FACULTY OF JURIDICAL SCIENCES

Lecture-33

Models of MNCs

The following are the different models of multinational corporations:

1. Centralized

In the centralized model, companies put up an executive headquarters in their home country and then build various manufacturing plants and production facilities in other countries. Its most important advantage is being able to avoid tariffs and import quotas and take advantage of lower production costs.

2. Regional

The regionalized model states that a company keeps its headquarters in one country that supervises a collection of offices that are located in other countries. Unlike the centralized model, the regionalized model includes subsidiaries and affiliates that all report to the headquarters.

3. Multinational

In the multinational model, a parent company operates in the home country and puts up subsidiaries in different countries. The difference is that the subsidiaries and affiliates are more independent in their operations.

Role of MNCs

Multinational corporations (MNCs) are huge industrial organizations having a wide network of branches and subsidiaries spread over a number of countries. The two main characteristics of MNCs are their large size and the fact that their worldwide activities are centrally controlled by the parent companies. Such a company may enter into joint venture with a company in another country. There may be agreement among companies of different countries in respect of division of production, market, etc. These companies are to be found in almost all the advanced countries, with the USA perhaps the biggest amongst them. Their operations extend beyond their own countries, and cover not only the advanced countries but also the LDCs.

Many MNCs have annual sales volume in excess of the entire GNPs of the developing countries in which they operate. MNCs have great impact on the development process of the Underdeveloped countries.

Let us discuss the arguments for and against the operation of MNCs in underdeveloped countries.

Arguments for MNCs (The positive role): The MNCs play an important role in the economic development of underdeveloped countries.

1. Filling Savings Gap: The first important contribution of MNCs is its role in filling the resource gap between targeted or desired investment and domestically mobilized savings. For example, to achieve a 7% growth rate of national output if the required rate of saving is 21% but if the savings that can be domestically mobilized is only 16% then there is a 'saving gap' of 5%. If the country can fill this gap with foreign direct investments from the MNCs, it will be in a better position to achieve its target rate of economic growth.

2. Filling Trade Gap: The second contribution relates to filling the foreign exchange or trade gap. An inflow of foreign capital can reduce or even remove the deficit in the balance of payments if the MNCs can generate a net positive flow of export earnings.

3. Filling Revenue Gap: The third important role of MNCs is filling the gap between targeted governmental tax revenues and locally raised taxes. By taxing MNC profits, LDC governments are able to mobilize public financial resources for development projects.

4. Filling Management/Technological Gap: Fourthly, Multinationals not only provide financial resources but they also supply a "package" of needed resources including management experience, entrepreneurial abilities, and technological skills. These can be transferred to their local counterparts by means of training programs and the process of 'learning by doing'.

Moreover, MNCs bring with them the most sophisticated technological knowledge about production processes while transferring modern machinery and equipment to capital poor LDCs. Such transfers of knowledge, skills, and technology are assumed to be both desirable and productive for the recipient country.

5. Other Beneficial Roles: The MNCs also bring several other benefits to the host country.

(a) The domestic labour may benefit in the form of higher real wages.

(b) The consumers benefits by way of lower prices and better quality products.

(c) Investments by MNCs will also induce more domestic investment. For example, ancillary units can be set up to 'feed' the main industries of the MNCs

(d) MNCs expenditures on research and development (R&D), although limited is bound to benefit the host country.

Apart from these there are indirect gains through the realization of external economies.

Arguments against MNCs (The negative role): There are several arguments against MNCs which are discussed below.

1. Although MNCs provide capital, they may lower domestic savings and investment rates by stifling competition through exclusive production agreements with the host governments. MNCs often fail to reinvest much of their profits and also they may inhibit the expansion of indigenous firms.

2. Although the initial impact of MNC investment is to improve the foreign exchange position of the recipient nation, its long-run impact may reduce foreign exchange earnings on both current and capital accounts. The current account may deteriorate as a result of substantial importation of intermediate and capital goods while the capital account may worsen because of the overseas repatriation of profits, interest, royalties, etc.

3. While MNCs do contribute to public revenue in the form of corporate taxes, their contribution is considerably less than it should be as a result of liberal tax concessions, excessive investment allowances, subsidies and tariff protection provided by the host government.

4. The management, entrepreneurial skills, technology, and overseas contacts provided by the MNCs may have little impact on developing local skills and resources. In fact, the development of these local skills may be inhibited by the MNCs by stifling the growth of indigenous entrepreneurship as a result of the MNCs dominance of local markets.

5. MNCs' impact on development is very uneven. In many situations MNC activities reinforce dualistic economic structures and widen income inequalities. They tend to promote the interests of some few modern-sector workers only. They also divert resources away from the production of consumer goods by producing luxurious goods demanded by the local elites.

6. MNCs typically produce inappropriate products and stimulate inappropriate consumption patterns through advertising and their monopolistic market power. Production is done with

capital-intensive technique which is not useful for labour surplus economies. This would aggravate the unemployment problem in the host country.

7. The behavior pattern of MNCs reveals that they do not engage in R & D activities in underdeveloped countries. However, these LDCs have to bear the bulk of their costs.

8. MNCs often use their economic power to influence government policies in directions unfavorable to development. The host government has to provide them special economic and political concessions in the form of excessive protection, lower tax, subsidized inputs, cheap provision of factory sites. As a result, the private profits of MNCs may exceed social benefits.

9. Multinationals may damage the host countries by suppressing domestic entrepreneurship through their superior knowledge, worldwide contacts, and advertising skills. They drive out local competitors and inhibit the emergence of small-scale enterprises.