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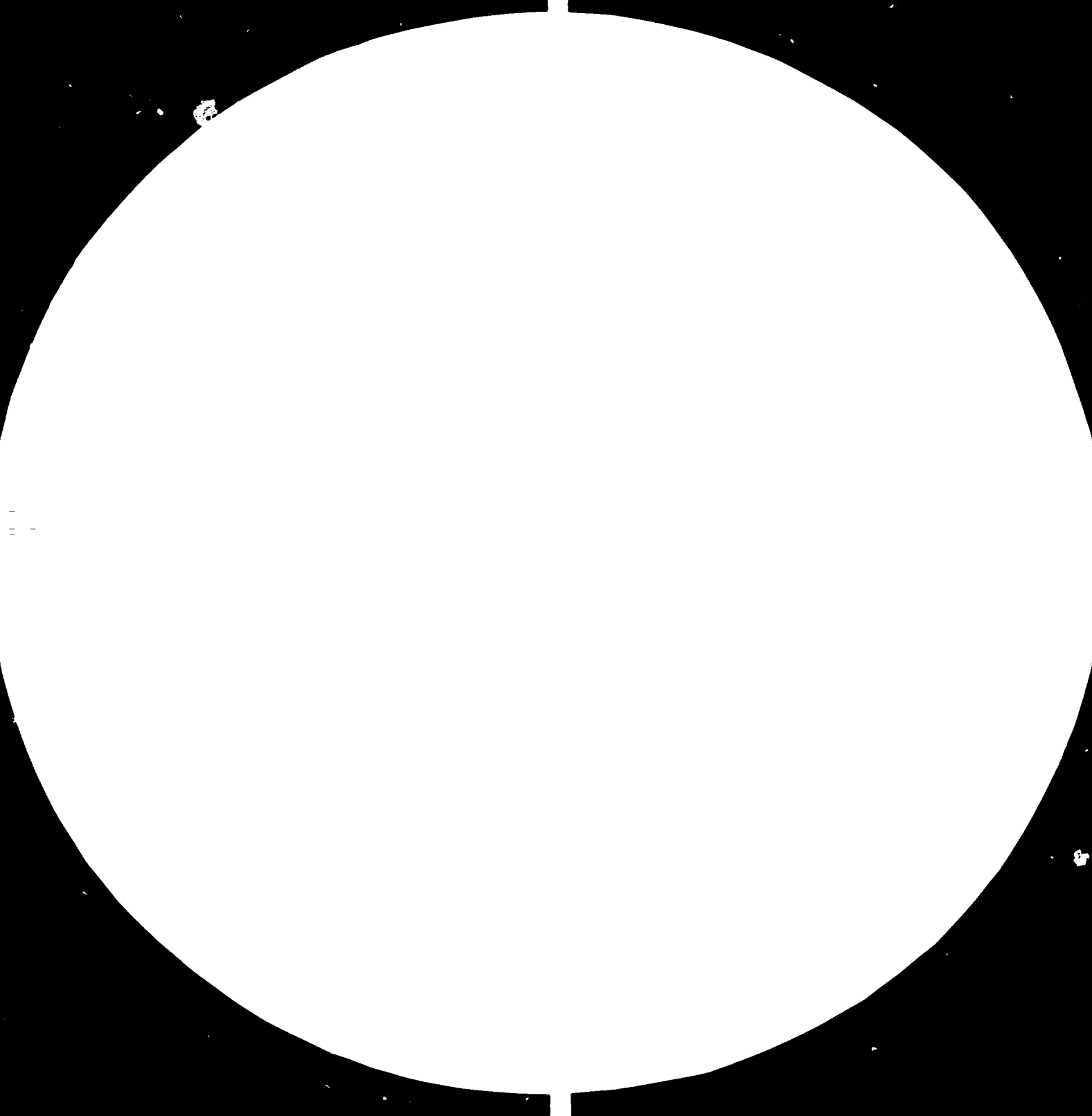
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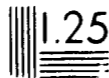


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Resolution Test Chart

Resolution Test Chart

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Final Draft  
October, 1982)

Inter-LDC Direct Investment: Pattern and Prospect\*

by

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\*My thanks are due to Dr. Galen Fox, Senior Visiting Research Fellow, the East-West Center for helpful comments on an early draft and also to Mrs. Helen Palmore for typing the final version.

## INTRODUCTION

This paper reviews the recent trends and the emerging pattern of foreign direct investment and other business collaboration among the less developed countries. In particular, it will examine expanding "inter-LDC" joint business ventures and other collaboration as a new and essentially private approach to South-South economic cooperation.

Some conceptual clarification about several key terms used in this paper is necessary to avoid possible confusion. International investment and other business collaboration beyond the traditional form of commodity trade will include both the equity and the non-equity forms: the former will include wholly-owned subsidiaries and joint ventures (with majority or minority equity participation) and the latter will cover many "new forms" of international investment, including turnkey operations, international subcontracting, licensing and technical assistance agreements, management contracts, and trilateral cooperation (or tripartite industrial cooperation).<sup>1)</sup> Because of the paucity of statistical information on the international investment data in general and on the new forms of investment activities in particular, this paper will confine itself to the equity forms of international investment, namely, foreign direct investment (FDI) covering both wholly-owned subsidiaries and joint ventures.

By the less developed country (the LDC) we mean all non-socialist countries of Africa, Asia and the Pacific, and Latin America that are not the members of the Organization for Economic Cooperation and Development (OECD). We thus use the term as a synonym for the Third-World countries (or nations).

Following the broad definition adopted by the U.N. Commission on Transnational Corporations, we define multinational corporations (the MNC) as "enterprises which own or control production or service facilities outside the

country in which they are based."<sup>2</sup>) Such corporations can be private, cooperative or state-owned entities. Those multinational corporations based on the developed country (the DC) will be abbreviated as the DCMNC, and those from the less developed country as the LDCMNC.

Inter-LDC direct investment implies that both the home (investor) and the host countries of the LDCMNCs are LDCs. Our choice of both the home and host countries is based on (a) the availability of statistical data and (b) the degree of the author's familiarity with specific countries or region. Greater attention will be devoted to Asian and the Pacific LDCs than to their Latin American counterparts.

Broad research questions that this paper raises and attempts to help answer are as follows:

(1) What are the pattern of industrial composition and other characteristics (such as size, ownership pattern, sources of funds, government policies, and so on) of inter-LDC FDI?

(2) What are the LDCMNC motivations for FDI in other LDCs? How are these motivations related to the growth and changing industrial structure of investor (home) countries?

(3) What are the comparative advantages of the LDCMNCs over the DCMNCs and locally-owned firms in the recipient (host) country market? What are potential impact of the LDCMNC investment on the recipient country economy?

(4) What are the prospects for expansion of FDI by the LDCMNCs into the new industrial areas and new regions? What are the prospects for development of trilateral cooperation among the LDC and DC investors in the recipient LDCs?

(5) What are the implications of our findings for policy actions on the parts of the recipient and investor governments and international public agencies including UNIDO?

Once again, it must be pointed out that this study relies on data and information available from the existing literature and publications. This paper attempts to put together these available pieces of evidence to produce a composite picture no clearer than a sketch drawn by several different witnesses.

## I. Overview and Industrial Composition of Inter-LDC Direct Investment

### I.A. An Overview

The internalization of the LDC firms is, by now, a most impressive and familiar phenomenon in the international economic scene. The emergence of the LDCMNCs in the world business arena is reflected in the rapid increase in the number of LDC firms among Fortunes list of the the 500 largest industrial corporations outside the United States. As shown in Table I-1, the number of the LDC firms listed in the magazine increased from 25 in 1975 to 40 in 1980. Totals for South Korea, Mexico, Brazil, Taiwan and Turkey are the most impressive.

The total stock value of FDI stock in the LDCs made by firms from other LDCs is not available from the existing sources of statistical data. One thing is quite clear, however, from the scattered data. The cases of inter-LDC direct investment are not only numerous but also growing rapidly.

Table I-2 which is based on statistical reports prepared by the UN Center on Transnational Corporations (UNCTC) and the Japan External Trade Organization (JETRO), breakdown DFI in selected recipient LDCs in Asia and the Pacific by the nationality of investor countries over selective years. The host LDCs included in the table are Hong Kong, South Korea, Singapore, Indonesia, Thailand and the Philippines. The investor countries are divided into the DC, the LDC and the other groups. (The "other" group includes both DCs and LDCs for which no separate data are available.) The

Table I-1

The LDCs' Firms Listed in the Fortune 500 Largest Industrial Corporations  
Outside the U.S.

| Country     | 1975 | 1981 | Increase |
|-------------|------|------|----------|
| Argentina   | 1    | 1    | 0        |
| Brazil      | 8    | 7    | -1       |
| India       | 2    | 2    | 0        |
| Mexico      | 1    | 6    | +5       |
| S. Korea    | 1    | 10   | +9       |
| Taiwan      | -    | 2    | +2       |
| Indonesia   | 1    | --   | -1       |
| Iran        | 1    | --   | -1       |
| Kuwait      | -    | 1    | +1       |
| Venezuela   | -    | 1    | +1       |
| Chile       | 1    | 2    | +1       |
| Columbia    | -    | 1    | +1       |
| Israel      | 1    | 1    | 0        |
| Peru        | -    | 1    | +1       |
| Philippines | -    | 1    | +1       |
| Portugal    | -    | 1    | +1       |
| Turkey      | 1    | 3    | +2       |
| Zambia      | 1    | 1    | 0        |
| TOTAL       | 25   | 40   | +15      |

Sources: Fortune - World Business Directory, 1976, 1982



DC group is divided into North America, Western Europe, Japan and Australia. The LDC group consists of thirteen home countries (Hong Kong, South Korea, the Philippines, Singapore, Malaysia, India, Thailand, Taiwan, Israel, Panama, Iran, Saudi Arabia and Kuwait). The table illustrates the following :

1) Total stock value of FDI in the selected recipient LDCs has increased rapidly. In Hong Kong, total FDI more than tripled from US\$759 million in 1971 to US\$2,465 million in the mid-1980. In South Korea, the total jumped from US\$582 million in 1973 to US\$1,153 million in the mid-1980. In Singapore, the total jumped by more than 7.6 times from 1971 to 1977. In Indonesia, the total expanded by 4.6 times from 1971 to 1980. In Thailand and the Philippines, the totals more than doubled from 1971 to the mid-1980 and from 1972 to 1975, respectively.

2) The stock value of FDI by the LDCMNCs increased much more rapidly than DCMNC investment over the 1970s. For example, the total value of LDC FDI stock increased more than tenfold from 1971 to the mid-1980. In South Korea and Singapore, the totals increased more than sixfold from 1973 to the mid-1980, and from 1971 to 1977, respectively. In the Philippines, the total increased more than ninefold from 1972 to 1975. In Thailand, the total increased by 2.3 times from 1971 to the mid-1980.

3) As a result, the relative share of the LDC group in the total stock of FDI in the selected LDCs has continued to increase and the relative share of the DC group has accordingly decreased. By mid-1980, the LDC group share in the total stock of FDI was 28.4 percent in Thailand, 17.2 percent in Indonesia, 10 percent in Hong Kong, and 5.4 percent in South Korea, respectively. The corresponding share in the Philippines was 3.5 in 1975. No figures were available for Singapore.

Table I-2

Stock of Direct Investment in Selected Developing Countries in Asia and the Pacific by Country of Origin, Selected Years

| Investing Country                         | Host Country  | Hong Kong      |                 |                 |                 |                 | South Korea     |                |                |                |                |                |
|---|---------------|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|----------------|----------------|----------------|----------------|----------------|
|   |               | 1971           | 1975            | 1977            | 1978            | 1979            | 1980            | 1973           | 1975           | 1976           | 1977           | 1978           |
| (million HK \$)                           |               |                |                 |                 |                 |                 |                 |                |                |                |                |                |
| Total Value of Stock<br>(Million U.S. \$) |               | 759            | 749             | 1973.5          | 2106.1          | 2301.1          | 2445            | 582            | 927            | 953            | 1015           | 1004           |
| Distribution of Stock                     |               |                |                 |                 |                 |                 |                 |                |                |                |                |                |
| (DC)                                      | N. America    | 406<br>(53.5%) | 321<br>(52.6%)  | 920<br>(46.5%)  | 949<br>(45.1%)  | 1046<br>(45.5%) | 1043<br>(42.8%) | 125<br>(21.5%) | 151<br>(17.4%) | 159<br>(16.6%) | 171<br>(16.8%) | 193<br>(19.2%) |
|   | W. Europe     | 122<br>(16.2%) | 269<br>(38.4%)  | 387<br>(19.7%)  | 436<br>(20.3%)  | 444<br>(19.4%)  | 450<br>(18.7%)  | 15<br>(2.6%)   | 52<br>(6.4%)   | 65<br>(6.8%)   | 73<br>(7.2%)   | 125<br>(12.4%) |
|   | Japan         | 170<br>(22.4%) | 300<br>(42.7%)  | 333<br>(16.9%)  | 400<br>(19.0%)  | 474<br>(20.6%)  | 556<br>(22.8%)  | 417<br>(71.7%) | 616<br>(70.5%) | 533<br>(56.4%) | 663<br>(65.3%) | 583<br>(58.0%) |
|   | Australia     | 34<br>(4.5%)   | 101<br>(14.8%)  | 90<br>(4.6%)    | 90<br>(4.3%)    | 90<br>(3.9%)    | 30<br>(1.2%)    |                |                |                |                |                |
| (DC)                                      | <u>Total</u>  | 732<br>(96.6%) | 1591<br>(90.6%) | 1700<br>(86.1%) | 1875<br>(89.2%) | 2054<br>(89.4%) | 2148<br>(87.9%) | 551<br>(94.8%) | 845<br>(93.3%) | 857<br>(89.9%) | 923<br>(90.9%) | 908<br>(90.4%) |
| (LDC)                                     | Hong Kong     |                |                 |                 |                 |                 |                 |                |                | 5<br>(0.5%)    | 3<br>(0.3%)    | 3<br>(0.3%)    |
|   | S. Korea      |                |                 |                 |                 |                 |                 | 4<br>(0.8%)    | 5<br>(0.6%)    |                |                |                |
|   | Philippines   | 2<br>(0.3%)    | 15<br>(2.1%)    | 11<br>(0.6%)    | 11<br>(0.6%)    | 12<br>(0.6%)    | 25<br>(1.0%)    |                |                |                |                |                |
|   | Singapore     | 3<br>(0.4%)    | 60<br>(8.1%)    | 53<br>(2.7%)    | 53<br>(2.5%)    | 54<br>(2.3%)    | 54<br>(2.2%)    |                |                |                |                |                |
|   | Malaysia      |                |                 |                 |                 |                 |                 |                |                |                |                |                |
|   | India         |                |                 |                 |                 |                 |                 |                |                |                |                |                |
|   | Thailand      | 2<br>(0.3%)    | 13<br>(1.7%)    | 52<br>(2.6%)    | 58<br>(2.8%)    | 53<br>(2.3%)    | 53<br>(2.1%)    |                |                |                |                |                |
|   | Taiwan        |                |                 | 13<br>(0.7%)    | 21<br>(1.0%)    | 25<br>(1.1%)    | 25<br>(1.0%)    |                |                |                |                | 15<br>(1.5%)   |
|   | Israel        |                |                 |                 |                 |                 |                 |                |                |                |                |                |
|   | Panama        |                |                 |                 |                 |                 |                 | 5<br>(0.9%)    | 13<br>(1.5%)   | 23<br>(2.4%)   | 15<br>(1.5%)   | 16<br>(1.6%)   |
|   | Iran          |                |                 |                 |                 |                 |                 |                |                |                |                | 17<br>(1.7%)   |
|   | Latin America |                |                 |                 |                 |                 |                 |                |                |                |                | 17<br>(1.7%)   |
|   | Kuwait        |                |                 |                 |                 |                 |                 |                |                |                |                | 17<br>(1.7%)   |
| (DC)                                      | <u>Total</u>  | 732<br>(96.6%) | 1591<br>(90.6%) | 1700<br>(86.1%) | 1875<br>(89.2%) | 2054<br>(89.4%) | 2148<br>(87.9%) | 551<br>(94.8%) | 845<br>(93.3%) | 857<br>(89.9%) | 923<br>(90.9%) | 908<br>(90.4%) |
| All Other                                 |               | 27<br>(3.6%)   | 158<br>(21.4%)  | 273<br>(13.9%)  | 231<br>(10.8%)  | 247<br>(10.7%)  | 297<br>(12.1%)  | 31<br>(5.3%)   | 82<br>(9.4%)   | 66<br>(6.9%)   | 92<br>(9.1%)   | 96<br>(9.6%)   |
| TOTAL                                     |               | 1000           | 1000            | 1000            | 1000            | 1000            | 1000            | 1000           | 1000           | 1000           | 1000           | 1000           |

SECTION 1

Asia, Selected Years

| South Korea            |                |                |                |                |                 | Singapore      |                 |                 | Indonesia       |                 |                 |                 |                 |                 |
|------------------------|----------------|----------------|----------------|----------------|-----------------|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| 1973                   | 1975           | 1976           | 1977           | 1978           | 5/1980          | 1973           | 1975            | 1977            | 1973            | 1975            | 1977            | 1978            | 1979            | 1980            |
| (million Singapore \$) |                |                |                |                |                 |                |                 |                 |                 |                 |                 |                 |                 |                 |
| 582                    | 927            | 953            | 1025           | 1004           | 1153            | 543            | 1523            | 4145            | 1631            | 5362            | 5192            | 5371            | 7389            | 9571            |
| 125<br>(21.5%)         | 161<br>(17.4%) | 159<br>(16.6%) | 171<br>(16.7%) | 193<br>(19.2%) | 241<br>(21.0%)  | 172<br>(31.8%) | 501<br>(32.9%)  | 1366<br>(32.9%) | 461<br>(28.2%)  | 462<br>(8.7%)   | 1000<br>(19.2%) | 1020<br>(18.9%) | 778<br>(10.5%)  | 732<br>(8.5%)   |
| 15<br>(2.6%)           | 58<br>(7.4%)   | 65<br>(6.8%)   | 79<br>(9.0%)   | 126<br>(12.0%) | 177<br>(15.4%)  | 207<br>(37.4%) | 484<br>(31.8%)  | 1309<br>(31.4%) | 57<br>(3.5%)    | 426<br>(8.2%)   | 603<br>(11.6%)  | 652<br>(12.1%)  | 778<br>(10.5%)  | 982<br>(10.2%)  |
| 411<br>(70.7%)         | 616<br>(66.5%) | 633<br>(66.4%) | 663<br>(64.8%) | 683<br>(67.9%) | 610<br>(52.7%)  | 36<br>(6.6%)   | 213<br>(14.0%)  | 533<br>(12.8%)  | 547<br>(33.7%)  | 2347<br>(43.8%) | 2044<br>(39.3%) | 2079<br>(38.7%) | 2519<br>(34.0%) | 1201<br>(12.5%) |
|                        |                |                |                |                |                 |                |                 |                 | 31<br>(1.9%)    | 165<br>(3.1%)   | 185<br>(3.5%)   | 185<br>(3.4%)   | 215<br>(2.9%)   | 225<br>(2.3%)   |
| 551<br>(94.8%)         | 845<br>(91.3%) | 857<br>(89.9%) | 923<br>(90.5%) | 902<br>(90.0%) | 1029<br>(89.5%) | 411<br>(76.0%) | 1190<br>(78.7%) | 3308<br>(79.8%) | 1148<br>(62.8%) | 3354<br>(51.4%) | 3832<br>(73.2%) | 3936<br>(73.2%) | 4290<br>(58.0%) | 5040<br>(58.8%) |
|                        |                | 5<br>(0.5%)    | 9<br>(1.0%)    | 9<br>(0.9%)    | 12<br>(1.1%)    |                |                 |                 | 115<br>(6.3%)   | 655<br>(10.3%)  | 546<br>(10.5%)  | 575<br>(10.7%)  | 722<br>(9.7%)   | 618<br>(6.5%)   |
| 4<br>(0.8%)            | 5<br>(0.6%)    |                |                |                |                 |                |                 |                 | 51<br>(2.3%)    | 57<br>(0.9%)    |                 |                 | 56<br>(0.7%)    | 68<br>(0.7%)    |
|                        |                |                |                |                |                 |                |                 |                 | 251<br>(14.3%)  | 267<br>(4.2%)   |                 |                 | 311<br>(4.2%)   | 311<br>(3.6%)   |
|                        |                |                |                |                |                 |                |                 |                 | 59<br>(2.6%)    | 114<br>(1.8%)   | 152<br>(3.1%)   | 164<br>(3.0%)   | 131<br>(1.7%)   | 150<br>(1.6%)   |
|                        |                |                |                |                |                 |                |                 |                 |                 |                 |                 |                 | 51<br>(0.6%)    | 55<br>(0.6%)    |
|                        |                |                |                |                |                 |                |                 |                 |                 |                 |                 |                 | 76<br>(1.0%)    | 75<br>(0.8%)    |
|                        |                |                |                | 0.5<br>(0.1%)  | 0.5             |                |                 |                 |                 |                 |                 |                 |                 |                 |
| 6<br>(1.0%)            | 23<br>(2.5%)   | 23<br>(2.4%)   | 23<br>(2.2%)   | 19<br>(1.9%)   | 31<br>(2.7%)    |                |                 |                 |                 |                 |                 |                 |                 |                 |
|                        |                |                |                | 17<br>(1.7%)   | 17<br>(1.5%)    |                |                 |                 |                 |                 |                 |                 |                 |                 |
|                        |                |                |                | 3<br>(0.3%)    | 5<br>(0.4%)     |                |                 |                 |                 |                 |                 |                 |                 |                 |
|                        |                |                |                | 4<br>(0.4%)    | 5<br>(0.5%)     |                |                 |                 |                 |                 |                 |                 |                 |                 |
| 3<br>(0.5%)            | 15<br>(1.6%)   | 28<br>(2.9%)   | 28<br>(2.7%)   | 27<br>(2.7%)   | 27<br>(2.4%)    |                |                 |                 | 477<br>(26.2%)  | 1003<br>(17.0%) | 708<br>(13.6%)  | 740<br>(13.7%)  | 1347<br>(18.2%) | 1478<br>(17.0%) |
| 20<br>(3.5%)           | 50<br>(5.4%)   | 65<br>(6.8%)   | 64<br>(6.2%)   | 45<br>(4.5%)   | 10<br>(0.9%)    | 129<br>(23.9%) | 310<br>(20.3%)  | 337<br>(8.1%)   | 101<br>(6.2%)   | 1307<br>(24.4%) | 687<br>(13.2%)  | 615<br>(11.4%)  | 1151<br>(15.7%) | 1052<br>(11.0%) |
| 100%                   | 100%           | 100%           | 100%           | 100%           | 100%            | 100%           | 100%            | 100%            | 100%            | 100%            | 100%            | 100%            | 100%            | 100%            |

SECTION 2



Sources:

UN = United Nations Economic and social Council, Commission on Transnational corporation, Transnational Corporations in World Development: A Re-examination, 1978, Table III - 49. Stock of direct investment in selected developing countries and territories, by country of origin, selected years, pages 256-258.

JETRO = Japan External Trade Organization, KAIGAI SHIJO HAKUSHO (white paper on overseas market), several years.

| Country        | Year of Data | Sources of Data  |
|----------------|--------------|--|
| 1. Hong Kong   | 1971         | UN, page 257   |
|                | 1976         | UN, page 257   |
|                | 1977         | JETRO, 78/79, pp. 280-281 (unit: 1 million Hong Kong dollar) |
|                | 1978         | JETRO, 1980, page 281  |
|                | 1979         | JETRO, 1981, page 294  |
|                | 6/1980       |  |
| 2. South Korea | 1973         | UN, page 257   |
|                | 1975         |  |
|                | 1976         | JETRO, 1977, page 308  |
|                | 1977         | JETRO, 78/79, page 279                                       |
|                | 1978         | JETRO, 1980, pages 279-280                                   |
|                | 1980         | JETRO, 1981, page 292  |
| 3. Singapore   | 1971         | UN, page 257   |
|                | 1976         |  |
|                | 1977         | JETRO, 78/79, page 283 (unit: 1 million Singapore dollar)    |
| 4. Indonesia   | 1971         | UN, page 257   |
|                | 1976         |  |
|                | 1977         | JETRO, 1977, page 313  |
|                | 1978         | JETRO, 78/79, page 284                                       |
|                | 1979         | JETRO, 1980, page 286  |
|                | 1980         | JETRO, 1981, page 296  |
| 5. Thailand    | 1971         | JETRO, 1972, page 74 (unit: 1 million Bhats)                 |
|                | 1976         | JETRO, 1977, pp. 310-311                                     |
|                | 1977-1980    | JETRO, 1981, page 295  |
| 6. Philippines | 1/1972       | JETRO, 1972, page 67 (unit: 1 million U.S. dollar)           |
|                | 1975         | JETRO, 1980, page 283  |

4) Hong Kong is the largest investor with nearly US\$1 billion in combined stock value invested in our five host LDCs. Other major LDC investors are the Philippines (nearly US\$400 million mostly concentrated in Indonesia), Singapore (US\$214 million), South Korea (US\$73 million), and Taiwan (US\$63 million) in that order.

Table I-3 shows a matrix of intra-regional FDI in Latin America over the 1976-1978 period. Argentina, Brazil, Venezuela and Mexico are the region's major investors. According to one account, the annual average of actual outflows of FDI by the Argentine firms was around US\$4 million during the period between 1973 and 1978, and more than ninety percent of Argentine firms overseas investment were located in other Latin American countries.<sup>3)</sup> The presence of Argentine MNCs is particularly notable in Brazil and Ecuador, and also in neighboring Uruguay and Paraguay. Brazil's FDI amounted to US\$60 million in 1978, more than US\$41 million of which was in Latin America. Argentina and Chile are the major recipient countries for Brazilian FDI in Latin America. The impressive internationalization of Brazilian firms is also reflected in their entrance into the DC markets such as the U.S. and Western Europe, as well as into Nigeria and other African markets. FDI by Mexican firms is not adequately covered in official statistics. According to Table I-3, the registered amount of accumulated flows of Mexican FDI in nine Latin American countries amounted to only US\$22.8 million as of the 1976-78 period, which seems only a fraction of the FDI actually undertaken by Mexican firms. Mexico's intra-regional FDI is concentrated in Brazil, Ecuador and Columbia. Venezuela's FDI in intra-regional investment amounted to US\$64 million, thus making her the largest intra-regional investor whose investment activities spread throughout Columbia, Argentina, Chile, and Ecuador.

Table I-3

## Intra-Latin American Direct Investment Stock

(Thousands of U.S. Dollars)

| Countries of Origin    | Host Countries                   |                              |                               |                                  |                              |                                 |                                |                              |                                   | Total   |
|------------------------|----------------------------------|------------------------------|-------------------------------|----------------------------------|------------------------------|---------------------------------|--------------------------------|------------------------------|-----------------------------------|---------|
|                        | Argentina <sup>a</sup><br>8/1976 | Bolivia <sup>b</sup><br>1976 | Brazil <sup>c</sup><br>6/1978 | Colombia <sup>d</sup><br>12/1978 | Chile <sup>e</sup><br>8/1978 | Ecuador <sup>f</sup><br>12/1977 | Mexico <sup>g</sup><br>12/1978 | Peru <sup>h</sup><br>12/1977 | Venezuela <sup>i</sup><br>12/1978 |         |
| Argentina              | ---                              | 441                          | 20,031                        | 1,062                            | 662                          | 10,846                          | 986                            | 1,771                        | 2,058                             | 37,857  |
| Bolivia                | 2,605                            | ---                          | 17                            | 5                                | 133                          | ---                             | ---                            | 431                          | 49                                | 3,240   |
| Brazil                 | 16,889                           | 1,301                        | ---                           | 2,404                            | 13,969                       | 4,752                           | 734                            | 949                          | 338                               | 41,336  |
| Colombia               | 22,043                           | ---                          | 244                           | ---                              | 50                           | 10,347                          | ---                            | 695                          | 1,499                             | 34,878  |
| Chile                  | 355                              | 271                          | 273                           | 195                              | ---                          | 11,097                          | 218                            | 1,240                        | 82                                | 13,731  |
| Ecuador                | ---                              | ---                          | 148                           | 17,620                           | 100                          | ---                             | ---                            | 825                          | 21                                | 18,714  |
| Mexico                 | 762                              | ---                          | 7,650                         | 4,142                            | 2,552                        | 4,771                           | ---                            | 1,156                        | 1,846                             | 22,879  |
| Paraguay               | ---                              | ---                          | 1                             | ---                              | ---                          | ---                             | ---                            | ---                          | 77                                | 78      |
| Peru                   | 8                                | 594                          | 14                            | 1,719                            | 47                           | 1,186                           | 133                            | ---                          | 193                               | 3,894   |
| Uruguay                | 7,930                            | ---                          | 16,475                        | 1,110                            | 300                          | ---                             | ---                            | 2,256                        | 3,812                             | 31,884  |
| Venezuela              | 10,090                           | ---                          | 13,333                        | 26,123                           | 5,697                        | 5,525                           | 1,205                          | 2,011                        | ---                               | 63,984  |
| Others Central America | ---                              | ---                          | 194                           | 278                              | 82                           | ---                             | ---                            | 38                           | 731                               | 1,323   |
| Total                  | 60,682                           | 2,607                        | 58,380                        | 54,659                           | 23,592                       | 48,524                          | 3,276                          | 11,372                       | 10,706                            | 273,798 |

Source: Adopted from Eduardo White, "The International Projection of Firms from Latin American Countries," K. Kumar and M.G. McLeod (eds.), *op. cit.*, page 160.

One characteristic of intra-Latin American FDI is the relative balance between outflow and inflow of intra-regional FDI seen in Table I-3. More advanced countries like Argentina, Brazil, and Mexico, and intermediate countries such as Chile and Columbia have all played a somewhat balanced role as both the investor and the recipient countries of intra-regional FDI. Only small, less developed economies in Latin America have remained mainly recipient countries for FDI.

In sum, we may note the following:

First, proportional inter-LDC FDI has grown more rapidly than FDI by DCMNCs in recipient LDCs, with the percentage share of inter-LDC FDI increasing in each host LDC.

Second, inter-LDC direct investment has been almost exclusively within the region. In other words, Asian LDCs, invest in Asia region, and Latin American LDCs invest in Latin America.

Third, LDCs tend to become both the recipient and investor countries of intra-regional FDI, thus increasing regional economic interdependence among LDCs beyond the traditional form of international commodity trade.

Fourth, the more advanced LDCs tend to become important home countries for FDI in the region's less advanced LDCs.

#### I.B. Industrial Composition of Inter-LDC Direct Investment

While limited data prevents us from constructing weighted average measures of the industrial composition of inter-LDC direct investment even on a regional basis, we can appreciate the pattern by looking at the industrial and regional distribution of inward direct investment in certain host LDCs and of outward direct investment from some sample home countries.



Hong Kong

Table I-4 shows the industrial composition of Hong Kong manufacturing investment in several Asian LDCs. Since the Government of Hong Kong does not keep any record of FDI outflow, our analysis relies on statistical data provided by the LDCs where MNCs from Hong Kong have made significant FDI. Although Hong Kong FDI includes non-manufacturing activities, such as construction, hotels, financial services, entertainment, and primary production, overseas Hong Kong firms in most cases either do not have headquarters in Hong Kong or their Hong Kong headquarters are in different lines of business.<sup>4)</sup>

Let us begin with the case of Indonesia. Hong Kong FDI in Indonesia has been traditionally concentrated in textiles and is mainly export-oriented. Hong Kong investment in Indonesia's textile industry is still dominant, taking up more than a half of Hong-Kong FDI in Indonesia. In recent years, Hong Kong's investment in Indonesia's chemical industry, which is more or less local-market oriented, has increased to nearly 15 percent.

In contrast to Indonesia, Hong Kong FDI in Malaysia is concentrated in such export-oriented industries as textiles, garments, and electronics in which Hong Kong has long experience and expertise in production and export. It is also worth noting that Hong Kong has started making FDI in such industries as foods, chemicals, wood, and wood products in order to take advantage of local markets and locally available raw materials.

Hong Kong ranks third after the U.S. and Japan in the total value of FDI in Taiwan. Hong Kong's earlier manufacturing investment in Taiwan was concentrated in textiles, garments, and plastic and rubber products. A large proportion of its recent FDI in Taiwan is in electronics and

**Table I-4**  
**Hong Kong's Manufacturing Investment in Some Asian Countries**  
 (percentage of Hong Kong's total investment in each country)

| Industry                          | Indonesia<br>(the end of 1977) | Malaysia<br>(the end of 1977) | Taiwan<br>(01/74 - 07/79) | Singapore<br>(the end of 1973) |
|-----------------------------------|--------------------------------|-------------------------------|---------------------------|--------------------------------|
| Food & beverages                  | 7.1%                           | 9.1%                          | 2.6%                      | 9.1%                           |
| Textiles & garments               | 55.3                           | 57.9                          | 4.7                       | 61.0                           |
| Paper                             | 1.3                            |                               |                           |                                |
| Wood and wood products            |                                | 6.3                           |                           |                                |
| Chemicals and chemical products   | 14.6                           | 8.3                           | 52.9                      | 7.2                            |
| Electrical products & electronics |                                | 8.3                           | 28.8                      | 7.5                            |
| Metal and metal products          | 10.9                           |                               | 2.6                       |                                |
| Machinery                         |                                |                               | 2.9                       |                                |
| Others                            | 1.6                            | 10.1                          | 5.5                       | 15.2                           |
|                                   | -----<br>100.0%                | -----<br>100.0%               | -----<br>100.0%           | -----                          |

Sources: Reconstructed from Tables 5-1 - 5-6 in K.Y. Chen, "Hong Kong Multinationals in Asia: Characteristics and Objectives," K. Kumar and M.G. McLeod (eds.), Multinationals from Developing Countries (Heath, 1981).

chemicals. According to Professor Edward K.Y. Chen, the changing pattern of Hong Kong's manufacturing investment in Taiwan follows very closely the shift in industrial structure of the Hong Kong economy.<sup>5)</sup>

There is no official published data on Hong Kong direct investment in Singapore industries. The statistical breakdown of Hong Kong's direct investment in Singapore (Table I-5) is gathered from the second hand sources. Direct investment by Hong Kong firms up to the mid-1960s was concentrated in textiles, food and chemicals. Since then, the shares of food processing and chemicals has declined and those of textiles and electronics have increased rapidly. In recent years, the growth of Hong Kong direct investment in Singapore has declined partly due to the growing attractiveness of other Asian LDCs and partly because of the Government of Singapore's policy favoring more-capital and technology-intensive industries, areas where Hong Kong firms do not yet have a competitive edge.

According to one account, at least 500 Hong Kong-based firms in 1980 were engaged in various non-equity international production arrangements with China, including subcontracting, and joint collaboration. Lower land cost and lower labor cost in China may be the most immediate attraction for Hong Kong investors. Hong Kong subsidiaries in China are usually engaged only in the labor-intensive stage of the total production process, whereas Hong Kong subsidiaries in other Asian LDCs are normally responsible for producing the final products for export and/or local sale.<sup>6)</sup>

Table I-5

Hong Kong Investment in Singapore, by Industry  
1966 and 1973

| Industry                            | As a Percentage of Hong Kong's<br>Total Investment in<br>Singapore Industries |       |
|-------------------------------------|---|-------|
|                                     | 1966  | 1973  |
| Food and beverages                  | 27.8  | 9.1   |
| Textiles and garments               | 38.8  | 61.0  |
| Chemicals                           | 25.6  | 7.2   |
| Electrical products and electronics | 5.5   | 7.5   |
| Others                              | 2.3   | 15.2  |
|                                     | 100.0   | 100.0 |

Source: Edward K.Y. Chen, "Hong Kong Multinationals in Asia: Characteristics and Objectives," K. Kumar and M.G. McLeod (eds.) Multinationals from Developing Countries (Heath, 1981), p. 87.

Taiwan

Table I-6 summarizes the industrial and regional breakdown of Taiwan's outward direct investment for the 1959-1979 period. As the table indicates:

1) Taiwan's direct investment in food and beverages, textiles, plastic and plastic products, and non-metallic minerals accounts for more than 60 percent of its total FDI, which amounted to US\$57.1 million as of the end of 1979. Most of Taiwan's manufacturing investment is concentrated in Indonesia, the Philippines, and Thailand. The major investors within the food and beverage industry are monosodium glutamate (MSG) producers. Most of the non-metallic materials industry firms are cement manufacturers. Taiwan investors in the four above industries all possessed specific technical expertise and long experience in their respective industrial areas before going overseas.

2) Direct investment in the forestry, fishing and lumber product industries constitutes about 8 percent of Taiwan's total FDI. Malaysia, Indonesia, Thailand and Costa Rica are the major recipients of this investment, typically undertaken by plywood producers and fishing and canned pineapple companies.

3) Investment in the electronics and electrical appliances and foreign trade industries makes up nearly 20 percent of Taiwan's total. More than 47 percent of Taiwan's investment in the electronics and electrical appliance industry went to the U.S. as did nearly 80 percent of that involving foreign trade activities.

Table 1-6

Industrial Breakdown of Taiwan's Outward Direct Investment (1959-1979)  
(US \$1,000)

| Industries                          | Total      |               |
|-------------------------------------|------------|---------------|
|                                     | Cases      | Amount        |
| Agriculture & Forestry              | 2          | 425           |
| Fishery & Animal Husbandry Industry | 2          | 1,013         |
| Mining                              |            |               |
| Food & Beverage Processing          | 12         | 7,304         |
| Textile                             | 12         | 3,860         |
| Garment & Footwear                  | 7          | 749           |
| Lumber & Bamboo Products            | 7          | 3,945         |
| Pulp Paper & Products               | 1          | 1,960         |
| Leather & Fur Products              |            |               |
| Plastic & Rubber Products           | 11         | 2,985         |
| Chemicals                           | 7          | 13,633        |
| Non-metallic Minerals               | 9          | 7,879         |
| Basic Metals & Metal Products       | 12         | 2,079         |
| Machinery Equipment & Instrument    | 2          | 322           |
| Electronic & Electric Appliances    | 17         | 5,116         |
| Construction                        | 5          | 1,221         |
| Trade                               | 25         | 6,508         |
| Banking & Insurance                 |            |               |
| Transportation                      |            |               |
| Services                            | 2          | 166           |
| Others                              | 3          | 95            |
| <b>Total</b>                        | <b>136</b> | <b>59,260</b> |

Source: Investment Commission, Ministry of Economic Affairs

### South Korea

Table I-7 breaks down South Korea's outward direct investment and highlights the following points:

1) Investment in natural resource-related projects such as timber, fishing and mining occupies about 26 percent of the US\$28.8 million FDI total. Timber and mining activities are exclusively confined to Southeast Asian countries. Most of fishing ventures are concentrated in Africa or Latin America.

2) Almost all manufacturing investment projects -- which account for about 16 percent of the total -- have taken place in the LDCs in Southeast Asia and Africa. A typical developed-country region manufacturing investment is Gold Star Company's direct investment in color-television assembly plants in the United States.

3) Investment in trading, transportation and warehousing industries accounts for about 20 percent of the total. Trade-related investment is diffused throughout the DC and LDC regions. Transportation and warehousing activities are concentrated in Middle East (81 percent) and North America (19 percent).

### India

As of July 1, 1979, the Government of India approved 359 FDI projects of which 107 were in operation, 95 were under implementation, and 157 had been abandoned. Of all the Indian ventures approved by the Government of India, about 42 percent took place in Southeast and South Asia, about 25 percent in Africa, about 17 percent in West Africa and the remaining 13 percent in the DC group.<sup>7)</sup> Table I-8 gives the industrial breakdown of India's FDI. About one quarter of the total value of India's direct investment is in the engineering-intermediate industrial goods and consumer

Table I-7

Direct-Investment Inflow and Outflow and Technological Licensings : The Case of South Korea  
(Thousand of U.S. Dollars)

| Year             | Foreign Direct Investment (a) | Overseas Direct Investment by Koreans (b) | Ratio (b/a) | Inflow of Technological Licensing |
|------------------|-------------------------------|---|-------------|-----------------------------------|
| 1962-1966        | 16,765<br>(17) <sup>a</sup>   | -----                                     | -----       | 777.3<br>(31)                     |
| 1967-1970        | 59,838<br>(11)                | 7,453<br>(19)                             | -----       | -----                             |
| 1971             | 36,716<br>(80)                | 5,690<br>(9)                              | 15.50       | 26,520.4<br>(326)                 |
| 1972             | 61,232<br>(131)               | 3,183<br>(16)                             | 5.20        | -----                             |
| 1973             | 158,435<br>(239)              | 3,749<br>(18)                             | 2.37        | 11,489.9<br>(67)                  |
| 1974             | 162,629<br>(96)               | 22,950<br>(30)                            | 14.11       | 17,791.0<br>(86)                  |
| 1975             | 69,170<br>(34)                | 5,923<br>(34)                             | 8.56        | 26,540.5<br>(99)                  |
| 1976             | 105,574<br>(43)               | 7,878<br>(35)                             | 7.46        | 30,423.4<br>(131)                 |
| 1977             | 102,286<br>(46)               | 13,939<br>(62)                            | 13.63       | 58,056.0<br>(173)                 |
| 1978             | 100,457<br>(50)               | 40,086<br>(91)                            | 39.90       | 85,065.4<br>(297)                 |
| Cumulative Total | 872,812<br>(846)              | 110,851<br>(314)                          | 12.70       | 256,663.9<br>(1,210)              |

Sources: The Bank of Korea (for overseas direct investment) and the Economic Planning Board (for foreign direct investment and technological licensing):

<sup>a</sup> Figures in parentheses refer to the number of cases.



Table I-8

Indian Joint Ventures Abroad  
Distribution by Industry, Classification as on 1st July 1979

| Sl. No | No   | No. of Joint Ventures Proposals |     |                      |     |           |     |       |     | Illustrative Products   |
|--------|--|---------------------------------|-----|----------------------|-----|-----------|-----|-------|-----|---|
|        |  | In Production                   |     | Under Implementation |     | Abandoned |     | Total |     |   |
|        |  | No                              | %   | No                   | %   | No        | %   | No    | %   |   |
| 1      | Engineering-Intermediates<br>Industrial Goods, etc.                    | 25                              | 23  | 13                   | 14  | 37        | 24  | 75    | 21  | Foundry, Rolling Mills,<br>Cylinders, Pumps, Diesel<br>Engines, Autoparts,<br>Steel Files, Pipes, etc.      |
|        | Consumer Durables  | 4                               | 4   | 1                    | 1   | 8         | 5   | 13    | 4   |   |
|        | Sub-Total  | 29                              | 27  | 14                   | 15  | 45        | 29  | 88    | 25  |   |
| 2      | Service-Consulting,<br>Construction, etc.<br>Hotels, Restaurants, etc. | 16                              | 15  | 25                   | 26  | 8         | 5   | 49    | 14  | Including Trading,<br>Repair Services, etc.   |
|        |  | 12                              | 11  | 10                   | 11  | 6         | 4   | 28    | 8   |   |
|        | Sub-Total  | 28                              | 26  | 35                   | 37  | 14        | 9   | 77    | 22  |   |
| 3      | Textiles   | 18                              | 17  | 5                    | 5   | 13        | 8   | 36    | 10  | Spinning, Weaving,<br>Garments, including<br>Cotton, Jute, &<br>Synthetics                                  |
| 4      | Oils, Chemicals, & Drugs   | 10                              | 9   | 21                   | 22  | 19        | 21  | 50    | 14  | Including Palm Oil,<br>Soaps, Vanaspathi,<br>Hydrogenerated Fats  |
| 5      | Electricals  | 5                               | 5   | 6                    | 6   | 22        | 14  | 33    | 9   | Motors, Fans, Cable,<br>Electrical Accessories,<br>Graphite Products<br>Electrodes                          |
| 6      | Wood, Pulp-Paper Products  | 4                               | 4   | 4                    | 4   | 6         | 4   | 14    | 4   |   |
| 7      | Sugar, Cement, Cement Products   | 2                               | 2   | 3                    | 3   | 9         | 6   | 14    | 4   |   |
| 8      | Shipping   | 1                               | 1   | -                    | -   | 1         | -   | 2     | 0   |   |
| 9      | Miscellaneous  | 10                              | 9   | 7                    | 8   | 28        | 18  | 45    | 12  | Glass, Leather, Flour<br>Mills, Stationery,<br>Canning, Mosaic Tiles,<br>Rubber Products,<br>Plastics, etc. |
|        | Total  | 107                             | 100 | 95                   | 100 | 157       | 100 | 359   | 100 |   |

Source: K. Balakrishnan, MNCs from LDCs: The Case of Indian Joint Ventures Abroad (March 16, 1980).

durables industries, about 22 percent of the total in the service industries, including trade, construction, repairing, hotel and restaurants, 10 percent in textiles, 14 percent in oils, chemicals and drugs, and 9 percent in electronics.

#### Latin America

Intra-Latin American direct investment is diversified to a wide range of activities, including ,manufacturing, mining, construction, trade, banking and agriculture. Table I-9 gives the industrial breakdown of intra-Latin American direct investment in four host countries. As shown in the last column of this table, 44.5 percent of intra-Latin American FDI in these countries is in manufacturing, 15.1 percent in banking, 14.8 percent in trade, 9.7 percent in construction, 9.0 percent in services, and the remaining 6.9 percent in others including agriculture. Table I-3 shows the industrial breakdown of intra-Latin American manufacturing investment measured on the basis of seventy-seven cases of intra-regional projects. A great proportion (about 37 percent) of this investment is in industries linked to agriculture, that is, food products, agricultural machinery, agro-chemicals and cotton textiles. Chemicals and electronics each took up 10.8 percent of the total.

The following emerges from our review of the industrial composition pattern of selected LDC investment in Asia and Latin America.

First, FDI made in low-wage Asian LDCs by more advanced Asian investor LDCs tends to concentrate on labor-intensive export industries (such as textiles, garments and footwears, electronic components) and export-related service industries (such as trading, warehousing and transportation, and banking services). Investment of this type, designed to serve

Table I-9  
Industrial Distribution of Latin America Direct Investment in Some Latin America Countries

| Industry                       | Country | Argentina | Ecuador | Columbia | Venezuela | Total Weighted Average |
|--------------------------------|---------|-----------|---------|----------|-----------|------------------------|
| Manufacturing                  |         | 23.2      | 33.2    | 80.7     | 45.6      | 44.5                   |
| Finance                        |         | 67.2      |         | 8.1      |           | 15.1                   |
| Trade                          |         |           | 9.4     |          | 40.2      | 14.8                   |
| Construction                   |         |           | 16.6    | 6.1      | 9.8       | 9.7                    |
| Services                       |         |           | 22.9    |          |           | 9.0                    |
| Others (including agriculture) |         | 9.6       | 21.7    | 5.1      | 4.4       | 6.9                    |
|                                |         | 100.0%    | 100.0%  | 100.0%   | 100.0%    | 100.0%                 |

Sources: Constructed from Figure 10-1 in Eduardo White, "The International Projection of Firms from Latin American Countries," in K. Kumar and M.G. McLeod (eds.) Multinationals from Developing Countries (Heath, 1981), p. 162.

third-country export markets, is particularly pronounced in the early stage of FDI by export-oriented small LDCs like Hong Kong, Singapore and Taiwan.

Second, an increasing proportion of inter-LDC direct investment goes to natural resource development, particularly mining, oil, timber, and fishing. This type of investment characterizes inter-LDC investment in both Asia and Latin America. LDCs make this type of investment in order to secure sources of industrial raw-material supplies of which they are net importers.

Third, recent manufacturing sector investment by Asia and Latin America LDCs in other LDCs has concentrated on import-substitution industries, and is designed to take advantage of the sheltered and growing local markets these countries are developing in the process of rapid industrial transformation. Examples include investment projects in chemicals (including plastics), pharmaceuticals, tire, metal and steel, food, wood products and other capital-intensive products.

## II. Other Characteristics of Inter-LDC Direct Investment

### II. A. Size

Statistical information about average size distribution by industry of inter-LDC direct investment is available only for the cases of South Korea, Taiwan, India, and Hong Kong.

Table II-1 shows the case of South Korea. The average size of outward direct investment projects by South Koreans firms is US\$372,000 in terms of net equity participation by South Koreans. The average size of timbering project is nearly US\$3 million, that of manufacturing projects, US\$129,000, and that of trading subsidiaries, US\$66,000.

Table II-1

Size Distribution of Korea's Overseas Direct Investment  
(Thousands of U.S. Dollars)

| Industry                          | Less than<br>US\$100,000 |        | US\$100,000-<br>US\$500,000 |        | US\$500,000-<br>US\$1,000,000 |        | More than<br>US\$1,000,000 |        |
|-----------------------------------|--------------------------|--------|-----------------------------|--------|-------------------------------|--------|----------------------------|--------|
|                                   | Cases                    | Amount | Cases                       | Amount | Cases                         | Amount | Cases                      | Amount |
| Mining                            | 1                        | 80     | 1                           | 306    | --                            | --     | --                         | --     |
| Timbering                         | --                       | --     | 1                           | 200    | 1                             | 982    | 5                          | 19,689 |
| Fishing                           | 14                       | 502    | 4                           | 1,197  | 1                             | 895    | 1                          | 5,000  |
| Manufacturing                     | 3                        | 91     | 6                           | 1,302  | --                            | --     | 5                          | 16,803 |
| Construction                      | 4                        | 213    | 6                           | 1,212  | 1                             | 891    | 5                          | 12,103 |
| Transportation<br>and warehousing | 5                        | 184    | --                          | --     | 1                             | 800    | --                         | --     |
| Trading                           | 122                      | 6,032  | 16                          | 4,220  | 1                             | 650    | 2                          | 10,481 |
| Others                            | 5                        | 178    | 2                           | 624    | --                            | --     | 3                          | 15,214 |
| Real estate                       | 1                        | 71     | 4                           | 1,066  | --                            | --     | 2                          | 8,203  |
| Subtotal                          | 155                      | 7,351  | 40                          | 10,127 | 5                             | 4,218  | 23                         | 87,493 |

Source: The Bank of Korea

Table II-2. Taiwan's Outward Direct Investment and Average Size by Industry (1959-1979)

(unit: US \$ 1,000)

| Total                               |       |        |              |
|-------------------------------------|-------|--------|--------------|
| Industries                          | Cases | Amount | Average Size |
| Agriculture & Forestry              | 2     | 425    | 212.5        |
| Fishery & Animal Husbandry Industry | 2     | 1,013  | 506.5        |
| Mining                              |       |        |              |
| Food & Beverage Processing          | 12    | 7,304  | 608.6        |
| Textile                             | 12    | 3,860  | 321.6        |
| Garment & Footwear                  | 7     | 749    | 107.0        |
| Lumber & Bamboo Products            | 7     | 3,945  | 563.6        |
| Pulp Paper & Products               | 1     | 1,960  | 1,960.0      |
| Leather & Fur Products              |       |        |              |
| Plastic & Rubber Products           | 11    | 2,985  | 271.3        |
| Chemicals                           | 7     | 13,633 | 1,947.5      |
| Non-metallic Minerals               | 9     | 7,879  | 875.4        |
| Basic Metals & Metal Products       | 12    | 2,079  | 173.2        |
| Machinery Equipment & Instrument    | 2     | 322    | 161.0        |
| Electronic & Electric Appliances    | 17    | 5,116  | 300.9        |
| Construction                        | 5     | 1,221  | 244.2        |
| Trade                               | 25    | 6,508  | 260.3        |
| Banking & Insurance                 |       |        |              |
| Transportation                      |       |        |              |
| Services                            | 2     | 166    | 133.0        |
| Others                              | 3     | 95     | 31.6         |
| TOTAL                               | 136   | 59,260 | 435.7        |

Source: Statistics on Overseas Chinese and Foreign Investment, Technical Cooperation and Outward Investment, the Republic of China (Investment Commission, December 31, 1979).

Table II-2 shows the average sizes of Taiwan investors equity participation by industry. The overall average size of Taiwan's outward direct investment (in terms of equity participation) is around US\$435,000. The largest average size investment is in the paper mill and chemicals, amounting to nearly US\$2million.

The smallest sized investments are in the garment and footwear, machinery equipment and service industries. Investments in food and beverage, lumber and bamboo products, non-metallic minerals and textiles industries fall into the medium range.

According to a recent case study on Indian joint-ventures, the average size of equity participation by Indian firms has been somewhere between US\$187,000 and US\$312,500.<sup>8)</sup> This figure is comparable with the average figures for the Korean and Taiwan cases. One should remember that the average size of equity participation by partners from investor LDCs does not necessarily reflect the total size of the investment project in question. Let us take the case of India, for example. If a typical equity participation of 30-40 percent for the Indian investor is assumed, the total equity (for both Indian and local partners) of an average project would reach US\$1.04 million for the maximum. (i.e.  $US\$312,500 - (.3) = US\$1.04$  million) If debt-equity ratio of 2:1 is assumed, the total size (in terms of total asset value) of the average joint-venture will be around US\$2.08 million.<sup>9)</sup>

Table II-3 shows the average total size of Indian joint ventures by industry. The paper industry has the highest average size (total assets) amounting to US\$9 million, and the basic steel industry the lowest average size amounting to US\$2 million.

Table II-3 Average Size of Total Assets of Indian Joint Ventures by Industry

| Industry             | Average size of Total Assets (US\$million) |
|----------------------|--|
| 1. Food and Beverage | 3.0  |
| 2. Textiles          | 6.7  |
| 3. Basic Metals      | 2.0  |
| 4. Paper             | 9.0  |

Source: Economic Cooperation Association of Indonesia and India (BKII), quoted from Kian-Wie Thee, "Indonesia as a Host Country for Indian Joint Ventures" in K. Kumar and M.G. McLeod (eds.) Multinationals from Developing Countries (Heath, 1981), p. 142.



Table II-4 shows the average size of Hong Kong's equity investment in Taiwan which has steadily increased over time, particularly from the mid-1970s on. It is generally assumed that within the same industry group in the recipient country, the average size of investment by LDC investors is much smaller than that of investment by the DCMNC and is larger than that of the local firms. However, statistical data on this general proposition are available only in the limited cases. Professor D.J. Lecraw has found that the average size of investment projects from the LDCs is less than one half of that of the DCMNCs in his sample study which compares 25 LDC-invested firms with 130 DCMNCs operating in the same industries within the ASEAN region.<sup>10)</sup>

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Table II-4 Changing Average Size of Hong Kong's Investment Equity

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| Year | Cases | Amount<br>(US\$million) | Average<br>Size |
|------|-------|-------------------------|-----------------|
| 1965 | 19    | 2.7                     | .142            |
| 1970 | 51    | 8.3                     | .162            |
| 1975 | 21    | 29.5                    | 1.40            |
| 1976 | 25    | 17.3                    | .69             |
| 1977 | 26    | 11.3                    | .43             |
| 1978 | 22    | 16.5                    | .75             |

---

Source: Industrial Development and Investment Center, Taiwan.

According to Table II-5, in the case of Nigerian textile industry which is the country's largest manufacturing sector and in which the largest number of the LDC firms operate, the LDC-invested firms tend to fall in intermediate range in terms of the number of employees, with DCMNCs financing the large firms, and the smaller firms locally financed.

Table II-5 Size Distribution of Textile Firms in Nigeria

| Size<br>(Nos. of employees) | DMNCs | LDC<br>Firms | Local<br>Firms |
|-----------------------------|-------|--------------|----------------|
| Over 2000                   | 5     | 2            | 0              |
| 1000-1999                   | 2     | 0            | 4              |
| 500-999                     | 2     | 2            | 6              |
| 200-499                     | 0     | 7            | 22             |
| 100-199                     | 0     | 1            | 10             |
| 50-99                       | 0     | 0            | 0              |
| 25-49                       | 0     | 0            | 18             |
| 10-24                       | 0     | 0            | 32             |
| Total                       | 9     | 12           | 92             |

Source: C.N.S. Nambudiri et al, "Third-World-Country Firms in Nigeria," in K. Kumar and M.g. McLeod (eds), Multinationals from Developing Countries (Heath, 1980), p. 147

In sum, the following points can be made about the size distribution of inter-LDC direct investment.

First, within the same industry in recipient countries, the average size of equity participation for the LDC investor may be smaller than that for the DCMNC investor and larger than that for the local partner.

Second, the over-all average size of the LDC-invested projects tends to increase over time.

Third, the average size tends to vary from one industry to another. The general tendency is that the largest LDC investment projects are for natural resource development, manufacturing investment falls in the intermediate range and trade-related investment gets the smallest average total.

#### II.B Ownership Pattern

The vast majority of LDC investors enter other LDC markets through joint ventures with recipient and country partners. Indian overseas investment offer perhaps an extreme example. The Government of India has not only insisted Indian investors go into joint ventures with local partners, but has also encouraged Indian minority ownership as a "rule" for joint ventures. The rationale for the Indian Government's insistence on joint venture with minority ownership position may have been based on (a) foreign exchange savings and (b) ideological and political commitment.<sup>11)</sup>

Table II-6 shows ownership pattern of overseas direct investment by South Korea. More than one third of South Korea's FDI investment was in the form of joint ventures. Two thirds of joint ventures were with Korean majority ownership and the remainder with Korean minority ownership. Joint ventures are the predominant form of Korean equity participation in fishing, timbering, mining, and construction. Professor L.T. Wells Jr. has pointed out that joint ventures appear to be the typical pattern of ownership of LDC investors in Indonesia and elsewhere.<sup>12)</sup> Professor D.J. Lecraw has presented a clear evidence of such a pattern in his case study of the 153 sample foreign firms operating in ASEAN countries. Average equity participation was 89.5 percent for the U.S.-based MNCs, 88.2 percent

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Table II-6  
 Ownership Pattern of Overseas Korean Firms  
 (Number of Firms)

| Industry                          | 100% | More than<br>50% | Less than<br>50% | Subtotal       |
|-----------------------------------|------|------------------|------------------|----------------|
| Mining                            | 1    | --               | 1                | 2              |
| Timbering                         | 1    | 6                | --               | 7              |
| Fishing                           | 1    | 10               | 12               | 23             |
| Manufacturing                     | 2    | 11               | 6                | 19             |
| Construction                      | 5    | 9                | 2                | 16             |
| Transportation<br>and warehousing | 4    | 2                | 1                | 7              |
| Trading                           | 134  | 12               | 3                | 149            |
| Others                            | 5    | 6                | 1                | 12             |
| Real estate                       | 8    | --               | --               | 8              |
| Subtotal                          | 161  | 56               | 26               | 243<br>(total) |

Source: The Bank of Korea

for Europe-based MNCs, 54.7 percent for Japanese MNCs, and 39.0 percent for the LDC-based firms.<sup>13)</sup> In the Latin American case, horizontal investment in which technical change very slow involves subsidiary to a greater extent than the case of the DCMNCs.

In sum, the LDC investors in general tend to enter joint venture arrangements with the local partners in the host LDC to a much greater extent than do their DC counterparts.

#### II.C. Sources of Funds for Investment

Information available from the scattered statistical sources does not permit us to trace the sources of funds for investment by the LDC firms. Table II-7 identifies the sources of funds for equity investment by South Korean investors as of the end of 1978. About 70 percent of the total equity was paid in cash, 17 percent was locally raised through use of stand-by credit guaranteed by Korean banks, 10 percent came from loans, 2.5 percent was in kind investment (equipment and materials), and only 0.2 percent was financed from profits.

According to an unpublished sample survey study on FDI by Taiwan firms, about 71 percent of the equity Taiwan put into subsidiaries and joint ventures was financed by recipient country banks and credit institutions, mostly through arrangements made by local partners, 22 percent came from parent firms, and only 7 percent from Taiwan banks and credit institutions.<sup>14)</sup>

Professor D.J Lecraw in his study of the 153 sample MNCs operating in the ASEAN region has traced the sources of funds, as shown in Table II-8. The main sources of funds for LDC investors are parent firms (56 percent) and local financial institutions (41 percent), whereas those for the DCMNCs are parent firms (43-71 percent) and overseas financial institutions (13-28

**Table II-7**  
Sources of Funding for Equity Investments by Korean Investors  
 (U.S. Dollars)

| Industry                          | Cash       | In Kind   | Standby<br>Credit | Loans     |
|-----------------------------------|------------|-----------|-------------------|-----------|
| Mining                            | 386,000    | --        | --                | --        |
| Timbering                         | 6,149,851  | --        | 3,099,561         | 4,400,000 |
| Fishing                           | 4,264,651  | 327,000   | 561,985           | --        |
| Manufacturing                     | 12,136,622 | 100,239   | 1,300,000         | --        |
| Construction                      | 4,908,102  | 1,571,871 | 2,588,575         | --        |
| Transportation<br>and warehousing | 184,000    | --        | 800,000           | --        |
| Trading                           | 12,354,091 | 29,410    | --                | --        |
| Others                            | 12,290,481 | --        | --                | 3,696,650 |
| Real Estate                       | 4,104,373  | 40,423    | 5,194,800         | --        |
| Subtotal                          | 56,778,175 | 2,068,951 | 13,550,921        | 8,096,650 |

Source: The Bank of Korea

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| Profits | Total      | Repatriation | Balance    |
|---------|------------|--------------|------------|
| --      | 386,000    | --           | 386,000    |
| --      | 13,649,413 | --           | 13,649,413 |
| --      | 5,159,636  | 65,900       | 5,093,736  |
| --      | 13,536,862 | --           | 13,536,862 |
| 150,000 | 9,218,555  | --           | 9,218,555  |
| --      | 984,000    | --           | 984,000    |
| --      | 12,383,502 | --           | 12,383,502 |
| 29,400  | 16,016,531 | --           | 16,016,531 |
| --      | 9,339,597  | --           | 9,339,597  |
| 179,400 | 80,674,097 | 65,900       | 80,608,197 |

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Table II-8  
Source of Funds to Finance the Original  
Investment in the Subsidiary

| <u>Source of Funds</u>         | <u>HOME COUNTRY</u>  |               |              |                  |
|--------------------------------|----------------------|---------------|--------------|------------------|
|                                | <u>United States</u> | <u>Europe</u> | <u>Japan</u> | <u>LDC Firms</u> |
| Local Financial Institution    | 21                   | 17            | 12           | 41               |
| Overseas Financial Institution | 28                   | 31            | 13           | 3                |
| Parent Firm                    | 47                   | 43            | 71           | 56               |
| Funds (loans & equity)         | 23                   | 22            | 20           | 5                |
| Supplier's Credit              | 11                   | 13            | 30           | 13               |
| Machinery                      | 13                   | 8             | 21           | 38               |
| Local Subsidiary               | 4                    | 9             | 4            | 0                |
|                                | <u>100%</u>          | <u>100%</u>   | <u>100%</u>  | <u>100%</u>      |

Source: D.J. Lecraw, "Structure and Competitive Practices of TNCs in the ASEAN Region," (March 1980), Working Paper Series No. 237, School of Business of Administration, The University of Western Ontario (London, Canada).



percent). It is also interesting to note that the predominant proportion of funds from the parent firms of the LDC investors was contributed in kind (i.e. machinery) rather than in cash funds.

The following points can be noted from our limited information on the sources of funds for LDC investors FDI:

First, the LDC investors tend to rely on recipient country financial institutions, while the DCMNCs use outside financial institutions.

Second, the LDC investors use cash funds less and machinery more than do the DC investors.

#### II.D. Government Policy Toward Inter-LDC Direct Investment

While LDC governments often evaluate the economic and socio-political consequences of inward direct investment from the DCMNCs LDC investors are now learning to assess the consequences of their own investment abroad. Prospective investors may show how their ventures would promote export of machinery and parts and brighten the prospect for increasing foreign exchange earnings from overseas ventures subsidiaries. Listed below are the basic principles and objectives the Government of India employs to encourage Indian joint ventures overseas . It seeks:<sup>15)</sup>

- a) To share the experience and expertise of Indian industrial and technological development with other countries;
- b) To create an industrial image of India in the country concerned, thereby create an environment receptive to Indian export efforts;
- c) To play the role of "partners in development" in the industrial growth of the host country;
- d) To foster a new kind of economic relationship and partnership;
- e) To provide India with a better access to the market of the recipient country for its products; and

- f) To earn foreign exchange through dividends, royalties, and fees derived from managerial and technical know-how.

As pointed out in a recent study on Indian joint ventures by Raju and Praharad, the regulations and guidelines imposed by the Indian Government in the process of implementation have promoted a short-term foreign-exchange earnings at the expense of developing long-run strategic and managerial benefits as well as profitability.<sup>16)</sup> The Government's insistence on joint venture with a minority position is a case in point.

In the case of South Korea, the Government has emphasized the role investment plays in (a) securing access to raw materials, (b) expanding exports, and (c) promoting international cooperation with developing regions. The Korean Government offers a set of incentives for outward direct investment: (a) protection from investment risks, (b) financial assistance, including loans and guarantees, (c) tax incentives, and (d) information services.

The stated objectives and guidelines established by the investor-country governments may be similar (for example, access to raw materials, export promotion, technical cooperation, and encouragement of joint ventures). But governmental approval for specific FDI projects may be largely influenced by short-term factors such as a shortage or surplus in current balance payments, and fluctuations in international prices of raw materials. A number of the LDC investors, however, have found ways to get around short-run restrictions, as long as their ventures appear to be potentially profitable.

No LDC host government has explicitly adopted guidelines that would either discourage or favor FDI from other LDCs. In practice, however, the government actions taken result in discrimination against the LDC investors for one reason or another.

One of the causes is ethnic bias. In some Southeast Asian countries, where resident Chinese minorities alone are allowed to undertake foreign investment projects, direct investment by Chinese from Taiwan and Hong Kong is discouraged by recipient country government agencies.<sup>17)</sup> Indian investors tolerated in neighboring LDCs, are discriminated against in other LDCs where Indian minorities have proven unpopular.

In many LDCs there may be discrimination against the LDC investors because of government regulations on the minimum size of investment projects, or because of pollution control. A number of the LDCs have imposed explicit minimums on the size required for approval of foreign direct investment projects. Even where there is no size requirement, size is an important factor in securing loans and tax incentives. Such policies favoring large-scale and capital-intensive industrial projects, work against the LDC investor's advantage in small-scale labor-intensive modern technologies.<sup>18)</sup>

Another source of discrimination against the LDC investors is the behaviour of bureaucrats in foreign-investment authorities. The civil servant who fears of the consequences of any investment project failure is likely to prefer a well-known DCMNC to an unknown smaller firm from another LDC.<sup>19)</sup>

In some Latin American countries, the government authorities do tend to encourage intra-Latin American joint ventures as a means of combatting DCMNCs.<sup>20)</sup>

In balance, except in the very limited cases where the LDC investors become the preferred choice of the government authorities for political reasons, the policies and practices of LDC governments tend to discriminate against investors from other LDCs.

### III. Motivations for Inter-LDC Direct Investment

#### III.A. Types of Motivations

Specific LDC investors motivations for FDI in other LDCs can be as many as the number of the investors. Motivations at firm level can be, however, grouped into the following categories, each related to the changing phases of the investor LDCs' industrial growth:

- (a) to secure access to supplies of raw materials for home-based industrial production;
- (b) to facilitate the investor country's export activities by investing in on-site export-related services facilities;
- (c) to take advantage of low-cost production for re-export; and
- (d) to diversify the home-based industrial production and export.

The first type, consisting of investments in mining, timbering and fishing, is mainly import-oriented and natural resource-related. The second type, consisting of investments in on-site trading, transportation, warehousing, and distribution channels to facilitate home country's exports to the host country, is export-related. The third type, consisting of horizontal investment in production of labor-intensive export-oriented industrial goods seeks low-labor factor cost of production for re-export to third-country markets. The fourth type is manufacturing investment projects to promote the exports of machinery and components from the home-based industrial complex of parent firms. Large business groups in some advanced LDC in recent years have exploited "internalization

advantages" by strengthening the connections between overseas investment projects and exports of machinery, components and materials from their own heavy engineering and chemical process industries.

### III.B. When Do the LDC Firms Go Overseas?

Let us now try to link the motivations for FDI to the phase of industrial growth of the "typical" LDCs (excluding the city states of Hong Kong and Singapore).

We propose the following scenario to explain both why and when a typical LDC starts FDI in the process of its industrial growth.

(1) In the process of its growth, a typical labor-rich resource-poor developing economy is likely to pass through several distinctive growth phases, starting with consumer-goods import-substitution industrial growth and moving to labor-intensive export-oriented industrial growth and then to diversified export-oriented industrial growth that responds to the changing pattern of domestic and overseas demands.<sup>21)</sup> In the real-world situation in which international movement of commodities and factors is partly free, partly impeded, the LDC in different growth phases combines domestic and foreign factors locally and/or overseas in order to increase growth and generate employment in its own economy. International production is as the totality of different ways of combining domestic and foreign factor inputs locally and overseas along lines dictated by its own comparative advantages and external constraints.

(2) a) In the early consumer-good import-substitution growth phase, LDC critical factor inputs for industrial expansion are foreign capital, industrial entrepreneurship and technical expertise. These inputs are partly supplied direct investment from abroad and by licensing arrangements

with DCMNCs motivated to protect local markets previously served by exports or seeking to take advantage of sheltered and growing local markets.

b) In the subsequent labor-intensive export-oriented phase of industrial growth, critical factor inputs the LDC needs most to expand industrial exports are export market information, marketing techniques and new product and process technology. These inputs are supplied mainly through FDI and licensing arrangements from DCMNCs seeking low-cost labor for export processing and recipient LDC government incentives for export promotion. At this point, the LDC may invest in overseas trade-related services and then in overseas production facilities. The LDC primarily seeks to expand its home-based industrial exports and to secure sources of critical raw materials imports required for continuous domestic industrial growth at a time of growing uncertainty about the overseas markets for both industrial exports and resource imports. In the phase of export diversification and gradual movement out and ending of cheap labor industries, the LDC's industrial exports and domestic production shifts from simple industrial consumer-goods exports through semi-skilled labor-based exports to high value-added industrial goods for export and internal use. The critical factor inputs the LDC now most needs for both industrial export and import-substitution production are export marketing information and technical knowledge about new products and processes. These inputs are supplied mainly through licensings and other contractual arrangements with the DCMNCs. The outward flow of overseas direct investment and contractual arrangements continues to expand in terms of output mix and geographical spread. The LDC seeks to expand outward direct investment not only to overcome imperfections in overseas markets for industrial exports and resource imports, but also to diversify the

industrial structure of export and domestic production. Such diversification strengthens interrelations between the industrial export sector and the import-substitution sector producing intermediate and durable goods.

(3) During the sustained industrial export growth phase the LDC imports of natural resources, marketing know-how and new product and process technology on the one hand and exports of semi-skilled and skilled manpower and labor-intensive modern technology on the other. The specific pattern of local and foreign factor inputs is largely dictated by the combination of its own factor endowment, overseas market imperfections, and other constraints.

The scenario outlined above applies at least to the small group of Newly Industrializing Countries (NICs) that share a relatively large manufacturing sector for both export and import-substitution -- Brazil, South Korea, Taiwan, Argentina, and Mexico.

Though mainly motivated by a desire to better service export markets, the NICs also support FDI because their conglomerates seek to diversify industrial production of not only consumer-goods export goods but also of intermediate and capital goods through network of overseas and local subsidiaries. Overseas manufacturing investment by one subsidiary would lead to exports of different goods for other subsidiaries of the same business group.

From the standpoint of the NIC business groups and/or from that of the national economy as a whole, overseas manufacturing investment and exports tend to complement rather than compete with each other. It is very important to note that both the industrial-export drive and the expansion of import-substitution industries have been simultaneously pursued by the

same business groups under the same protective policy package that provides incentives such as, tariff reductions and/or exemptions for the import of raw materials and plant and equipment, preferential interest rates and direct subsidies. Since the minimum efficient size of import-substitution production far exceeds the size of domestic markets, the NICs business groups' search for export markets for their new products will intensify during the 1980s. The export of the intermediate inputs and capital goods would call for different kind of marketing strategies, including direct participation in overseas construction and engineering-related activities, establishment of overseas and manufacturing subsidiaries, and long-term financial arrangements. In the future, the NICs business groups will probably further strengthen the connection between export and import-substitution activities within their own industrial production complex, thus accelerating the process of their own countries' export-oriented industrialization.

#### IV. Competitive Advantages of LDC Direct Investment in the Host-Country Markets

In the preceding chapter we have asked why and when the LDC firms start to make outward direct investment in other LDCs. Let us now ask how the foreign subsidiaries of the LDC firms compete with their DCMNCs counterparts and with locally-owned firms. As mentioned, the characteristics of LDC firms operating in other LDCs differ from those of the DCMNCs. These differences have been found to be quite pronounced in terms of size, ownership pattern, technology choice, product quality, import and exports, etc.



Table IV-1, prepared by Professor D.J. Lecraw, indicates the characteristic differences between the LDC and the DC firms operating in the ASEAN countries. The LDC firms are smaller in size, use more labor-intensive techniques, import fewer foreign inputs and export less of their products. They tend to have a slightly larger ratio of foreign/local employees, and lower equity participation. They produce low-quality, undifferentiated, low-R&D, and low-advertised products that compete only on the basis of low price-cost margins in the host-country market.

Table IV-1 Characteristic Difference between the LDC and the DC Firms

| Characteristics                    | LDC Firm Compared with Other MNCs |
|------------------------------------|-----------------------------------|
| 1. Size (S)                        | Smaller (-)                       |
| 2. Capital intensity (K/O)         | Lower (-)                         |
| 3. Foreign/local employees (F/L)   | Higher (+)                        |
| 4. Equity participation (EP)       | Lower (-)                         |
| 5. Exports (X)                     | Lower (-)                         |
| 6. Imports (M)                     | Lower (-)                         |
| 7. Product quality (Q)             | Lower (-)                         |
| 8. Price-cost margin (PC)          | Lower (-)                         |
| 9. Profits (P)                     | Uncertain                         |
| 10. Research and development (R&D) | Lower (-)                         |
| 11. Advertising (A)                | Lower (-)                         |

Source: D.J. Lecraw, "Internationalization of Firms from the LDCs: Evidence from the ASEAN Region", in K. Kumar et al (eds.) Op. cit., p. 43

On the one hand, these LDC subsidiaries do not appear to be effectively competitive with their DC counterparts, but on the other hand, these LDC firms have special assets that compare favorably with their DCMNC and local competitors. Where do the special LDC investor assets come from?

The special assets or advantages of the LDC investors, like those of the DCMNCs, appear to derive from the peculiar nature of home markets for both products and factor inputs. LDC markets for a wide variety of products are characterized by the small size and the low-income level of the LDC customers. The LDC markets for factor inputs are characterized by the relative abundant (inexpensive) labor and the relative shortage of capital and imported inputs and components. Capital rationing, high tariffs, foreign-exchange control, and licensing make imported equipment and materials relatively expensive and difficult to get hold of. Such characteristics of the LDC markets for products and factor inputs have led the LDC firms to develop small-scale, labor-intensive and imported-input saving technology for production of relatively undifferentiated mature products of low quality at low cost.

Such innovations were the result of small modifications in technology and product designs emanating from the machine shops and assembly lines of the LDC plants in the labor-intensive home environment, developed over a long process of trial-and-error learning. Evidence from various case studies indicates that most of these modifications consist of (a) labor-using innovations peripheral to the modern machine or modern core processes, including handling, packaging, storing, and so on, (b) greater manual quality control, (c) more intensive machine maintenance, (d) the upgrading of lower-quality raw material inputs via manual sorting (e.g.

wool and cotton yarn), (e) more utilization of locally produced materials, and (f) finding ways of using multi-purpose equipment.

When the LDC firms move toward FDI in order to preserve their traditional export markets in the recipient country, they can use the same appropriate small-scale and labor-intensive "modern" technology to produce low-cost products in the recipient LDC. Both production technology and product specifications that the LDC investors have produced for their own home markets may be best suited for factor markets and demand conditions existing in another LDC.

It may be true that some of the specific technologies adopted by the LDC firms may have been the ones that had been originally used but later abandoned by the DCMNCs. But many of the technologies used by the LDC firms are quite modern offering major adaptations to factor input markets and demand conditions in the recipient LDC.

Another advantage may be that the parent firms of the LDC subsidiaries have the home-based production capacity to supply appropriate low-cost machinery, components and intermediate inputs to their subsidiaries in the recipient LDC. According to one study, more than one third of the machinery used by the LDC subsidiaries was produced<sup>d</sup> in their home countries, and most of this machinery was produced by their parent firms and/or modified by them to suit the LDC conditions better than the machinery available from the DCs.<sup>22)</sup> The same is true with the supply of components and intermediate inputs produced at lower cost by LDC parent firms in the home-country

Table IV-2 shows a series of advantages that Hong Kong investors reported that they had over the DCMNCs in other LDCs.

Table IV-2 Advantages of Hong Kong Investors Over Other Multinationals in Recipient Countries

| Advantage  | Rank |
|--|------|
| 1. Lower costs for managerial and technical staff  | 7    |
| 2. More appropriate technology for the local conditions in the host countries  | 5    |
| 3. Longer experience in production and operation   | 0    |
| 4. Greater flexibility and adaptability  | 3    |
| 5. Better understanding of the conditions in the less-developed countries  | 6    |
| 6. Better connections with export markets  | 2    |
| 7. Government policies in the host countries prefer overseas firms from developing countries to these from developed countries | 0    |
| 8. Better local connections in the host countries  | 4    |

Source: Edward K.Y. Chen, "Hong Kong Multinationals in Asia: Characteristics and Objectives," K. Kumar and M.G. McLeod (eds.) Multinationals from Developing Countries (Heath, 1980), p. 95.

Hong Kong investors considered their lower cost for managerial and technical personnel as their most important advantage over their DC counterparts. They thought that they understood the LDC conditions better and used more appropriate technology, thus confirming our finding stated above.

Table IV-3 indicates the advantages Hong Kong investors thought they had over local competitors in the recipient country. They thought

Table IV-3 Advantages of Hong Kong Investors Over Local Firms in Recipient Countries

| Advantage   | Rank |
|---|------|
| 1. Better management skill  | 7    |
| 2. More advanced technologies   | 5    |
| 3. More appropriate technologies for the local conditions in the host countries | 3    |
| 4. Longer experience in production and operation                                | 6    |
| 5. Better connections with the export markets                                   | 4    |
| 6. Greater flexibility and adaptability   | 2    |
| 7. Government policies in the host countries in favor of foreign firms          | 1    |

Source: Edward K.Y. Chen, "Hong Kong Multinationals in Asia: Characteristics and Objectives," K. Kumar and M.G. McLeod (eds.) *Multinationals from Developing Countries* (Heath, 1980) p. 95.

better management and longer experience were the greatest advantages over local firms. More advanced technologies and better connections with the export markets were ranked next in importance.

A set of advantages indicated above for the LDC investors may explain the co-existence of the LDC firms with DCMNCs in recipient countries, but do not imply that the presence of the LDC investors can increase the LDC's bargaining power vis-a-vis the DCMNCs or reduce the profits attained by DCMNCs operating in the LDC. According to findings from Professor D.J. Lecraw's study on the MNCs operating in the ASEAN countries, the DCMNCs and the LDC firms in the recipient LDC do not compete "head on" with each other, though their products are classified into the same industry group. The products of the DCMNCs are R&D intensive, highly differentiated and have low price-elasticity, whereas those of the LDCMNCs are low

R&D-intensive, have high price-elasticity, low cost and low quality. The LDC subsidiaries do not take an active part in the rivalry between the MNCs from different DCs which are quite keen and which certainly reduce the profitability. Based on this finding, Professor Lecraw concludes that foreign direct investment by the LDC firms can best serve as a complement to direct investment by the DCMNCs, not as a supplement.<sup>2,3</sup>

The assets of the LDC investors mentioned above can be also considered as providing benefits to recipient LDCs, including use of labor-intensive modern technology most appropriate to LDC factor endowments, the production of products that are most suitable to the needs of the majority of the consumers in the LDC, and the extensive utilization of locally produced raw materials and other inputs.

In sum, the LDC firms have advantages over their DC counterparts in their use of small-scale, labor-intensive, imported materials-saving technologies. They compete or co-exist with the DCMNCs on the basis of their appropriate technology for low-cost production of less differentiated products. The LDC investors tend to have advantages in managerial and technical competence and export marketing over their local counterparts in the host country. Such advantages of the LDC invested-firms are also the major sources of benefits for their host LDC. Though the products of the LDC investors compete in price with those of the DCMNCs and local firms in their host country, the presence of the LDC firms in any industry may not reduce much the amount of profits earned by the DCMNCs in the same industry as much as does the presence of another DCMNC. In this sense, direct investment by the LDC firm may have so far served as a complement to direct investment by the DCMNCs in other host LDCs in the past.

## CONCLUSIONS: Prospects and Policy Guidelines

### A. Summary of Recent Trends

In accessing the prospects for inter-LDC direct investment and non-equity collaboration, it will be useful to recapitulate the broad trends in recent inter-LDC investment that have been noted in the preceding chapters.

- a) The degree and speed of internationalization of the LDC firms is rapidly increasing, and the share of LDC direct investment in the total value of foreign direct investment in recipient LDCs is increasing far more rapidly than that of developed country FDI.
- b) The inter-LDC direct investment activities have been taking place mainly on intra-regional basis, whether in Asia and the Pacific or in Latin America.
- c) The average size of investment projects has gradually increased over time.
- d) The pattern of industrial composition of inter-LDC direct investment is gradually shifting from the predominance of traditional export-oriented industries like textiles, garments and footwear toward local-market-oriented, import-substitution industries such as food and beverage, chemicals and rubber, cement, wood products, metals, machinery.
- e) The predominant form of ownership used by LDC investors is the joint venture partnership either with a foreign minority or foreign majority position.
- f) The LDC investors have become almost the exclusive suppliers of small- and medium-scale, labor-intensive modern technologies appropriate to the factor prices and market demand conditions in the

recipient LDCs. The DCMNCs supply capital- and technology-intensive technologies.

g) LDC investors seek primarily to shift from preserving traditional export markets in the other LDC toward taking advantage of factor endowments in the recipient country by investing in on-site natural resource development and in local-market-oriented manufacturing. The firms or "business groups" in some advanced LDCs also seek to increase relations between their overseas investment activities and the expansion and diversification of their home-based industrial production.

h) Thus far, the government policies of most recipient LDCs have not provided investors from other LDCs with preferential treatment. On the contrary, the regulations and practice of recipient country investment authorities have acted, perhaps unintentionally, to discriminate (in terms of size requirement for entry screening, minimum requirements for capital size for tax incentives and financial incentives, etc.) against investors from other LDCs as compared with those from the DCs.

#### B. Prospects for Inter-LDC Direct Investment and Non-Equity Collaboration

In view of these trends as well as developments within the international economy which will influence the future of the MNC activities in general, the following can be said about the prospects for inter-LDC direct investment and collaboration:

First, the process of internationalization of the LDC firms will undoubtedly accelerate, and FDI by the LDC firms will continually expand in terms of industrial and geographical areas, perhaps much more rapidly than DCMNCs direct investment. In particular, inter-LDC



direct investment on a regional basis will intensify in view of increasing trends towards regional economic cooperation.

Second, the long-sustained industrial growth and diversification of some advanced LDCs (NICs) and its accompanying investment expansion, seems likely to cost the DCMNCs managerial and technological advantages. To that extent, inter-LDC direct investment will provide host LDCs with increased bargaining power vis-a-vis the DCMNCs.

Third, increased recipient LDC control over ownership and the operational conditions of foreign direct investment, along with greater choice over the elements of the MNCs "package," joint-ventures, more licensing and technological assistance agreements, and other non-equity arrangements seem to be the more likely LDC alternative forms of FDI. In this respect, the LDC investors do possess more flexibility than their DC counterparts in accommodating the recipient country's development needs.

Fourth, the "critical" elements of direct investment package provided by the DC and LDC investors may be changing. For example, financial capital may become less important than managerial and technical know-how in some cases, or technical know-how may be less critical than export-marketing know-how in other cases. The growing trend towards use of multiple firms for multiple needs will certainly improve the prospects for industrial cooperation. One firm from a DC, one from an advanced LDC (or the NICs), one from an OPEC country, and one from the LDC may join together to carry out a common industrial development project in a recipient LDC. The project in question may be the construction of physical overhead needed for capital

development of natural resources, or possibly installation of industrial plants and training centers. Partners from the DC could contribute sophisticated technology and specialized equipment, partners from the advanced LDC certain kinds of capital equipment, technicians and skilled workers, OPEC partners financial resources, and the LDC partners manpower for general and civil construction and raw materials.

### C. Policy Guidelines

Let us consider what investor and recipient governments as well as international public agencies can do to promote inter-LDC direct investment and non-equity collaboration.

#### a. the Recipient Government

First, regulations and practice regarding screening and provision of financial and tax incentives for foreign investors have often acted to discourage LDC investors and to have aided the DCMNCs in their efforts to keep out foreign competition and thereby increase profits. Recipient LDC governments would like competitive environment conducive to the development of appropriate technology. Therefore, recipient LDC governments should eliminate all restrictions and practices that block LDC investors entry.

Second, advanced LDCs (the NICs) and the poorer LDCs should create a closer partnership to utilize the former's experience and technical know-how for the benefit of the latter. The LDC recipient governments should especially promote LDCs direct investment by providing LDC direct investment preferences in terms of requirements for entry approval, or tax and financial incentives. Such preferences would encourage (i) small- and medium-scale processes, (ii)

labor-intensive (employment-generating and capital-saving) technologies, (iii) import-saving through the use of locally produced materials, (iv) more immediate transfer of technology through joint ventures, etc.

b. the Investor Government

The impact of direct investment on investor countries can be distinguished between its short-run and long-run effects. The former relates to adverse effects on balance of payments and on level of employment, and the latter to positive effects on national income and output of investor countries (e.g. higher returns from capital and technology expressed in terms of profits and royalties). In most cases, governments have expressed more concern about the short-run effects of outward direct investment. Their preoccupation with the outflow of foreign exchange, for example, may result in their imposing undue constraints on overseas investment projects. Such constraints are responsible for the unusually high incidence of abandonment, and the extremely low profitability, of Indian joint ventures.

Overseas investment project failures not only represent outright economic losses but also lead to the deterioration of the investor country's business relationship with the recipient country. In formulating its policy toward FDI, the investor government must balance short-run and long-run considerations.

c. Utilization of the Existing U.N. and Other International Public Agencies

The UNIDO, the World Bank Group, and other U.N. agencies should be utilized (i) to promote inter-LDC direct investment (ii) to create a more fruitful cooperation between the DCs and the advanced LDCs in

order to utilize the latter's experience, insight and technological know-how for the benefit of the poorer LDCs, and (iii) to maximize positive aspects and to minimize negative aspects of the DCMNCs' experience and contacts with the LDCs.

First, the agencies should undertake a major effort to improve the flow of information about development technology and experience among the LDCs, between the LDCs and the DCs, and between different regions.

Second, the World Bank Group and other international agencies should actively solicit, and improve, participation by the LDC firms in multinational industrial projects which they are promoting and financing.

Third, the agencies should take measures to increase their efficiency in coordinating laws, regulations and policies governing foreign direct investment (including entry, ownership and management control, taxation, and financial incentives, and others), among investor and recipient countries for the benefit of all, especially LDC, parties.

## Notes and References

- 1) As to the "new forms" of international investment, see OECD Observer (No. 112, September, 1981), pp. 9-15.
- 2) The U.N. CTC definition is found in U.N. Economic and Social Council Commission on Transnational Corporations), Transnational Corporations in the World Development: A Re-Examination (May, 1978), pp. 158-161.
- 3) Eduardo White, "The Internationalization of Firms from Latin American Countries," in K. Kumar and M.G. McLeod (eds.) Multinationals from Developing Countries (Heath, Lexington, Mass.), pp. 158-159.
- 4) The point has been stressed by Professor K.Y. Chen in his article, "Hong Kong Multinationals in Asia: Characteristics and Objectives," in K. Kumar and M.G. McLeod (eds.) op. cit., p. 80.
- 5) Ibid., pp. 84-85.
- 6) Ibid., pp. 89-91.
- 7) M.K. Raju and C.K. Prahalad, The Emerging Multinationals - Indian Experience in the ASEAN Region (September, 1980, Madra, India), p. 5.
- 8) Ibid., p. 34.
- 9) Ibid.,
- 10) Donald J. Lecraw, "Internationalization of Firms from LDCs: Evidence from the ASEAN Region," K. Kumar and M.G. McLeod (eds.), op. cit., p. 45.
- 11) M.K. Raju and C.K. Prahalad, op. cit., pp. 36-37.
- 12) Louis T. Wells, Jr., "Foreign Investors from the Third World," in K. Kumar and M.G. McLeod (eds.) op. cit., p. 27.
- 13) Donald J. Lecraw, "Structure and Competitive Practices of TNCs in the ASEAN Region" (March, 1980), The University of West Ontario School of Business Administration Working Paper (Series No. 237), Table 5-14.

- 14) From questionnaire sheets for "Taiwan Multinational Study" undertaken by Professor Chi Schieve and Dr. Krishna Kumar.
- 15) M.K. Raju and C.K. Prahalad, op. cit., p. 4.
- 16) Ibid., pp. 35-37.
- 17) Louis T. Wells, Jr. op. cit., pp. 33-34.
- 18) This point is well documented by Professor Lecraw in his Working Paper (Series No. 237).
- 19) Louis T. Wells Jr., op. cit., p. 34.
- 20) Carlos F. Diaz-Alejandro, "Foreign Direct Investment by Latin Americans," in T. Agmon and C.P. Kindleberger (eds.), Multinationals from Small Countries (Cambridge, Mass.: MIT Press), p. 180.
- 21) The theory of transition growth of open dualistic economies is well summarized by Professor Gustav Ranis and John C.H. Fei, "A Model of Growth and Employment in the Open Dualistic Economy: The Cases of Korea and Taiwan," Journal of Development Studies (January, 1975).
- 22) Donald J. Lecraw, "Structure and Competitive Practices of TNCs in the ASEAN Region," The Working Paper cited.
- 23) Donald J. Lecraw "Internationalization of Firms from LDCs: Evidence from the ASEAN Region, in K. Kumar and M.G. McLeod (eds.), op. cit., p. 48.



