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The Role of Multinational Companies in the Deployment of Foreign Direct Investments

In the last decades multinational firms have become the leading actors of the international markets, including markets in developing countries. A multinational firm's decision to open a branch or a subsidiary in another country, thus to invest abroad, is based on efficiency criteria, the obtained profit having a primordial aspect. We mustn't forget the various advantages the host country befits of, here mentioning the transfer of technology. The unprecedented foreign amalgamation of multinational firms was brought on by the continuous liberalization of international commerce and investment fluxes

The foreign direct investment theory is an integrated segment of the multinational firm's theory because they do not represent a mere capital transfer but are an extension of the enterprise from the country of origin to the host-country. Mainly all foreign direct investment fluxes are generated by multinational firms. In virtue of the international resource transfer and the direct participation of the foreign investor to the organization and activity administration of the newly created entity, the international assets and services production appeared in the world economy (along side commercial and traditional financial fluxes).

The structure of the activities unreeled by the multinational firms contains the following three domains: the national space where the mother society has its quarters, the foreign space where the filiations are found and the international space where economical exchanges initiated by the entities that make up the multinational firm are realized.

The primordial criterion that determines a firm to choose between the exports of products manufactured in the country of origin and manufacturing them in other countries thus gets the valence of a multinational firm and is related to the insurance of economical efficiency. We must analyze the costs bared by the firm in both cases. In the first case we must necessarily have in mind the costs related to the external transport of the product, their safety during an international traffic, the level of custom duties etc., and in the second case we must consider costs generated by centers, communication, personnel qualification, adapting to local legislations etc. If the cost of manufacturing merchandise abroad is smaller than the cost generated by manufacturing that same merchandise in the country of origin and then exporting it, then the firm will choose to build branches that are productive in certain countries, thus acquiring a multinational aspect.

By considering the opportunity to invest in a certain country, multinational societies must have in mind certain indicators that allow the shaping of an image regarding the transaction of the financial resources and resources obtained from the investment process.

To settle the quantum of efficiency indicators we must emphasize the investment effort (expenses) and effects (income) by using the update approach.

We have a sum S available in the moment $t_{0,}$ and considering the current update rate it becomes:

- in the moment t_1 $S_1 = S(1+r)$
- in the moment t_2 $S_2 = S(1+r)^2$

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- in the moment t_n $S_n = S(1+r)^n$

The update rate problem stands for the new guardian in establishing efficiency indicators. The factors that are generally regarded when determining the proportion of the update rate for a foreign country that is about to invest are: economical growth, inflation, currency rate etc. The update rate for Romania was 15% at the level of the entire national economy used in different specific research.

Amongst the economical efficiency indicators preferred by international organizations we recall the relation between costs and income also known as profit/cost. Thus we can compare the annual income achieved through out the entire period of activity of the economical objectives that stand under the control of foreign investors and amounts that represent annual foreign direct investments as well as production costs of the formerly stated objectives.

Updated costs and income made by ISD in Romania:

Table 1

Year	ISD and production costs bil. Lei	Income bil. Lei	Update Factor r = 15%	ISD and updated costs bil. lei	Updated income bil.lei
1991	6	2	8.13	49	16
1992	30	14	7.07	212	99
1993	156	107	6.15	959	658
1994	724	568	5.35	3873	3039
1995	4236	4125	4.65	19697	19181
1996	11670	11375	4.04	47147	45955
1997	32984	35720	3.51	115774	125377
1998	35011	39082	3.05	106784	119200
1999	43476	46251	2.66	115646	123028
2000	50339	53720	2.31	116284	124093

2001	56187	58910	2.01	112935	118409
2002	70048	91120	1.74	121884	158549
2003	79345	98368	1.52	120604	149519
2004	91593	113437	1.32	120797	149737
2005	108271	124350	1.15	124512	143003
Total				1127108	1279861

Effort = annual ISD + annual production expenses
Effect = profit amount after realizing ISD

$$R = \frac{1279847}{1127108} = 1{,}13$$

Because R>1, foreign investors have retrieved expenses they made in our country and also obtained a certain profit. For this reason the least, Romania should present an interest for potential foreign investors.

The firm has another alternative at hand also and that is cessioning manufacturing licenses in favor of foreign manufactures. This is a rarely used possibility because multinational firms do not approve of alienating the result of their own scientifically and technical research activity. They prefer on the other hand, the transfer of technology towards their own foreign branches, thus having control over that certain technology. It would appear that at present this is the easiest way to insure the participation of developing countries (where multinational firms have opened branches) to the benefits that result from scientifically and technical world research. Considering that multinational firms make up 80% of the entire world's research-development activity, nowadays we are witnessing a tendency of polarizing activities displayed by these firms. This way the multinational firm will mainly unreel the research-development activity in the country of origin, leading the productive activity towards it's own foreign branches.

Entire sectors of the industry have been participating to the integration of their activity on the manufacturing markets and international outlets since 1970. The dimension of the international manufacturing and the number of multinational enterprises was determined by the impact of international and transport techniques (that have diminished the costs and the risks of the remote control process), by creating new technologies of manufacture and by the great variety of financial instruments that are being use to support the growth in volume and complexity of international transactions. The development of multinational firms was also brought on by the continuous liberalization of the international commerce and investment fluxes.

This category of investments is one of the most sought-after and it takes various forms, such as:

- the minority participation to the firms of a host country by the buying of actions at the local stock market.
- the participation at the birth of a mixed firm with local partners

• the main participation to the firms of a host country by acquiring stocks, the transition to a private property, swap or other approaches.

• giving licenses to firms belonging to the host country.

Multinational firms do not take action only in developed countries, but in all the countries of the world; they are a powerful cohesion force of the world economy, cement that bounds national economies, in the process of extending economy to a world scale. With the help of complex enterprise strategies and a system of structures that have planetary dimensions, multinational firms are involved in the international production of assets and services, based on a sophisticated work division between the mother society and it's foreign branches. Approximately a third of the live private manufacturers of the world are ran by multinational firms that have different degrees of integration on a vertical scale. As the vertical integration between the manufacturer and the merchandiser grows, the role of multinational enterprises in international economical relations gains supremacy.

In the last three to four decades the number of multinational firms has grown significantly. If seven thousand multinational firms existed in 1969, their number reached 24.000 in 1990, 63.000 in 2000 and by 2008 they will have reached 68.000. Those 68.000 multinational firms held 866.000 foreign filiations.

The multinational firms' production value has grown 7 times it's value over period of 20 years (1982-2002), when the world GDP only grew 3, 5 times it's value. The value of the multinational firms' turnover has evolved from 24% to 55% in the world GDP in that period.

Some multinational firms have gained a considerable economical sturdiness, which exceeds that of certain nations. According to statistics the classification made, at the beginning of this millennium, was based on the turnover for multinationals and GDP for countries, in the first 100 hierarchies entities, 51 of them were multinational firms and 49 were countries. The turnover realized by the first 200 multinational firms was larger than the integrated GDP of the whole world's countries, diminished by the one registered in the first 10 developed countries.

We must observe that multinational firms that have their headquarters in developed countries are much more powerful then those originating from developing countries. In the world classification of multinational firms established pending on their market value, the first places are occupied by American societies.

The competitive advantages of enterprises from developed countries were consolidated by centuries of capital accumulation, economical growth and technological improvements. Over 50% of multinational firms origin in the first 5 developed countries (France, Germany, Japan, England and USA). From the developing countries only large and newly industrialized countries hold multinational firms. If we were to consider only statistics that are representative for USA and Japan, 60% of multinational firms are active in the manufacturing industry, 37% in services and only 3% in primary sectors. If we were to consider domain distribution, the largest multinational firms can be found in the following industrial sectors: chemical and pharmaceutical, electronical, computers and automobiles.

From the industrial network of enterprises with foreign affiliations, almost half are situated in developing countries, a number much larger than that of investment fluxes (30%). This shows that the value of capital size appropriate to affiliated enterprises is much larger in developed countries than in developing countries. On sectors, most affiliated enterprises were built in services (60% of the filiations of multinational firms from Germany, Japan, and USA).

By their present nature, multinational firms organize the manufacture and distribution of assets and services on a world level based on the property relation over production assets or other means of control. Certain strategies are adopted by multinational firms in order to reach short term objectives as well as long run objectives like the profit estimated when the investment is made, the growth of market value or the growth of operation value, all in the context of the economical and political environment of the country in which they operate.

Per the ensemble of the world economy of the last decades, international merchandise and services trade has grown faster than the GDP, the connections between the international financial markets have amplified and foreign investments have rapidly increased, which has also attracted the improvement of the multinational prestige as leading actors in the international economical transactions.

Multinational firms have a tendency of turning their focus on countries with the best growth prospect and that have abundant natural resources, large national markets, educated and relatively cheap workforce, favorable field of legislation. Through a mutual stimulation process, multinational firm are attracted to this perspectives and influence the development ability of these countries. Integration and interaction thus imply continuous interactions between the government and enterprises.

To conclude, the network of multinational firms and their filiations around the world form an integrated system, with economical, social and ethnical common values, and play a leading role in the evolution of world economy and the economy of each and every country.

Throughout the last two decades of the 20th century, foreign direct investment fluxes have grown more rapidly than the internal investments of single countries and their internal production. Foreign direct investments have grown, between 1985-2000, four times faster than the internal production of the world's countries and almost two times faster than their internal investments.

The participation rate of foreign direct investments to the internal production on a world level is still slim (approximately one third), but it's value finds itself in a continuous expansion due to the much more faster growth of external investments in relation to the internal investments. We could also add that the trade between international firms approximately represents 20-25% of the world trade, fact that has a major consequence to certain countries.

At the end of the decade past, ISD became the primary source of foreign capital that most of the developing countries were deprived of. We must have in mind that they do no create an external debt for that certain country and the capital outlets they imply (profit repatriation), depend on the economical result of the enterprise and as much to the investor's interest as to the interest of the state that encourages the economical growth.

The participation of the ISD stock to the making of the GDP is an indicator that shows the importance of these investments to the process of economical growth and development. In 1982 the turnover of the multinational firms was 23% of the world GDP, rising up to 55% by 2002.

The multinational firms' are much more complex and their impact on the national economies of the host countries is much higher than the statistics might show. Their indirect effect is mirrored in the orders transmitted to the national enterprises, creating new work places, encouraging horizontal industries, indirect export etc. We can thus state that in relation to the production, trade, transfer of technology and capital fluxes in the world economy, foreign direct investments have become more and more important, and multinational firms play a meaningful role in the economies of the host countries. Also the impact of foreign direct investments can manifest itself as a powerful force in the process of efficiency growth in what the distribution of resources on a world level is regarded and as transmission route for economical impulses regarding production, technology and quality of labor.

Foreign direct investments are considered to be a propulsion factor of the development of comparative advantages, in the extent to which the multinational firms can raise the level of production complexity, amongst their filiations, from simple assembly operations to more extended operations, by using new technologies that they integrate in their foreign production system.

Considering that the developing countries receive 30% of international ISD fluxes, the positive effects of the multinational societies' actions are more obvious than in developed countries. From the host country's point of view usually, the subsidiary owned by the multinational company brings its share to the growth of the degree of professional readiness to the workforce, to the research-development activity or productivity growth in that certain domain, at a larger scale than the national company does.

Multinational companies have a large contribution to the forming of capital in host countries, by cutting down expenses and investing they create new work places and generate higher salaries than that of local enterprises. More than that local suppliers have the possibility of obtaining increased income.

Through their business relations, multinational companies transfer a series of knowledge to local enterprises, in some cases offering them technical and financial assistance. The strategies of the local firms are also influenced, as are their enterprising wit and orientation towards exporting, this having favorable impact on the efficiency of economical activities in the host country.

Foreign direct investments contribute to the integration of less developed countries in the world economy; stimulate international commerce, especially by making imports of cars, equipment and plants. Multinational enterprises along with external commerce stimulate the offer of services necessary to international commerce (banking, insurance, transport, telecommunication services) that contribute to the economical growth of the host countries.

The relation established between the multinational company and the host state has stirred many discussions along the years. This relation basically depends on the group on countries (developing or already developed) to which the host country belongs. When host markets display a high economical potential, multinational companies pursue the application of the mutual advantage principal considering the perspective of obtaining a better profit, as well as the powerful competition between investors. If the hosts are developing countries, the multinational firms become more and more influential in their relation with the governments of the respective states. This phenomenon only takes place in the case of an non-existing legislative framework correspondent to the host country, doubled by the high number of corrupt deeds. In less developed countries, multinational companies try to compensate shortcoming caused by high inflation, monetary instability, political instability, by offering a series of advantages like cheap workforce, abundant natural resources, and the access to the internal market.

The impact of foreign direct investments over the economy of the developing countries is also valid for countries transitioning towards market economy. Starting from the fact that the level of foreign direct investments is pretty low in what the economy of transitioning countries in concerned and that they are unevenly distributed between countries, their implications are specific aspects of every country belonging to this category.

The analysis of the foreign investments' evolution in transitioning countries, made by the Economical Commission for Europe of the ONU, stress out those significant changes took place concerning flux and foreign invested capital stock dynamic, in the structure of foreign investments, volume of investments per inhabitant and regarding branches that benefit from foreign direct investments.

In UNCTAD's last report, special attention is given to the impact of the multinationals on developing economies, including here countries from Africa, Asia, Latin America and Central and Eastern Europe. The report reached positive conclusions. The report, based on the evolution of Asian countries, states that foreign direct investments can encourage the development of indigenous economical factors. The authors of the report stress that multinationals can initiate circles of re-organization by introducing branch offices into their global networks, this way creating direct and indirect connections to local companies.

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