

05-013

Bringing History into International Business

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August 28, 2004

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Abstract

We argue that the field of International Business should evolve its rhetoric from the relatively uncontroversial idea that “history matters” to exploring *how* it matters. There are three conceptual reasons for doing so. First, historical variation is at least as good as contemporary cross-sectional variation in illuminating conceptual issues. As an example, we show that conclusions reached by the literature on contemporary emerging market business groups are remarkably similar to independently reached conclusions about a very similar organizational form that was ubiquitous in the age of empire. Second, history can allow us to move beyond the oft-recognized importance of issues of path-dependence to explore the roots of Penrosian resources. Third, there are certain issues that are un-addressable, except in the really long (that is, historical) run. Exploring the causal relationship (if any) between foreign direct investment, a staple of the International Business literature, and long-run economic development provides one important example.

International Business scholars often talk about history, but rarely take it seriously. Or so it would seem from reading the pages of JIBS. A simple search showed that the word “history” was mentioned in 119 articles and notes published in the journal since 1990. The word “evolution” occurred in 135 articles and notes. Yet not a single article was explicitly devoted either to the history of IB or employed historical data to explore an issue. Only a handful of articles contained longitudinal data covering more than a decade.

This was not always the case. The first generation of IB scholars placed a high priority on evolutionary and historical perspectives and methodology. Among the pioneers of the discipline, Raymond Vernon’s product cycle model employed an evolutionary approach to explain the wave of U.S. manufacturing investment in post-war Europe (Vernon, 1966). Subsequently Vernon undertook a vast research project at the Harvard Business School to establish the historical origins of the largest U.S. multinationals. This remains the largest longitudinal source of data on the evolution of historical firms (Vaupel and Curhan, 1969, 1974; Curhan, Davidson and Suri, 1977).

Vernon was not alone. Dunning’s first major book, which examined U.S. multinational investment in Britain, published in 1958, traced the evolution of those firms back to the nineteenth century. Many of the key concepts of the OLI paradigm were first developed in that book, as the result of empirical research and historical observation, before being formally stated in later work (Dunning 1958, 2001).

Subsequently, Dunning made major contributions to understanding the historical origins of international business. In 1983 he published the first – and to date only – set of estimates of the size of world FDI in 1914 and 1938, long before any official statistics had been collected. Prior to that date, it had been assumed that most nineteenth century capital movements were portfolio in nature. Dunning suggested that upwards of one third of the huge amount of world foreign investment before 1914 was FDI. If this order of magnitude is correct, this probably represented a similar share of world output to that seen in the 1990s (Dunning 1983; United Nations 1994). This research, conducted nearly two decades before the “first globalization” of the world economy before 1914 became a fashionable research area for economic historians and others (O’Rourke and Williamson, 1999) has been largely neglected by international business researchers, although it was

taken up with enthusiasm by business historians, who were working on a parallel track to identify the appearance and growth of multinational firms from the nineteenth century (Wilkins 1970, 1974; Jones 1996, 2005).

Among other pioneers of IB, the Uppsala internationalization school was also decidedly historical. Johanson and Wiedersheim's (1975) classic article used mini-histories of four Swedish companies to develop the stages model of internationalization.

Subsequently there has been only limited progress in building on these early achievements. During the 1980s there was interest in using "history" to test emerging theoretical models. Casson and Hennart explored how transaction costs theory could be employed to explain historical patterns of horizontal and vertical integration in natural resource and manufacturing industries (Casson 1986; Hennart 1986, 1991, 1994). There were several broad attempts to facilitate dialogue between the "theory" and the "history" of multinationals (Casson 1983, Hertner and Jones 1986). However this early research momentum was not sustained.

The greatest impact of Vernon, Dunning and Casson was on business historians, whose work increasingly employed the main theoretical concepts developed in IB to understand historical dynamics. The history of international business became a vibrant sub-field within business history. This research stream has done more than map the contours of the historical growth of multinationals. Business historians have showed the diversity of strategies and organizational forms employed over time by firms crossing borders, and how this diversity has been shaped by home and host country factors. A noteworthy feature of this work has been its willingness to explore international business strategies beyond the high tech manufacturing sector in developed markets (See recent surveys in Wilkins 2001 and Jones 2003, 2005.) However this stream of literature has had minimal impact on the research agendas of mainstream IB scholars.

In IB, there appeared major professional and methodological roadblocks to further interaction with historical evidence. As the discipline matured, there was a growing pressure for a standardized social science methodology, especially multiple regressions, which became almost *de rigueur* for an article to be published in JIBS. The general pressure for quantification felt in all the social sciences did not encourage deeper engagement with the often patchy or partial data available historically.

It was also as hard to cross disciplinary boundaries in this field as elsewhere. While business history scholars wrote extensively about the history of international business, this literature took forms which were not very accessible to management scholars. It was often contained in large monographs, either analyzing the growth of single firms, or pursuing more wide-ranging topics. Particular problems arise using the data from corporate histories. In recent years major studies have been published of multinationals industries including petroleum, fiber optics and automobiles using in-depth research in business archives and oral history (Bamberg 1994 and 2000; Dyer and Gross 2001; Bonin, Lung and Tolliday, 2003). Given the lack of empiricism in IB research, such studies represent rich sources of data for understanding the evolution of firm-specific competences in international business. Yet their sheer size and approach make access to non-specialists difficult. In addition, they often present a “holistic” view of firms dealing with multiple subjects, from organization, marketing and innovation.

We turn now to considering three categories of reasons why history can illuminate conceptual issues of interest to scholars of contemporary IB. The first of these provides a ‘base case,’ as it were. That is, historical variation is at least as good as contemporary cross-sectional variation in illuminating conceptual issues. The second suggests that history can allow us to move beyond the oft-recognized importance of issues of path-dependence. The third suggests that history can help us expand the domain of inquiry of IB. That is, there are certain issues that are unaddressable, except in the really long (that is, historical) run.

Argument 1

Augmenting sources of variation: Business groups in history and in contemporary emerging markets

The most interesting recent evidence relates to two parallel, but entirely separately conceived, streams of research on business groups in emerging markets. This example illustrates the manner in which studies of phenomena exploiting cross-sectional (contemporary) variation can be complemented by studies exploiting the much under-used time-series variation afforded by history.

Khanna and Palepu (1997, 2000) and others have challenged the conventional view of business groups – collections of legally independent businesses, often extensively diversified, and inter-connected by a medley of economic and social ties – as pure rent-seeking devices (see Khanna 2000 for a review). They argue that the evidence instead favors a more nuanced view of groups. In particular there is, in the jargon of economists, a welfare-enhancing view for groups which compensate for the poorly functioning markets within which they typically operate. For example, when it is hard to allocate talent to its best use, the internal talent markets that operate among the diverse businesses perform a useful function. This entire stream of work is based on contemporary (mostly late 1980s through late 1990s) data collected from fifteen emerging markets in Asia, Latin America, the Middle East and Africa.

Meanwhile an entirely different stream of research on this issue was undertaken in parallel by business history researchers concerned to explain the historical development and resilience of European trading companies. There was a large literature on Japanese trading companies, especially the *sogo shosha*, which had tended to assume that they were primarily a Japanese form of business organization (Yoshino and Lifson 1986). Closer consideration, however, led to the identification of the historical importance of trading companies in many European countries, including Britain, the Netherlands and Switzerland (Jones 1998). Before 1914 they accounted for a high percentage of trade flows between Europe and developing countries. Intriguingly, their importance did not cease after 1914. They continued to flourish as large-scale trade intermediaries and diversified business enterprises up to the present day in some cases.

To investigate this phenomenon, Jones undertook a large-scale research project on the growth and strategies of UK-based trading companies from their nineteenth century until the present day. Initially a large number of multinational trading firms were engaged in trade intermediation between Britain and host economies in (mostly) developing markets. The study included firms such as Jardine Matheson and Swires, which remain important components of the Asia Pacific economy until the present day, and other firms such as Balfour Williamson, Anthony Gibbs, Inchcape, and the United Africa Company (UAC), which were once major regional players – UAC employed around 70,000 in West

Africa in the 1960s, and was the largest modern business enterprise in the region – but which for one reason or another no longer exist, at least in their current form.

A striking conclusion from this study was the importance of business groups. A general pattern was diversification from trade to related services, and then to FDI in resources, and processing. A classic pattern can be seen in the case of Harrisons and Crosfield. Founded as a Liverpool-based partnership engaged in tea trading, buying tea in India and China and selling it in Britain, from the 1890s the firm opened branches outside Britain in Sri Lanka, India, Malaya, the Dutch East Indies (Indonesia), the United States, Canada, Australia and New Zealand. These branches were usually established to trade in tea, but soon acquired a wider range of import and export business, and began acting as agents for insurance and shipping companies. Tea trading led to the purchase of tea estates in South Asia from 1899 onwards, and then the development of distribution facilities in tea consuming countries in Britain and North America. After 1903 the firm diversified into rubber plantations. During the interwar years, Harrisons & Crosfield deepened its involvement in South-east Asia through investment in logging in Sabah, while in Malaya it diversified from rubber plantations to rubber manufacture. These tea and rubber plantations were all placed in publicly quoted companies in which Harrisons & Crosfield retained some equity.

The motives for such diversification, and the way it was organized, have many parallels with the emerging market business groups investigated by Khanna and his colleagues. The systematic influences included strong internalization incentives arising from asset-specificity, uncertainty, frequency of transactions and opportunism. These, in turn, arose from information and contracting problems that underlie transaction costs. For example, Chang Khanna and Palepu (2001), in a study of analysts' behavior around the world using contemporary data, show that the difficulty of gaining access to accurate, unbiased information on corporate activity around the world. That information was inaccessible in 19th century Britain is also evident from Jones' (2000) telling description of the evolution of Britain's Companies Act. Under the liberal Companies Acts of 1856 and 1862, public limited companies had no statutory obligation to reveal information even though it was considered advisable to supply a balance sheet before the annual general meeting (AGM). Only in 1929 was sending a balance sheet to shareholders prior

to the AGM made mandatory for public limited companies, and in 1948 that the same was required of profit and loss statements. The requirements for private companies were, unsurprisingly, even less onerous.

Evidence of contracting difficulty also abounds. Extreme examples perhaps illustrate this best. Jardines and Swires were subjected to forced divestment of their assets by the Communist regime in China after 1949. In only slightly less draconian fashion, India's post-independence socialist government confiscated some prized assets of the Tata Group, India's oldest and most celebrated business house (including airlines and insurance companies). Thus the grabbing hand (Shleifer and Vishny, 1998) of government was evident cross-sectionally today and in history.

British trading companies historically and contemporary business groups in emerging markets operate in environments of scarcity of talent. The responses of the groups are remarkably parallel. Samsung runs a de facto business school, a training center, where they attempt to capture expertise from their various businesses and channel it to other (often very different) businesses. Tatas run the Tata Administrative Services which seeks to develop an elite cadre of managers who are rotated across, again very diverse, businesses. This de facto business school function is valuable in an environment where the nurturing of commercial talent is in short supply, relative to the demand for it (Khanna and Palepu 1997). Similar elite corps of managers were evident in Jardines and Swires, recruited initially from particular communities and educational backgrounds. For several generations Jardine Matheson not only recruited most of its managers from Scotland, but from a discrete region of Scotland: the county of Dumfriesshire. (Jardine Matheson, 1947). When it began to experiment with recruiting university graduates during the 1930s, it much preferred them to have attended Scottish universities. Swires, in contrast, recruited from the leading English universities of Oxford and Cambridge. Today's HSBC – formerly the Hong Kong and Shanghai Banking Corporation, founded in the 1860s – traditionally ran its business using a small number of expatriate managers – again heavily recruited from Scotland (King, 1984-1991). That bank, continues to run an expatriate corps of highly skilled British graduates who can help manage the worldwide businesses of one of the world's largest banks.

The organization of the diversified businesses of these British trading firms had even more parallels with that seen in contemporary emerging markets. While trading operations and certain agency businesses were wholly owned, diversified activities in ownership of plantations and mines were placed in partially owned firms which were often floated on the equity market. Harrisons and Crosfields had floated around 40 plantation companies by 1914, with shares in the equity of between 1 and 70 per cent. Equity provides only one link within these “business groups,” and rarely the most important ones. Ties of debt, management, cross-directorships and trading relationships were at least as important. Similar ties hold together business groups today. Indeed, it is not even clear that the equity ties are the most salient. In a contemporary study of Chilean business groups, Khanna and Rivkin (2000) argue that they are not the most salient delineators of business group boundaries.

In much of the older literature the organizational forms employed by the British trading firms in South and Southeast Asia were looked upon with the greatest suspicion. The complexity and costs of interest within such groups appeared costly and inefficient. Outside shareholders looked vulnerable to exploitation compared to the owners of the core trading firms, which were often families (Bauer, 19xx). However the thrust of this historical research was to suggest that there were real benefits from these groups also. They functioned as venture capitalists in countries where capital markets were highly undeveloped. They could recruit far better management than lots of atomistic small firms as they could offer far better career prospects. They facilitated the international marketing of products, and provided a mechanism for spreading information and knowledge between firms. In both cases, thinking of these business groups as investment groups drastically understates their true role and function – they perform a wide range of market intermediation functions in the face of an equally wide range of market imperfections. The study of contemporary business groups documents the same patterns (Khanna 2000) and similar skepticism regarding minority shareholder exploitation (La Porta, Lopez-de-Silanes & Shleifer, 1999). The extreme view of the skeptic’s school was mistaken then, and is mistaken now. A nuanced approach, emanating from an understanding of the contextual environment, remains the more sensible interpretation.

Consider also the longevity of the business group organizational form. Again, the two parallel studies yield the same conclusion. Jones and others have documented that the European trading companies lasted well beyond the initial circumstances in the nineteenth century which encouraged and facilitated their roles as trade intermediaries, especially the poor state of transport and communications which gave rise to a high degree of information asymmetry, and the spread of colonialism which provided a favorable political context for direct investment.

In practice, European trading companies and their business groups proved remarkably robust. They survived radical improvements in the information environment – which occurred in stages with the progressive introduction of the telegraph (1860s), telephones, faxes and the internet. They also survived momentous shifts in the political environment – associated with the end of Empire and widespread nationalizations as in China and in technological paradigms. The companies frequently “reinvented” themselves to suit the evolution of context, but always outperforming sensible comparable companies. As sea transportation gave way to air travel after World War II, Swire’s – which had owned a large commercial shipping fleet since the late nineteenth century – established Cathay Pacific, which remains today one of Asia’s leading airlines, still controlled by Swires. British trading companies such as Harrisons and Crosfield and Inchcape – the product of amalgamations of a number of nineteenth century trading firms such as the Borneo Company and the Anglo-Thai Corporation – functioned as highly diversified general trading companies with striking resemblances to Japan’s *sogo shosha*. In the early 1980s Inchcape operated in 44 countries and marketed the products of 2,750 manufacturers. Its business group included general merchandising, shipping, port operators, tea producers and manufacturing (Jones, 2000). It was only during the 1980s that capital market pressures in Britain resulted in the restructuring of diversified firms such as Harrisons and Crosfield and Inchcape specialty into perceived “core businesses.” Nor was this evidence of a peculiar British aberration. A similar tale could be told about Dutch and other European trading companies (Sluyterman 1998).

Similarly, Khanna and Palepu (1999) demonstrate that contemporary Chilean and Indian groups respond to dramatic improvements in ambient information and dramatically higher levels of competition, not by disbanding (as skeptics would have us

believe) but by reinventing themselves and seeking out newer areas of business. See Figure 1 for a one hundred-year plus evolution of India's leading Tata Group wherein the reinvention of the group over time is clearly evident from the pattern of exits and (mostly) entries into new lines of business (Khanna & Palepu, 2004).

Thus, we see that intra-country market failures in an array of contemporary contexts results in certain patterns regarding the structure and effects of business groups. The historical context, focused on inter-country market imperfections, also yields the same patterns.

Argument 2

Illuminating path dependence: The roots of Penrosian 'Resources'

The history of a firm is now widely regarded as a crucial determinate of its distinctive competences. In the words of Edith Penrose in the third edition of her classic *The Theory of the Growth of the Firm* (1959, 1995), "one of the primary assumptions of the theory of the growth of firms is that history matters: growth is essentially an evolutionary process and based on the cumulative growth of collective knowledge, in the context of a purposeful firm." Penrose herself deeply engaged in empirical historical research, notably on the growth of international petroleum industry (1968). *The Theory of the Truth of the Firm* should have included a chapter containing a historical case study of Hercules Powder Company, a chemical company demerged from Du Pont, but it was dropped by the publisher to economize in space, and later published in *Business History Review*, published at Harvard Business School (Penrose 1960).

Penrose is acknowledged as a major influence on resource-based and path dependent theories of the firms (Foss, 1997). Yet the "history" in most of this literature is treated in a highly stylized fashion, as an immutable entity which is fixed before the analysis begins. This is very much a feature of Nelson and Winter (1982), although Nelson (1991) later wished they had been aware of the American business historian Alfred D. Chandler's work (Chandler 1962, 1977, 1990). Chandler's compelling accounts of the historical evolution of corporate strategies and structures are cited in the IB and management literatures, but rarely used. The voluminous literature apart from business

history. Chandler, much of which has either extended or taken issue with his arguments, is rarely mentioned (Amatori and Jones, 2003).

The knowledge-based theory of the multinational enterprise is strongly evolutionary. Beginning with Kogut and Zander (1993), this perspective maintains that that multinationals specialise in the transfer of knowledge that is difficult to understand and codify. They have a superior efficiency as an organizational vehicle to transfer knowledge across borders. Firms define a community in which there exists a body of knowledge regarding how to co-operate and communicate. Through repeated interactions, individuals and groups within firms develop a common understanding by which to transfer knowledge from ideas into production and markets. The whole argument is evolutionary, and cries out for testing historically. Yet the literature has largely proceeded at a conceptual and abstract level, although there are a limited number of empirical studies (Ghoshal and Bartlett 1988; Zander and Kogut 1995; Gupta and Govindarajan, 2000) even though there is widespread suspicion that multinationals are not particularly well equipped to continuously transfer knowledge across national borders (Solvell and Zander, 1998).

There is much to be gained by following in Penrose's path of closer engagement with historical evidence. There is strong evidence from many of the historical examples that intra-firm knowledge transfers have not been smooth. This emerges as a persistent issue in a major historical study of Ford in Europe. During the 1960s Ford's research and development centers in Germany and Britain operate with almost no co-ordination between them, reflecting their embeddness in their respective national organizations (Bonin, Lung and Tolliday, 2003). An archivally-based study on the relationship between Unilever and its U.S. affiliates between the 1950s and the 1980s has shown not only the "stickiness" of knowledge even within such a highly internationalized corporation, but that knowledge flowed more or less easily according to geographical direction and product category (Jones 2002).

It is not simply that addressing available historical evidence can add depth to the analysis of issues already identified as being dynamic. It can also illuminate issues sometimes obscured by inadvertent aggregation. In *Managing Across Borders*, by Bartlett and Ghoshal (1989), employ the concept of "administrative heritage" to explain the

different responses of the consumer goods multinationals Unilever and Procter & Gamble (P & G) from the 1950s to European integration and globalization. P & G had a much more centralized approach, with ultimate power clearly residing in its headquarters in Cincinnati, while Unilever had strongly autonomous national companies in Europe and elsewhere, and moved slowly to co-ordinate and rationalize their factories and brands. Bartlett and Ghoshal argue that the strategic choices open to these firms were constrained by their different pasts. Unilever's multinational growth stretched back, in the form of its predecessor companies, to the late nineteenth century. Its national affiliates had long histories, and were often independent firms before being acquired by Unilever. They grew autonomous and independent during the economic nationalism of the 1930s and the Second World War. In contrast, P & G only began large-scale internationalization after the Second World War. It had no historical inheritance of proud and long-established affiliates, and its internationalization coincided with falling tariff barriers and growing European economic integration.

Although this is a plausible hypothesis, a closer reading of Unilever's history shows a more complex picture. It is possible to observe within Unilever different parties and interest groups advocating their cases. These partly represented different product categories. Unilever was active in foods as well as detergents, and in the foods industry markets remained – and even now remain – far more “national” than in detergents, P & G's core area. It partly reflected differences between the two head offices in London and Rotterdam. Actual outcomes were the result of power struggles between these groups. Sometimes Unilever strategies moved towards greater centralisation, and other times it went into reverse. The original observation at the aggregate level is not undercut by this research, but it opens up the possibilities of going more deeply into the issues of how paths originate, and what determines why one path is taken rather than another.

History can provide a means of exploring phenomenon which prevalent methodologies find difficult to explain. It is widely observed, for example, that multinationals not only pursue divergent strategies when faced with similar market conditions, but that these differences persist over long periods of time. Consider the strategies pursued by Swire and Jardine. Both firms share ostensibly similar backgrounds as British traders in Far East in the nineteenth century, and remain to the present day

ultimately owned and controlled by families based in Britain. They also shared similar experiences, experiencing the chronic political instability of interwar China, and the loss of much of their business in the Second World War followed by the Communist Revolution. Both rebuilt their businesses from the British colony of Hong Kong after 1949.

Yet there have been substantial divergences between the two firms. While the origins of the families behind Jardines lay in Scotland, the Swires came from Yorkshire. While the Swires pioneered appointing Oxbridge university graduates to management positions in 1920s – stressing academic ability and Chinese language skills and “thoroughly understand the Chinese” – Jardines was sceptical of graduates, and preferred “practical” Scottish recruits. The two companies developed quite distinct “corporate cultures.” Over a long period Jardines sought to recruit “risk-taking” entrepreneurial types, whilst Swires preferred low profile “modest” types. Swires had long term aversion to “making money out of money” – a view of the early Swire family – which Jardines did not mind at all. During the 1970s Jardines launched a successful joint venture with the London merchant bank Robert Fleming. Swires pioneered the recruitment of Chinese into management rather than use of “comprador” intermediaries in the 1930s. It took Jardines much later to follow this route. In fact, even before 1914 Swires moves to more modern distribution methods in China using sole agency agreements with independent Chinese merchants (Cox, Biao, Metcalfe, 2003).

These differences played out in quite different strategies. Jardines appeared more entrepreneurial, acting as de facto venture capitalist, from late nineteenth century to the present. Swires took a more evolutionary pattern, avoiding financial activity and moving in an evolutionary fashion from shipping to airlines. The ownership of dockyards etcetera became the basis for a real estate business, while distribution and sugar refining activities led into Coca Cola bottling, first in Hong Kong and subsequently in the United States. Swires also demonstrated a long-term interest in working with the Chinese. “As far as she is able China intends to become a manufacturer, first for her own needs and ultimately for export”, a senior executive of Swire’s advised the management of a British-owned shipping company with which they had long-term collaborative arrangements. “This development may take two or three decades during which – if

Britain is to increase her trade to China – we must go all out in equipping Chinese industry and participating therein. When China becomes a successful industry economy we shall reap our future reward in her higher standard of life, and our increased sales to her of our quality goods.” (Jones 2000)

The significance of historical ties can be seen in market entry strategies. Consider the opening of China in the early 1980s. China had been effectively closed to foreign firms since 1949, but before that had been a large host to foreign MNEs. This is more than a historical curiosity. The previous period of curiosity exercised a constraint on the new period of openness. When Unilever opened its first operation in China in 1984, it did this in a joint venture with the successor to its former Shanghai affiliate, even though there had been no contact between the two parties for 35 years.

Another example can be seen in the case of AIG, the world’s largest international insurance company. The company originated in Shanghai in 1919 when it was started by an American who established the Asia Life Insurance Company insurance agency to act as an agency for U.S. insurance companies. It was the first foreign life operation to offer products and services in China, and it grew rapidly. In 1927 AIG moved into a large building at No. 17 The Bund in Shanghai. On January 1, 1949 40 employees and their families of the Shanghai head office were airlifted out to Hong Kong. Over the following decades AIG developed a large business in Latin America, and during the 1960s diversified into the U.S. domestic market. However AIG re-entered the China market unusually early, and ahead of Deng’s liberalization beginning in 1978. Three years earlier AIG was the first U.S. insurance company to negotiate a claims and reinsurance agreement with the People’s Insurance Company of China. In 1980 the two companies formed a joint venture, and in the same year AIG opened the first representative office set up in China by a foreign company. AIG was the first foreign organization to be granted an insurance license in China, and in 1992 opened a branch in Shanghai. In 1996 AIG signed a thirty-year lease on No.17 The Bund and moved back into its former headquarters.

Finally, there can be little dispute that debates about performance and longevity could be revitalized by a new willingness to engage seriously with history. The literature on post-entry performance, profitability and divestment is still far smaller than that on

growth and entry (Caves, 1996). By definition this issue can only be approached using longitudinal studies, and rich rewards await those who venture into this research area. A relatively new database has identified all new entrants and exits into the United Kingdom between the 1860s and 1962 (when government statistics began to be published in that country). This database tracked the post-entry growth of these entrants, including exits. The study not only confirmed that there were high levels of exits, but uncovered wide variations in exits by product groups. Like the Vernon database, there were a higher number of exits from subsidiaries founded by merger and acquisition than those established through Greenfield investment. (Bostock and Jones, 1994, 1996; Curhan, 1977).

Argument 3

Expanding the domain of inquiry: FDI and development in the really long run

There are a further set of issues which can only be rigorously addressed by incorporating a historical dimension. The most important is the impact of international business on development. Given the serious and apparently growing inequality in world incomes, and the heavy emphasis awarded by policy makers to the role of FDI in stimulating growth, it is remarkable that the literature on FDI and development remains so inconclusive (Fortonier 2004). Among the many reasons for this situation, the restricted methodologies of IB researchers and the disinclination to engage with accumulated historical evidence on the economic – and political – impact of multinationals must rank as a significant contributory factor.

There are major benefits to be achieved from incorporating historical evidence into debates about the long-run effects of countries opening up to foreign competition. This is an extensively studied topic today. For example, Sachs and Warner (1995) catalogued a series of countries that have “opened up,” as evidenced by a series of objective economic indicators. Several authors have investigated the causes of opening up and its various effects on industrial organization and the operation of markets for capital and labor (see, for example, Ghemawat, Khanna and Kennedy, 1998). However, these studies take a “recent history” view of the world, in most cases investigating

changes over a few years or, at most, a decade. Several of the longer-run effects simply cannot be studied using such research designs.

Yet many of the effects associated with multinational activity are most likely to manifest themselves over the longer haul. Consider the raging debate today about the effects on the contextual environment of multinationality (<cite Kofi Annan speech>) – for example, to what extent are multinationals harmful to the environment versus helpful to it? *The Economist* (Jan 29-Feb 4, 2000 issue), a popular London-based newsweekly, published a cartoon demonstrating the shifting opinions on this issue over the past four decades. The cartoon suggested that society’s attitude to multinationals had evolved from fear (1970s) to nonchalance (1980s) to exuberance (1990s) and back to fear (2000). This time-series variation in societal attitudes is arguably due to inappropriate extrapolation of the immediately accessible empirical evidence as a generalizable truth. An arguably closer approximation to the real effects of multinationality would come from a longer-run historical study (as in several decades, or even centuries long study).

Consider the impact of foreign multinationals on the U.K. economy. The U.K. has long held a position as one of the world’s largest host economies. Since Dunning’s pioneering study in 1958, studies have regularly pointed to the potential benefits in upgrading production techniques and developing improved organizational and management practices which indigenous suppliers could gain from developing long-term business relationships with inward investors. (Dunning 1958; Stopford and Turner 1985, Dunning 1986, Young, Hood and Hamill 1988; Munday 1990). Yet a substantial “productivity gap” has remained between foreign and domestically-owned business decade after decade. Spin-off and demonstration effects have been hard to find, most notoriously in the case of the Scottish electronics industry, which has remained a volume low cost assembly base. Putting together these studies suggests that the theoretically plausible improvement never happened.

As an example of an historical study that sheds light on the channels through which FDI affects development, consider how China and India responded to their forced, at British gunpoint, opening up of their economies in the mid 1800s. Rhoads Murphy (1977), in *The Outsiders*, points out that, whereas the British sought to use the treaty port model in both China and India, the outcomes were drastically different in the two

countries. “Treaty ports” (or their equivalent since this is a term usually applied to Chinese ports) in India – Bombay, Calcutta, and Madras – became commercial centers of the country and radically affected the nation’s development. Treaty ports built in China – constructed after the Indian ports and after others in Colombo, Rangoon, Bangkok, Singapore and Batavia – had a much more circumscribed effect. The Chinese managed to isolate the effect of the ports to their immediate geographic vicinity.

Murphy goes on to argue that this differential effect is because China had a functioning, vibrant market economy whereas India was in economic and political shambles in the twilight of the Mughal era. Taking this interpretation at face value, this is already interesting since it validates the viewpoint of multinationals as arbitrageurs (Foley), a viewpoint that has become somewhat discredited today as capital mostly flows among rich countries rather than from rich to poor (Easterly, 2001).

But the example is more interesting since it sheds light on the channel through which the FDI had the alleged effect. In particular, an elite developed in India that was willing to embrace the British ways – if not the British – and use them to try to develop India. There was no “demand” for such an elite in China, satisfied as the latter society was with its indigenous trading system and extensive intra-country commerce.

The Indian pattern shows further regional and ethnic complexities. The first elite group to respond to the British was the tiny Parsee community around Bombay. They had already been extremely active in developing a modern cotton textile industry by the second half of the nineteenth century. It was not until the interwar years that Marwaris around Calcutta began building powerful business groups which began to erode the British commercial presence in the interwar years, well before the end of colonialism in 1947. Different elite groups may respond at different times to foreign multinationals.

This mechanism of the development of an elite to facilitate widespread foreign influence could not be documented in any of the current attempts to investigate effects of FDI, confined as these are to measure short-run productivity differentials. It was evidently influenced by multiple factors, of which divergent historical patterns in responding to the external world was one important factor. The European presence in India dated from the fifteenth century, far earlier than their substantive impact on China

which began in the 1840s. India's long tradition of "absorbing" external influences can be contrasted with China's long tradition of relative isolation.

The difficulties in using history in this second way, as a database to help shed light on long-run questions, are evident. Professional historians would stress that historical "facts" are strongly embedded in interpretation. The British India example is illustrative. Some might look at the legacy of British India and say that the civil service, railways and legal code were gifts of Britannia and ultimately outweighed the negative aspects of losing independence. Nehru, in his *Discovery of India* (19xx), has a scathing rejoinder to the same "facts." Historical interpretations change each generation. Currently, historians are re-interpreting the nineteenth century era of imperialism in terms of the building of a global economy. The building of co-operative networks between Western capitalists and resilient indigenous business networks is emphasized (Cain and Hopkins, 2002). It looked different to the earlier generation of nationalists which strove to remove European imperialists from Asia and Africa.

Second, it is difficult to attribute causality to a historical story in the absence of a sensible counterfactual. What would have happened if the phenomenon being investigated had not occurred? To some extent comparative historical studies get around this, but, since random samples cannot be created in history, a purist empiricist will always object.

Conclusion

This article has suggested that there is a major opportunity to move beyond assertions that "history matters" to explore how it matters. We have suggested that it can widen the sources of variation in IB research; provide new ways of looking at research issues already identified as essentially dynamic; and re-invigorate research on issues development which can only be satisfactorily addressed by a historical perspective.

The argument is twin-headed. The first is that longitudinal analysis is important. The second is that "history" needs to be treated as rigorously as statistical analysis. This means crossing methodological boundaries to engage with the research of business historians. It might mean following the Penrose model and doing historical research. It

should be seen within the context of the broadening of the IB mindset to take institutions seriously, and to broaden the methodological tools available to address key issues.

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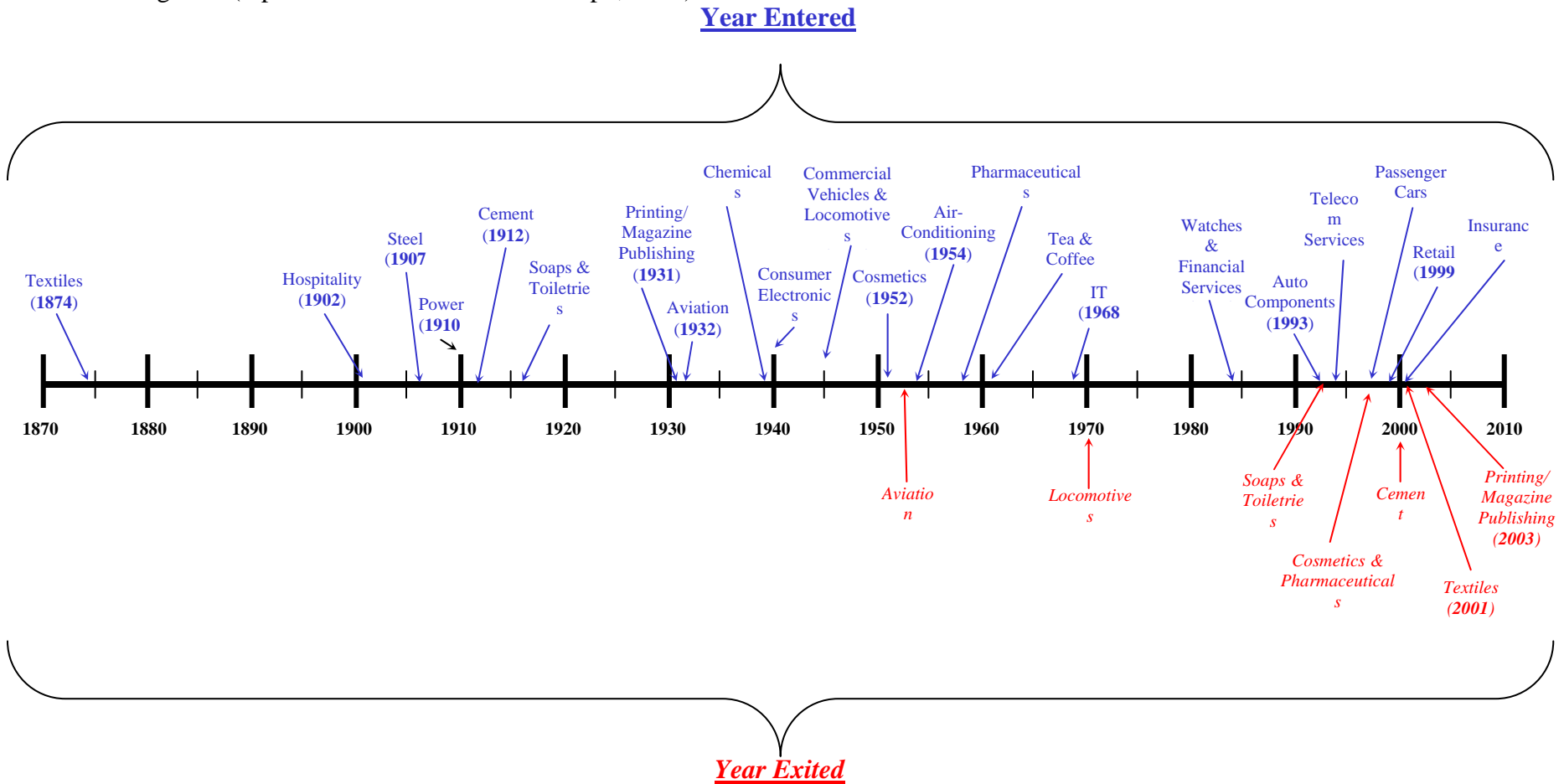
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Figure 1 (reproduced from Khanna & Palepu, 2004)



Source: Bombay House, Tata Group