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Sequence of value-added activities in the multinationalization of developing country firms ☆

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Abstract

This paper studies the sequence of value-added activities in the multinationalization of firms from developing countries. Analysis of twenty Latin American multinational firms, or Multilatinas, reveals three alternative sequences: start multinationalizing with marketing subsidiaries in all countries, start multinationalizing with production subsidies in all countries, or start multinationalizing with marketing subsidiaries in some countries and production subsidiaries in others. These alternative sequences are explained through the integration and extension of arguments from the incremental model of internationalization and its discussion of difficulties, and the eclectic paradigm of foreign production and its discussion of advantages. I argue that firms that benefit from a location advantage in the country of origin are more likely to start multinationalizing using marketing subsidiaries, firms that benefit from a location advantage in the host country are more likely to start multinationalizing using production subsidiaries, and firms that face difficulties in the transfer of products across countries are more likely to start multinationalizing using production subsidiaries.
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I study the sequence of value-added activities that enable a developing country firm to become a multinational enterprise (MNE), that is, a firm with value added activities abroad. Despite

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perceptions about developing-country MNEs being technologically backward and unable to compete against developed-country MNEs, developing-country firms are increasingly expanding across borders. While in 1992 there were only 3100 transnational firms from developing countries, by 2005 there were 20238 (UNCTAD, 1993, 2006). Some have even become leaders in their industries, like the Mexican cement producer Cemex, which is the second largest cement producer in the world.

However, little is known about the multinationalization process of these companies, and predictions from existing theory, which has been developed by studying developed-country MNEs, may not be fully applicable. Developing country firms differ in their advantages and internationalization from developed country ones (Dunning, 2000; Dunning, Narula, and van Hoesel, 1998). Additionally, developing-country firms suffer from location disadvantages, such as underdevelopment of institutions in their home country, which induce them to follow unrelated diversification in a profitable manner, in contrast to developed-country firms (Khanna and Yafeh, 2005). These location disadvantages may also affect their multinationalization process.

I analyze twenty Latin American MNEs, or Multilatinas, to explore whether, how and why their multinationalization process differs from that proposed in existing literature. I find three alternative sequences of multinationalization: start with marketing subsidiaries in all countries, start with production subsidies in all countries, and start with marketing subsidiaries in some countries and production subsidiaries in others.

I argue that these three sequences can be explained by integrating the incremental internationalization model (Johanson and Vahlne, 1977), which argues that the selection of value-added activities abroad is driven by difficulties in internationalization, with the eclectic paradigm of international production (Dunning, 1977), which proposes that the selection of value-added activities abroad is driven by advantages. The resulting integration extends each model to develop three explanations of the selection of value-added activities: firms that benefit from a location advantage in the country of origin are more likely to start multinationalizing using marketing subsidiaries first; companies that benefit from a location advantage in the host country are more likely to start multinationalizing using production subsidiaries first; and firms that face difficulties in the transfer of products across countries are more likely to start multinationalizing using production subsidiaries first.

The rest of the paper is organized as follows. In the next section I briefly review the literature on developing-country MNEs and discuss two theoretical models: the incremental internationalization model and the eclectic paradigm. I then explain the process of selecting the case studies and present the insights from their analyses. A discussion of how these insights inform existing theory follows. I conclude with a summary of contributions.

1. Multinationalization process of developing country firms

To understand the sequence of value added activities in the multinationalization of developing-country firms, we must link three sets of literature: studies of Third world or developing country MNEs (e.g. Lall, 1983; Lecraw, 1977, 1993; Wells, 1983)[1], the sequence of value-added activities

[1] There are other related but separate decisions on the international expansion of firms that I will not discuss in this paper (for a recent review of internationalization processes, see Cuervo-Cazurra and Ramos, 2004). First, I do not discuss the internationalization of the firm, where a firm that only sells in its home country decides to start exporting (for a review see Andersen, 1993). Second, I do not discuss the selection of countries into which to expand, where a firm first chooses countries that are similar to the country of origin and then moves into countries that are different (e.g. Vernon, 1966; Johanson and Vahlne, 1977). Third, I do not discuss the selection of entry modes, where a firm chooses to acquire, establish an alliance, or set up a greenfield investment in its foreign expansion (for a recent review of entry modes see Datta et al., 2002).

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