Assessing the impact of transnational corporations

1. Introduction

The main features of the contemporary global economy are integration, transnationalization and globalization of economic activity. The internationalization level of national economies is significantly increasing in a result of the activities of transnational corporations (TNCs). Transnational corporations are a new powerful force in the global economy; their activities are increasingly turning the world economy into a single market for goods, services, capital, labor and knowledge. The world becomes a single market for thousands of parent companies and hundreds of thousands of their affiliates. Thus, the study of the major factors, ways, methods, models and mechanisms for the participation of transnational corporations in the life of the contemporary society is particularly significant for understanding the current tendencies in the globalized world.

2. Problem Statement and Research Goal and Objective

The relevance of the research is basing on an increasingly growing role of multinationals in the development and strengthening of the economies of the world. TNCs provide the foundation of the modern world economy, determine the vector of its development and are one of the main levers of economic power. Transnational corporations form the foundation of world industrial production and services, as well as international trade, being leaders in research and development practices and playing a leading role in foreign direct investment. The current research will discuss the problems associated with this influence and attempt to answer the question if it bears positive or negative character.

The purpose of this study lies in the comprehensive study of TNCs and determining their impact on the economic development of world economy. To achieve the objective, we are aiming to solve the following key problems: 1) based on the general trends of transnational corporations at the present stage, to show that their activities is an integral part of international economic relations; 2) to identify the features of the activities of transnational corporations and their place in the modern world economy; 3) to identify the role of TNCs in the economies based on the analysis of major corporations; 4) to describe investment flows and determine the role of transnational corporations in organizing these processes; 5) to determine the forms of TNCs' impact on the processes of integration and economic policies.

3. Study Area and Data Collection

The object of the research are the largest transnational corporations. The subject of the research are economic relations arising in the course of multinational corporations' activities and their impact on national economies. The presented data is compound from available statistical data on the largest TNCs, starting from 1950's and up to the contemporary period. The analyzed data is presented in a form of 1 graph and 5 tables.

4. Analysis

4. 1. The scale of modern TNCs

TNCs united the global trade with international production. They operate through their subsidiaries and branches in dozens of countries under a unified scientific, production and financial strategy, formed in their " brain trusts", own a huge research, production and market potential, providing high development dynamics.

At the present stage, since the end of the 20th century, the main feature of TNCs' development is creation of networks of production and marketing on a global scale. Statistics shows that the increase in the number of foreign affiliates of TNCs is much faster than the increase in the number of TNCs themselves (Figure 1). The major role in selecting locations for the establishing subsidiaries belongs to analysis of production costs, which are often lower in developing countries; but the products are sold where the demand for them is higher, which is mainly in developed countries (World Investment Report, 2001).

Figure 1. Dynamics of Growth of TNCs and Their Affiliates

Source: World Investment Report, 2001

The flow of investments of transnational corporations has increased, but became increasingly concentrated in the richest regions of the world. While in 1970's about 25% foreign direct investment flew to developing countries, in late 1980's their share dropped below 20% (Bergesen & Fernandez, 1995; The Universe of the Largest Transnational Corporations, 2007).

In early 2004 there were 64 thousand TNCs in the world, controlling 830 thousand foreign affiliates. For comparison: in 1939 there were only about 30 TNCs, in 1970 – 7 thousand, in 1976 – 11 thousand (with 86 thousand branches) (The Universe of the Largest Transnational Corporations, 2007).

What is a modern economic power of TNCs? Their role in the modern world economy is assessed by the following indicators (World Investment Report, 2001; The Universe of the Largest Transnational Corporations, 2007):

– TNCs control about 2/3 of world trade;

– They cover about 1/2 of world industrial production;

– TNCs employ approximately 10% of all employees of non-agricultural production (of which almost 60% work in the parent companies, and 40% – in the subsidiaries);

– TNCs control about 4/5 of the world's patents, licenses and know-how.

Just as the TNCs are the elite of business, TNCs also have their own elite – superlarge companies competing with many countries in production, budget, and in the " population". The 100 largest TNCs (less than 0. 2% of the total quantity) control 12% of the total amount of foreign assets and 16% of total foreign sales (The Universe of the Largest Transnational Corporations, 2007).

Table 1. 10 World's Largest TNCs ranked by foreign assets in 2000

Companies

Rank by the volume of foreign assets

Foreign assets, % of total assets of the company

Foreign sales,% of total sales

Foreign personnel,% of total company staff

General Electric (USA)

1

34, 8

29, 3

46, 1

ExxonMobil Corporation (USA)

2

68, 8

71, 8

63, 4

Royal Dutch/Shell Group (UK, Netherlands)

3

60, 3

50, 8

57, 8

General Motors (USA)

4

24, 9

26, 3

40, 8

Ford Motor Company (USA)

5

25, 0

30, 8

52, 5

Toyota Motor Corporation (Japan)

6

36, 3

50, 1

6, 3

DaimlerÐ¡hrysler AG (Germany)

7

31, 7

81, 1

48, 3

Total Fina SA (France)

8

63, 2

79, 8

67, 9

IBM (USA)

9

51, 1

57, 5

52, 6

British Petroleum (UK)

10

74, 7

69, 1

77, 3

Source: World Investment Report, 2001

Table 2. 10 World’s Largest TNCs ranked by their market value

Ranking 2004

Ranking 2003

Companies

Country

Market capitalization, mln USD

Sector of economy

1

2

General Electric

USA

299 336, 4

Industrial conglomerate

2

1

Microsoft

USA

271 910, 9

Software &Services

3

3

Exxon Mobil

USA

263 940, 3

Oil and Gas

4

5

Pfizer

USA

261 615, 6

Pharmaceuticals and Biotechnology

5

6

Citigroup

USA

259 190, 8

Banks

6

4

Wal Mart Stores

USA

258 887, 9

Retail trade

7

11

American International Group

USA

183 696, 1

Insurance

8

15

Intel

USA

179 996, 0

Computers, IT Equipment

9

9

British Petroleum

UK

174 648, 3

Oil and Gas

10

23

HSBC

UK

163 573, 8

Banks

Source: The Universe of the Largest Transnational Corporations, 2007

The composition of TNC becomes over time increasingly international in origins. Among the world top ten largest companies U. S. firms totally dominate (Table 1, 2). But while considering the composition of larger groups of the world's largest TNCs (Table 3, 4), the American leadership is much less pronounced. According to Fortune magazine, TNSs developed from the absolute dominance of U. S. companies in the 1950's to the dominance of Western European companies since the 1980's (Bergesen & Fernandez, 1995). The number and importance of TNCs from developing countries is also growing (especially from the Asian " dragons" like Taiwan, South Korea, and China). It is expected that in the coming years the share of TNCs from new industrial Third World countries and countries with economies in transition will continue to increase.

Table 3. National belonging of the 50 largest TNCs in 1959-1989

Years	USA	Western Europe	Japan	Developing countries
1959	44	6	0	0

1969

37

12

1

0

1979

22

20

6

2

1989

17

21

10

2

Source: Bergesen & Fernandez, 1995.

Table 4. National belonging of the largest TNCs in 2004

The groups of companies

USA

Western Europe

Japan

Developing countries

10 largest corporations

8

2

0

0

50 largest corporations

30

16

3

1

(“ Samsung”, South Korea)

100 largest corporations

55

35

6

3

(“ Samsung”, South Korea; “ China Mobile”, Hong Kong, “ Gazprom”, Russia)

Source: The Universe of the Largest Transnational Corporations, 2007

Objective requirements of economic globalization force practically all truly major national companies to involve in the global economy, thereby transforming into transnational corporation.

4. 2. Positive results of the activities of TNCs

TNCs are increasingly becoming the determining factor in deciding the fate of any country in the international system of economic relations, as well as for the development of the system itself.

Host countries benefit in many aspects from inward investment. Large involvement of foreign capital helps to reduce unemployment, increase state budget revenues. The organization of production of the products in the country removes the need for importing those products in the future. Companies producing globally competitive products and targeted mainly for export are significantly strengthening the country’s foreign trade position (Macleod & Lewis, 2004).

TNCs activity also forces the management of local companies to make adjustments to the technological process, the existing industrial relations practices, allocate more funds for training and retraining of workers, pay more attention to product quality, design and consumer features. Most often, foreign investments are followed by the introduction of new technologies, launching new products, new management style, applying the best practices of foreign businesses. Realizing the benefits from TNCs to the host countries, international organizations directly provide developing countries to attract TNCs to carry out technical modernization, and the governments of these countries, in turn, are actively struggling for the involvement of TNCs in their economy, competing with each other (like in case of General Motors offering Philippines or Thailand to run the production) (Martinelli, 2003).

TNCs activities also bring great benefit to the countries from which they export capital. Since transnationalization increases both average revenue and reliability of its receipt, the TNC shareholders can count on high and stable income. Highly skilled professionals working for TNCs use benefits from the formation of global labor market, moving from one country to another without fear of being unemployed (Macleod & Lewis, 2004).

Most importantly, TNCs activities result in import of institutions, those " rules of the game" (norms of labor and antitrust laws, taxation principles, contract signing practices, etc.), which formed in developed countries. TNCs objectively strengthen the influence of countries exporting capital on countries importing it. For example, German companies in the 1990's conquered almost the entire Czech business; thus, according to some experts, Germany established much more effective control over the Czech economy than in 1938-1944, when Czechoslovakia was invaded by Nazi Germany. Similarly the economy of Mexico and many other countries in Latin America is controlled by American capital (Martinelli, 2003).

4. 3. Negative results of the activities of TNCs

It should be noted that along with the positive aspects of TNCs activities in the world economy, there are negative impacts on the economies of the countries where they operate, and the countries where they are based.

It is possible to distinguish the following major negative features of the impact of transnational corporations on the economies of host countries that threaten their national security (Sklair, 2002):

– possibility of imposing dead-end trends in the international division of labor to companies of the host country, danger of turning the host country into the place for dumping obsolete and environmentally hazardous technologies;

– occupation of the most advanced and promising segments of industrial production and scientific research institutions of the host country by the foreign companies, displacement of the national business;

– increased risks in the development of investment and production processes;

– reduction of state budget revenues due to the use of internal (transfer) prices by TNCs.

Many national governments (especially in Third World countries) are interested in increasing the economic independence of their countries and are seeking to increase their share of the profits of multinationals. Multinational corporations, having an enormous financial power, can deal with attempts on their revenues through forced pressure on host countries, bribing local politicians and even financing plots against undesirable governments. Particularly often the self-interested political activity was applied by U. S. multinationals like American Fruit (1950-60’s, Latin America) and ITT (1972-73, Chile) (Martinelli, 2003).

Transnationalization of economic activity reduces the risks for corporations, but increases risks for host countries. The fact is that multinational corporations can quite easily move their capital across countries, leaving the country in economic difficulties, and shifting to a more prosperous one. Naturally, in such circumstances, the situation in the country from which TNC abruptly takes away its capital gets even harder because disinvestments (mass withdrawal of capital) lead to unemployment and other negative phenomena (Sklair, 2002).

Host countries also tend to believe that the profits of transnational corporations are excessively large. Getting taxes from TNCs, they are convinced that they could receive much more if the multinationals did not post their profits in countries with low taxation level. The similar view of TNCs as negligent taxpayers is shared by the tax authorities of host countries. The thing is that a substantial proportion of international trade (about 30%) consists of intra-firm flows of transnational corporations, and the sales of goods and services of one TNC unit to another are often conducted not by the world, but by conventional intra-firm, transfer prices. These prices may be intentionally understated or overstated, for example, to divert profits from countries with high taxes and transfer them to countries with liberal taxation (Sklair, 2002; Martinelli, 2003).

Apart from tax losses, the countries exporting capital with the development of TNCs are losing control over the activities of big business. TNCs often put their own interests above the interests of their country, and in crisis situations TNCs can easily “ change their face”. Thus, during the Second World War a number of German firms established TNCs with the headquarters based in neutral countries, particularly in Cuba (which was under the control of the USA warring with Germany) (Martinelli, 2003).

Moreover, if national governments are under the control of their citizens, and supranational organizations under the control of their founders, the leaders of transnational business are not elected by anyone and are not accountable to anyone. For the sake of profit international oligarchs can cause serious damage to the economy of even highly developed countries, avoiding any responsibility.

5. Conclusion

Active production, investment and trading activities of TNCs allow them to perform two functions, which are of great importance for the world economy: 1) stimulation of economic integration; 2) international regulation of production and distribution of products.

TNCs contribute to economic integration, creating stable economic relations between different countries. It is largely due to them that national economies gradually assimilate in the common world economy, which results in a spontaneous creation of the global economy by purely economic means without the use of violence. TNCs play an important role in the socialization of production and the development of planned establishments. This socialization of production creates the conditions for the transition to the centralized management of the global economy for the benefit of all mankind, for the creation of the “ social world economy.” However, the centralized regulation of the world economy carried out by TNCs brings many serious problems.

The activities of strong TNCs, whose economic power is greater than the potential of many countries, qualitatively change the system of control over the world economy. While in the middle of the 20th century the key regulator of the world economic order were the governments of strong powers, by the end of the 20th century a kind of a “ triple power” formed: in addition to national governments, global economic relationships are effected by TNCs and supranational organizations (such as the World Bank for Reconstruction and Development, International Monetary Fund, etc.). Sovereign states have to share their power with these new actors of global economic relations first in the economic, and then in the political sphere. Some economists believe that the influence of states is declining, the real power is increasingly moving into the hands of self-seeking transnational corporations and international institutions they control.

Balance of gains and losses from the TNCs’ activities (Table 5) depends on the control over their activities on the part of governments, public and supranational organizations.

Table 5. Consequences of the activities of TNCs

Hosting country

Exporting country

World economy

Positive effects

additional resources (capital, technology, managerial experience and skilled labor);

growth of production and employment;

promotion of competition;

additional tax revenue for the state budget

unification of economic rules of the game (import of institutions);

growing influence on other countries;

revenue growth

promotion of globalization, the growth of the unity of the world economy;

global planning perspectives (creation of the preconditions for “ social world economy”)

Negative effects

external control over the choice of specialization of the country in the world economy;

replacement of the national business in the most attractive areas;

growth of the instability of the national economy;

tax avoidance of big business

reduction of state control;

tax avoidance of big business

emergence of powerful centers of economic power, acting for private gain, which may not coincide with universal objectives

In general, the policy of developing countries in relation to TNCs is aimed at the greatest possible harmonization of foreign capital inflows with the solution of priority economic tasks. That is why, in its policy towards TNCs, developing countries combine restrictive and stimulating measures, seek and usually find the necessary parity between their own goals and interests of TNCs.