand and cross-border movement of short-term capital (hot money) on the other (see, e.g., Stiglitz 2000, 2002; Wade 1998). In fact, a prominent feature of the globalized world economy is the increase in the frequency and depth of international financial crises (Stiglitz 2000, 1075).

Interestingly, the current pressures for policy change again stem from the stark contrast between the experience of the East Asian tigers and the bulk of developing countries where liberal trade and investment policies have brought little growth or development of technological capabilities. However this is now based on a new realization: East Asian economies were far from being model implementers of the Washington Consensus. As Stiglitz (2002) has recently observed, a major achievement of East Asian tigers was to successfully resist international pressures to abandon industrial policies. In fact, these governments took industrial policy to be one of their central responsibilities and Stiglitz (2002, 26) pointedly observes that “It is crucial that the successful development we have seen in East Asia be achieved elsewhere.”

However, criticism of the World Bank’s analysis should not be taken as a
justification for indiscriminate and wholesale government intervention in the economy. Such indiscriminate intervention, including indiscriminate promotion of all industrial exporting would be counterproductive precisely because it would not discriminate in favor of selected activities promising high rates of technological and industrial learning. Gup and Num (1999) for example, argue that in Thailand the government’s heavy push of export activities helped to create a glut in many markets such as the steel market because other governments were promoting their exports at the same time. Gup and Nam (1999) consider that such policies were at least in part responsible for the financial crisis of 1997. In another study (Nam and Gup 1999), they put similar arguments forward in relation to heavy intervention in financial markets.

The emerging consensus relating to the lessons of the East Asian experience is thus a two-track policy approach and may be more promising. The two-track policy would retain the broadly open economy orientation while employing industrial policy to direct and shape investment activity, including those by the multinational companies in the direction of promoting industrial deepening and technological learning. According to the International Bank for Reconstruction and Development (1997), the role the governments play should be matched with the capabilities that they have, as shown in Table 13.4.

It is important to note that even the World Bank now appears to accept the important and broadly positive role that state intervention played in fostering technological learning in East Asian economies. As noted already, in its 1993 study, it dismissed the relevance of selective intervention and explained the miracle exclusively in terms of the adoption of market-friendly policies. However in the 1999 World Development Report, it had clearly revised its original assessment. Thus with respect to the Korean experience we read:

Some researchers argue that what is behind the emergence of this Asian “tiger” is a strong, interventionist state—a state that deliberately and abundantly granted tariff protection and subsidies, manipulated interest and exchange rates, managed investment, and controlled industry using both carrots and sticks. Relative prices were deliberately set “wrong” to generate and reap the benefits of evolving comparative advantage, instead of letting them adjust to the “right” levels by the free play of market forces. Korea’s leaders judged that getting prices right would lead to short-run efficiency but long-run economic anemia.

Korea’s development strategy has been mainly one of pragmatic trial and error, based on a twofold commitment: to the growth of exports and to the nurturing of selected infant industries through protection . . . these and other technology investments in the 1970s enabled Korea’s firms to move up the technology chain, closing the knowledge gap. (World Bank 1999, 32)

We also observe a similar reassessment of the role of MNEs in economic development by UNCTAD, although this organization was not as firmly attached to the Washington Consensus as the World Bank. A comparison of
Table 13.4
Reinvigorating Functions of State

<table>
<thead>
<tr>
<th>Minimal Functions</th>
<th>Addressing market failure</th>
<th>Improving equity</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Providing pure public goods:</td>
<td>Protecting the poor:</td>
</tr>
<tr>
<td></td>
<td>Defense, Law and order, Property rights, Macroeconomic management, Public health</td>
<td>Antipoverty programs</td>
</tr>
<tr>
<td></td>
<td>Regulating Monopoly</td>
<td>Disaster relief</td>
</tr>
<tr>
<td></td>
<td>Utility regulation</td>
<td>Providing Social insurance</td>
</tr>
<tr>
<td></td>
<td>Antitrust policy</td>
<td>Redistributive pensions</td>
</tr>
<tr>
<td></td>
<td>Overcoming Imperfect Information</td>
<td>Family allowances</td>
</tr>
<tr>
<td></td>
<td>Financial regulation</td>
<td>Unemployment</td>
</tr>
<tr>
<td></td>
<td>Consumer protection</td>
<td>insurance</td>
</tr>
<tr>
<td></td>
<td>Coordinating private activity:</td>
<td>Environmental</td>
</tr>
<tr>
<td></td>
<td>Fostering Markets</td>
<td>protection</td>
</tr>
<tr>
<td></td>
<td>Cluster Initiatives</td>
<td></td>
</tr>
</tbody>
</table>

Source: Based on IBRD (1997): 27.

the analyses in *World Investment Report 1992* was optimistically titled *Transnational Corporations as Engines of Development*. *World Investment Report 1999*, entitled *Foreign Direct Investment and the Challenge of Development*, reveals a significant reduction in optimism in relation to the developmental impact of multinational firms between the two reports. The latter report puts much greater emphasis on needed policies to raise the quality of investments and formulates a strong and detailed infant industry case for the protection of domestic enterprises vis-à-vis multinational enterprises (UNCTAD 1999, 36–44). The following observation is particularly interesting and encapsulates perhaps the central dilemma for policy makers:

There are risks that the presence of TNCs [Transnational Corporations] inhibits technological development in a host economy. TNCs are highly efficient in transferring the results of innovation performed in developed economies, but less so in transferring the innovation process itself. . . . This may be acceptable for a while in the case of countries at low levels of industrial development, but can soon become a constraint on capability building as countries need to develop autonomous innovative capabilities. (UNCTAD 1999, 44, emphasis added)
The most recent publication of UNCTAD (2002) is even more critical of the liberal approach to international economic policy and presents a distinctly gloomy analysis of the consequences for LDCs from the current modality of participation in the global trade and investment system.

Mainstream scholars in international business also reject as simplistic policy prescriptions that limit the role of government to encouraging liberalization and ensuring macroeconomic stability (Dunning 1997b; Dunning and Narula 1999; Ghauri and Buckley 2002; Narula and Dunning 2000). In a number of recent contributions, Dunning has stressed that precisely because globalization has increased the mobility and flexibility of multinational enterprises, it is particularly important for governments to promote the creation and upgrading of created assets that would enhance their location-bound advantages:

> It is the responsibility of national administration to ensure the availability quality and effectiveness of location bound societal assets, which firms need to use jointly with their core advantages to produce goods and services. At one time, these assets mainly consisted of transport facilities and public utilities. Today they embrace all forms of educational and telecommunication infra-structure necessary to foster an efficient and modern innovation-led economy. (Dunning 1997b, 117–8)

In the particular context of LDC policy toward MNEs, Dunning and Narula (1999, 484) note that the role of governments has a broader scope, going beyond created assets of a general type to providing and upgrading created assets at an industry specific level (and also at specific locations within the country) including the creation of institutions to support the acquisition and creation of knowledge and wealth-creating assets. In the absence of these supporting policies and institution, it is unlikely that countries can benefit greatly from FDI inflows.

**CONCLUDING REMARKS**

In this paper we have focused on the change in the intellectual climate. Whether and to what degree it translates to pressure for a policy change is difficult to predict, although it is clear that policy change will not usually come about without strong academic and intellectual advocacy. However, we already observe a certain pressure toward policy notably among the second tier tigers. In a study of technological capabilities in emerging economies in Asia, Lall (1998) found that the second tier tigers, which had mostly relied heavily on FDI, had failed to develop a significant technological base of their own. South East Asian economies in particular have participated in the international economy largely as subcontractors and have experienced little technological spillover from the export sector to the rest of the economy (Wade 1998, 1537). Not surprisingly, as Lall (1998, 317) observes, these economies are now “conscious of the constraint of this strategy” (that is, heavy reliance
on FDI) adding that they are “making efforts to upgrade from essentially low-level assembly to more value added manufacturing with deeper local roots.” Lall utilizes a distinction between know-how and know-why to explain the nature of upgrading faced by these economies. Know-how refers to skills and operational knowledge relating to an existing production system that may be transferred by MNEs to less developed countries. Know-why represents a more advanced level of learning, generated by more risky research and experimentation that can result in core capabilities for the organization. Multinational activities are more likely to promote local know-how rather than know-why. The latter requires a more significant embeddedness of MNEs in the local economies with resources committed to developing local content and technological activities. A recent study by UNCTAD (2001) has shown that existing linkages within LDCs are rather shallow with MNEs using local companies only as second or third tier suppliers.

REFERENCES


