

2. Compare and contrast these explanations of FDI: internalization theory and Knickerbocker's theory of FDI. Which theory do you think offers the best explanation of the historical pattern of FDI? Why?
3. What are the strengths of the eclectic theory of FDI? Can you see any shortcomings? How does the eclectic theory influence management practice?
4. Read the Management Focus on Cemex, and then answer the following questions:
 - a. Which theoretical explanation, or explanations, of FDI best explains Cemex's FDI?
 - b. What is the value that Cemex brings to a host economy? Can you see any potential drawbacks of inward investment by Cemex in an economy?
 - c. Cemex has a strong preference for acquisitions over greenfield ventures as an entry mode. Why?
5. You are the international manager of a U.S. business that has just developed a revolutionary new personal computer that can perform the same functions as existing PCs but costs only half as much to manufacture. Several patents protect the unique design of this computer. Your CEO has asked you to formulate a recommendation for how to expand into western Europe. Your options are (a) to export from the United States, (b) to license a European firm to manufacture and market the computer in Europe, or (c) to set up a wholly owned subsidiary in Europe. Evaluate the pros and cons of each alternative, and suggest a course of action to your CEO.

Research Task


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Foreign Direct Investment

Use the globalEDGE website (globaledge.msu.edu) to complete the following exercises:

Exercise 1

The *World Investment Report* published annually by UNCTAD provides a summary of recent trends in FDI as well as quick access to comprehensive investment statistics. Identify the table of *largest transnational corporations* from developing and transition countries. The ranking is based on the foreign assets each corporation owns. Based only at the top 20 companies, provide a summary of the countries and industries represented. Do you notice any common traits from your analysis? Did any industries or countries in the top 20 surprise you? Why?

Exercise 2

An integral part of successful foreign direct investment is to understand the target market opportunities as well as the nature of the risk inherent in possible investment projects, particularly in developing countries. You work for a company that builds wastewater and sanitation infrastructure in such countries. *The Multilateral Investment Guarantee Agency* (MIGA) provides insurance for risky projects in these markets. Identify the sector brief for the water and wastewater sector, and prepare a report to identify the major risks projects in this sector tend to face and how MIGA can assist in such projects.

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CLOSING CASE

Walmart in Japan

Japan has been a tough market for foreign firms to enter. The level of foreign direct investment (FDI) in Japan is a fraction of that found in many other developed nations. In 2011, for example, the stock of foreign direct investment as a percentage of GDP was 3.9 percent in Japan. In the United States, the comparable figure was 23.5 percent, in Germany 23.4 percent, in France 39 percent, and in the United Kingdom 48.4 percent.

Various reasons account for the lack of FDI in Japan. Until the 1990s, government regulations made it difficult for companies to establish a direct presence in the nation. In the retail sector, for example, the Large Scale Retail Store Law, which was designed to protect politically powerful small retailers, made it all but impossible for foreign retailers to open large-volume stores in the country (the law was repealed in 1994).



Walmart entered Japan in 2002 by acquiring a stake in Japanese retailer Seiyu.

Despite deregulation during the 1990s, FDI in Japan remained at low levels. Some cite cultural factors in explaining this. Many Japanese companies have resisted acquisitions by foreign enterprises (acquisitions are a major vehicle for FDI). They did so because of fears that new owners would restructure too harshly, cutting jobs and breaking long-standing commitments with suppliers. Foreign investors also state that it is difficult to find managerial talent in Japan. Most managers tend to stay with a single employer for their entire career, leaving very few managers in the labor market for foreign firms to hire. Furthermore, a combination of slow economic growth, sluggish consumer spending, and an aging population makes the Japanese economy less attractive than it once was, particularly when compared to the dynamic and rapidly growing economies of India and China or even the United States and the United Kingdom.

The Japanese government, however, has come around to the view that the country needs more foreign investment. Foreign firms can bring competition to Japan where local ones may not because the foreign firms do not feel bound by existing business practices or relationships. They can be a source of new management ideas, business policies, and technology—all of which boost productivity. Indeed, a study by the Organization for Economic Cooperation and Development (OECD) suggests that labor productivity at the Japanese affiliates of foreign firms is as much as 60 percent higher than at domestic firms, and in service firms it is as much as 80 percent higher.

It was the opportunity to help restructure Japan's retail sector—boosting productivity, gaining market share, and profiting in the process—that attracted Walmart to Japan. The world's largest retailer, Walmart entered

Japan in 2002 by acquiring a stake in Seiyu, which was then the fifth-largest retailer in Japan. Under the terms of the deal, Walmart increased its ownership stake over the next five years, becoming a majority owner by 2006. In 2008 it acquired all the remaining stock in Seiyu. Seiyu was, by all accounts, an inefficient retailer. According to one top officer, "Seiyu is bogged down in old customs that are wasteful. Walmart brings proven skills in managing big supermarkets, which is what we would like to learn to do."

Walmart's goal was to transfer best practices from its U.S. stores and use them to improve the performance of Seiyu. This meant implementing Walmart's cutting-edge information systems, adopting tight inventory control, leveraging its global supply chain to bring low-cost goods into Japan, introducing everyday low prices, retraining employees to improve customer service, extending opening hours, renovating stores, and investing in new ones.

It proved to be more difficult than Walmart had hoped. When Walmart acquired a majority stake in Seiyu, it promptly laid off 1,500 employees at the retailer's headquarters. While this reduced costs, it also created resistance from former and remaining employees, who complained vocally to the press about how Walmart was trying to impose American management practices on a Japanese corporation. This was a public relations setback for Walmart. Walmart also stumbled when it began to stock low-priced (and low-perceived-quality) Chinese goods in its Japanese stores. Japanese consumers did not respond favorably, and Walmart found that it had to alter its merchandising approach, offering more high-value items to match Japanese shopping habits, which were proving to be difficult to change. Walmart's entry also prompted local rivals to change their strategies. They began to make acquisitions and started to cut their prices to match Walmart's discounting strategy. Also, many Japanese suppliers were reluctant to work closely with Walmart due to their belief that Walmart would force them to cut prices to the bone.

Despite such setbacks, Walmart has slowly started to make progress in Japan. The retailer has been adjusting to the Japanese market. For example, it has created special products to cater to the aging Japanese population. "One of its most popular products is a '298-Yen Bento,' a single-serve, freshly prepared meal that sells for about \$4 and is tailored to 'someone on a pension with limited funds.'" Walmart has also drawn on its global supply chain to introduce products into Japan that have caught on with local consumers, such as Reese's Pieces peanut butter candies from Hershey Co. The company has also found that by bypassing Japan's traditional multitiered distribution system, and importing food directly from other countries, it can undercut local competitors. For example, grapes imported straight from California can

be 20 percent cheaper than those sold by competitors. Due to actions like these, Walmart may ultimately become profitable in Japan. The company is certainly betting on this. In 2012, after a four-year hiatus, Walmart announced that it would open 22 new stores in Japan over the next two years.⁵²

Case Discussion Questions

1. Why, historically, has the level of FDI in Japan been so low?
2. What are the potential benefits to the Japanese economy of greater FDI?

3. How might the entry of Walmart into the Japanese retail sector benefit that sector? Who could lose as a result of Walmart's entry?
4. Why has it been so hard for Walmart to make a profit in Japan? What might the company have done differently in its early years in Japan?
5. Why did Walmart announce in late 2012 that it would expand its operations in Japan after opening no new stores in four years?

Endnotes

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