

# Perception and Facts on the Activity of Multinational Enterprises

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## Abstract

MNEs are considered to be major global players with an overwhelming influence on the local economies they operate in, believed to be expanding in dimension and influence. Various opinions are divided between them having a positive and negative, not necessarily based on an objective economic analysis rather on a subjective perception. In this paper we bring forward arguments of the important dimension of MNEs based on statistics and facts.

We first provided a synthesis that highlights both the positive and negative impact of MNEs, based on key Statistics on their financial results and effects on the regional economy. Then we showed that MNEs impact on the region of activity and have a more efficient output than a whole country based on a comparison of the value added per number of workers for the U.S. MNEs and the ratio of GDP per capita for the country in 2008 and 2000, as opposite to some findings from the literature review. We continued with a survey on the small and micro local IT firms from Bucharest to find out their perception about the influence MNEs have on their activity and found that it mainly consistent with the statistics above.

**Key words:** multinational enterprises, foreign direct investments, impact, perception, multiplier effect.

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## 1. INTRODUCTION

Multinational enterprises (MNEs) account for economic growth and development of regions, have knowledge spillover effects, induce competition, thus greatly influencing the macroeconomic frame.

On local firms the impact of MNEs induces productivity growth, jobs creation, increasing the level of the human capital, technological improvements, developing the export capacity by opening the access to external markets. On the regional economy MNEs contribute to: economic growth, to GDP components, increasing the interest of external investors, stimulating competition as they are increasing the innovation capacity and discouraging monopolies; lower pollution for the environment as a consequence of MNE partnerships but also ecological disasters as in the case of oil tanks accidents.

On one hand, they contribute to the development of the economy and on the other they are also a major source of inefficiencies and inequalities within and among various development regions. Although pros and cons on MNEs are largely debated in the literature review, the grounds for various statements are not necessarily based on objective economic analysis rather on subjective perception. In this paper we bring forward arguments of the important dimension of MNEs based on statistics and facts.

## 2. THEORETICAL BACKGROUND

The influence, power and expansion of MNEs have been largely debated. Statistics are objectively supporting their large dimension and importance. Thus, approximately one fourth of the global GDP, a value of \$16 trillion is represented by the value-added generated by the MNEs' production across the globe in 2010 (UNCTAD, 2011). Also, one third of the world exports was generated by foreign affiliates of MNEs in 2010 (UNCTAD, 2011).

It was found that between 1990 and 2005 the inflow of foreign direct investments (FDI) in GDP at a global level, in current prices, had risen from 1% to 3% (UNCTAD, 2006). MNEs employ an impressive number of people; 73 million persons are directly employed within MNE (ScriGroup Int., 2012). Moreover, MNEs own 75% of humankind innovation capacity (ScriGroup Int., 2012).

Between 2003 and 2008, the growth rate of employment by U.S. MNE in China attained an impressive figure of 153% (Wolverson, 2011). One fourth of U.S. jobs were created in Asia out of the total

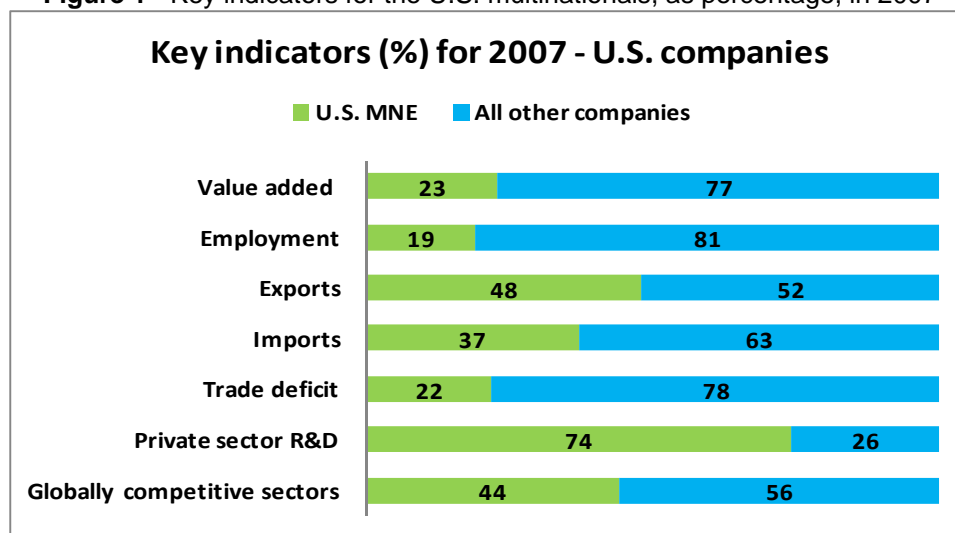
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employment of U.S. MNE abroad (Wolverson, 2011). In 2007, U.S. MNEs in U.S. private sector represented only 20% of its economic activity, nevertheless they accounted for over a third of the sales and almost a quarter of GDP; they also employed one-fifth of the workforce, generated a quarter of its gross profits (Cummings, Manyika, Mendonca et al., 2010). Besides, 41% was the productivity gains from 1990 to 2007 (Cummings, Manyika, Mendonca et al., 2010). While U.S. MNE accounted for less than 1% of all U.S. companies in 2007, their contribution to economic welfare was disproportionate (Fig.1).

**Figure 1 - Key indicators for the U.S. multinationals, as percentage, in 2007**



Source: Cummings, J., Manyika, J., Mendonca, L. et al. (2010). *Growth and competitiveness in the United States: The role of its multinational companies*. McKinsey Global Institute

We can derive from the graphic above that in 2007 U.S. MNEs accounted for a half of the country's exports and more than one third of the total imports, and contributed up to 75% of the private sector R&D spending; they employed 19% of the private sector workers. Up to 44% of their economic activity was concentrated in eight most competitive sectors: manufacturing, information, professional services, retailing, mining and resource products, finance, wholesale trade and utilities.

Nevertheless, several authors and groups of influence state that there are also negative effects not only on regional economic activity but also on social, cultural and political life, due to economic, financial and political power MNEs encompass combined with frequent excesses on ecological or social plan. The value added can disappear once the final products are exported in the country of origin and the employees are fired.

It is even believed that, sometimes, these economic entities influenced greatly the markets, rivaling with national governments, implementing their own norms and values and changing business cultures (Postelnicu, 2005).

A report sponsored by the Business Roundtable and the United States Council Foundation (Slaughter, 2010), reiterates the same conclusions as in previous years about the U.S. MNEs: they contribute to economic growth through capital investments, trade and research and development. In the end these lead to multiplier effect, job creation and higher compensation.

Thus, the contribution of parent MNEs can be summarized below:

- Output: 24.3% of all private-sector output, around \$2.6 trillion;
- Capital investment: represented 29.4% of all private-sector, which had been \$482.5 billion in new property, plant and equipment;
- Export: 45.2% of U.S. total or \$515.4 billion in goods worldwide;
- Research and Development: 74.4% of the total R&D performed by all U.S. companies; investments in R&D raised to \$200.4 billion;
- Employment: 19.1% of total private-sector payroll employment, meaning more than 22 million U.S. workers;
- Average compensation per worker: 18.7% above the rest of private sector average;
- Multiplier effect: \$6.03 trillion in intermediate inputs, out of which 88.9% or \$5.36 trillion was bought from other companies in the U.S..

Indeed MNEs have a multiplier effect interacting with local firms and raising the added value on the growth of the local economy. It is estimated that the total contribution of U.S. MNE to the GDP private

sector rises from 23% (direct contribution) to 34% (comprising also indirect contributions) in 2007. Same multiplier effect can be seen in the U.S. MNE employment private sector, raising the total impact on employment to 28% from 19% which represented the direct impact (Cummings, Manyika, Mendonca et al., 2010).

The support of MNEs during the deep recession is also highlighted here. The analysis had been undertaken on 24755 majority-owned affiliates and their 2202 U.S. parents in 2007, using data from the Bureau of Economic Analysis of the U.S. Department of Commerce.

Unfortunately, MNEs bring not only benefits but also costs to economic regions. Thus the following issues cannot be neglected:

- job migration from developed countries to developing ones with lower wages and less regulations;
- 26% was the share of MNEs in U.S. GDP that remained relatively constant from 1990 to 2006, at a value of \$3.5 trillion (Wolverson, 2011);
- incomes and profits tend to shift to low-tax countries; for example, in Ireland there is nearly 0 rate on royalty income and 12,5% on corporate tax rate. In comparison to that, within OECD countries the average tax rate on MNEs is about 27%, compared to 39% in the United States (Wolverson, 2011);
- in 2008, 83 of 100 largest U.S.-based multinationals had subsidiaries in tax havens that brought basically no benefits to the government's budget (United States Government Accountability Office, 2008);
- one third of world trade consists in commerce among subsidiaries of a MNE (ScriGroup Int., 2012).

MNEs are major global players mainly through their large financial power and as the impressive dimension of operations scale and networks on the market and bargaining power in the policy-making arena.

The results of MNEs have frequently been compared with that of entire countries, threatening the democracy of countries.

In addition, several authors like S. Anderson and J. Cavanagh, aver that out of 100 biggest economies in the world, 51 are MNEs and the rest are countries (Anderson and Cavanagh, 2000).

An interesting result was found by M. Desai, averring that 10% increase in FDI leads to a 2.6% of additional domestic investment (Desai, Foley, and Hines Jr., 2009). Not only do MNEs have to face global competition but they also are sensitive to changes in global economy being linked to the global business network.

Despite the positive impact, what happens when they take their operations overseas?

Indeed, nowadays, the trend of MNE evolution is to migrate towards the developing countries to third ones that offer better regulation systems and low cost workforce. This is a frequent case within automotive and textile industry (Scalera and Uruci, 2011a).

Most effects have resulted in sharp declines in exports, as registered by Bureau of Labour Statistics in U.S., once with the expansion of giants companies like General Electric and IBM worldwide.

Also, unemployment in the home country seemed to be another problem faced by the home economy due to their expansion. Nevertheless the finding of M. J. Slaughter averred, through the expansion of foreign affiliates, U.S. MNEs continue to enhance the parent economy, complementing the activity in the home country (Slaughter, 2010).

The idea of a higher concentration abroad rather than in the country of origin, is contradicted by facts, maintaining a "large presence in America relative to the overall U.S. economy and relative to their foreign affiliates".

We summarized below the major pros and cons of the perception about MNEs impact on regions of development (Tab. 1).

**Table 1 - Perceptions on positive and negative impact of MNEs**

No.	POSITIVE IMPACT	NEGATIVE IMPACT
1	FDI contribution to domestic capital formation and thus to economic growth (technological improvements, productivity growth, jobs creation), positive impact over the balance of payments; large capital investments including research, development and innovation	Increased consumption of manufactured products whose profit is then sent back to the country of origin instead of being reinvested in the country where it operates in
2	Increasing revenues at the state budget of the host country and increased life standard	Avoiding taxation
3	Transfer of technology, knowledge and managerial expertise within the regional business environment	Negative impact over the democracy, human development (inclusively the increase of drogues and arms traffic), the quality of the environment

No.	POSITIVE IMPACT	NEGATIVE IMPACT
4	Capital flows enhancement in parallel with the development of the exchange of goods and services, leading to improved international economic relationships among countries	Processes inefficiencies and unreasonably high consumption of resources within MNE
5	Jobs creation	Relocation depending on economic conditions and job losses as a consequence and of other economic advantages; moreover, workforce exploitation and few skilled workers are employed
6	Increasing the level of workforce qualification at a national level for developed countries	Externalizing under-qualified activities to developing countries
7	Transforming some enterprises into profitable ones or stimulating the activity of some local adjacent enterprises (like local suppliers for MNE or externalizing some MNE activities to local firms), increasing the export capacity by accessing external markets	MNE can lead to the bankruptcy of certain local enterprises (competition growth through price reduction, replacing local suppliers with international ones)
8	Infrastructure development through public-private partnerships	Profits repatriation
9	Standardization and increasing quality of products	Using informal intermediaries to enter a particular market for advertising, selling counterfeit products
10	Major contribution to GDP	Due to very large financial resources, can influence certain markets and political decision makers
11	Improving business environment and enhancing the attractiveness of developing economies for foreign investors	Widening the gap between economic development levels of various regions
12	Contribution to increased competition (resulting in lower prices, diversification and improvement in products and services); in parallel, reducing monopoly profits	Artificial creation of cartels or artificial competition
13	Development of energy resources and manufacturing and production capacity in the country	Automatic processes and mechanization lead to lower demand for labor

Source: author's synthesis from literature review

State owned multinationals constitute an important source of FDI. Although small in number worldwide (650 state owned multinationals with 8500 foreign affiliates, less than 1% of the total MNE), their outward investments accounted for 11% of the global FDI in 2010 (UNCTAD, 2011).

Given the increasing importance of the MNE (mainly in the contribution to the real GDP growth), it is crucial that governments compete to attract them both at home and abroad or to enable the creation of new ones. Nevertheless, SMEs (small and medium enterprises) do also have a large contribution to GDP and to economic development.

### 3. ANALYSIS

F. Camerman and P. De Grauwe pointed out in their work that, following a comparison between the value added of multinationals and the GDP of the countries, the size and power of multinationals was extremely small compared to that of nations (Camerman and De Grauwe, 2002). Moreover, between the time interval of 1980-2000 there has been a decline in the size of MNEs relative to the size of countries, yet the perception was the opposite. They offer a plausible explanation, that "perceptions are subject to large cyclical movements, even if the underlying reality does not exhibit such movements".

We try to add more accuracy to the analysis, therefore we compare the percentage of the value added per number of workers for the multinationals and the ratio of GDP per capita for the nations-states.

First of all, sales of the companies were not taken into account for the comparison with GDP for the obvious reason of not overestimating the intermediate consume (deliveries). Then, taking into account the absolute value was not a proper alternative either because it would have produced a disproportionate comparison, therefore we divided both the GDP and the value added to the number of inhabitants and respectively, the number of workers. Additionally, we considered that it would be more precise to

compare the GDP per capita of a country, which is an aggregate measure to that of the sum of value added of MNEs divided by the total number of workers from the country.

We have chosen the United States as a country of reference, for two reasons: first, representativeness among the most powerful and large multinationals are based there and second, because of data availability.

As we can see from Table 1 below, the value of U.S. GDP per capita computed for 2008 is almost a half (40.51%) less of the value added per employee created by multinationals.

This is a suggestive result that shows the large importance and impact MNEs have on the region they operate in. By using these relative measures instead of absolute ones, we get a more accurate result (Tab. 2).

**Table 2 - Values of GDP per capita and Value Added per employee**

<b>2008</b>	<b>GDP, billion dollars, current prices<sup>3</sup></b>	<b>Inhabitants<sup>4</sup></b>	<b>GDP/capita</b>
United States	14296.9	304,059,724	0.047
<b>2008</b>	<b>Value added, billion dollars<sup>5</sup></b>	<b>Employment<sup>3</sup> (1000)</b>	<b>Value Added per employee</b>
U.S. multinationals <sup>6</sup>	3608	31227	0.116

Source: World Bank, (2008). BEA.

<http://www.data.worldbank.org/indicator/NY.GDP.MKTP.CD/countries?display=default>

We performed the same steps for the year 2000 and the results were similar: 0.035 was the GDP per capita of the U.S. (in billion dollars, current prices) compared to a value more than double created by the MNEs: 0,088 and representing the value added per employee.

As opposed to conclusions drawn of the analysis of F. Camerman and P. De Grauwe we can state that in the case of United States, MNEs impact more efficiently on economic output than a whole country. Taking into account the large influence MNE have worldwide, we questioned the perception of small and micro Romanian local firms about the influence of MNE on their own firms and match it with the above findings.

The objective of the questionnaire was the analysis of the perception of the impact of MNEs over the Romanian local firms. The sample was comprised of 36 micro, small and medium local enterprises in Bucharest, activating in IT field, during the time interval of August 2011 on to October 2011. The type of survey was simple random sampling.

Several characteristics were derived as descriptive Statistics of the sample:

- 36% of the respondents were females while 64% were males.
- Most of the respondents (12 persons) aged between 31 and 40 year's old, followed closely by 10 respondents aged between 41 and 50 year's old and 9 respondents between 20 and 30 year's old. Only 5 persons were above 50 year's old.
- The average number of employee was 16 persons, the smallest enterprise having 3 employees and the largest having 45 employees.
- The majority of the respondents had graduated a university (61%) and just a few had completed post-graduation studies (19%), while 19% had only secondary studies.
- 14 out of 36 respondents were more 15 years old in the company; 8 have had between 11 and 15 years within the company, and only 2 of them have had less than 1 year within the company.
- Most of respondents (58%) belonged to the Board of Management.
- Net income intervals ranged between 301 and 500 euro a month for 10 of the respondents and between 501 and 700 euro a month for 11 respondents. 14 respondents declared a net income superior to 701 euro a month.

The results of the survey pointed out several facts:

The most part of the respondents (81%), think that MNEs dominate the market within the national economy to a large and to a very large extent. Nevertheless, 31% of the respondents think that MNE contribute to a small extent to the development of the regional economy, while 58% reckon MNE bring a large contribution to it.

Asked about the most important competitive advantage of a MNE, 33% chose the management of the company, followed closely (28%) of the capital owned. Approx. 17% replied that the object of activity

<sup>3</sup> <http://www.data.worldbank.org/indicator/NY.GDP.MKTP.CD/countries?display=default>

<sup>4</sup> [http://www.census.gov/popest/data/historical/2000s/vintage\\_2008/index.html](http://www.census.gov/popest/data/historical/2000s/vintage_2008/index.html)

<sup>5</sup> <http://www.census.gov/compendia/statab/2012/tables/12s0797.pdf>

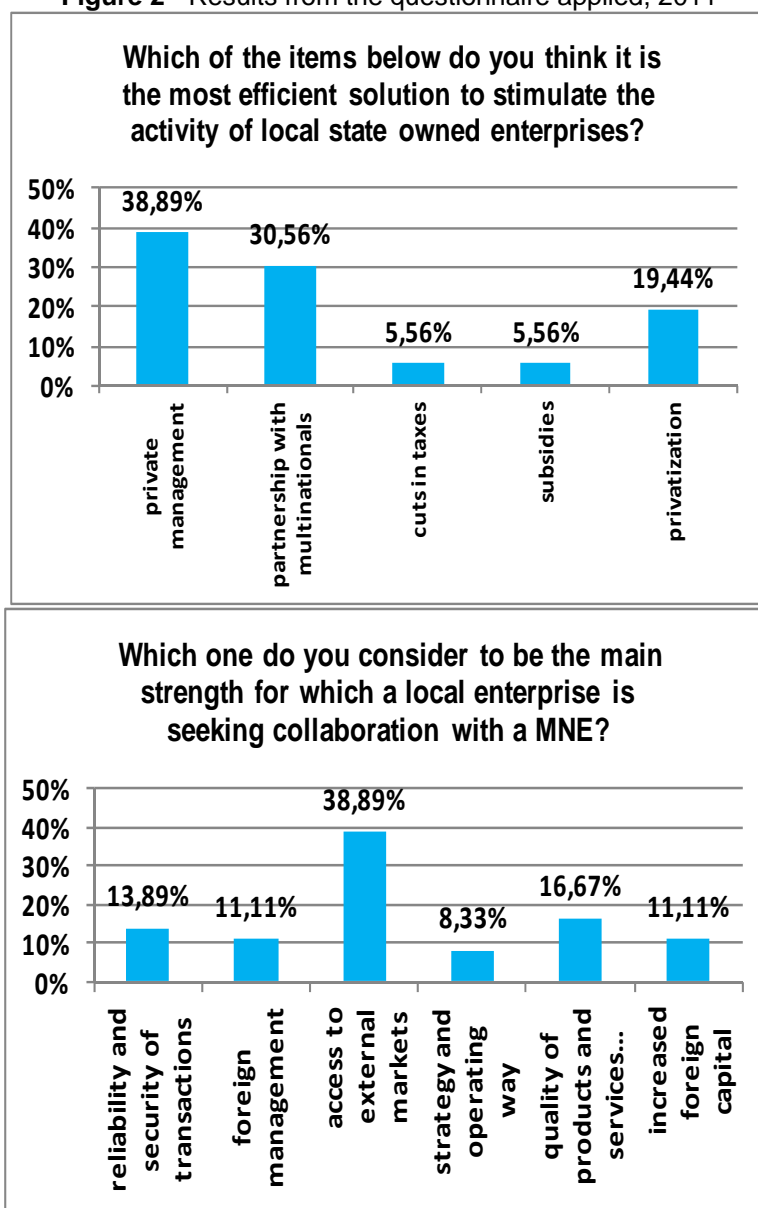
<sup>6</sup> Parent companies comprise U.S. parents and Majority Owned Foreign Affiliates

matters the most and 14% that the strategy followed made the difference. Only 8% chose access to foreign markets. One answer worth mentioning was that the most important advantage had been the short time of presentation and sale at an international level.

The majority of respondents considered their enterprise to be able to cope with foreign competitors having the same profile: 56% to a large and to a very large extent. Though, 25% had a moderate view, choosing the option - to a small extent and 8% to a very small extent. This difference of perception could be explained by the lack of complete information of the respondents.

The issue of state intervention in protecting the local Romanian enterprises of MNE competition was considered necessary by the large majority (78%). This result can be interpreted either as a remnant of the communist period either as the need of a stabilizing hand of help within the unfair and fierce competition. Most of the enterprises selected in the sample are profitable (64%), while 33% manage to survive (probably due to difficult economic and financial crises) and only 3% it is exposed to the risk of bankruptcy. The answers to the most efficient solution to be applied in order to stimulate the activity of the local state owned enterprises are depicted below. It was found that private management and partnerships with multinationals are among the favored solutions. As a main strength for which a local enterprise is seeking collaboration with a MNE was the access to external markets, chosen by the majority of respondents (Fig. 2).

**Figure 2 - Results from the questionnaire applied, 2011**

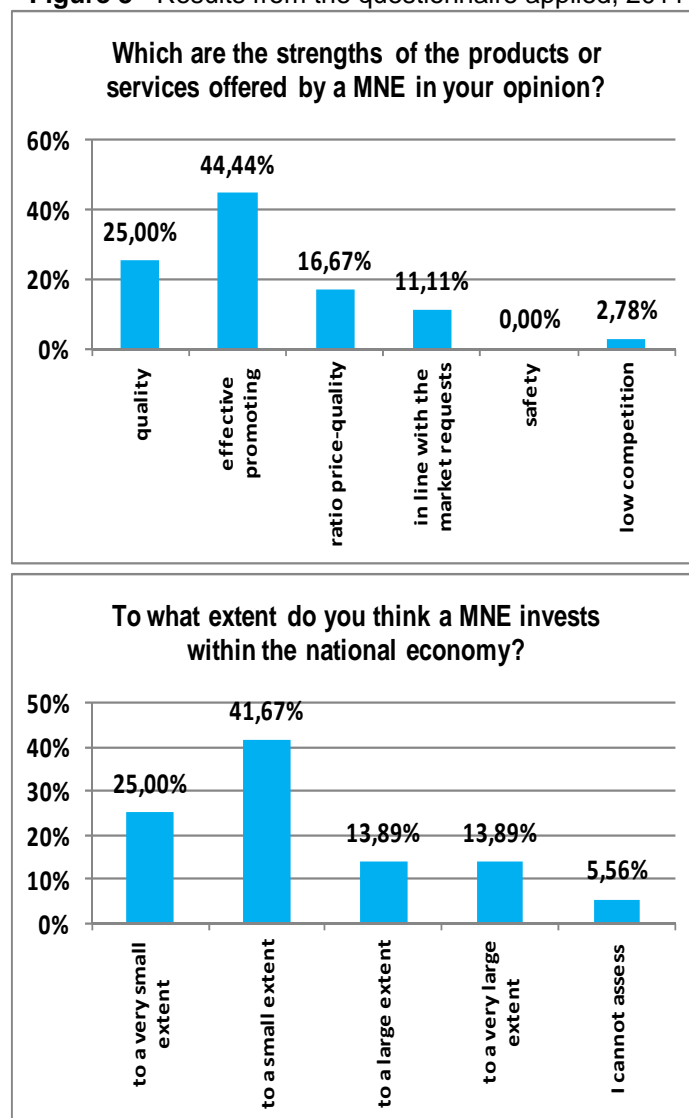


Source: author's analysis

An interesting result was the fact that 53% of respondents considered MNE activity impacts negatively local enterprises on regional market to a large and a very large extent. On the other hand 42% thought the negative impact of MNE over the local enterprises to be small and very small.

Slightly more than half of the respondents, 53% said that workforce is more inclined to choose MNE than local enterprises to a large extent and 11% to a very large extent. 67% of them think that the workforce is migrating towards the MNE. The competition between MNE and local enterprises is thought to be unfair by 61%, while 31% considered it equal. More than a half (67%) of respondents said the products and services offered by a MNE are more appreciated than those offered by the national companies to a large and a very large extent. Only 19% considered to be comparable. As we can see below, the strengths of the products or services offered by a MNE is the effective promoting, chosen in majority; next is the quality delivered; in a smaller percentage impact the ratio price – quality, complying with the market requests and the low competition. MNEs are believed to be investing within the national economy to a small extent and to a very small extent by almost 67% of respondents in the sample, as is shown below (Fig. 3).

**Figure 3 - Results from the questionnaire applied, 2011**



Source: author's analysis

MNE represent a model to the local enterprises to a large and a very large extent for 58% of respondents. 19% said they are comparable. MNE determined the increased competition for 47% of respondents to a large extent. Nevertheless, to an equal percentage of respondents, MNE did not play an important role in increasing the competition. The existence of national companies is also conditioned by the expansion of MNE for 42% of respondents to a large extent and for 28% to a small extent. Asked about the impact of MNE on their own enterprise, the opinions are diversified: 31% said the impact is negligible, 28% said it does impact to a large extent on their activity, only 6% admitted a large impact, 19% thought there was no impact.

#### 4. CONCLUSIONS AND FUTURE WORK

MNEs are considered to be major global players with an overwhelming influence on the local economies they operate in, and believed to be expanding in dimension and influence.

In the current paper we focus on the benefits and costs of MNEs, discussing the effects of their activity on the home and host economies based on statistics, then compare the perception with objective results. Although there are both pros and cons to the impact of MNEs, they bring along mainly positive effects on both home and host economies. Even though they tend to search the most profitable locations of operating thus generating unemployment, decline in exports and other similar consequences, they tend to compensate with the activity in the home economy. Also, state owned multinationals and small and medium enterprises contribute largely to economic development.

We showed that MNEs impact on the region of activity and have a more efficient output than a whole country based on a comparison of the value added per number of workers for the U.S. MNEs and the ratio of GDP per capita for the country in 2008 and 2000, as opposite to some findings from the literature review. The results of the survey highlighted the perception of local businesses that MNEs dominate the market, increase competition and considerably contribute to the development of the regional economy. Although they seemed to cope with the competition of MNEs having the same profile, they considered state intervention to protect local enterprises necessary because the competition among the two types of enterprises is unfair and the workforce is more inclined to work for a MNE.

The opinion about the general impact on the regional economy is divided, slightly more than a half considering to have a negative impact, while the other half of the respondents saw a positive impact on economy. MNEs main strengths are the access to external markets, the management, the effective promoting and the capital owned. The most efficient solution to stimulate the activity of local state owned enterprises chosen were implementing the private management and creating partnerships with the multinationals.

We conclude that, due to the significant contribution to the wealth and economic growth of a country, governments should attract and support their operations. An improvement in the business climate within the respective country would enforce the liberalization of the strategic sectors of the economy by the governments and favours the foreign direct investments (Scalera and Uruci, 2011b).

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