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DIRECT INVESTMENT AND INTERNATIONAL ECONOMIC ORDER

by

Takashi Shiraishi

I. World Economy and Direct Investment

1. World economy as the background

Among the moves of the world economy in the past ten years what has come to draw our special attention is the remarkable increase in direct foreign investment and its economic effects.

True direct investment showed an annual growth rate of 11.3% for 1967~1971 on average and this rate, surpassing that of world trade, was supposed to continue till 1985. J. H. Dunning[1] has commented on this, "The world has entered a new epoch of international capital movement." Indeed this trend has come to be noted not only for its volume but also as expression of a great change in the moves of the world economy itself.

By figures for 1972 the current balance of foreign investment of America has reached 8.1% of GNP, and that of Britain, a traditionally active foreign investor, 16.5%. The balance per capita of population is estimated to be 450 dollars for both countries, and its weight in national income to be considerably great. These figures, however, represent only the balance of investment, not the value of total foreign assets. Since, according to an analysis by the U.S. Department of Commerce, reinvestment in the locality is roughly three times as large as new investment, the economic value of direct investment must be said all the more greater. And their real worth, not book values, must be still higher. In Japan the significance of foreign assets is apt to be ignored, with attention being paid to flows of foreign exchanges. Yet the ways of assets-holding is supposed to become an important theme in view of our pattern of international payments of tomorrow corresponding with stages of economic growth, seen from both the macro-base and firm-base.

Furthermore, appreciation of direct investment increases significance if viewed from the aspect of goods and services produced by it. Now it has become what constitutes the base of world production as well as consumption, governs growth rates and affects the development and pattern of world trade. In fact a large portion of world trade may be produce of direct investment. By an estimate it will make up more than a half sooner or later.

1) John H. Dunning, *Studies in International Investment*, 1970.

However, such a picture of increase in foreign investment had the following features.

(1) The increase far surpassed that of world trade, and mostly depended on American investment. Breaking down the balance into countries as of 1972,[2] America accounts for 52% while the total of Britain, West Germany and France is 25%, and if the above-said reinvestment is taken into account American foreign assets may be tremendous. Of course, although America is thus the mainstay, the rapid growth rates of the Western Europe and Japan since the end-1960s must not be overlooked, and this trend is a natural course by S. E. Rolfe,[3] whose historical progress should be observed.

(2) Direct investment is not simple transfer of capital but package transfer including technology, know-how and managerial ability. This makes a feature indispensable to understand direct investment of today. For this reason emphasis may be put on the aspect that direct investment has provided main pipes for international spread of economic growth and functioned as the bearer of international extension of technical progress and new-product development. This tells its economic significance which cannot be grasped from the customary viewpoint of transfer of factors.

(3) The directions of investment by America, Britain and Germany —putting Japan aside—are mostly toward developed areas, which makes a difference from the 19th century investment. Sixty eight percent of American and 72~75% of British and German investment lie in such areas, gradually intensifying mutual permeation.[4] This is a picture similar with world trade in which expansion among developed nations has been its substance, that is, horizontal rather than vertical trade. It must be kept in mind that such investment to developed countries has been an important factor of recent economic growth.

(4) As the backgrounds of direct investment there have been technological innovation, regional integration such as EEC and industrialization policies of developing countries, providing strong incentives. These should be observed as macro-term push or pull factors and also as the background in terms of the world economy.

(5) A feature as business is the form of the multinational firm, as seen in American investment. Of course this may not be a new phenomenon if viewed differently. Already R. Vernon[5] says tracing back history: "By the late 19th century, while America was importing vast European capital for railway construction and land speculation, on another hand big American makers having production facilities in Canada and Britain had increased to two or three dozens;

2) Dep't of Commerce, Survey of Current Business.
3) S. E. Rolfe & W. Damm ed., The Multinational Corporation in the World Economy, 1970. Japanese tarnsl. by Wada et al., pp. 15–16.
4) Ratios of developed areas in total direct investment as of end-1972: America 68.2%, Britain 72.7% and W. Germany 77.5%. Source: Survey of Current Business; material by the Dreadner Bank and the Bank of Japan.
5) R. Vernon, The Multinational Spread of U.S. Enterprises, 1971.

at the beginning of the 20th century American subsidiaries engaging in production under parents' control are estimated to count 75 to 100 firms."[6] From this viewpoint this feature of today's direct investment may be said a mere difference of degrees. Nevertheless it is a fact that since the latter half of the 1950s this form of business has rapidly grown to work strong effects on the patterns of trade and investment of many nations, posing a problem not to be said a difference of degrees. Now we cannot speak of direct investment without referring to "creation and development of international business systems that make concentrative control over production and marketing subsidiaries of multinationality under single strategy overriding state borders."[7] In fact its importance can be pointed out by many events. Especially a point to draw attention is that these firms are sharply competing and often causing conflicts with national interests or sovereignty, a big theme relevant to creation of new international economic order.

Anyhow, we must consider anew how the behaviour of enterprisers, the bearer of direct investment, has given fundamental changes to the world economy through these features. To look back the postwar thirty years for this analysis, five periods may be distinguished.

The first is the period from the war-end to 1955, that is, economic resurrection and quickening of new growth. It involved two parts of literally important turns. The former part was represented by dollar shortage in the resurrection period, and in the latter part, 1953 and 1954, the gap between America and the Western Europe began to be filled and technological innovation started to cause dynamic cycles in the mechanism of economy. In fact, to observe production indices on 1951-base, all European nations came to show higher figures than America by 1955;[8] the growth rate of world trade reached a level of 8%; the 1953~54 recession of America, with industrial production declining by 10% from the previous year, did not spread to Europe, where a boom was coming by increasing investment. And in 1955 America itself showed an up-turn of business never seen in the past.

The second is from 1955 to about 1963. Important events in this period were the rise of regionalism shown by the birth of EEC, the price fall of primary products including natural resources, and the emergence of the south-north problem. Also international spreading of economic growth was seen, which worked a great impact on American direct investment. In this period, however, there was the recession of 1957~58 which was not a simple decline but involved appreciably dynamic structural adjustment, and is to be noted as an essential

6) It is doubtful whether such empirical analysis of Vernon is meaningful for the theory of today's multinational firms. Refer the writer, *Keizai Kakushin to Kyōsō no Sekai* (*world of innovation, renovation and competition*), 1975. p. 12.

7) The concept of multinationality is varied; this feature is seen in Itarō Irie, ed., *Takokuseki Kigyō* (multinational firms), 1974. p. 4.

8) Twenty-sixth Annual Report of BIS.

background for understanding American direct investment.

In the third period, 1963 to 1969, the basic features were the expansion of the European economy and the dollar crisis due to red ink of American balance of payments. Therein opposition and collision between globalism and nationalism were born, and among developing countries import-substitutive industrialization began to be employed as a pillar of growth strategy. It was also in this period that the expansion of direct investment, regarded as development of the multinational firm, became remarkable.

The fourth period extends to 1973. Creeping inflation became apparent in developed countries, prices of resources rose due to the gap of rate between resource exploitation and economic growth,[9] and catch-up of developing nations pushed developed nations to changing or adjustment of industries. On another hand spread of technology in the developed countries became almost completed, resource transfer among industries was stiffened, and surplus fluidity of currency grew. The increase of direct investment under these situations is conceived to have had positive grounds somewhat different from past ones.

The fifth period is around 1975 when overall economic changes, which had been observed since the beginning of this decade, appeared on the surface causing the well-known rise of oil prices, the protracted simultaneous recessions in industrialized nations, the maldisbution of dollar reserves to oil-producing countries, and further decline of expansive force of world trade itself. True world trade had shown extraordinary growth in 1973~74. Its growth rate, which had been 11% from 1965 to 1970 on average, recorded 15% for 1970~1972, 37% for 1973 and 44% for 1974. Such abnormal growth, however, depended mainly on rises of unit prices; only 5% in volume. Therefore the drop of world trade of 1975 may be said to mean adjustment of price rises.[10]

Here, as the background of such a turn of 1975 in the world economy the advance of the following events is not to be overlooked.

The first is widening of south-north and south-south differentials. World trade had grown in parallel with economic growth of nations up to that time, but for the most part growth had been among industrialized countries, a pattern of horizontal trade. And it should be remembered that such growth had been supported by low prices of primary products and was possible only on it. In the former half of the 1960s industrialized countries could obtain these commodities at low prices and at any time, place and quantity. And in fact this was the condition that rendered scale expansion in the latter half of this decade possible. Many nations widened home markets and regional markets such as EEC, and on this ground trade among America, Europe and Japan was promoted

9) The writer, Shigen Mondai to Sekai Keizai Chitsujo (resource problems and world economic order), *Bōeki to Kanzei*, August 1975.

10) The writer, Sekai Bōeki no Shukushō to Taisaku (shrinkage of world trade and countermeasures), Keizai Dōyukai, Nov. 1975; growth rates by annual report of GATT.

by multiplier effects. This worked to enlarge south-north differentials, as has been often argued.[11] On another hand in developing countries, although the postwar spread of innovation by direct investment of developed nations brought about a base of industrialization, unstability of primary product export always oppressed their balance of payments, import-substitution policies did not advance to any efficient scales due to narrowness of home markets, and hence the differentials against developed countries were still on a trend of increase. This came to the fore gradually in the 1970s and generated differentials also among developing countries, the so-called south-south problem. This was accelerated further by the oil shock, widening differentials between oil-producing and non-oil countries.

The second is the tendency of protective trade born from the dynamic structural changes of trade among developed countries. Formerly industrialized nations had built up their directions of relative superiority under free trade, and as the result, in accompany with product diversification, basically shifted weight to technology-intensive or knowledge-intensive products. This led world trade from homogenizing to heterogenizing. Indeed the trade expansion among developed nations from the late-1960s to the early-1970s was accompanied by structural changes of international division of labor. International competitive power came to depend not always on price factors alone; non-price factors played a substantial role. Just for this reason relative superiority under free trade was maintained mutually, and in reverse competition produced necessity of creating superiority in quality and technology, which oriented export products toward further technology-intensification.[12] This direction, however, was to cause industrial polarization in developed nations, that is, a sector of higher technology- or knowledge-intensiveness and another deserted from this trend. The former comprises R&D-type industries such as information or space, and the latter the fields of textile, miscellaneous goods and agriculture. Of course the former group rests on huge R&D expenditures and involves sectors of strong national concern, and so protection and bring-up policies are required. Again in the latter sector protective color is deep because it includes smaller firms and represents civil-life fields with strong social influences. Accordingly, while free trade is fostering industrial changes to maintain relative superiority as the principle of competition, and working to push high-income structure, on another hand such structural adjustment itself is producing an inclination to protective trade or sale by government's intervention, instead of market approach relying on price structure or private firm's strategy. I think this is to be noted as

11) This is evident in the Reuter Index for thirty years. This worked to offset inflationary effectcs of demand creation and rendered scale expansion with no rises of real costs possible. Refer the writer, *op. cit.*, *Gijutsu Kakushin;* do, Keizai Seichō to Shigen Kaihatsu no Jidai (resource exploitation), *Sekai Keizai Hyōron,* July 1975.

12) The writer, Wagakuni Sangyō no Kokusai Kyōsō Taisaku (countermeasures to international competition in Japan), Japan Trade, Foreign Association, 1975.

a dynamic effect of the two contraries.

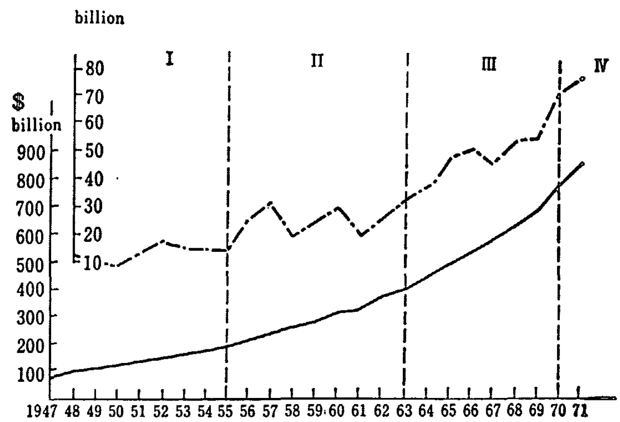
Direct investment may be grasped as what expands itself against such backgrounds, creates dynamic replacement in international labor division and is induced by such changes.

2. Direct investment of America

It may be meaningful to put historical examination anew on American direct investment that has played a main role in that of the world. Through its path we can see several distinctive points as follows.

The trend of American direct investment in book values is shown by Chart 1.

Chart 1.



Prepared from Statistical Abstract, U. S. A.

A very fine upward curve is seen, too fine to mark periodical division, but by taking annual increases, as the curve in the upper part of Chart, four periods are broadly divisible.

The first period is 1947~1954, in which slow increases with little fluctuation were followed.

The second is 1955~1963, a remarkable period of scale-up over the preceding period and big fluctuation.

The third is 1964~1970, showing an evident trend of growth, with an annual increase reaching about 5 billion dollars.

The fourth is 1970 and subsequent years showing some slow-down of increase.

Among these, especially noteworthy is the second because there were a change of direction from Latin America to Canada and a rapid increase toward Europe, and furthermore dynamic factors of growth are seen.

As regards such growth, five factors have been mentioned by J. Behrman:

(1) American home markets becoming narrower and high profit rates abroad;

(2) The birth of EEC;

(3) Intensified application of American anti-monopoly laws;

(4) Favored tax treatment by the government on firms advancing abroad;
(5) Recovery of currency convertibility of EEC countries.[13]

What I should like especially to focus is the first point. In this connection the 1957~58 recession of America must be pointed out as an important event because it was accompanied by a big structural change on the postwar American economy. Of course prior to it America had experienced two recessions, 1948~49 and 1952~53. Yet the 1957~58 recession may be said of different character at least in that it was born from investment cycles moved by innovation appearing since 1955.

True in America private investment became remarkably brisk with the beginning of the 1950s. Its total reached a level of 40 billion dollars, increasing year after year. However, it was only after 1955 that such investment beared fruits of productivity-rise, and spread over the country as an effect of innovation. And at this time over a half of the increase of investment was directed to new equipment, which should prove investment for modernization.[14] Two problems, however, were latently advancing. One was that, although innovation gave vast enterpriser's profits through technical reform, capacity expansion and new products, not all innovational firms were successful, and innovation involved possibility of over-supply due to its immediate spread among firms.[15]

Another problem was that, while investment for automatization, mechanization and new technology widely extended over agriculture, mining and basic energy sectors and brought about not only horizontal but also vertical expansion of industrial organization, it was already the time to question whether such vertical organization of industry—generalized after the war—was really efficient for business. Indeed in 1957~58 reorganization of units from this standpoint posed a big problem.

In addition, market prospects for firms were not bright because fluctuation of investment was being accelerated by changes of defence orders and expenditures for durable consumer goods were widening fluctuation.[16] In fact the profit rate on owned capital, which had been 15.4% in 1950, dropped to about 9~10% in 1957 and subsequent several years. It may have been natural that many firms began to reconsider their vertical production organization and to contrive reorganization of business units orienting to world markets. And in order to win in competition under such situations and obtain enterpriser's profits, firms directed strategy to new-product development in line with behavior and taste of consumers. Another way of response of innovational firms was direct investment. High profit rates of foreign investment was a basic motive to investment abroad, yet comparison against risks was of course necessary and

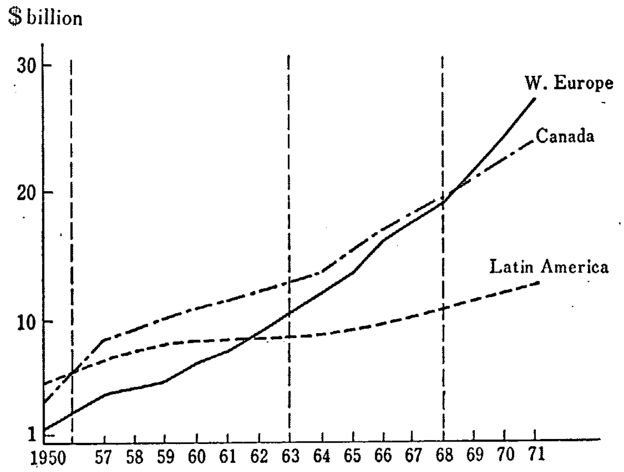
13) Jack N. Behrman, Promoting Free World Economic Development through Direct Investment, American Economic Review, March 1960.
14) F. Molnar, *Economic Growth and Recessions in the U.S.*, 1970, p. 28.
15) See the writer, *op. cit.*, *Keizai Kakushin*, esp. the Schumpeter model.
16) Thirtieth Annual Report of BIS, Japanese transl. by the Bank of Tokyo, p. 42; Survey of Current Business, 1962.

width of markets was a prerequisite. Already at this time in Europe economy was tending to stability after recovery, and the expanded market of EEC increased attractiveness. And needless to say Canada with rich resources and taking active expansion policies as well as developing countries promoting import-substitutive industrialization were regarded as America's exclusive frontiers when other developed countries were still lacking spare capacity. Thus by the moment of this period American direct investment advanced, diversifying itself for borth regions and industrial fields.

As another point, the position of America in world trade was greatly changing at the same time. The late-1950s marked the end of America's absolute superiority on trade. And, as if to replace it, direct investment became active in pursuit of market frontiers. In this sense this was a period of trade → investment turning. And in this historical shift important were the process of sloping from Middle-South America to Canada and the stronger orientation to Europe.

Chart 2 exhibits this. Indeed the 1930s and 1940s were a Latin American

Chart 2.



Prepared from Statistical Abstract U.S.A.

age for American investment. Latin America had close political and economic relations and provided an important source of resources during World War II. After the war the foundation of the Pan-American Union made such relations more definite, and the trade between two regions prior to the resurrection of the world economy completely reflected their inter-dependence. True Latin America belonged to America's economic sphere. As regards the orientation of investment in this period C. Layton says "this backgarden of America seemed relatively safe compared with Europe being split by war," and "Latin America was an important supplier of oil and other resources and provided favorable lands to build new foreign plants."[17] In fact in 1945 American firms holding subsidiaries

17) Christopher Layton, Trans-Atlantic Investments, 1968.

in Latin America counted 93 and in 1950 reached 113. However, this picture was greatly changed through the post-war twenty years. Such firms showed no increase after 1960 and remained unchanged still in 1965~67. Expansion of numbers had stopped, and the stage moved to buy-up of locale firms or unification-cooperation of existing subsidiaries.[18] By A. Sunkel, "American direct investment to Latin America reached its peak in the mid-1950s and a maturity period by the latter half of the 1960s.[19]

As the Chart shows investment to Canada surpassed that to Latin America already in the latter half of the 1950s. Originally foreign capital in Canada was by British investment in public loans and securities, but gradually direct investment came to replace it and today American investment has grown up to command Canadian industries. Positive backgrounds of such active investment were firstly rich and varietiful resources, secondly expansive national policies and strong tariff protection and thirdly racial homogeneity as neighboring nations.[20]

In fact in Canada important resources adjacent to the American border have been exploited one after another and most of her population dwell in regions near to America. It is not too much to say that the Great Lakes region forms part of America's economic sphere. American investment in such Canada was contrastive to British in many points. While Britain's investment had been traditionally in railways and public utilities, America's was direct investment in industries raising profits far above Britain's. And also after the war Britain's profits have been lower, and the selection of investment objects is said less successful. Anyhow in 1960 American investment in Canada made up 35% of her total direct investment, and to view from Canada's side 80% of total was American in 1964.[21] A feature of such American investment was that in 1960~68, a period of its expansion, it increased at almost the same rate over all industries. This tells the large variety of investment-worthy fields and Canada's national industrial policy.

Of course orientation of investment to manufacturing is observable. For example, it accounted for 44% in 1968. Canadian manufacturing had developed to supply necessary basic goods to resource industries and to make processing of materials directly, and to answer demand of home markets expanding with increases of population and income indirectly. Yet doubtless attractive to American firms was protective tariff, which invited investment in manufacturing, resulting in increases in Canadian exports. This may be said a natural result of the economic relation between the two countries. Yet it should be noted, as was stated in the Watkin's Report, that in the industries of auto, rubber,

18) Vaupel & Curhan, *The Making of Multinational Enterprise.*
19) A. Sunkel, *The Pattern of Latin America Dependence*, p. 16.
20) *Watkins Report*: M. H. Watkins, *Foreign Ownership and Structure of Canadian Industry*, Ottawa, Privy Council Office, 1968.
21) *Watkins Report, op. cit.*, pp. 10–12.

chemicals and electric equipment American capital governed respectively 97, 90, 54 and 66%.

Again in the Chart it may be seen that direct investment to Europe was increasing at a very high rate compared with Latin America and Canada, and by 1968 it surpassed Canada in absolute terms.

Primarily American investment to Europe was overwhelmingly centered on Britain, with its balance in 1960 making up one-third of total of Europe. This was because this country was important as a foothold of advance into the British Commonwealth and at the same time was the core of European regional economy. And investment was centered on new-technology industries, and American firms dwelling in Britain were growing to fully completed organization.[22] However, since about the birth of EEC American investment began to increase toward the six continental countries.[23] To observe growth rate on a 1950-base, Britain was 143% and EEC 176% in 1958. Although at this time in absolute terms EEC was about one-half of Britain, growth was obviously higher for EEC. By the 1960s investment in the Western Europe came to show 30% of total, near 20 billion dollars, in which EEC was an essential factor.

For such increase in direct investment in EEC reasons are conceivable as follows:

(1) Market expansion by abolition of intra-region customs;

(2) Increased demand for capital and economies of scale;

(3) Rises of income levels by economic growth;

(4) Expectation of creation of trade;

(5) Response to possible emergence of trade conversion effects.

Of course it is not difficult to suppose that at the beginning EEC's future involved too many unknowns to most American firms. In fact the American Management Association expressed prospects on it as follows:[24]

(1) In view of too rapid technological and economic changes, forecast about Europe for ten years to come is indefinite;

(2) EEC is scheduled to developed gradually, and the charatcer and effectuation of the treaty itself are not clear;

(3) Joining of Britain, Scandinavian countries, Switzerland and Austria is not clear, and hence great changes of its economic character and scale in future are supposable.

(4) Attitudes of the Six to common monetary and banking policies are uncertain, and hence possibly in recession times these countries will fortify self-guard of themselves rather than of EEC.

22) J. H. Dunning, *op. cit.*, pp. 206–233.

23) The writer, Beikoku no Chokusetsu Tōshi to EEC (American direct investment and EEC), Keizai Chōsa Kyōgikai, *Takokuseki Kigyō to Keiei.* (Multinational Enterprise and its Business Administration), 1975.

24) AMA, *The European Common Market, New Frontier for American Business,* 1958, p. 58–60.

Thus at this time 1958 a general view was that its effects were impossible to grasp. And, what affected American direct investment more strongly than such ambiguity in EEC may have been the following features:

(1) Presence of south-north differentials divided by a diagonal line within the region;

(2) Latin traditions and their effects;

(3) Nationalism and regionalism in consumers' character;

(4) Communism and the sense of intellectual superiority against America;

(5) Despotism and concentration-tendency of enterprisers, and family-group ownership on business;

(6) Tight connection with customers and distribution systems;

(7) Value orientation of hand-made goods.

An aspect must be considerd that the foundation of EEC itself was not the reason of rapid increase in investment. Nevertheless it is conceivable that EEC stimulated behavior of American business right because in 1957~58 American firms were pursuing higher profit rates and new production-demand combination in world markets.

After, 1966, however, American direct investment to Europe showed a notable increase and was especially accelerated after 1969. This was a period when EEC came to possess a large market scale and growth potentiality, and when American-type labor-saving production systems increased importance due to manpower shortage. During the seven years after 1966 investment to Britain increased by 9.2% annually while to EEC by 14%, telling that for America investment to Britain had passed its peak, that to non-EEC European countries got slow-down, and concentration on EEC was intensified.

3. Direct Investment of Western Europe and Japan

As is well known, the economic growth of developed nations was accelerated after the latter half of the 1960s. In America, after the 1962~63 recession private investment rose straight and expenditures for new plant and equipment reached a high level. Again in Europe and Japan growth constantly raised its rate and expanded its scale. Reflecting these, industrial structure changed in each country, horizontal trade among developed countries expanded, and at the same time direct investment by other countries than America increased.

As regards EEC's economic growth the following points shall be mentioned.

First, its gross production PIB rose from 188.4 billion UC of 1960 to 478.2 billion of 1970, some 2.5-fold.[25] This was remarkable after 1967.

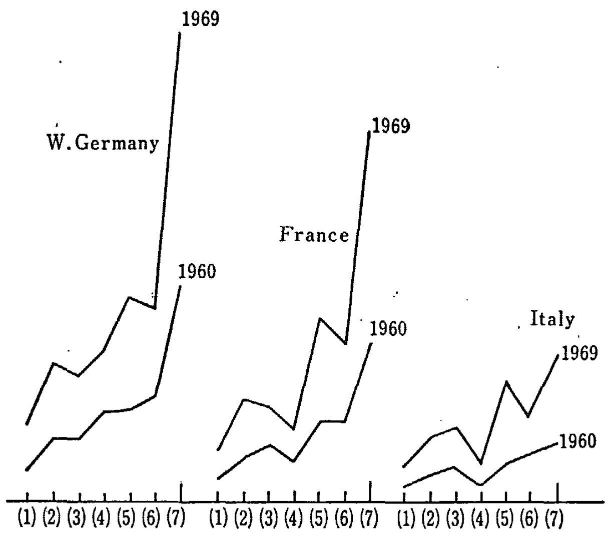
Second, differentials of scale among the Six were still wide. For 1960 Germany made up 38% of total PIB of EEC and France 32% while Italy only 18%, one-half of the two countries. Three Benelux countries held the rest,

25) *La Concentration des Entreprises dans la Communaté Economique Européenne*, 1974.

still larger differences. And in 1970 Germany developed at a rate over the EEC average, while France remained stagnant, and hence also between these two countries differentials were widening. Although EEC should be evaluated as a unity such large weight of Germany and France must be noted. Anyhow EEC showed 9.7% growth of PIB per annum during these ten years, and especially in the latter half of this period highs of 12~15%.

The third point is structural changes of industry. To observe manufacturing of Germany, France and Italy between 1960 and 1969 there were not only differences of growth rate but also of scales of industries. Chart 3 exhibits

Chart 3.



Prepared from source in Foot note 25.

comparison between the two years of PIB for seven industries of 1) ceramics & glass, 2) wooden furniture & paper, 3) textile, 4) basic metals, 5) oil & chemical products, 6) food & drinks and 7) machinery. Growth in furniture-paper is seen for all countries, and jumpy development in oil-chemicals and machinery is noticeable. To look relative growth rates among the three nations, however, in France growth is with food and ceramics and in Italy with textile. Thus EEC shifted to new industrial structure through the process of growth, yet actually scale differentials were widened and there was no reverse of superiority. This is a noteworthy point and must be kept in mind in understanding the direction of investment in EEC.[26] That is, in EEC industrial adjustment was advanced on relative superiority through trade liberalization and transfer of factors, and direct investment was performed along this line. This tells that structural changes did not lead to reverse of superiority, if to homogeneity.

Now we shall observe flows of direct investment from outside and toward outside of EEC against the background of such growth. Of course beside these

26) The writer, *op. cit.*, *Keizai Kakushin;* figures by *op. cit.*, *La Concentration.*

two directions intra-Six investment must be considered, which ought to be said a large mark point. Data about these flows are still insufficient, yet according to a survey of EEC Commission[27] four categories can be distinguished: 1) from member countries to third countries, 2) from third countries to members, 3) from members to members and 4) between firms of the same country. Firstly in the former half of the 1960s the category 2) (from third to member) showed a sharp increase, and in the latter half 3) (between members) grew rapidly and 1) (from members to third) showed a slow rise, bringing about a notable increase in 1967. By industries, advance from third countries to members was numerous in electronics (46.4%), medical goods (39.7%), paper (35.7%) and machinery (32.3%), while mutual advance between members was seen in chemicals-petrochemicals-plastics and electric equipment. Anyhow an important fact here was that, while investment from outside was brisk, EEC itself had grown to make outward investment.[27] Of course great differences lie by countries. Germany is most evident in this phenomenon of turn, from receiver to investor, with 1966 making the turning point. For France investment from third countries rather increased in 1969 and 1970, and again in Benelux and Italy there were small increases. So the increase from EEC to outside must be regarded to depend on Germany's rapid increase, and such turning to investor is not so clear except for Germany. And there are differences of regions and industries between Germany and France. That is, Germany oriented one-third to North and South American continents, and the industries, on average from 1952 to 1970, were in the order of chemicals (24.7%), electronics (11.7%) and auto (9%), while for France the major regions were non-EEC Europe and French Community countries, and the industries were for 1970 oil (46%) and trade (28%).

To summarize, direct investment from third countries to EEC increased, with 1964~67 taking a peak, to create new industrial structure there and to cause transfer and spread of innovational firms. At the same time it produced countermoves of firms, promoted mutual business approach within member countries, and by the end of the 1960s resulted in the increase of outward investment.

Then what characteristic features can be observed in the economic growth and direct investment of Japan as a developed nation?

Of course in the former half of the 1950s Japan was still on a stage of contemplating how to attain econmic self-dependence. A remarkable event in this period was participation in the emergency procurement program of American Army, the so-called special demand. It accounted for most part of Japan's foreign exchange receipts at the time and doubtless contributed to the production level. It stimulated production of traditional goods, and at the same time it meant an opportunity for Japan to contact with different industrial technology and organization and to accept various impacts. However, recovery of life-goods production was being considerably delayed, and with the end of the Korean

27) *Investissements directs des pays de la CEE dans la Pays tiers*, 1974.

turmoil an adjustment period came in which a gap between production and demand sharply expanded, worsening balance of payments. Expansion of export was considered to be the sole solution of this gap, a memory still alive in us.

Exports expanded sharply after 1954, showing annual growth of 28% (1954), 23% (1955) and 18% (1956). A cause for such favorable trade was true the recovery of business in America as well as many other countries. The rapid growth of consumer demand in America, caused by the above-said dynamic trend, was just what enhanced export of Japan's traditional superiority.

Thus it may be said that in the latter half of the 1950s the cycle of innovation[28] of America exerted two effects on Japan.[29] One is the said consumption boom and another is brisk absorption of new technology, equipment and products. Introduction of capital and techniques increased. Renovation permeated in our industrial organization, working gradually to reform industrial structure itself toward the former half of the 1960s. But here two particular pictures of Japan is seen.

The first is that at that time there was rigid regulation on foreign capital, and hence the American global advance was not the main player. Rather Japan's response was active introduction of technology by firms striving for enterpriser's profits under protective trade aiming at import substitution. It tells a particular picture of Japan's businessmen of this time that a large number of inspection teams visited America after 1955 in order to absorb not only technology but also business management and strategy.

The second is that by such spread of American innovation Japan's industrial structure was improved on the presupposition of international competition. Of course, as a result in the fields of metals, machinery and chemicals production raised growth rates and the structure became higher, yet on the aspect of export traditional products still remained in its composition, making a structural problem in the former half of the 1960s. It may do suffice to remember that the main theme of the Five Year Plan was how to fill this gap. In other words, although introduction of innovation was for import-substitution, it was insufficient to improve export structure, the balance of payments was always restricted by traditional export, threatening growth by credit creation.

Under these situations in the 1950s Japanese foreign investment in manufacturing was meagre. The mainstay of advance to abroad was commerce corresponding with export growth, with only some part of traditional export sectors advancing into Asia and Middle-South America in a small scale. The pattern of investment described referring to EEC here applies, that is, it is governed

28) This is empirically a Kondratiff cycle, but theoretically I wish to have it taken as "a development cycle representing non-sequential replacement due to emergence of innovational enterprisers." Refer the writer, *op. cit.*, *Keizai Kakushin*, Chap. 6, Sect. 3.

29) The writer, Utsuriyuku America no Shōhi Shijō (changing American consumer markets), *Tōyō Keizai Shimpō*, Dec. 1958.

by trade and industrial structure. Direct investment, which began to appear in the latter half of the 1950s, was that in manufacturing to developed countries and in commerce to developing. This pattern was not changed through the 1960s, which makes a characteristic of Japan's direct investment.

The growth process of Japan's economy, however, came to show drastic changes in the latter half of the 1960s.

First to mention is the rapid growth of export. Its annual growth rate, which had been 15.1% in 1955~1960 and 15.9% in1960~1969, appreciably high, further rose to 19.3% for 1965~1969, with considerable expansion of market shares. Of course this was backed by the favorable growth of world trade and markets, yet in the back scene of share expansion there were rises in labor productivity and resultant decreases in labor costs. Such productivity improvement was born from growth of investment, and that it was notably in heavy-chemical industries was the ground of such share competition.[30]

The second point is the large increase in equipment investment. For the four years after 1965 its annual rates had been over 20%, and that representing innovational big-sacle investment. Innovation comprised three aspects. One was enterprising of new products, which may be evident by the fact that these goods made up more than a half of industrial production increases. Most new products were born in the latter half of the 1950s and some showed expansion of production, but it was in this period of after-1965 that their producers became of big type. Another aspect was adoption of labor-saving or capital-saving technology. This can be expressed as substitution of capital or labor, different from creation of a new production such as new products. The third was cultivation of new markets. This was exhibited in the active fortification of sales power in foreign markets as well as formation of domestic routes and expansion in the tertiary industrial sector.[31]

The third one of drastic changes was the rapid growth of personal consumption and its grade-up and diversification. Entering the so-called third-round baby boom consumption scales of food, clothing and dwelling rose, which invited growth of tertiary and consumption related sectors. In the fields of textile, household electric appliances, cars, food and so on there was mushroom birth of innovational firms, which created a big cycle of sales expansion through mutual response under the mechanism of market competition.

Of course such expansion in itself led to export growth, which in turn rendered further scale expansion possible, cummulative and multier effects. An important point here is that the expansion of export destructed previous walls of international payments. This makes a great difference of this period from the former half of the 1969s.

30) MITI, *Tsūshō Hakusho* (trade white paper), 1970 issue.
31) As for illustrative examples by industries see the writer, *Wagakuni Sangyō no Kokusai Kyōsō Taisaku* (countermeasures for international competition in Japan), by Japan Trade Association.

In this period Japan's direct investment of course increased. But the increase was made in the first three years of the 1970s rather than in the 1960s. To look by statistics of licences of overseas the increase from 1960 to 1972 registered as high as near 65%.[32]

As the reasons for such growth of direct investment four points may be mentioned in respect of economic situations home and abroad.

(1) Protective tariff in developing countries accompanying their policies of import-substitutive industrialization, and bring-up and invitation of export industries, and active attitudes to foreign capital introduction on the condition of such policies.

(2) Necessity of defence of export markets against local production and scale by direct investment of America and Europe.

(3) Increase of demand for resource exploitation accompanying production growth in developed countries, especially Japan, and need of stable supply.

(4) The most-favored treatment given to developing countries in 1971 caused competition in the customary export markets, and on another hand worked strong impacts on domestic import-competitive goods sectors, which came to necessitate adjustment of industrial structure as countermoves of firms as well as from mast macro-standpoint. Notably in case of traditional sectors adjustment had been already required and its one way was moved to developing countries.

II. Direct Investment and The Multinational Firm

1. Incentives to direct investment

Then what were the causes of such increase in direct investment? Some explanations have been given in the foregoing description of world-economic backgrounds, but consideration shall be made anew here.

Before going into this discussion, it must be pointed out that, looking as a broader category of international investment, three great differences are found between the present and prewar days.[33]

The first point is that prewar international investment was exclusively from Europe while today America makes the principal investor.

Secondly prewar investment was basically private investment while today additionally government investment and aid are mixed.

Thirdly, while in prewar days investment in securities was the main form, after the war direct investment is playing the main role, which is closely connected with development strategy of developing countries themselves, in place of plantation investment of colonial types.

The most characteristic feature of today lies in this form of direct investment.

32) Money values of licenses by laws on trade and foreign exchanges, by the Bank of Japan.

33) Gilles Y. Bertin, L'Investissement International, 1967, Jap. transl. by Noda, pp. 17–33.

This can be divided into three types according to motives or objects, that is, resource-oriented, low-wage oriented and market-oriented. Actual motives are varied, for example, 1) sale of export goods on locale markets, 2) market defence, 3) market cultivation or 4) export to third or home countries.[34] Anyhow, what I wish to stress here is that such advance represents a result of strategic consideration of response to environments.

Then what were the environments that produced such response? To divide into push and pull factors they are as follows.

(A) Push factors

The first one is the mechanism of overseas transfer inherent in the product cycle itself. This means, as is popularly known as Vernon's chart[35] or Hirsh's model, that a product has a life cycle of introduction, growth, maturity and decline, and along this flow its production moves from developed countries to other developed countries and then to developing. At the stage of introduction such factors as scientists, engineers or outer economy have important roles, and hence countries with superior endowment of them are more favored in production. In the growth stage an element of management ability to control production becomes important because mass production is employed, and countries superior in this aspect are advantageous. Further in the maturity stage what determines superiority in production is whether unskilled labor is affluent rather than special technology because most products are standardized. In other words, developing countries are more suitable. This is a phenomenon seen actually in the sectors of electric household appliances and primary-processing textile goods, and may be said an empirical law explaining international moves of industries. Most current theories on the multinational firm stand on such a Vernon-type idea, and are noteworthy in their correspondence with the principle of international labor division determining directions of export and import. This may involve many problems about generalization of empirical laws common in the Harvard business School. Yet it may be at least pertinent to point out that such a push factor exists as national business behavior deriving from the inner aspect of product cycles.

The second push factor, what is relevant to the first, is that home industries will be obliged to move to abroad as a countermove to international competition. With the progress of industrialization in developing countries, industries and products of low-grade processing are inevitably exposed to catch-up. In such a case if room of product changing is domestically found it will do well, but if not strategic response either by grade-up of processing or a move to over abroad will be inevitable. This is intensified also by the above-said favored-tariff and is all the more necessary when, as is today, developing countries are enhancing

34) Genchi Hōjin no Tōshi Dōki (motives of corporations abroad), material of Bank of Japan.

35) R. Vernon, International Investment and International Trade in Product Cycles, *Quarterly Journal of Economics*, May 1966.

inland primary-processing to increase added values of products. And foreign advance against such backgrounds will be accompanied by structural changes of international division of labor.

The third is increasing scarceness of resources. Resources are varietiful including oil, iron, copper, coal, wood, etc. They are different in economic character and their states of presence in absolute terms are varied by countries,[36] yet it is a fact that the past economic growth of developed countries depended on the cheap and stable supply of these basic mterials. Oil had entered an over-supply period by 1953 and official prices had to be cut as much as by 15% in 1959~60 in order to meet actual market positions. Copper also had a protracted period of low prices from 1957 to 1964, resulting in autonomous production curtailment and buying-support by LME. Nickel began price rises since the latter half of the 1950s due to its nature, yet prices remained unchanged from 1957 through 1967. Similar was bauxite. As the result of high grwoth, however, scarceness advanced in owned resources, and secure of stable supply became a big problem for the national economy as well as utilizer indusries. Thus advance into foreign resources by participation in management or joint exploitation, in place of purchasing, has been generally performed. This is different in nature from the advance of manufacturing yet a point to be mentioned as a factor.[37]

The fourth is a factor lying in the growth of firms itself rather than being an environment. For example, as long as firms are to procure and utilize managerial resources on the principle of minimum-cost combination, under the internationally disproportionate distribution naturally location at internationally optimal places must be considered. And if growth means expansion of business scales, on this process the so-called Penrose restriction[38] works, which may always require organizational adjustment including the divisional system, shift of units to foreign countries, so to speak, an autonomous form of development of organization and market. This is a factor originating from firm's behavior, a micro-factor to be distinguished from the above-mentioned three factors. Anyhow, it seems necessary to take into account such an inner factor in order to give logical explanation to the present pattern of direct investment.

(B) Pull factors

The first is of cource concrete growth strategy of developing countries. After the war these countries were faced with stagnancy in export of primary products, low rate growth and red-ink balance of payments, and as a measure to solve these interwound situations industrialization of two types was oriented. The one was transplanation of export industries on an outward-looking standpoint and the other was import-substitution policy on an inward-looking standpoint.

36) A thinking to divide Ricard-type scarceness and Malthus-type scarceness is explained in the writer, Keizai Seichō to Shigen Kaihatsu no Riron (theory of economic growth and resource exploration), *Asia Keizai*, Dec. 1974. vol. 12.

37) The writer, Shigen Mondai to Sekai Keizai Chitsujo (resource problem and world economic order), *Bōeki to Kanzei*, August 1975.

38) Penrose, *The Theory of Growth of the Firm*, 1968.

The former is promotion of export industries by foreign capital as has been in Korea and Taiwan. The latter, typically seen in Brazil, is to introduce foreign capital for inland production of customary import goods and, once it has started, to give protection by tariff and other means in order not only to save foreign exchanges but also to absorb employment and raise people's technical levels. Accordingly foreign firms tend to turn to production and selling in the locality in place of export. This import-substitution policy was most actively taken between 1958 and 1969, and thereafter advance of firms along this line became numerous. Another policy of export-industry transplantation was employed for two aims of international payments and industrialization, and cases of advance motivated by it were appreciable numerous. These two policies, however, are not always adoptable and actually are mixed in general policies. For import-substitution, even if inland production is possible, is accompanied by high costs and shift to export industries is not easy, resulting merely in saving of foreign exchanges and inclination to inflation. Again, bring-up of export industries, even though industrialization for export has been advanced, level-up of industrial structure does not follow. However, it is a fact that advance of foreign firms was derived strongly by such strategy.

The second pull factor is the most-favored treatment given to developing countries. Its background was the expansion of south-north differentials mentioned already. As was asserted by the UNCTAD, under a situation that developing countries were unable to grasp moments of advance by aid from developed countries alone, what was necessary was market-opening by the latter countries. If markets restrict industrialization it must be said natural that cooperation by favored treatment is required to developed countries as markets. However, this affects two aspects. The one is that non-tariff import from developing countries oppresses home industries lying in competitive positions, which may necessitate industrial changing or moves to abroad. The other is that competition with developing countries on third markets becomes disadvantageous by that much, dealing a blow on export to there. If so, firms must move production facilities to developing countries to take advantage of such favored treatment for export. In fact advance of this type is supposed to count a considerable number.

The third is regionalism internationally seen. Although EEC developed from liberalized markets within the region to a common market in the end-1950s, this inevitably caused distriminated trade for outsiders, and hence advance into this region for market defence or for potential growth was natural. Such regionalism extended not only to EEC but also LAFTA and other regional organizations, which now make a presupposition in considering the world economy. This is similar for firms. For firms decision of patterns of strategy of overseas approach —whether export or patent sale or direct advance—is based on market scales and tariff walls. In this sence foundation and development of free trade areas or common markets greatly affect business strategy, possibly leading to selection of direct advance.

2. Logic of the multinational firm

Now let's place focus on the multinational firm—a concrete form of direct investment and the most modern feature—and consider its logic as a future bild.

J. H. Dunning says it makes a great characteristic point that firm's foreign advance of today takes a form of multinational firm, and many theorists take this as if a self-explanatory theory in their discussion.[39] However, the concept of multinationality is not always clear. Nevertheless today people regard as direct investment=firms advance=multinational firm because this identity not only expresses the historic character of direct investment but also a result of firm growth, and this pattern is grasped empirically as an inevitable step. This is just an evolution theory of firm growth, as will be explained later. Anyhow, in various theories the logic and future Bild of the multinational firm are carved in relief so it may be said.[40]

It is R. D. Robinson[41] that I should like to take up firstly. He defines patterns of international firms as stages of growth by the place where authority of decision-making on overseas activities lies, that is, 1) Domestic, 2) Foreign-oriented, 3) International, 4) Multi-national, 5) Transnational and 6) Supernational. And firm's foreign business develops from 1) annexed trade division to 2) independent trade division, further to 3) central division of overseas activities and becomes 4) multinational firm. This last form has a nationality but gradually transfers to a form of ownership and management by people of two or more nations as 5), and lastly to Supernational 6) where inter-race opposition is adjusted by government agreements. By his prospect for 1972 and later many 5) and 6) firms develop amounting to 300 firms with annual sales of 160 billion dollars. Of course such development is achieved through dynamic mutual effects of home and foreign oppression and inner reform of management, and as a result of within-firm friction accompanying growth of foreign sales, or rivalcy of loyalty between home and abroad.

However, it must be said H. V. Perlmutter,[42] a representative theorist of this theme standing on the theory of evolution, that has given great influences by referring to the future picture of society. He classifies growth into three patterns; 1) Ethnocentric (home-oriented), 2) Polycentric (locality-oriented), 3) Geocentric (world-oriented). In the pattern 1) important decisions are made by brain staffs of the home office. Subsidiaries have no authority of decision,

39) The writer, Book Review, *Dunning; Studies in International Investment, Kokusai-keizai*, 1972.

40) Itaro Irie, *Takokuseki Kigyō no Milaizō* (future figure of multinational firm), Sekai Keizai Hyōron, June 1974.

41) R. D. Robinson, *International Management*, 1967; *do, Beyond the Multinational Corporation*, 1972.

42) R. V. Perlmutter, Tortuious Evolution of the Multinational Corporation, *Columbia Journal of World Business*, Jan.–Feb. 1969; do, The Multinational Firm and the Future, *The Annuals of American Academy of Political and Social Science*, Sept. 1972.

receiving one-way advices from the parent in the home land, and important posts are taken by men dispatched from home. Actually most of multinational firms come under this type yet this is not multinational in a true sense. In the pattern 2) decision-making on daily or customary affairs is delegated to subsidiaries, but that on finance, technological development and other important matters is reserved at the main office, in which authority transfer is made from a view that native-mode behavior is advantageous. This also is not the ultimate figure by Perlmutter. Then the pattern 3) appears, in which a group of subsidiaries and the home office are organically interrelated to deploy business activities on a global base, and most effective solution within the overriding state borders is intended. Such Geocentric firms are the true figure of the multinational firm, thus he concludes.

The point lies in his prospect of realization of the the new future society —global industrial system (GIS)—during the remaining thirty years of the 20th century, which he divides into three stages. He calles 1970~80 the age of national global system, in which governments of developed countries encourage foundation of private and public enterprises of big scale that may bring about multinational-grade profits, and thus regional or global industrial constellations are founded. The second stage, 1980~90, is called the age of bi-national, tri-national and regional global-system. On the third stage lastly comes the age of Geocentric system when firms of multinational and super-big ideology, firms of non-national big ideology and global systems of industry, finance, trade and service play the main role. Furthermore he forecasts that by 1985 50% of world production will be made by 300 super-big firms, and firms that can survive to this age and success will be only a handful of mega-firms or petty firms.

In contrast with this argument from the logic of business, a new angle of prospect of international business has been shown by J. N. Behrman.[43] He says there must be three alternative routes in future:

1) a customary pattern in which decisions are made by a business center placed in developed countries preserving national color, 2) a pattern of international-color development based on inter-government agreements and 3) diffusion of structure of ownership and control. This is a view paying more concern to environmental changes, and emphasis is shifted from the principle of efficiency to that of equity. As the methods of internationalization he mentions 1) private internalization (diffusion of ownership, participation of foreigners in personnel affairs), 2) international investment charter, 3) file on the U.N. in order to avoid direct intervention of home governments and 4) inter-governmental adjustment. And as new future systems joint production agreements, inetrnational corporations for joint social development, and international organizations for industrial integration are presented. This theory may be said to give many sugges-

43) J. N. Behrman, *The Multinational Enterprise in 1976 and After: A Revolutionary View*, 1972.

tions about the relation between multinational firm and international economic order to be discussed in the below.

Lastly let's see another view of J. M. Stopford.[44] This view refers to future patterns of organization and ownership. Firms have become multinational in pursuit of economies of scale, yet this is becoming an uneconomical system because problems of time and costs are arising such as 1) shortage of big-type managers, 2) increase in information-system costs and 3) increase in expenses of meetings and education. Also as regards ownership, joint ownership will shift to perfect ownership but a direction toward nationalization is inevitable. So international business must place emphasis on technology impossible to substitute and export to third countries. Now, by these views it may be said that angles different from the customary theory of evolution are found among economists, and such prospect as straight development of the multinational firm is not a general view. In fact these firms are causing many conflicts with environments. So next we shall inquire into such conflicts.

3. The multinational firm and locale conflicts

Conflicts with advancing firms in developing countries involve three aspects.[45]

The first aspect is gaps between the business behavior and strategy of advancing firms and the development policies of host countries.

The second is impacts on the traditional society modernization=industrialization exerts.

The third is cultural gaps between advancing firms or dispatched men and natives.

Of course these are not indifferent each other and will be mixed in any actual conflicts. However, the problems involved in these three aspects vary in quality, and what is most essential to advancing firms, whether multinational or not, may be those born from the first aspect. This is because developing country's strategy, while inducing direct investment, inevitably causes gaps against the logic of business behavior.

Here we shall again put the import-substitutive industrialization policy on analysis. This strategy expects at least four points as below, of course varying by countries.

(1) Foundation of foreign-capital firms will increase employment and absorb latent unemployment, namely employment effects.

(2) Modern technology may be learned and quality of labor be raised, namely learning effects.

(3) Growth and bring-up of national firms will become possible by gradual raising of the rate of inland production, namely inter-industry effects.

(4) Inland production of import-dependent goods saves foreign exchanges,

44) John M. Stopford & Louis T. Wells, *Managing the Multinational Enterprise*, 1972.
45) The writer, Takokuseki Kigyō no Conflict no Ichi Dammen (a section of conflicts with multinational firms), *Kaigai Jijō*, No. 6, 1974.

namely international payments effects.

Supposedly these are the merits of this policy for all developing countries.

Then, form another viewpoint, what appreciation is given by foreign-capital firms introduced on this policy?

Since primarily import-substitution itself suggests presence of home demand and its future increase accompanying economic growth, these firms will consider that advance has a market merit so long as demand for their products is not temporary but has prospects of expansion.

Second, if other firms or countries receive favored tariff treatment after advance, present export will be dealt a blow and so strategy of advance rather than export will be taken for defence of markets, a strategic turn from export to direct advance.

Third, after start of production, if of high costs, locale sale will be possible by tariff protection, and as another merit supply of materials, equipment and parts to the locale will be given favored treatment at least for some period and export of these goods can be increased. In fact in most countries in case of import-substitution 100% inland production since the beginning is not required. Usually only a gradual rise of the rate is indicated.

Fourth, taxation and other privileges will be given for advance, of course depending on the country's basic thought on foreign capital, and so firms may judge that receipt of such benefits by earlier advance is more advantageous. Indeed privileges of this kind tend to be decreased as time passes.

Thus merits for advancing firms cover a wide range including market defence, favored treatment, expectation of export increase of parts and other goods, and exploitation of present as well as potential markets without competition. However, generally advancing firms will face various managerial problems as follows.[46]

(1) Procurement of working capital is difficult.

(2) Although subcontract processing at the locality is possible by the inland-production promotion policy, costs are high and quality is low.

(3) Mass markets are absent because of economy-of-points and hence locale selling is inefficient.

(4) Labor is of low quality, the illiteracy rate is high, and so technical training requires long time. Also labor fixity is low, making inner accumulation of techniques difficult.

(5) Management ability as modern enterprise is short.

(6) Collection of information is difficult due to undeveloped communication facilities.

(7) Reliability of statistics to use for scientific researches is low.

It is indispensable for firm's strategy to overcome these seven conditions, apart from the said four merits.

46) Refer the writer, Brazil ni okeru Nihon no Shinshutsu Kigyō (Japan's advancing firms in Brazil), *Keio Business Forum*, 1971, No. 11.

First, locale subcontracting is inevitable by government's request, but the higher the inland production rate, the lower becomes the business efficiency due to involved defects. And so often measures to lower dependence on outward orders are taken by raising inner processing. Since subcontracting and inner processing are the same in being inland production, this measures does not in appearance contradict with government's request, but it reduces development-strategic worth of the import-substitution policy, i.e. bring-up of surrounding industries. Especially if the so-called forward-relevant effects are expected for development, a gap between business behavior and development strategy arises because such effects are not produced.

Under the condition of low labor quality and scarce skilled labor, labor costs rise unless wage rates are relatively low. So advancing firms will contemplate to transfer modern equipment of labor-saving technology or to build anew, and plan operation suitable to unskilled labor. In fact there is a problem that in developing countries employment rates remain low[47] and absorption of latent unemployment is unsuccessful despite high growth rates of manufacturing. One of its reasons lies here. This means that such response of firms will fail to produce employment effects expected in import-substitutive industrialization, and a possible gap between the two.

For the reasons of low education levels and long time for engineer bring-up firms depend on dispatch of personnel from homelands side by side with the said mechanization. And the low labor fixity decreases the effect of planting modern techniques among laborers. Accordingly the import-substitution policy aiming at learning effects will be fruitless in the short run, if effective in the long run.

On another hand the inefficiency of selling due to the economy-of-points gives a big restriction to firm's mass production system. It gives a substantial restriction if the condition for cultivating competitive power by import-substitution or protection lies in the realization of economies of scale by expanded markets. And if firms advance into the same field competitively regional price differentials will be born, rather than price-cut for market shares, or there is a great probability of an oligopolistic situation in a region.

Thus the problem is that firm's strategy, if rational in itself, reduces expected effects for government's policy. Accordingly if targets or expectations of a developing country is high, a change of appreciation on foreign-capital firms will naturally be caused. However, here remarks of Hirschman should be remembered. "Although cooperative and creative elements in enterpriser's spirit are equally important, it is obviously difficult to keep balance between them. Absence of the cooperative element in developing countries is the result of too strongly self-centered understanding of progress, and the resultant spread of

47) W. Baer & M. E. A. Herice, Employment and Industrialization in Developing Countries, 1966.

tension and antagonism among people."[48]

Of course these situations may be different for resources industries.

First, economic merits of introducing foreign capital for resource-endowed countries can be reduced to three points; 1) resource utilization effects, 2) demand effects and 3) factor employment effects. Yet exploitation of resources by foreign capital does not always conform with the interest of the country.

First, the biggest problem is sale prices. For if prices are determined by foreign firms and cheap-price export is performed to homelands, receipts of the resource-endowed country are decreased by that much. In fact the conflict between Anaconda and Chilean government was on this point,[49] as is well known. Reversely if transacted at high prices, this becomes increase in profits of foreign capital in the end.

Second, according as mining advances for long, rights on mine fields are extensively set up by foreign firms, and these mines are left unexploited until currently operating mines exhaust their lives. Thus the primary expectation of resource utilization is not fulfiled, and the scale of expected production increase is decided by foreigners.

Third, what seems to make the biggest problem for these countries is that the entire economy depends on resources. Public revenues, foreign exchange receipts as well as the industry itself are decisively related with output and export of resources. If their resources are exploited and sold by foreign firms the base of the entre economy is controlled by their strategy and decisions, making government's autonomous planning impossible.

Fourth, since reproduction of natural resources is impossible their deposits are limited. And since the right of land utilization and that of ownership make two sides of coin, people hold fears about nationality of land.

Thus advance of foreign firms does not always become interests of host countries, and contradictions are inevitably borne by firm's rational behavior. Furthermore as regards the multinational firm, because its principles of behavior are global and it contrives effective distribution of business resources over the whole world market, often its decision-making does not agree with national interests. And if a large portion of home industries were owned and managed by such a firm, national policies would lose subjectivity or become difficult to work. Herein lies the origin of the problem of control on the multinational firm.

III. The Multinational Firm and International Economic Order

1. National regulation on foreign capital

Actually many countries have regulation on foreign firms from various

48) Albert O. Hirschman, The Strategy of Economic Development, 1958. Transl. by S. Asada, pp. 33–34.

49) The writer, Beikoku Sandō Gaisha to Shigen Kaihatsu (American copper company and resource exploitation), *Mita Shōgaku Kenkyū*, 1973, No. 1, 2, 3.

viewpoints and by various means. Especially developing countries have enforced measures of control or favored treatment on the base of laws concerning foreign capital, investment promotion, limitation of foreigner's business, industrial development and so forth reflecting situations of respective countries. Basic ideas for these measures may be classified into 1) weight on promotion of economic merits largest possible, 2) avoidance of demerits, though recognizing merits and 3) weighty regard of demerits themselves. And a general change from 1) to 3) may be pointed out.

In fact many developing countries at first have adopted favored treatment such as below.

(1) Favored taxation. For example, overall exemption of inland and local taxes for 5 years and 50% reduction for subsequent 3 years (Korea), income tax exemption for 5 years after beginning of business or profit gain (Thailand), tax exemption for 3 years on priority industries in development regions (Malaysia) and 50~100% reduction for investment in the northern and Amazon regions (Brazil). Beside these privileges for specific regions or industries there have been various treatment such as exemption of commodity tax and customs on introduced capital goods (Korea), exemption or reduction of customs on specific goods and materials and corporate tax (Thailand), exemption or reduction on dividends, and exemption on interest payable to borrowings from abroad (India) and exemption for reinvestment (Peru).

(2) Protection and promotion. These include security of invested assets, protection or nationalization of patents and asset rights, and compensation to compulsory buy-up (Indonesia) as well as protective tariff on competing foreign products, favored treatment for export, utilization of facilities of public financial organs, and government's guarantee on debts.

(3) More important, every country has industries to encourage. This reflects development strategy or programs of each country, and is noteworthy as expression of standards of selection on foreign capital. Of course many patterns must be pointed out ranging from indication of broad frames of export and import-substitutive industries (Korea), concrete names of industries included in government's X-th investment priority plan (Philippines), decision of investment fields by the finance ministry (Indonesia), standards such as labor-intensive and export-oriented industries or industries that raise added values of home materials (Malaysia) to "encourage industries to contribute heavy-chemical industries (Brazil). In some countries concrete names of goods instead of industries are exhibited as in Nigeria and Kenya". In Kenya integrated production is avowed as government's desirable guide line, for example, spinning-weaving-dying-finishing-product. Anyhow, by an overview of these encouraged industries it may be seen that foreign capital is posited as a link of development programs.

On another hand restriction naturally has been put on foreign-capital firms.

(1) Restricted industries. For example, public utilities such as electric

power, communication and broadcasting (Malaysia), prohibition or restriction by laws, prohibition by industrial policies, and restriction for home industry protection (Korea), business under government's monopoly or undertaken by contracts with government (Thailand), industries under overall prohibition such as defence industries; public utilities under prohibition of overall control by foreign capital or limitation on investment (Indonesia). Another type is seen in Brazil where (a) foreign investment is free in principle but is regulated by administration for basic sectors such as electric power, steel or fuels and (b) as for heavy-chemical industries joint enterprising is advised.

(2) Restriction on investment ratio. Most countries provide this restriction, but with substantial differences. Legally 100% investment is allowable but actually the ratio is checked to 49% excepting firms exporting whole produce (Korea); similarly there is no legal regulation but the administration holds it below 49% (Thailand); case by case, below 49% by administrative guide for pioneer firms and 50% for non-pioneer firms (Malaysia); 100% is allowed for investment over 2.5 million dollars but as for below this amount a joint firm is advised (Indonesia); legal 30% regulation for financial business (Brazil); and in some countries restriction on specific industries.

(3) Restriction about employment. This is also considerably respected in some countries. In the Philippines only in case manning by Philippines is difficult for technological reasons 2-year visas are warranted to foreign engineers; field firms of priority industries can employ foreigners for posts of manager, engineer and counselor subject to limits of 5 years and 5% of total employees. In Malaysia racial formation of employees is requested to be identical with that of population; 50% employment of Malaysians is compulsory; foreigners are restricted to cases where natives are unavailable; and foreigner's pay is limited to a certain amount in principle. In Mexico the ratio of Mexican must be more than 90% of employees, and more than a half of managers must be Mexicans. In Indonesia training of natives to alternate for engineers and managers is obliged, and in Iran administrative guide is put toward management by natives.

(4) Control on inland production ratio. This has been described above in relation with the import-substitution policy. In most countries this is provided because an expectation on foreign capital lies in foreward- and backward effects. In the Philippines the ratio for cars is set at 15% for the first year of production, 25% for the second and 50% for the third. In Mexico by administrative instruction the usual ratio is set at more than 60%, and if any other competitive maker has attained a higher ratio the same is required.

(5) Restriction on fund raising. Here the point is that, in developing countries with poor capital accumulation, financing of medium and short term funds oppresses native firms. In the Philippines loan of government's funds from the central bank and the development bank to firms of above-33% foreign capital is prohibited. The bank law of Thailand limits loan to a firm to one-third of bank's capital. These are for this reason of financial resources. Another aspect

of restriction is to check debts from foreign countries. Fund raising of foreign-capital firms from abroad invites increases in debts of the host country and inflows of short money, and so control is contemplated. In Brazil 25% of borrowings from abroad must be deposited compulsorily on the central bank. In Korea fund procurement from parents is limited to beginning 6 months, and that only for import of materials, and credits from third countries is rigidly regulated.

These various measures of protection and regulation on foreign-capital firms are of course not fixed ones but have changed gradually. Speaking generally since the late 1960s appreciation on foreign firms has turned more rigid. In Latin America many criticisms began to appear especially against American direct investment=advance. Their main points were as follows. (1) American technology and management are too excellent and of big scales and hence far foreign to self-dependent development, often rather oppressive. (2) American subsidiaries tend to follow laws of the homeland rather than of the locale land. (3) American subsidiaries like political regimes supporting their vested interests and intend to oppose new shifts by intervention. (4) Introduction of American capital has not contributed to solve social rifts, unequality of wealth and poverty, but have rather fostered. (5) Production systems and resource allocation have been directed to a consumption-priority pattern, with demonstration effects being enlarged. (6) National willingness has been decreased and development as a race is constrained. In short in Latin America critical currents to American investment are considerably strong, which has led to policies of mexicanization, peruvianization and chileanization.

Again among developed countries the merits and demerits of American direct investment have long been discussed. As the merits 1) introduction of new products 2) that of new ideas and 3) utilization of American control techniques have been mentioned, and as the demerits 1) flow-out of profiting bases, 2) decline of research efforts and 3) domination by technological superiority. Notably the Watkins Report[50] of 1968 of Canada analyzed domination by foreign capital, gave appraisal of merits and demerits and presented objectives of the national policy as follows:

1) Foreign-capital firms in Canada should behave as good citizens so as to conform perfectly with Canada's economic and political interests;

2) In order to increase potential of continuous growth comprehensive efficiency of all firms, not only American but also native, should be improved;

3) For the sake of self-dependence and growth positive measures to retain Canada's ownership and control in economic activities should be made.

However, it is not until recent years that views have appeared that regard the demerits of the multinational firm as what lie in its strategy itself. They

50) See footnote 20.

comprise 1) price cartels, 2) market allocation, 3) monopoly of technology, 4) parent's restriction on subsidiary's output and prices, 5) buy-up, fusion and merger of firms and 6) high-grade secrecy.[51] Anyhow, it is not too much to say that contradictions and conflicts always exist between national interests of host lands and rational behavior of firms. Especially as for the multinational firm, so long as it takes global and efficient allocation of resources within the logic of enterprising for its principle, disconformity always arises between its decision-making and national interests. Therefore this problem is to be taken up as what surpasses adjustment or regulation at the level of individual nations.

2. International regulation on the multinational firm

Since the influences of the multinational firm on the world economy have become concern of many people, and economic nationalism has arisen among developing countries, an inclination has appeared to consider adjustment on international bases rather than as institutions or policies of individual nations. One of such moves was seen in OECD, which had taken up the problems of international investment in the form of capital liberalization in lines with its nature. In late 1972 it set up a new working committee to investigate national policies that might distort effective distribution of investments and production means, and at the same time asked its industry and other special committees to examine activities of the multinational firm. Then a task group including specialists of many countries was started, and study of standards or guide lines for such firms was begun. The themes covered the role of these firms had played in transfer of technology, their effects on industrial structure and improvement of information about these firms. This may be called the No. 1 view of developed countries expressed as an international organization. True it was worthy of many supports, and guide lines it suggested were appreciated as autonomous standards of business behavior. Nevertheless many doubts have been casted as is well known—they cannot have legal bases and their practicability reflecting actual states is doubtful because of differences of steps, forms and scales among developed countries.

Again EEC presented various views about guide lines. They were made to include 1) publishing of states of affiliated companies, 2) of whole-firm and regional activities, 3) of R&D, 4) exhibition of pricing policies, 5) control on restriction of competition, 6) respect of labor practices as well as mass-discharge, buy-up and stockholder protection. And standardization of laws within EEC was contemplated. Of course its standpoint is supposed to be recognition of merits and elimination of demerits so that capital movement might not be hindered.

Most noteworthy on the international stage, however, was the Report of

51) Shintarō Hayashi, Shihon no Kokusai Idō to Takokuseki Kigyō (capital movement and multinational firm) in Hayashi, ed., *Kokusai Keizai Kyōshitsu*, 1973.

the "study group of informed people" to "study" the role and effects of the multinational firm on the development process, especially of developing countries, following a resolution of the U.N. Economic and Social Council adopted in July 1972. It was obviously a reflection of problems presented from the south side since 1970, or so to speak it appeared as a link of the south-north problem. True the group consisted of ten members of developed nations, eight of developing and two of Eastern Europe block appointed by the Secretary-General, telling how far the south countries were committing themselves on it. This Report contained as many as 53 recommendations and a proposal to set up a multinational-firm committee under the U.N. Security Council.

Now, important viewpoints involved in this report may be picked out as follows.[52]

(1) "Public aid for development must be increased, which should be directed to growth of local industries as well as food, construction, dwelling, education and social services in order to fulfil most basic needs of poor people within LDC." This is recommended in the "International development strategy for ten years of the second UN development program." This points out increase of public aid and its role, and may be said objective expression of basic assertions of the south.

(2) "Developing countries should explore insertion of a clause to let the multination firm approve possibility of future lowering of equity ratios of foreign capital in the basic agreement with the multinational firm." By this clause restriction on foreign capital ratios, which has been actually enforced as described in section 1 of this chapter, is included into agreement, and foreign capital explicitly accepts the request of domestication. Insertion of this clause is reasonable but since legal bases of such agreement in actual cases are questionable and policies on foreign capital differ by governments, implementation of this recommendation may involve many problems.

(3) The receiving country (of the multinational firm) should clearly define the boundary of public activities of subsidiaries, and provide penalty on offence. This means regulation and publishing of money contributions, as mentioned already in connection with criticisms in Latin America. And the Report additionally says We repreach that in the activities of the multinational firm there is an aspect of political intervention to upset government or to produce such a situation (say, strong tone of expression), and if such possibility exists the government of the receiving country should take sanctions by own legal procedures, and on another hand the homeland of such a firm should consider a similar step within its scheme of investment protection.

(4) "The receiving country must secure that in case of nationalization of assets of the multinational firm fair and adequate compensation shall be made

52) Refer the writer, Takokuseki Kigyō no Ayumu Michi (roads of the multinational firm), in the writer, ed., *Kokusai Keizai no Tenbō to Shin Shiten*, 1976, pp. 163–166.

according to legal procedures or conciliation between concerned persons." In fact nationalization has occurred in many countries causing troubles of compensation. On one aspect this problem hinders positive activities of foreign firms, and on another aspect attitudes of developing countries have not always been consistent between evaluation based on development strategy and existing policies on nationalism. And so solution of compensation may be complicated.

(5) "Developing countries should positively preserve ownership of resources and control on their utilization." This concerns with the sphere and condition of foreign capital the receiving country is ready to allow, and should depend on clear legal stipulations. However, the contents of control in this recommendation are not clear.

(6) "The receiving country should request the multinational firm to make full contribution about innovational products most pertinent to national or regional needs and about processing." This involves two meanings. One is negative expression of dissatisfaction against such cases as machines or techniques after full depreciation were brought in or product lines already obsolescent in homelands or developed countries were transfered by the multinational firm. Another is positive request of contribution for development and modernization.

(7) "The mother land of the investing firm must not impede transfer of labor-intensive or unskilled-labor production to developing countries." As explained already, while transfer of such production is desirable, developed countires may possibly restrain it for fears of threatening to domestic industries. This recommendation warns against this, and urges developed countries to take active policies of industrial adjustment.

(8) "The mother land and the receiving country should give adequate compensation to laborers who have lost jobs due to decision of production by the multinational firm through budgetary steps, utilization of social security systems or set-up of social funds." This represents concern of the study group on employment problems. It requires planning of international social funds for aid because developing countries have little means. And, supposedly reflecting joining of the Eastern Europe, it is asked to secure participation of laborers and labor unions in decision-making of the multinational firm on domestic and international levels.

(9) "The mother land should publish measures for prohibition and control on products regarded as harmful to consumers' health as well as their contents, and must contemplate to prohibit export or to make special approval of importing countries a condition."

(10) "Division of export markets by the multinational firms should be prohibited unless it is conceived necessary to protect other interests of countries concerned." Market allocation is a kind of competition-restrictive agreement and implies two meanings. One is that export markets of the receiving country are naturally confined by it, and another is that their export becomes rather easy because a territory is given. Therefore actually judgement will not be easy. And

the Report adds an advice that "a principle must be internationally settled that competition-restrictive agreement and market allocation by the multinational firms should be made ineffective within a regional group.

Since this Report comprises 53 recommendations as mentioned above, these 10 points alone described here are of course impossible to exhaust its intent, yet they may show the points being contemplated at the U.N. level and its backgrounds and viewpoints. Especially it suffices to see that south-north opposition was exposed and that the south propounded "principles" being aware of absence of reality in the concrete level.

Anyhow, such study by the U.N. suggests two problems. One is that whether it is pertinent to deal this problem of multinational firms on the stage of the U.N., and another is a question that the guide lines shown are whether adjustment or control. Hence a new theme was born by this moment that adjustment or control may include three areas to be considered respectively at three levels— international, national and firm. Section 1 of this chapter has treated mainly problems of the national level and section 2 focal points of the international level. It may be seen that the problems are more complicated as they become more international, and the background extends over world-economic opposition, as is shown between the U.N. plan reflecting the south's views and the OECD plan centered on the developed nation's views. Therefore it is imaginable that, either the U.N. or OECD, the intention was to formulate only basic order from the side of developed nations as an autonomous broad charter, on which each government shall advise guide lines to firms. It must not be forgotten, however, that direct investment of developed countries has been directed mainly developed regions, as described in chapter I. In the case of our country, if among the developed, investment is mainly toward developing countries, and so it is necessary to examine such guide lines taking differences of viewpoints into account.

3. Japan's multinational firm and behaivor guides

Of course it must first be questioned whether Japan's direct investment comes under the so-called multinational firm. Theories about these firms have been introduced already. No one denies internationalization of Japan's firms, yet is it true the process of evolution to multinational ones?[53] Many business economists adapt views of Harvard Business School as they are to our country, assume such step-up, and discuss what should be done for it and what hurdles must be overridden. Supposedly these arguments derive from a belief that, in view of past absorption of American technology and management strategy, the growth pattern of American firms will appear also in Japan's growth steps and this is logical on the theory of business growth.

However, various particularities of management in Japan must be considered. First we can mention that Japan is homogeneous in people and business manage-

53) The writer, Nihongata no Takokuseki Kigyō wa Umareruka? (birth of Japanese type multinational firms?), *Trends*, No. 24.

ment stands on this ground. For example, in America, a multi-race state, unification of people into an organization requires common agreements of various forms and by these rules firms have been managed, while in Japan business behavior has been advanced not by manuals but by tacit comprehension and communication. Accordingly for America's overseas advance integration is possible by applying the same managerial principles. The sole problem is how to organize units; no problems lie in the management of units. Right the multinational firm can be said expansion of the same principle over state borders. In case of Japan foreign subsidiaries depend on management by homeland parents, or else become adapted to localities. If the latter, inevitably managerial principles become heterogeneous. Isn't it possible to say that herein lies the Japanese pattern of internationalization essentially different from the American-type multinational firm?

Second, businessmen of Japan are not a professional category in an American sense. Although in some sectors their professional significance is recognized and a social-occupational stratum is being born, still the seniority order system is general, in which managerial ability is appreciated within individual firms. No markets of professional managers are not yet established. This is a fact combined with lack of general usability of managerial methods, and substantially different from American organization in which appreciation by common measures and management by general techniques are seen.

Third, there is a difference between the "divisional system" of America, which has provided the base of the multinational firm, and that of Japan. The transit from centralization to decentralization and the introduction of this system as a profiting center have long history in America. In Japan only fifteen years have passed since its appearance and spread, and there is a great difference in its operation and behavior because in America the criterion of appreciation lies all in profit, rates, while in Japan various thinkings are multidimensionally involved. Therefore growth of Japan's firms cannot be considered on the same dimension with the American basic pattern that the divisional system inevitably leads to organizational expansion and the multinational firm.

Thus the logic that internationalization of Japan's firms will follow the same way with the American-type multinational firm can be regarded as inapplicable, and for this reason particular conflicts between our advancing firms and localities are conceivable.

First in the locality countries multistratum labor administration comprising different races is supposable, which is liable to invite communication gaps with natives with progress of assimilation.

Second, when it has become necessary to give important managerial posts to natives after some years as mentioned already, this may cause many gaps against the home office because of discrepancy of consciousness, which not only decreases incentives to natives but also contains possibility of conflicts on personnel management.

Third, in Japan nationality of capital ownership is very intense. The multinational firm is often said an enterprise of multinational people but in Japan, however international a firm's strategy may be, it is still a firm of the same nationality and race. Such nationally is more strong as for ownership.

These particularities involved in Japan's business naturally characterizes overseas activities at firm's level, and make their guide lines differ from those of other countries. And the often-mentioned larger weight of developing countries in Japan's foreign activities again is producing different response. Such particularity is obviously seen in the "guide lines of investment activities in developing countries" published in 1973 by the Japan Federation of Economic Organizations, in which the following points have been emphasized.

(1) Firms shall respect conditions and customs of business in the receiving country, and make efforts so that investment may contribute to cultivate enterpreneuer spirit and make it fixed in the land on the principle of self-responsibility.

(2) Investment shall be advanced along a line that it is welcome and established there, and the firm and the receiving country shall be compatible in development and growth on a long-range viewpoint.

(3) Coexistence and coprosperity shall be the principle; appropriate consideration be made such as exhibition of long-run plans and establishment of reasonable labor-management relations; opportunities of participation be given to native investors at some suitable time.

(4) Efforts shall be made of active employment and promotion in locality firms.

(5) In selecting personnel to dispatch to foreign firms personal property such as cooperative mind, willingness and ability shall be considered.

(6) In order to make dispatched men have willingness and responsibility, transfer of wide authority, length of residence matching to local conditions as well as perfection of other conditions shall be considered.

(7) For the sake of technology spread in the receiving country opportunities of learning shall be given to native employees such as within-firm education and training, dispatch to the home firm and resident study.

(8) From the viewpoint of international labor division, balance of payments of the receiving country and bring-up of local industries, utmost efforts shall be made to use local-produced machines, equipment or parts, along with technical education.

(9) In order to contribute to economic growth of the receiving country, profits of locality firms shall be reinvested for expansion of the firms and bring-up of surrounding industries there.

(10) Coordination with the receiving country, avoidance of concentration on specific regions or industries, and respect of native trade customs and systems shall be considered.

(11) For the sake of coordination and harmony with the society of the receiving country, conservation of environments shall be considered, contribution

to education and welfare be made, and participation with local industrial organizations be advanced in order to promote intimate intercourse with native businessmen.

These are principles prepared and published by the JFEO, the Japan Chamber of Commerce and Industry, the Keizai Dōyūkai (employers' friendly society), the Japan Association of Employers and the Japan Foreign Trade Association, and hence must be said guide lines by private circles. They begin with basic attitudes and cover 3) mutual confidence, 4) employment and promotion, 5) and 6) dispatched men, 7) technical training, 8) bring-up of local industries, 9) reinvestment, and 10) and 11) coordination with local society and industries. Since the problems attendant to Japan's advance are said management and employment policies, the basic point is how to adapt the above-said Japanese-type management. And these principles are different from the various guide lines of the multinational firm mentioned above, and do not presuppose such problems as are born from the character of multinationality. Nevertheless most people seem to identify the two. This is because, putting aside conceptual difference, there is confusion between the American empirical fact, with the multinational firm making the principal form of direct investment, and the Japanese-type advance. And distinction is not clear whether these guide lines refer to investment behavior of the multinational firm or that of overseas investment at large. So I thing.

4. The multinational firm and international economic order

Lastly I should like to observe direct investment and multinational activities as its main form anew in a dynamic perspective of the international economy.

First, as mentioned in section I, overseas advance of firms was nothing but major response of enterprisers amid the postwar innovation waves beginning in America. It may well be said an international removal of innovational enterprises, through which innovation moves internationally spread. It was also an engine for the growth of the world economy. Indeed through it new industrial systems were born, new structure of international labor division was created, and on these grounds there was expansion of world trade in the 1950s and 1960s. Such absorption of innovation and operation of inductive devices rendered high-rate growth possible along the basic line of trade liberalization advanced with some time lag.

Through the mushroom growth of innovation, however, a turn was reached. In developed countries innovational force of economy tended to decline and foregoing growth rates began to fall. In developing countries spread of innovation produced gaps against traditional socio-economic structure and conflicts with advancing firms bearing social tension. World trade showed a remarkable decrease of volume in 1975. Many countries suffered from a trilemma of inflation, depression and balance of payments. Developing countries were dealt a big blow excepting some oil producers. Direct investment to these countries, which had been expanding, was consolidated or restrained due to perplexed economic situations of homelands, causing social tension of another sense. That is, in these countries there emerged not only conflicts but also such problems as employment security and warps of industrialization plans. In addition primary commodity prices, which had risen at one time, dropped due to recessions in developed countries, and their exports sharply dwindled in the process of reduction of demand and progress of inventory adjustment. Thus the past growth moved by two engines was obstructed. On another hand developed countries simultaneously began to gather concern on oil-producing countries, changing weight of trade and investment. These countries make up large part on export growth of Japan, yet no one would think that these are truly persistent market frontiers. Nevertheless in view of their tremendous dollar reserves and their position as big customers in world markets, it is natural that they draw attention as new capital and trade markets. However, it is doubtless that this fact has caused a great change of themes of international economic order around capital and trade that had been flowing as the south-north problem. In particular, with the expanding differentials among developing countries themselves being discussed, and new combination of capital and trade plus aid being required, it may be said that it is now the time to considered guide lines of investment under this new situation.

On another hand in developed countries innovation cycles are being placed under great adjustment. Profits by innovation are decreasing, scale expansion is being reexamined, and reorganization in business circles is unescapable for maintenance of firm growth, so to speak a period of revolution in macro-terms. This naturally affects overseas advance and after 1976 a great change is appearing in quality and quantity.

Then the question is what roles and problems advance of firms, notably of the multinational firm, may have in international economic order.

As regards international order of economy first we must observe the postwar globalism which purports to frame unitary order on world markets in line with the principle of indifferential free trade.

To this globalism a great trial was of course the foundation of the European Common Market. It may be still fresh in memory that it invited many discussions since the start. Some one regarded it as going the same road with the prewar block economy and feared possible division of the world market. Some said it was essentially different from the block economy; rather it was a small free trade area, a step toward world-wide one. And some argued that since its idea and objective were oriented to a political-economic community it should be taken as new blockism, an antithese to global liberalization.

Of course so long as this regional integration establishes common tariff and discriminate inside and outside, it must be opposed to globalism such as GATT. GATT admits customs unions yet it is difficult to say that EC comes under this admission. Neverthless EC was permitted for the reason of de facto status, which should naturally invite criticisms as above. The question is whether EC is opposite to globalism and destructs it from inside, or is a step of time inserted in globalism, or else globalism itself has been qualitatively changed at the time of recognition of EC.

A realistic material for judgement is the effects of EC on world trade. So long as outer trade is discriminated, import from outside was foreseen to be shifted to inner trade, and if so world trade would be evidently impeded. May countries held a fear on this point. Actually, however, its effects have been various on both inside and outside. One was that outside countries, being exposed to such trade transformation, decreased actual damages by having competitive power enough to fill price differentials, and in case of America capital moved to replace commodity trade. On another hand cut or abolition of customs within the region created new trade and increased purchasing power of EC promoted trade with outside. Accordingly on one aspect EC gave a new dynamic stimulus, in other words, there was something larger than the effect of globalism standing on formal equality and mutualism of give-and-take. Again it is conceivable that, as against the globalism of the 1950s and early 1960s reflecting substantial interests of American nationalism, there was presented a new principle of trade development, and only by embracing it globalism can be posited as the base of international economic order, say, realistic consensus. On top of it the advance of American multinational firms was successful enjoyment of the fruit of regionalism, and materialization of the principle of global business behavior. In this sense the global order colored with American nationalism on trade was recolored into new order of globalism with internationalism on the aspect of capital. And in a sense such advance was expression of new economic power of America in the world market. If so, the multinational firm may be said what neutralizes opposition between regionalism and globalism and serves as a bridge to American nationalism.[54]

Anyhow, as a result America's export strength began to decline. In fact her industries with international superiority and high growth rates shifted their footholds of production and selling to regions to where their export had been directed. On the firm base foreign activities and assets are all evalued as achievements in financial statements, yet on the national base capital outflows become net outflows unless their fruits are returned back to America, if foreign assets increase as stock, and foreign exchange receipts to be reckoned by export are lost by production and selling abroad as well as export to third countries. And as the result of such transfer of strong firms, domestic industries become inferior ones, or unmovable agriculture or aviation and space industries with less multinationality.[55] Here protectionism arises. In other words, the activity of

54) The writer, Kokusai Keizai Seisaku no Chōryu (currents of international economic policies), *Customs*, 1972, No. 11.

55) K. Kojima distinguishes American- and Japanese-types from a point that America transfers relatively superior industries while Japan relatively inferior, and makes contrasting of mechanism. *Kaigai Chokusetsu Tōshiron* (theory on direct investment) 1977.

the multinational firm—a challenge in the form of expression of America's new economic power against regionalism—resulted in multidimensional requests on trade policies of America itself. That is, in the fields of inferior home industries customary globalism is now incompatible with national interests, rather a harmful obstacle. Various acts and assertions offensive to GATT emerge from this aspect. Contrarily as for agriculture and the space industry it is globalism that enhances national interests. On another hand as to the multinational firm what are required are avoidance of conflicts and keeping of coordination with regional nationalism, and hence nationalism in America becomes their burdens, never interests. Thus three positions for three persons. It may be said that therein lie curious contradictions and realities of American policies on the world economy.

Again the favored treatment given to developing nations was a great shock to the postwar globalism. Following the proposal of the U.N. Trade Development conference of 1964 and the Algeria Charter of 1967 backed by 77 developing countries, in 1970 consensus among many countries was formed and effected, which produced at least four directions: first, promotion of firm advance into developing countries; second, changing of export structure among the developed; third, widened differentials among the developing; fourth, inclination from vertical to horizontal labor division between the developed and the developing. Especially essential was the first direction, which accelerated competition among advancing firms, in which most superior were America and its firms. This makes the reason why America accepts unlimited favored treatment, while on another hand avowing globalism. It realizes strategic advantages of globalism for the multinational firm in developing countries, and fruits of capital can be obtained by opposing to GATT's globalism in its sanction of favored treatment, an America's reality.

Advance into developing countries invites collisions with nationalism there. Yet today nationalism in these countries is not simple. In most countries it is combined with industrialization, being based on multiangular strategy including both high and low level technology. Its contents look like simulation of industrial organization of developed countries irrespective of demand-supply unbalance and many socio-economic contradictions. And so their attitudes to firm advance seem to be realistic response according to progress of development strategy including both repulsion and utilization. Here lies a posture of nationalism of developing countries.

One thing more, it may be necessary to refer to international economic problems oil-producing countries have. Economic development of these countries is causing resource problems in developed countries and is affecting the market mechanism of the world as a disturbing factor at least in that their development is based on price-up of oil and their voices are increasing strength. It is casting a theme on us how to embrace their development within international order and how to reorganize the latter. There seem to lie two aspects.

The first is that it is a disturbing factor and in addition is presenting the south-south problem. And this must be considered under a situation that capital and trade are biased to this region and the rest to other non-oil countries is becoming appreciable restricted. Because this makes a great obstacle to present international capital flows and checking force against world economic growth, an inclination is being born in which adjustment of nationalism is more difficult.

The second is an aspect that their development itself is inviting need of international cooperation in the long run. That is, their industrialization strategy requires such basic conditions as 1) intra-regional cooperation, 2) expansion of trade with America, Canada, Australia and so on, and 3) intensification of relation with EC. Accordingly with the progress of industrialization interdependence with developed countries has to become closer, and there is possibility of being woven into international labor division structure. If so, there may be born concern on international interests and a palliative to sharpening antagonism of nationalism contains.

IV. *Response in Japan*

From above observations I should like to emphasize the following points as a conclusion to the title of this essay, "direct investment and international economic order," keeping response in Japan in mind.

(1) Growth of world trade depends much on increase in direct investment, which makes a major engine for economic growth through international spread of innovation, creates dynamic changes of international labor division, and increases itself being induced through these. Hence it has not only a static effect of optimal distribution of economic resources but also a dynamic one of direct contribution to growth. It is undesirable to check it if the growth rate of world trade is to be maintained and raised. (Acceptance of the principle of capital liberalization).

(2) Direct investment is not simple transfer of capital but a package move of technology, know-how and managerial ability, viz. an important selective means of overseas activities. At the leveles of both firm and nation foreign activities of today are strategic mix of export, patent-giving and direct advance. Competitive power of a nation concerns not only with export but also with overall power. (Respect of international competitive power of firms).

(3) Business behavior of direct investment is always exposed to two-fold appreciation of utilization and repulsion in the receiving country. Side by side with merits, it works oppression by latent intervention, invites social tension and causes conflicts with the policies and expectations of the locality government. Hence some guide lines are necessary. For this aim possible spheres at each level of firm, government international organ should be made clear, and methods of advice, adjustment and control must be selected for application. (Set-up of guide lines of investment behavior).

(4) Direct investment is a selective strategic method of development for

receiving countries. In planning development process separte appreciation of trade, investment and aid is impossible. Rather it should be considered how these factors function each other amid international competition. (Organic appreciation on international cooperation).

(5) Direct investment brings about changes of industrial structure, and are countermoves of firms against them. Therefore it should be examined from the standpoint of industrial adjustment policies and be given weight in a long-range perspective of industrial structure. (Adjustment of industrial structure).

(6) The direction of the American-type multinational firm is presenting a basic problem of collision with state authority. On another hand doubts are arising about efficiency of such firms, and their future figure appears to be fluctuating. Rather there is appearing an orientation to interwind them into a new scheme under which they are induced to labor division on mutual consent founded on joint production agreements, international joint development agreements or inter-governmental cooperation. Accordingly actual directions of their transformation must be examined, instead of the customary evolution theory of the multinational firm. (Examination of the transformation of the American-type multinational firm).

(7) It is dangerous to identify firm's advance in the form of direct investment with multinational behavior. Rather attention should be paid to differences of patterns among Europe, America and Japan, and square countermeasures be considered. It is more proper to say "business internationalization," in which differnt routes and patterns are conceivable, and from this angle the characteristics of Japan's advance must be clarified. (Grasp of characteristics of Japanese-type advance).

(8) The multinational firm has played a role as a bridge between nationalism and globalism of America. This role should be evalued by merits and demerits, and internationalization of firms of many countries will provide a base of re-organization of international economic order of tomorrow, because it gives an effective opportunity to let nationalism to regard international interests. (Base of international economic order=international interests).

(9) In considering international economic order of today it must first be recognized that the cycle of innovation is already declining and going toward contraction. Its rapid downfall is being prevented by political cooperation and foreward-looking financial and banking policies of developed nations as well as by quickening of the third-round energy revolution. Today is just a refraction point of the innovation cycle.