

## Reply to John Cantwell's Commentary on Grazia Ietto-Gillies' paper: 'The Theory of the Transnational Corporation at 50+'

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My thanks to John Cantwell for taking the trouble to read carefully and respond to my paper *The Theory of the Transnational Corporation at 50+*. These comments greatly add to my contribution by deepening the discourse. Here I take the opportunity to add some comments and clarifications to those of John Cantwell.

Cantwell starts his comments with very interesting methodological remarks about the trajectory of the international business (IB) literature after its starting point from – or very closely to – economics. I very much agree with him on the positive role played by multi- and inter-disciplinarity in the development of the subject. Indeed, I would go further in saying that these developments need not be specific to IB only. I believe that other parts of economics would greatly benefit from liaisons with other disciplines – particularly sociological and political sciences. They would also benefit from more grounded links with empirics and from the use of a wider variety of methodologies.

We both agree that the trends towards externalisation need new approaches to the firm and particularly to the TNC. Dunning and Lundan's (2008) work is a good example of authors aware that old approaches may no longer suffice. Years ago, Cowling and Sugden (1987, p. 12) saw the need for a redefinition of the firm and the TNC on the basis of their control over units which are external in terms of ownership but are nonetheless dependent on the principal firm. They give the following definitions: 'A firm is the means of coordinating production from one center of strategic decision-making. A transnational is the means of coordinating production from one center of strategic decision-making when this coordination takes a firm across national boundaries.' This part of their work was further developed in their 1998 article.

I agree with Cantwell that the proponents of the Internalisation Theory saw as symmetrical the process of internalisation versus externalisation. After all, in a static sense, internalisation implies that, at the micro level, there is another choice and there always was. However, my criticism stems from historical developments at the macro level. Yes, managers always had the choice between growth via internal activities or via external ones such as licensing or sub-contracting. But the fact remains that, historically, there was a tendency towards internalisation up to the early 1970s (and this, in my view, helps to explain why the theory was developed at that point in time). However, the trend was reversed dramatically from the 1980s onwards. Given that the managers were always faced with the same choices, how do we explain the two different trends? In my view they can only be explained by bringing in external socio-political elements. The increased internalisation, combined with other socio-economic factors, led to a more powerful workforce in the late 1960s and early 1970s. As a

reaction to this, firms, and indeed public institutions, moved towards subcontracting and other externalisation modalities. This contributed to weaken the bargaining power of labour as we see today. In other words, the internalisation theory can explain the choice between situations in which externalisation may be preferred to internalisation (or *vice versa*), at the micro level. However, my point is that we need a theory that explains both micro and macro level patterns, as well as the historical trends, and how the macro and micro levels affect each other. This is a key example in which we need to analyse the links between micro and macro levels as well as use interdisciplinarity - two issues Cantwell emphasises in his comments. I would add the emphasis that historical trends help to clarify the interrelationships between the micro and macro levels.

In discussing internalisation, Cantwell introduces some poignant comments on Kogut and Zander's (1993) evolutionary theory. I would, once again, like to use external, historical trends to further support Cantwell's point. The political and economic contexts of the last three decades have brought about several changes, including the following two related to both the private and public sectors. First, labour has become more mobile in two different meanings. The gradual erosion of secure and stable employment contracts means that labour has become more mobile across firms and sectors. It has also become more mobile across countries, which is one of the characteristics of globalisation. As skilled labourers move across institutions, sectors or countries, they form wider networks. Second, universities and public research centres have been told for years that a measure of their success is the ability to forge links with private producers. Whether this is conducive to better research or not, the fact is that, increasingly, companies' skilled labour has the opportunity of networking with public researchers. All this points to the increasing relevance of networks that span outside the boundaries of the firm. Thus Kogut and Zander's idea of the firm as the hub of exclusive, privileged networks may be undermined by the empirics of historical trends.

One last point I would like to make refers to the role of nation-states in my approach to the explanation of TNCs' strategies and activities. Yes, the nation-state and the role of governments have often been included in IB writings: from Hymer post-dissertation work to Vernon to Dunning. In more recent writings the emphasis on policies of attractiveness (of inward FDI) necessarily implies a role for the state and its government. However, my point is not so much about policies of single states and the politics behind them – important though these are. The key point in my discourse is the fact the actors that can plan, organise and control across frontiers – as the TNCs can – have a bargaining advantage when dealing with actors who cannot do so, or not to the same extent. Thus the ex-ante contractual power of TNCs is considerably stronger than that of the workforce they confront in each country or of governments that try to outbid each other in sweeteners or suppliers who are often location bound. It is multinationality *per se* that gives advantages to the TNCs. The bargaining power over these three sets of actors can be turned into market power. There can also be further advantages of multinationality – including risk spreading and learning from the diverse innovation environments of different nation-states. The latter is a field to which Cantwell has made a major contribution. For these reasons the theory of the TNC cannot be just an extension of the theory of the firm in general, or of the big firm in particular. The different regulatory regimes of nation-states lead to situations that require a qualitatively different approach from the traditional theory of the firm. The stress on advantages of multinationality has policy implications: for the labour movement it implies building bridges across frontiers and avoiding the games of setting Poles against Italians or British against Romanians. The other relevant policy implication may be related to separatist movements which are springing up everywhere be it Scotland, Northern Italy or Catalonia. While devolution of some powers from the centre may be in the interest of regions and countries, the main beneficiaries of full

separation may end up being the TNCs as they will have more policy centres – i.e. more nation-states – in competition with each other. I recently read in the British press that one of the pledges of the aspiring separate Scotland will be to lower corporation tax in competition with the one – already quite low – of Britain.

Cantwell points out the role of cultural differences as well as the relevance of local and regional characteristics for TNCs' strategic decisions. I do not consider them in the paper under discussion, though there is a small role for cultural differences between nation-states and for regional variation in regulatory regimes in the relevant chapter in my book (Ietto-Gillies, 2012, ch. 14). I agree that cultural issues should play a bigger role. However, the tremendous increase in cross-country FDI in the last few decades is testimony that cultural barriers can be overcome. Inward FDI into Japan may have been constrained by cultural factors; however, had other conditions been favourable – such as government policies – the cultural barriers would have been overcome. Cultural distance is only part of the story. After all, Japanese companies coming from a different culture managed to overcome the barriers and successfully expand their FDI abroad. Why could not Western companies overcome the cultural distance – if that had been the only or main problem – and invest in Japan? After all cultural barriers have largely been overcome by Western TNCs investing in China. Cultural barriers can often be overcome by joint ventures, a modality of internationalisation more appealing to host countries, as well as of help to the foreign firm in learning about a new cultural and institutional environment.

Finally, I should say that I am pleased to see that my comments above have been fully considered in the final revised version of Cantwell's Commentary. This process has led to further interesting points by Cantwell on: the network firm; the drivers of externalisation; the advantages and disadvantages of nation-states *vis-à-vis* the TNCs. Our exchange has widened the debate beyond my original paper and has led to convergence of views on many points.

### **Additional references**

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<http://www.worldeconomicssociation.org/files/journals/economicthoughtWEA-ET-3-2-Ietto-Gillies-Reply.pdf>