Role of the Private Sector in Post-War Economic Development

A multi-national corporation (MNC) is **<u>a corporation or enterprise that manages production establishments or delivers services in at least two countries.</u>** Most MNCs are industrial corporations which make goods in factories in various countries and distribute them worldwide. They can take the form of financial corporations or service providers.

- Such companies have offices and/or factories in different countries and usually have a centralized head office where they coordinate global management. Nearly all major MNCs are American, Japanese or Western European e.g. Nike, Coca-Cola, Wal-Mart, Toshiba, Honda and BMW.

Very large MNCs have budgets exceeding those of countries, and can have powerful influence in international relations and local economies. Most MNCs are from developed countries, and play a major role in developing economies. Since 1945, MNCs have grown rapidly. In 1976, 371 MNCs had branches in 20 countries. Presence of MNCs have often contributed to the productivity and production of the host country, as well as aided and expanded its economic growth.

Background:

The earliest historical origins of multinational corporations can be traced to the major colonising and imperialist ventures from Western Europe, notably England and Holland, which began in the 16th century and proceeded for the next several hundred years. During this period, firms such as the British East India Trading Company were formed to promote the trading activities or territorial acquisitions of their home countries in the Far East, Africa, and the Americas. The multinational corporations as it is known today, however, did not really appear until the 19th century, with the advent of industrial capitalism and its consequences: the development of the factory system; larger, more capital intensive manufacturing processes; better storage techniques; and faster means of transportation.

During the 19th and early 20th centuries, the search for resources including minerals, petroleum, and foodstuffs as well as pressure to protect or increase markets drove transnational expansion by companies almost exclusively from the United States and a handful of Western European nations. Sixty per cent of these corporations' investments went to Latin America, Asia, Africa, and the Middle East. Fueled by numerous mergers and acquisitions, monopolistic and oligopolistic concentration of large transnationals in major sectors such as petrochemicals and food also had its roots in these years. The US agribusiness giant United Fruit Company, for example, controlled 90 per cent of US banana imports by 1899, while at the start of the First World War, Royal Dutch/Shell accounted for 20 per cent of Russia's total oil production.

Acceleration of MNCs after WWII

After WW2, multiple trends converged to accelerate MNC growth:

- Favorable post WW2 economic world order that favored trade over conflict.
- Banks in the US, Europe, and Japan began to lend vast sums of money to industrial companies, encouraging expansion and mergers.
- Technological advances in transport, IT, and communications.
- Emerging markets, burdened by debts and unemployment, began to view MNCs as a path to rapidly access technology, capital, and accelerate employment. The East Asia miracle was largely based on MNC trade.

Demand for natural resources continued to provide an impetus for European and US corporate ventures between the First and Second World Wars. Although corporate investments from Europe declined somewhat, the activities of US MNCs expanded vigorously. In Japan, this period witnessed the growth of the zaibatsu (or "financial clique") including Mitsui and Mitsubishi. These giant corporations, which worked in alliance with the Japanese state, had oligopolistic control of the country's industrial, financial, and trade sectors.

US MNCs heavily dominated foreign investment activity in the two decades after the Second World War, when European and Japanese corporations began to play ever greater roles after the 1970s. In the 1950s, banks in the US, Europe, and Japan started to invest vast sums of money in industrial stocks, encouraging corporate mergers and furthering capital concentration.

- Major technological advances in shipping, transport (especially by air), computerisation, and communications accelerated MNCs' increasing internationalisation of investment and trade, while new advertising capabilities helped MNCs expand market shares. All these trends meant that by the 1970s oligopolistic consolidation and MNCs' role in global commerce was of a far different scale than earlier in the century. Whereas in 1906 there were two or three leading firms with assets of US$500 million, in 1971 there were 333 such corporations, one-third of which had assets of US$1 billion or more. Additionally, MNCs had come to control 70-80 per cent of world trade outside the centrally planned economies.

Over the past quarter century, there has been a virtual proliferation of transnationals. In 1970, there were some 7,000 parent MNCs, while today that number has jumped to 38,000. 90 percent of them are based in the industrialised world, which control over 207,000 foreign subsidiaries. Since the early 1990s, these subsidiaries' global sales have surpassed worldwide trade exports as the principal vehicle to deliver goods and services to foreign markets.

How did MNCs contribute to the rapid growth of post war economies?

Western Europe was experiencing "worsening trade and payment deficit[s]" that stemmed from the considerable productivity gap and its inability to compete economically. Owing to these conditions, the United States expanded and focused the Marshall Plan by instituting the Technical Assistance and

Productivity Program in 1949. The main thrust of the **Technical Assistance Program (TAP)** was to increase productivity in Western Europe.

The conventional wisdom surrounding the productivity gap was that Europe had technologically fallen behind the United States. To address these concerns, the United States used the TAP as a conduit through which to **disseminate state-of-the-art technologies, technical knowledge, and managerial sciences**. The channels through which the technological transfer occurred inherently revolved around the lending of U.S. specialists to Europe and the allowance of their European counterparts to visit and observe processes in the United States.

- Additionally, U.S. government agencies played an important role in **transferring technological advances**. The Bureau of Labour Statistics, for example, contributed by providing statistical technical assistance that involved the exchange of specialists but also was focused on introducing a data- and statistics-rich approach to productive efficiency in Western Europe. Europe was not the sole beneficiary of these productivity and technology exchanges. The United States in 1955 initiated its TAP in Japan. Like the TAP in Western Europe, the Japanese assistance plan focused on increasing technological and productive know-how.

Anecdotal evidence provided in several studies reveals the very significant impact these TAPs had on the productivity of individual companies and industries as a whole. For example, Tiratsoo (2000) recounts that after the Mitsubishi Company received technical assistance from the United States in building a new assembly plant, it was able to increase productive capacity by roughly 40%. The International Directory of Company Histories (2001) describes how, in 1950, two leading executives of Toyota Motor Company,

"Seeking new ideas for Toyota's anticipated growth, … toured Ford Motor Company's factories and observed the latest automobile production technology. One especially useful idea they brought home from their visit to Ford resulted in Toyota's suggestion system, in which every employee was encouraged to make suggestions for improvements of any kind"

Similar stories emerged about the U.S. technical assistance in Europe. Wasser and Dolfman (2005, 49) cite one source as saying that productivity within individual industries "commonly increased by 25 to 50 percent within a year with little or no investment" as a result of the TAP. Thus the TAP was not about stimulating productivity gains through capital spending as much as it was focused on **the dissemination of technological and productive know-how about state-of-the-art technologies**. The extent of the knowledge transfers from the United States to Western Europe and Japan goes well beyond the formal TAP. U.S. efforts to boost productivity in its sphere of influence were part of a broader national security policy after 1953 and were in large part driven by the geopolitical realities of the Cold War.

U.S. manufacturing MNCs invested on a large scale in Western Europe – initially in response to the "dollar shortage" – encouraging U.S. firms to establish factories to supply customers in countries that lacked the dollars to buy American products. U.S. firms held large "ownership advantages" in management and technology over their European counterparts, and their affiliates often achieved much higher productivity than their indigenous counterparts.

Between 1950 and 1962, at least 350 new U.S. owned manufacturing affiliates were set up in Britain, the largest European host for U.S. manufacturing FDI. By the mid-1960s, U.S. owned firms employed nearly

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Theme II: Understanding the Global Economy
How did the Development of the Global Economy Impact the World?

10 percent of the British manufacturing workforce and held large market shares in many products involving either high technological content or advanced marketing skills. U.S. firms accounted for between 30 and 50 percent of the British market for computers, rubber tires, soaps and detergents, instant coffee, refrigerators, and washing machines among many other products. Throughout the 1950s and 1960s the labor productivity of U.S. affiliates in Britain was estimated to be almost 33 percent higher than that of all British manufacturing.

Although the fast growth of U.S. manufacturing affiliates was striking, there was little that could be considered global about multinational manufacturing in this era. On the one hand, this growth was little more than the story of U.S. firms shifting some of their production abroad – mainly to a few Western European countries. On the other hand, overseas affiliates remained very "national." There was little rationalized production, and intra-firm trade was very low.

However, from the 1960s new strategies for the organization of multinational manufacturing began to involve both geographical and functional integration. By the postwar decades, the considerable autonomy given to national subsidiaries had given rise to extensive duplication of products and functions such as FDI. The worldwide lowering of trade barriers under the General Agreement on Tariffs and Trade (GATT), cost reductions in transportation, a convergence of consumer demand in some developed countries and sectors, and the formation of trading blocs beginning with the European Economic Community (later the European Union [EU]) in 1957 provided new opportunities for the integration of formerly isolated subsidiaries

Case Study 1: The service industry

In the immediate postwar decades, multinational firms assumed an important role as conduits to the rest of the developed world of U.S. management practices and, more generally, of values and lifestyles. The importance of management consultancies lay in their diffusion of American (and, from the 1980s, Japanese) management practices and structures.

During the 1960s, McKinsey, in particular, played a major role in the spread of the M-form structure in Britain, France, and Germany even if, for institutional and cultural reasons, there was rarely a complete transfer of U.S. management practices to Europe or elsewhere. Large European firms made repeated and extensive use of McKinsey and other consultancies, often calling them in when internal disagreements among senior managers blocked change.

Hotels and fast food retailers were among other service industries in which MNEs played a substantial role in diffusing "global" lifestyles. The hotel industry, which had been primarily national before the Second World War, internationalized after it as hotel groups such as Holiday Inn, Hilton, and Inter-Continental expanded abroad, usually employing management contracts and franchising. The fast food industry, with multinational growth from the 1960s, used the same modes. The British-owned J. Lyons acquired the international franchise of the "Wimpy Bar" of the United States, and, through the 1960s, licensed hamburger chains in Europe, Asia, and Africa. McDonald's led the globalization of food tastes. Although it only opened its first foreign restaurant in Canada in 1967, over the following two decades it conquered widely different culinary traditions worldwide; by 1990 there were more than 2,500 McDonald's restaurants in 50 other countries.

Case Study 2: The finance industry

Although the wholesale and Euromarkets became truly global, retail banking markets remained local. Few banks made a serious and sustained attempt to provide global banking services even at the retail level. The most important to do so, however, were Citibank of the United States and the Hongkong Bank (now HSBC), the British overseas bank in Hong Kong until 1993 that built on its core Asian and Pacific business by acquiring banks in the Middle East, the United States, Britain, and (in the 1990s) Latin America.

Trading companies also resumed a new importance in the postwar decades. The extensive business of the European trading companies in the developing world encountered considerable difficulties because government intervention in commodity trading, import and exchange controls, and pressure for local ownership of resources decimated many aspects of their traditional business. However, in regions and countries where political conditions permitted, these trading firms continued to evolve, sometimes investing in manufacture in their host economies or in related services. From the base of the British colony of Hong Kong, the British trading companies, such as John Swire and Jardine Matheson, survived the loss of all their extensive assets in China in 1949 and built new diversified trading and distribution businesses in the Asian and Pacific regions and elsewhere. The Swire Group established a new airline in the late 1940s (Cathay Pacific), invested in Coca-Cola bottling in Hong Kong and the United States in the 1960s and 1970s to become one of the world's largest bottlers, and developed disused land from its former dockyards and sugar refinery in Hong Kong into a vast real estate business in Asia and the United States.

Although such European trading companies developed as regional multinational groups, other types of multinational trading firms built and developed global trading networks, benefiting from persistent information asymmetries – at least until the spread of the Internet during the 1990s changed the rules of the game – and in some cases from the opportunities to trade with Communist countries. Prominent among these firms were Japan's general trading companies (*sogo shosha*), which survived their dismantling by the Allied occupation after the Second World War to become the central players in both Japan's foreign trade and (until the 1970s) FDI as well as central components of Japan's horizontal business groups with a special role in financing and handling the foreign trade of Japanese SMEs. The *sogo shosha* accounted for more than 80 percent of Japan's total imports and exports during the 1960s and were counted as among the world's largest MNEs in terms of turnover. In a regional context, the *sogo shosha* were important in the postwar decades through their alliances with overseas Chinese firms, enabling their local production and trading networks to be refocused toward Japan and the United States.

The postwar decades also saw the rapid international growth of commodity trading firms like Cargill, the U.S. grain trader and largest private company in the United States, which took advantage of increased government intervention in the marketing of commodities and the nationalization of mines and plantations. By the 1970s a handful of commodity traders, including Cargill, Continental, Louis Dreyfus, Bunge & Born, and Andr´e, accounted for more than 90 percent of the European and U.S. wheat exports. Swiss-based trading firms, such as Andr´e and Glencore, built enormous global commodity and other trading links. By the 1990s Glencore had an annual turnover of more than $40 billion, trading in everything from base metals to soft commodities.

Hwa Chong Institution (College): History Paper 1
Theme II: Understanding the Global Economy
How did the Development of the Global Economy Impact the World?

To what extent were the effects of MNCs global in origin and impact?

European-owned companies lagged far behind their U.S. counterparts in response to regional integration. The contrasting examples of Unilever and Procter & Gamble have acquired almost a textbook status.

- Unilever had an extremely decentralized organization in the postwar decades reflecting, in part, the autonomy of national subsidiaries in Europe as a result of political developments in the 1930s and the Second World War and also Unilever's growing not as an organic company but through acquisitions and mergers.

An organizational culture based on consensus also meant that senior management in the firm's twin headquarters in London and Rotterdam sought to avoid forcing their wills on local managers. The result was that this leading European-based MNE was remarkably decentralized. Within Europe, Unilever's national managers had the greatest possible freedom – that is, national products and brand names varied enormously and there was no integration of production between countries. Both its trading company subsidiary, United Africa Company, and its U.S. business functioned as almost autonomous operations. This development might have reflected a more general trend, for the many European manufacturing firms with operations in the United States in the postwar decades were often left largely alone for antitrust reasons and because of a belief in the uniqueness of the American market and the superiority of its American management.

Unilever's position was severely challenged during the 1950s with the formation of the EU and the entry of U.S. MNCs led by Procter & Gamble and Colgate into Europe. Procter & Gamble, with relatively few international operations before 1945, began its internationalization process at a time of falling trade barriers. Its management had a strong belief in Procter & Gamble's "way of doing things" and sought to structure its overseas operations as replicas of the U.S. business. It moved quickly to integrate its European plants, and, in 1963, established a European technical center to service the common research and development (R & D) requirements of its European subsidiaries.

Although Unilever lost market share in detergents rapidly following the assault by U.S. MNCs, its attempts to integrate production and achieve more cohesive organization were prolonged. In 1952 it appointed two "coordinators" (a term used to emphasize that their role was advisory) for non-margarine foods and personal products (such as toothpaste) whose functions were to encourage transfer of products and brands between countries and to identify international brands. Only in 1966, after much internal dissension, were the coordinators given executive power and profit responsibility in a handful of Western European countries, and only in the 1970s, after a rigorous investigation by McKinsey, did conflicting jurisdictions between coordinators, national managers, and others begin to be sorted out. Even in the 1980s, Unilever lacked a coherent European strategy; during that decade the U.S. business was integrated in managerial terms with the rest of the firm.

The role of multinational corporations in promoting European integration

*Scan the QR code to read about **Unilever** and European integration*

Why did MNCs pale in comparison with other factors?

During the postwar decades, multinational investment became progressively marginalized in much of the world. In many countries the natural resource and service sectors were closed to foreign firms.

- North America and Western Europe and indeed manufacturing as a sector remained open, but even the Japanese economy was largely closed to foreign firms because Japanese governments, until the 1970s, blocked most wholly owned FDI in favor of licensing or joint ventures.
- For the first two decades after the end of the war, new FDI was largely a matter of U.S. firms' investment in Canada and Western Europe, and even in this case the flow was quite uneven geographically. In 1962, the United Kingdom alone accounted for more than 50 percent of the stock of U.S. manufacturing FDI in Europe.

During the 1950s and 1960s, the growth of world FDI resumed but was geographically and sectorally constrained. The firms of many developed countries preferred exporting over foreign production, and large areas of the world restricted the operations of foreign firms within their borders. By 1980 the stock of world FDI amounted to a mere 4.8 percent of world output, which was significantly less than in 1914.

The Second World War reinforced and intensified the political risks of FDI. The total loss of all German overseas assets once again led to an extremely subdued level of German FDI until the 1970s as German firms opted to export rather than engage in risking FDI. Although, during the interwar years Japanese FDI was small in absolute terms but considerable in comparison to the size of the Japanese economy, after the war a complex international business system involved worldwide Japanese trading and expansion of service sector companies as well as investments by Japanese cotton textile and mining companies in the markets and resources of Asia. After the loss of all Japanese FDI at the end of the war, Japanese firms, too, focused on exporting until the late 1970s.

Between 1945 and the mid-1960s, the United States may have accounted for 85 percent of all new FDI outflows. Among the Europeans, only British and Dutch firms opted to make substantial FDI in the era of the postwar "economic miracles." As a result, between 1945 and 1980 from two-thirds to three-quarters of all world FDI stock was accounted for by firms from the United States, the United Kingdom, and the Netherlands.

However, pent-up consumer demand at home, the scarcity of similar demand in war-ravaged Europe and elsewhere, the lack of convertible foreign currencies, the risks attendant upon overseas investments as illustrated by the experiences of two world wars, restrictions on remittances, and the fact that a new generation of chief executive officers with less of an entrepreneurial spirit and more of a concern with stability and predictability than many of their predecessors, all served to limit foreign investment in the years immediately after World War II.

Although investments in manufacturing, for example, grew from $2.4 billion in 1946 to $5.71 billion in 1954, most of this increase was in the reinvestment of profits of existing corporations, either because host governments blocked repatriation of scarce currencies or for tax and other reasons not related directly to growing consumer demand. Investments in other industries such as public utilities ($1.3 billion in 1946 and $1.54 billion in 1954) scarcely grew at all.

In at least one respect, US government policy discouraged overseas investment after the war, particularly in manufacturing. As never before, foreign economic policy became tied to foreign policy. As the Cold War hardened in the ten years following the war, Washington imposed severe restrictions on trade and investment within the communist bloc of nations. The Export Control Acts of 1948 and 1949, for example, placed licensing restrictions on trade and technical assistance deemed harmful to national security. During the Korean War (1950–1953) even tighter controls, extending to nonstrategic as well as strategic goods, were imposed on the People's Republic of China (Communist China).

It would be absurd to suggest that, absent these controls, American companies would have made substantial investments within the communist bloc. Nevertheless, the economic boycott of a vast region of the world contributed to the global economic uncertainty that normally inhibits direct foreign investment. According to the British, who were anxious to relax controls on the potentially rich markets of China, it also delayed its own economic recovery, another inhibitor to foreign investors.

The end of European colonial empires, the spread of communism, and growing state intervention in economies contributed to this trend. The 1949 Communist Revolution in China, one of the world's largest host economies before the war, led to the total exclusion of foreign MNEs until the late 1970s. Decolonization elsewhere was often followed by imposition of regulatory controls on foreign firms. Thus, in India, once a large host economy, first, high taxes and, from the 1960s, increasing control and regulations reduced foreign FDI by 1980 to minuscule levels as established foreign firms divested and new ones avoided the country. In the Middle East and Indonesia after the 1950s there was outright nationalization of foreign-owned oil fields, mines, and plantations. Although, until the 1970s the political and military hegemony of the United States deterred mass expropriations of MNCs, the deluge began in that decade as the influence of the United States declined and some developing countries acquired the technical and managerial abilities to run their own industries. During the 1970s many expropriations occurred in the developing world, and virtually all MNE ownership of mining, petroleum, and plantation assets was wiped out.

MNCs after the 1970s

The oil crisis-induced recessions of the early 1970s and early 1980s slowed economic activity, and with it MNC growth. Yet, some of the roots of later expansion of MNC activity were laid in this period. The American pattern of tighter coordination and global planning between parent company and subsidiaries was adopted by Western European and other MNCs. MNCs also became more willing to enter into joint ventures (co-owned firms) with governments or local investors, and many governments of developing countries became more willing to have manufacturing MNCs come into the country. The contrasting development performance of East Asian economies, with their government-encouraged policies of competing on global markets, over Latin American economies, with their continuing emphasis on replacing imports with locally made goods induced a broad rethinking of development strategy.

During the three decades or so after the Second World War, therefore, MNCs lost the great importance they had once held in the developing world. The process often proceeded rather slowly as with the disappearance of Africa from the orbit of international business. State intervention in commodity marketing even before Nigerian independence and growing competition had obliged the United Africa Company (UAC), a diversified trading company 100-percent owned by Unilever, to withdraw from producing, marketing, and general trading during the 1950s. The UAC venture was reborn as an importer of specialist products such as automobiles and tractors; through joint ventures it became a major brewer and textile manufacturer. Although compelled by West African governments to sell part of its equity to local interests in the 1970s, UAC employed more than 70 thousand people in the 1970s and, at times, contributed one-third of Unilever's total profits. Between the 1940s and 1980s UAC therefore remained Nigeria's – and West Africa's – largest modern business enterprise. Elsewhere in Africa, information asymmetries provided a continuing role for other European multinational trading companies such as CFAO (Compagnie Franc¸ais de l'Afrique Occidentale) and Lonrho.

Though the volume of international trade as a percentage of global production returned to 1914 levels by the mid-1970s, the value of all direct foreign investment did not reach its 1914 level of 9% of the value of annual world production until the late 1990s. Only with the end of the Cold war and the opening of all parts of the world to foreign trade and investment did the level of MNC investment get back to what it had been. Yet, the distribution of activities was very different; MNCs were far more active in manufacturing and service industries than they had been in 1914, and less active in raw materials and provision of transportation or public utilities.

The home countries of MNCs also became more diverse. In the mid1960s, US firms made more than 80% of direct foreign investments. More European companies took up multinational activity in the 1970s. In the 1980s Japanese manufacturers joined the older general trading companies in direct foreign investment, either to get closer to customers or to take advantage of lower cost labor in Southeast Asia. The more successful developing countries also became home to multinational firms of their own.

Conclusion on MNCs

From the 1950s onward a new global economy began to be constructed as MNE service firms started international dissemination of management practices, cultural values, and lifestyles – as well as the building of a new trading and financial infrastructure – and as multinational banks and trading companies moved money, commodities, and information around the world on an unprecedented scale. By the 1990s, multinational service firms were the largest and most dynamic components of the new global economy albeit with a distinct convergence between services and manufacturing.

Multinational manufacturers, starting in the 1960s, had begun to take advantage of new technological opportunities and regional integration to reorganize production systems, first integrating regionally and subsequently on a worldwide basis, and, beginning in the 1970s, Japanese and continental European firms again resumed FDI on a substantial scale while the United States grew as the world's largest host economy. But, under the pressure of fast internationalization, the boundaries of manufacturing and service firms had become blurred as they arranged for production and sought competitive advantages through alliances with other firms.

By the end of the 1980s, however, globalization was more a concept than a reality, and it is not evident that the level of international integration was greater than in the early 20th century. Global firms remained, in practice, national in many fundamental respects, whereas the huge flows of investment – and more important, knowledge and information – within MNEs largely bypassed the majority of the world's population in Latin America, Africa, Asia, and Eastern Europe.