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FOREIGN DIRECT INVESTMENT: ONE ELEMENT OF CORPORATE STRATEGY

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INTRODUCTION

The purpose of this paper is to explore the strategic issues associated with foreign direct investment (FDI). The literature review is based on an extensive reading of works categorised as international business research. The review aims to identify the central themes in the international business literature in relation to the establishment of foreign value adding activities. Since this paper cannot review the whole field of international business it will limit discussion to three fields:

- the link between strategy, structure and entry mode of international firms;
- stage models of internationalization that seek to interpret entry mode choices as part of a longer term, strategic process;
- strategic aspects of location and entry mode choices for international businesses.

Section 2 will survey the relevant theoretical literature on the topics of internationalisation, international strategy and strategic aspects of mode choice and locational choice. Section 3 identifies research issues of particular relevance to Australia. Section 4 discusses the factors that currently impede pursuit of these research issues.

LITERATURE REVIEW

Strategy and strategic management have been defined in different ways by different scholars. A common element of most definitions is that it is a pattern or plan that integrates an organisation's major goals, structure, policies and sequences of actions into a cohesive whole. A firm's strategy supplies a sense of direction for the enterprise. It assists in coordinating the geographic, functional and product bases of the firm, minimises intra-organisational conflict and serves as a guide for decision making (John et al, 1997; Hill, 1997; Quinn, 1980).

Internationalization has been defined as the process of increasing involvement in international operations (Welch and Luostarinen, 1988). A strategic interpretation of this process focuses upon the systematic, ongoing development and change in the international firm in terms of scope of business activities across different countries, choices of entry mode including exporting, licensing and foreign production and, in the case of the latter, ownership arrangements, and systems to coordinate these activities. The financing arrangements firms put in place to support their foreign operations, for example, foreign direct investment (FDI) is just one part of the broader picture.

The paper is restricted to research themes which address the process and strategic dimension of the international firm's formation and development. It therefore gives scant attention to the dominating theories on foreign investments, Dunning's (1980) eclectic paradigm and the internalisation theory. Neither of these theories elucidate the process of internationalization. Common to both these approaches is the assumption that each foreign market entry and mode choice is made in isolation (Eriksson, Johanson, Majkgard and Sharma, 1997) Instead, two models that have sought to focus on the long term, sequential nature of internationalization will be examined here: Vernon's (1966) product life cycle model and the (Uppsala) internationalization process model (Eriksson, Johanson, Majkgard and Sharma, 1997; Johanson and Vahlne, 1977). These models satisfy two criteria of a strategic interpretation internationalization, that is, that it is a long term process and that the different aspects of internationalisation are interrelated with each other and with the firm's strategy .

The product life cycle model seeks to bridge international trade theory and the individual firm's perspective of investment in product development. Vernon emphasised the role of product innovation and the standardisation of production methodologies over time as well as the gain and loss of comparative advantage of particular countries in the product as its market matures. He identified different stages in the life cycle of a product, each with different implications for the internationalization of the innovative company. The first stage is domestic in nature, the home country being the major market. Exports to other industrial countries support the emerging goal of achieving economies of scale in production. As the production process comes to be better understood and documented, and as price competition emerges following the entry of rival suppliers, the firm moves to the second stage. Production is transferred to other countries where wages are lower and technically skilled workers are available, the production process no longer requiring the highly skilled and innovative personnel involved in the original product development. Later again, in the mature stage, the production process becomes fully standardised and the market very competitive, the consequence of the production technology diffusing to rival firms. Manufacturing is transferred to countries with low labour costs.

This model is of interest because it brings exporting and foreign production into a single explanation of foreign market entry. It also offers a developmental view on relocation of production activities, with locational changes being driven by various national characteristics such as technological know-how, demand and labour costs. However, the descriptive value of the model is weak for products with short lives, a circumstance which applies to more and more products (McKiernan, 1992). The applicability of this model is also limited if products are developed in companies that already have considerable operations in other countries (Vernon, 1979).

A number of theories, mainly inspired by Johanson, Wiedersheim-Paul and Vahlne, and dubbed the *internationalization process* or *Uppsala* model, explain modal choice on the basis of a firm's knowledge gained through experience in international markets. This model posits that internationalisation occurs in stages, commencing with irregular export activity (Cavusgil, 1984; Johanson and Vahlne, 1990; Johanson and Wiedersheim-Paul, 1975). Businesses move from irregular exporting, through exporting via an independent agent, the use of a sales subsidiary, to, eventually, full production in foreign markets. Progression through the stages is driven by experiential knowledge accumulation. Each stage calls for more commitment to international markets and enables firms to gain in knowledge, skill and confidence. Because the knowledge relates to the existing mode of operation, firms tend to move gradually, adopting new modes which make most use of past experience.

The Uppsala model has a second strand which asserts that the locational pattern of FDI is determined by 'psychic distance', defined as the costs of acquiring and internalising relevant information about business conditions in other countries, the perception of risk and uncertainty involved in foreign operations, and the resources required to gain access to foreign networks (Johanson and Vahlne, 1977). The model asserts that the costs involved in overcoming psychic distance decline over time as a function of the experience gained by the firm in each market. Firms are thus expected to enter familiar, probably neighbouring markets first because of their historical familiarity and then to fan out into progressively more remote territory.

There are three exceptions to this incremental process (Andersen, 1993; Johanson and Vahlne 1990). First, large firms can take bigger internationalisation steps. Second, when market conditions are stable, knowledge can be gained in ways other than through experience. Third, experience in similar markets may allow a firm to generalise this experience. These exceptions allow firms to jump stages.

In contrast to Dunning's eclectic paradigm and the internalisation model, the Upsalla model explains internationalization as a pattern of growth. It is based on behavioural theories, with assumptions about lack of information and the importance of perceived risk and uncertainty (Cavusgil, 1984). In this view, the internationalization process is not seen as a sequence of deliberately planned steps founded on rational analysis. Instead, it is the incremental nature of successive learning through stages of increasing foreign commitment to foreign markets that is the main characteristic of the internationalization process, which according to Johanson and Vahlne (1990), will proceed along the presented stages whether strategic decisions are made in this direction or not.

The Uppsala model and the literature it spawned have been subject to criticism. These shortcomings, which have been accepted by Johanson and Vahlne (1990), include failing to explain how or why internationalisation starts and for emphasising the characteristics of firms in each stage but giving insufficient attention to the causes of modal change. Critics have argued that the model does not fully explain multi-step mode changes or disinvestment (McKiernan, 1992), is limited in applicability to the early stages of internationalization and is highly deterministic in nature (Anderson, 1993; Calof and Beamish, 1995; Melin, 1992). The model tells us little about the internationalization process of experienced companies having the benefit of many years of international activities in many countries. Furthermore, the model does not pay enough attention to acquisition, joint venture and strategic alliances as pathways to internationalization, options that alter the model's experiential knowledge imperative.

Forsgren (1989) has argued that the psychic distance theory is only valid in the early stages of internationalisation when lack of market knowledge and market resources are constraining forces. These cease to be as important when the firm has activities in a lot of countries. A study by Nordstrom (1991), for example, found that, while psychic distance played a role, market potential was the most important explanatory factor in locational choice (Anderson, 1993; Calof and Beamish, 1995; Melin, 1992).

Both stage models discussed suffer from distinct limitations. They pose a unitary progression where each stage is a necessary precursor of succeeding stages (Van den Ven, 1992). Each stage is the result of predetermined factors with unforeseen environmental developments playing no role. They disregard individual differences between large and small firms, service providers and manufacturers, and their deterministic nature offers little scope for managers to make voluntary strategic choices beyond the initial decision to expand into foreign markets.

The internationalization process school, for all its weaknesses, retains considerable influence based mainly on the very large number of empirical studies which have identified a sequential pattern of entry mode choices by MNCs. Hence, it is somewhat surprising that McKinsey and Co. (1993) observed a growing incidence of 'born global' firms, those which began exporting within two years of commencement of operation, among the population of Australian manufacturing exporters. This development may reflect the late entry of Australian firms into the internationalization process, giving these firms the opportunity to shorten or skip the initial 'domestic only', or primary stage in the Uppsala model. If so, it belies Johanson and Vahlne's contention that corporate strategy has no opportunity to circumvent the core role of experiential knowledge in entry mode choice. 'Born global' behaviour has been observed in other countries (Madsen and Servais, 1997). Welch and Luostarinen (1988), for example, found small English, Australian and Swedish firms skipped various stages and had foreign direct investments unexpectedly quickly. Similarly, Edwards and Buckley (1998) found the majority of Australian manufacturing firms which had invested in facilities in Britain had not passed through an export stage.

Madsen and Servais attribute this behaviour to new market conditions, technological developments and changes in the capabilities of entrepreneurs. First, the trend to specialisation and the development of niche markets, especially in high-tech products, may force firms to look for export markets very early in their history to secure economies of scale. Second, new production technology has meant that internationally competitive levels of costs can be achieved at lower levels of production than applied in the past. For example, efficiencies in transportation of goods and people mean that this barrier to international trade has been reduced. Third, entrepreneurs have more international skills than in the past based on changes in education, travel and the fact that many start new businesses having the advantage of experience and networks stemming from working with large, international firms previously. The uncertainty which the Uppsala model asserts determines the slow evolution of internationalization is therefore less significant than in the past.

A third area of the literature which identifies and seeks to explain internationalisation decisions in a long term and integrated manner is that which focuses on the organisational arrangements firms must put in place to coordinate and control their overseas operations. This literature argues that the coordination and integration of the firm's activities will influence choices on the ownership arrangements (wholly-owned subsidiaries or joint venture) and on the locational settings of the subsidiaries. In the first major study of organisational structures of international firms, Stopford and Wells (1972) found that managers in MNCs had followed similar strategies and had developed similar organisational structures in quite different industries. Based on a survey of 187 large, US manufacturing firms each having manufacturing facilities in at least six foreign countries, Stopford and Wells observed epochs of internationalization. In their first forays into the international market place firms established relatively autonomous foreign subsidiaries. They called this the *international* stage. It was followed by a stage in which the MNC established an *international business division*, separate from domestic operations, intended to increase control and coordination of the expanding international activities. This division was responsible for all foreign activities of the firm and became its locus of international expertise (Egelhoff, 1988).

In time, as the proportion of foreign sales to home market sales grew, the autonomous international division came to constrain the internationalization process since only the manager of the international division had responsibility beyond the home market. In the third stage, two new types of global structures replaced the international division: *worldwide product division* and *geographic area division*. In the former, the domestic product division assumed worldwide responsibility for its particular line of products. It centralised and integrated strategic decision making for a product line. This structure is especially suited to realising economies of scale in R&D, manufacturing and marketing (Martinez and Jarillo, 1991). A worldwide product division was more common for firms with great product diversity but which were less sensitive to local political and economic conditions since it emphasised optimising performance on a global basis. For firms with less product diversity but considerable geographic spread, a regional division was created which would be responsible for sales of all products in the region. Each region would have a headquarters responsible for all the company's products within its geographic area. Consequently, this structure tended to coordinate around and optimise performance within a geographic area. Coordination between areas might be poor (Egelhoff, 1988). To the extent that political and economic conditions within an area were more similar than they were between areas, this structure led to strategies that were more responsive to local conditions than those of a worldwide product division.

Stopford and Wells also identified a matrix model which was a combination of these two structures. Subsidiaries report along two different channels, to both regional headquarters and the product division. This may provide a strategic compromise that is both locally responsive and achieves economies of scale in product development and marketing but is likely to be costly in terms numbers of management personnel and in conflict resolution (Egelhoff, 1988; Hill, 1997). In other cases, hybrid models were used with some products sold on a worldwide basis and others through regional divisions (Egelhoff, 1988; Stopford and Wells, 1972).

Franko's (1976) study of 85 large, European industrial firms found a different pattern of internationalization. More firms retained the initial parent-subsidiary form with direct ties between the parent and each subsidiary than had been observed by Stopford and Wells. In this study, as firms expanded their international activities, most did not use an international division but went directly to a worldwide product structure. Studies of Scandinavian firms have shown that they have followed the European pattern, retaining the parent subsidiary pattern until the 1970s when most adopted the global product division structure (Hedlund, 1984).

The studies by Stopford and Wells (1972) and Franko (1976) gave valuable insights into the historic development of international strategies and structures and identify *which* particular structures and strategies emerged. However, their contributions are far more modest in regard to *why* these changed over time and *how* the changes were carried out. Although they take a longitudinal approach, they present steady states of structural forms rather than describing the processes of formation and implementation related to these structures (Melin, 1992). Importantly, they adopt a broad perspective where entry mode choice is just one part of the picture, operations in foreign countries requiring coordination whether they are served by exports or local production funded by FDI.

Egelhoff (1988) found that the Stopford and Wells model was limited in that it did not address the impact of foreign manufacturing on the choice of structure. He argued that this was important in explaining the choice between area division and worldwide product division. When a parent achieves foreign sales primarily through exports, the primary interdependency is between foreign entities and the parent. A worldwide product division structure provides the kind of information processing and integration necessary to coordinate this kind of dependency. However, when foreign sales are supported with extensive foreign manufacturing, important interdependencies usually develop between foreign subsidiaries in a region as the MNC tries to replace the economies of scale lost through central production with regionally rationalised production. The area division structure provides the kind of information processing and integration required to coordinate this kind of interdependency.

Emerging in the mid-1980s, the 'process school' of research in international management criticised the Stopford and Wells and Franko interpretation of organisational structure and strategy as being too *architectural* (Doz and Prahalad, 1984). Instead, they saw managers constantly facing the competing imperatives of cost reduction, achieved through economies of scale in rationalisation of global operations, controlled at the centre, and the need to accommodate the differing needs of governments and customers in individual national markets. No unique structure provides the solution to this dilemma. They argued that senior management develop *multifocal* strategies where responsiveness and integration needs are weighed against each other separately for each decision. MNCs are therefore not symmetrical. Different subsidiaries adopt a different stance on the integration versus localisation dilemma (Doz, 1986). This school emphasises the functioning and capabilities of the MNC rather than its structural form. Informal coordination mechanisms such as normative values and patterns of communication replace hierarchical control. The main driving forces for change are environmental, with strategy adapting to opportunity (Birkinshaw and Morrison, 1995; Martinez and Jarillo, 1991).

From this perspective, Bartlett and Ghoshal (1991) see the European model described earlier as a *decentralised federation* of assets and responsibilities which allow foreign units to respond to local differences. The US model, by contrast, is a *coordinated federation* where the subsidiaries are more dependent on the parent company, being subject to more formal control in pursuit of economies of scale. They also identified a third model, dubbed the global organization model, which they believed fits the managerial norms of Japanese MNCs. This can be characterised as a *centralised hub* in which most assets and decisions are centralised and foreign operations are used as pipelines to a generic global market. The subsidiaries are tightly controlled and highly dependent on the parent. Others in this school identify a trend to heterarchial MNCs with many centres, in which traditional headquarter functions are dispersed, subsidiaries have responsibility for strategy and where each part of the company shares information (Birkinshaw and Morrison, 1995; Hedlund, 1984). However, the school has been criticised as lacking theoretical underpinnings and relying unrealistically on corporate culture to coordinate managerial decisions. On the other hand, the school has identified new organisational patterns of MNCs and, usefully, they have emphasised the need for multidimensional approaches to interpreting international strategy (Melin, 1992).

Hill, Hwang and Kim (1990) in seeking to develop an all-encompassing theory, link the organisational structures, as described by Franko, Stopford and Wells and Bartlett and Ghoshal to mode choice. They argue that this choice will be determined by a strategic assessment of three variables: the degree of control offered by the mode; the resource commitment the mode requires, and; the risk the firm must bear. *Control* refers to authority over operational and strategic decision making. The least level of control is offered by licensing and the highest by a wholly owned subsidiary. In the case of licensing, control is given to the licensee in return for monetary payments and a commitment to abide by any terms set out in the licensing contract. In the case of the wholly owned subsidiary, control over day-to-day operations and certain strategic decisions *may* be delegated to the foreign subsidiary but ultimate control always remains with the parent. In the case of joint venture, the level of control is dependent on the ownership split. Control is shared. Thus the level of control of a joint venture falls between that associated with licensing and that of a wholly owned subsidiary.

Resource commitment refers to the extent to which the mode requires dedicated assets, tangible or intangible, that cannot be redeployed to alternative uses without cost. In the case of licensing, the licensee bears most of the cost of opening up and serving the foreign market. The resource commitment is therefore low. By contrast, a wholly-owned subsidiary requires that the MNC bear all the resource cost. Once again, the level of resource commitment of a joint venture falls between these extremes, depending on the resource sharing between the venture partners.

Dissemination risk refers to the risk that firm-specific advantages in know-how will be expropriated. Technological and marketing know-how constitutes the basis of the competitive advantage of many MNCs (Casson, 1982; Caves, 1982). The MNC will not want to see firm-specific know-how disseminated as this reduces the future income flow.

Strategy influences the choice of entry mode, and thus the level of FDI required, primarily through the control requirements that the strategies entail. Different strategies require different degrees of control over the operating and strategic decisions of foreign affiliates and thus different entry modes. A central strategic decision of the MNC is whether to adopt a 'multidomestic' or 'global' strategy, (being refinements of the structures identified by Stopford and Well, Franko and Bartlett and Ghoshal). In the former, subsidiaries may have their own marketing function, autonomous manufacturing facilities, products may vary with local consumer preferences and local strategy may vary depending on differences in competitive conditions. Assuming dissemination risk is not a particular concern, this implies that only a low degree of control is required. Thus, MNCs adopting a multidomestic strategy may prefer to choose joint venture or licensing entry mode as they represent a low-cost option, that is, they require less resource commitments.

However, where there is a potential for developing standardised products for the global market place, realising considerable economies of scale, firms may prefer a global strategy. This involves forgoing some of the benefits of a multidomestic strategy, preferring the cost savings of scale economies to any demand advantages of product differentiation. Global strategy may involve dispersing elements of the production process around the world on the basis of cost minimisation, with subsidiaries exchanging parts and products with other subsidiaries in the MNC's global system. Coordination of such an interdependent global production system necessarily involves a high degree of control over the operations of subsidiaries (Egelhoff, 1988; Martinez and Jarillo, 1991). The various production units must accept the parent's instructions on what they should produce, how much they should produce and how the output should be priced for transfer between units. Licensees and joint venture partners are unlikely to accept such a subservient role (Hill, Hwang and Kim, 1990). Thus, firms pursuing a global strategy are likely to favour a high-control entry mode, ie. wholly owned subsidiaries, a more FDI-intensive strategy than other options.

Where a firm is part of an international industry with a limited number of competitors who confront each other in many different national markets, oligopolistic interdependence may influence the strategic choices of the firms involved. For example, when they enter markets they may have strategic objectives that go beyond the standard assessment of cost and revenue. A subsidiary may be established to act as a competitive scanning post in an otherwise unprofitable market or to check the cash flow of a potential global competitor (Kim and Hwang, 1992). They may enter the home market of a rival, even though that market may not be viable on strictly economic grounds, simply to check their rival's ability to compete elsewhere. Such strategies must be controlled by the parent. Pricing, marketing and transfer pricing decisions must support the overall strategy. A foreign operation may even be required to operate at a loss, at least for a period of time. Licensees and joint venture partners are unlikely to accept such conditions. Thus, when there is a need for global strategic coordination, a wholly owned subsidiary will be the favoured entry mode (Hill, Hwang and Kim, 1992).

A global strategy approach to market penetration involves building significant market share in globally strategic markets. Such countries are important beyond their stand-alone attractiveness. They may be a source of volume to meet economies of scale, the home of global competitors, or they may be a major source of industry innovation. Failure to compete in strategic markets can undermine competitiveness elsewhere (Lovelock and Yip, 1996). This is especially true for network firms such as airlines, financial services and logistics firms. For example, no service firm with global ambitions can afford not to have a presence in New York, London and Tokyo.

Some writers have identified a trend for MNCs, under increasing pressure to reduce costs, to move away from multidomestic toward global structures (Levitt, 1983). Birkinshaw (1996) for example, argues that increasing liberalisation of trade has made the multidomestic structure uncompetitive. In his assessment, many subsidiary operations of firms with multidomestic structures have been closed and others have taken on specialised roles involving greater integration of the MNC's global operations. Two main types of specialisation are available: *rationalisation-integration and world product mandate.* Rationalisation-integration occurs when a subsidiary produces a component to be used by the MNC elsewhere in the production chain. The parent company retains control of all associated activities, notably the design and development of the product. The world product mandate, by contrast, gives the subsidiary responsibility for product development and export marketing. This arrangement ensures that high-value adding activities are undertaken in the subunit as well as providing its management with the opportunity to develop and grow the mandate over time.

Both rationalisation-integration and world product mandate versions of global structures imply a greater degree of interaction between and integration of the various units that comprise a global firm. In this light, MNCs may be seen as interoganisational networks in which, instead of all strategic decisions being made by the parent and handed down the hierarchy to each subsidiary, multiple centres of expertise around the world share products, expertise and initiatives (Ghoshal and Bartlett, 1990). Such organisational structures make the participation of separately owned licensees or joint venture partners problematic because each transfer of product, knowledge or strategic initiatives needs to be tracked and accounted for in the division of profit. The more complex, the more integrated the group, the more likely wholly-owned subsidiaries will be preferred to licensing and joint venture arrangements, with the consequence that FDI will be that much greater than if shared ownership arrangements were used.

Market liberalisation in a regional context will also influence the strategies of international firms, providing incentive for more interdependency and integration within the MNC's regional network. It also encourages firms to commit FDI to establish 'insider status' within the regional trade area. Hirsh (1992) studied the competitive position of firms outside regional trade areas (RTAs) as against insiders, and the position of insider firms relative to each other. He concluded that outsider firms exporting to an RTA are disadvantaged by comparison with insider firms exporting to fellow members. The 'inside' exporter enjoys reduced costs from the removal of tariffs or reduced border costs whereas the foreign firm exporting to the RTA experiences no cost savings. Additional export opportunities are created for 'insider' firms as a result of this advantage. Hence, Australian firms have the opportunity to capitalise on the trade creation effects available to members by establishing subsidiaries in member countries. Such a strategy allows firms to minimise the trade diversion effect that would apply should they remain exclusively domiciled outside the group. It allows them better access to the expanded market. Consequently, regional trade liberalisation will induce firms to reconsider their entry strategies, with many replacing export strategies with local production, funded by foreign direct investment.

Firms with existing operations in the trade area are likely to reorganise in two ways. First firms may adapt to the changed pattern of regional comparative advantage and pursue economies of large scale production made possible by the larger market (Cantwell, 1992; Doz, 1986). Rather than a multiplicity of relatively small, protected operations spread across the region, economic integration will see multinationals concentrate production in countries with a comparative advantage in those particular activities. Second, the possibility of promoting the internal division of labour within multiplant firms can be expected to lead to increased vertical integration. That is, firms will separate activities spatially in order to reduce costs. This may result in plants becoming more specialised and the number of plants may increase. Production will be sited where the input used most intensively in a particular process can be acquired at least cost. In time, this may lead to a divorce of locations for assembly and research and development (Cantwell, 1992). Such a situation calls for a high degree of control over each of the subunits that make up the regional MNC network. Control is strongest in the wholly-owned subsidiary structure. Hence, regional trade liberalisation may lead to an increase in FDI by firms to strengthen their control over their subsidiaries.

Many environmental factors such as country risk, location familiarity and demand conditions have been identified in the literature as being significant in determining the choice of entry mode. Hill et al argue that these factors can be interpreted as impacting on strategic decision-making through their implications for resource commitment, control and strategic flexibility (Hill et al., 1992). FDI creates sunk costs, establishing a physical and personal link in the foreign country that will remain even if the original market conditions which attracted the firm cease to apply (Buckley and Casson, 1981). Hence, firms may not be willing to commit resources to high risk countries, preferring entry through exporting (Agarwal and Ramaswami, 1992). Firms may seek to limit their exposure to country risk by minimising their resource commitment and increasing their ability to exit high risk markets without taking a substantial loss should the environment worsen (Hill et al, 1992). The appeal of this strategy is enhanced if, as found by Bradley (1977), joint ventures with local partners are less likely to be expropriated than wholly owned subsidiaries.

In summary, a strategic interpretation of FDI looks to the manner in which the investment contributes to the achievement of the firm's long term objectives. The internationalisation process model, Vernon's product life cycle model and various theories of corporate control and coordination have been examined to ascertain what insights they offer into understanding the relationship between FDI and strategy. The mechanistic nature of the product life cycle and internationalisation process models mean they did not offer a role for strategic decision-making, either in mode choice or locational choice. The literature addressing corporate governance systems, on the other hand, suggests that FDI, especially that funding wholly-owned subsidiaries, is likely in MNCs that have adopted integrated global structures of governance because of the control this mode offers, control being essential in highly integrated MNCs to ensure that the interdependent subunits behave in a mutually supportive manner. Rather than a decision taken in isolation, foreign market entry achieved by establishing value-adding facilities inside the target market, funded by foreign direct investment, is just one element of corporate strategy.

IDENTIFICATION OF A RESEARCH AGENDA

Research examining the internationalisation of the Australian economy has focussed primarily on macroeconomic aggregates such as the levels of imports and exports and the growing importance of these for the Australian economy (for example, see Athukorala, 1995; Pomfret, 1995; Snape Adams and Morgan, 1993). Relatively little attention has been given to the internationalization of the economy through offshore production by Australian firms or through production within Australia by foreign multinationals, the exceptions being the McKinsey & Co (1993), Yetton Davis and Swan (1991), Department of Industry, Science and Technology (1994) and Bureau of Industry Economics (1995). This section will propose a range of research questions that might give some direction for scholarly activity in this area.

The dynamic nature of internationalization, and associated financing methods such as FDI, calls for research that is responsive to the longitudinal character of internationalization as a development process through time. While it is valuable to study individual events, a more complete picture is supplied when the whole development of a firm from the time of its founding to the present time is examined (Melin, 1992). Hence, a rich, broadly focussed study that results from careful examination of a few organisations over a long period of time may be superior to statistically rigorous but narrowly focussed studies (Huff and Reger, 1987).

Stages model of internationalization, including those of Vahlne and Johanson, Vernon, and evolutionary models of international structure, including those of Stopford and Wells, Franko and Bartlett and Goshal, are based on surveys of manufacturing firms. The internationalization of service firms and firms that combine goods and services needs more attention (Lovelock and Yip, 1996). This observation is highly relevant for Australian scholars as the majority of Australian FDI abroad has been directed to service firms (ABS, 1997).

Research should give attention to new patterns of internationalization, including that of 'born global' firms. Have McKinsey's 'born global' firms performed as well as those Australian firms that have pursued more traditional, sequential entry methods? Have services firms followed the same pattern? Do Australian firms move more quickly through the exporting stage, or even skip the exporting stage, more rapidly than firms from other countries? If so, do geographic, structural or historical factors explain the difference?

Research should give more attention to the acquisition mode. Firms with what organisational patterns are more likely to acquire existing firms? In what stage of internationalization is acquisition more likely? This research should not assume that such decisions are always rational. It may be that irrational factors are important at times. For example, it might be that the rush to acquire businesses in Europe prior to 1992 and to acquire companies in Asia in the mid-1990s reflected a bandwagon effect with firms developing strategies to legitimise their investments after the decision has been made (Hellgren and Melin, 1991).

Research might also give attention to a broader range of entry modes beyond exporting, licensing and FDI. Strategic alliances with local or other foreign firms may involve no transfer of funds. Alliances are another entry mode option that deliver similar strategic advantages to joint ventures but have received little attention in the literature beyond those firms whose home country is either the US or Japan (Tse, Pan and Au, 1997; Yoon, Morash, Cooper and Clinton, 1996).

Studies of structure and coordination of MNCs have been characterised by cross-sectoral approaches and findings expressed in static models (Melin, 1992). How and why do control and coordination mechanisms change over time and how do these changes interplay with strategic actions? Have Australian firms altered their international organisational structures over time? If so, have they followed the US pattern incorporating international divisions, the European pattern that does so to a lesser degree, some other pattern, or none at all?

Changes in the structures of MNCs might have policy implications for Australian governments. Does Australia have less to offer MNCs that have moved to a global strategy than it does to MNCs in the 'multidomestic' stage? Do the global firms bring fewer benefits to the Australian economy than multidomestics? All subsidiaries require marketing, local R&D, accounting and other services. In a global strategy, more of these services are provided in a uniform manner from the parent or from regional centres, possibly by subsidiaries of other multinational corporations that enjoy a global relationship with the MNC. This may imply a reduction in linkages with purely local Australian firms. A stronger central role by the parent might diminish the capacity for Australia to benefit from the establishment of regional headquarters, a priority for the government in the past (Department of Industry, Science and Technology, 1994). Further, if the organisational structure of MNCs reflects their region of origin, and different structures leave host countries with differing levels of externalities, then government policies designed to benefit from FDI inflow would be strengthened if they were attuned to this fact.

Finally, a central issue for Australian researchers is: how 'internationalised' have Australian firms become? The lack of a systematic measure of internationalization has meant that researchers have not been able to develop a widely accepted measure of internationalisation. It is therefore difficult to assess the extent of internationalization of firms or to get accurate pictures of how internationalization takes place (Makhija, Kim and Williamson, 1997). Researchers have used various definitions of internationalization. At the level of the firm, various scholars have focussed on single variables to measure degree of internationalization (Sullivan, 1994). These include foreign subsidiaries' sales as a percentage of total sales (Stopford and Dunning, 1983), foreign assets as a percentage of total assets (Daniels and Bracker, 1989) and the number of foreign subsidiaries (Stopford and Wells, 1972). More recent works have used composite measures. Morrison and Roth (1992) for example, used the level of international trade, intensity of international competition, worldwide product standardisation and the presence of competitors in all key international markets as their 'dimensions' of globalization.

Reference to internationalization theories suggests that the degree of internationalization might be seen from three perspectives: *performance* (what goes on overseas, Vernon, [1971]), *structural* (what resources are overseas, Stopford and Wells, [1972]) and *attitudinal* (what is top management's international orientation, Perlmutter, [1969]). Sullivan (1994) uses a composite measure which operationalizes all three perspectives. His measure includes the single measures quoted above plus others reflecting behavioural models of internationalization: the total duration of top managers' foreign assignments and 'psychic dispersion', measured as the spread of subsidiaries across various psychic zones around the world.

In summary, the range of issues examined in the international business literature and reported on in European and US based journals remains largley unexplored in the Australian context. Research into the locational choices for FDI, the reasons FDI has been preferred to other entry modes and the nature of organisational structures would complement macroeconomic studies of imports and exports. This offers fertile ground for academics whose work might give great insights for use by both international managers and government policy makers.

IMPEDIMENTS TO IMPLEMENTING THE RESEARCH AGENDA

The primary impediment is the lack of an Australian community of scholars who are committed to these issues. Very few papers are presented by Australian academics at regional gatherings of the Academy of International Business (AIB). Three factors might be important in explaining this situation. First, no network of scholars is in place. The Australian chapter of the AIB has been effectively dissolved and is now administered as part of the South East Asian chapter. This means that researchers tend to work in isolation. Second, research into many aspects of MNC activities is typically conducted using survey data. This can be tedious and expensive and may give unreliable results if firms choose not to respond, a likely result if they fear that the information may become available to competitors. Third, there are very few journals based in Australia that are prepared to consider international business submissions.

The problem of access to data may also explain why very few economists in Australia pursue research in this field. A count of articles published in Economic Papers and the Economic Record since 1983 revealed only four articles that, judging by titles, dealt with FDI. Anecdotal evidence, supported by an examination of the departmental allegiances of academics that have presented papers at AIB and European International Business Academy conferences, suggests that research into MNCs and FDI is conducted mainly by personnel in departments of management and marketing. How can we get more economists involved?

One useful step to overcome these problems is to establish a central data base of Australian firms with operations abroad and foreign firms with operations in Australia. To provide a comprehensive data source it should include organisational as well as financial data. A data-base operated by Harvard University has been the source of many seminal papers on MNCs in the US. This would need to be maintained over time because a comprehensive understanding of the internationalization process of Australian firms needs to capture long periods of time and even histories of the whole development of the firm. Such a data base would facilitate this kind of research.

In conclusion, research into foreign direct investment must recognise that the foreign operations it funds will be one aspect of internationalization, a dynamic process that reflects the strategic direction of the firm. An understanding of FDI must presuppose an understanding of internationalization as a strategic process. While it is entirely appropriate to study FDI at a macroeconomic level, it is also worthwhile examining it at the level of the firm. In doing so, scholars should consider the strategic imperatives of firms as these will be reflected in management decisions which lead to foreign direct investment.

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