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Dunning's Eclectic Paradigm applied on Jotun Thailand

by

Nina Minde

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Abstract

I chose to write this thesis for three main reasons : First of all I wanted to write a thesis on Foreign Direct Investment (FDI)[1]. Second, Southeast Asia has had an impressive growth the last decades, and I found it interesting and important to learn more about the region and maybe get an idea of what is to come from the "Tigers". Third, I wanted to learn more about Thailand, its history, culture and economic performance. I therefore ended up writing my thesis about a Norwegian investment in Thailand .

The purpose of this thesis is applying one of the main theories on international production, Dunning's eclectic paradigm, on Jotun's investment in Thailand. Jotun is one of the handful of Norwegian companies that had established affiliates in Thailand before the boom started in the 1980s.

I hope the reader will find the thesis present interesting, both when it comes to choice of firm and country. I have learned a lot from writing this thesis, not only when it comes to the art of writing and application of a theory, but also when it comes to cultural and personal aspects. I have been happy to learn something about Jotun and its business culture, and have in addition got the possibility to learn more about the Thai culture in general.

Nina Minde

[1] Foreign Direct Investment (FDI) is, according to IMF: "Investments made to acquire a lasting interest in an economy other than that of the investor, the investors purpose being to have an effective voice in the management of the enterprise."

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Acknowledgments

I would like to extend a special thanks to Mr. Hans Jarle Kind at the Norwegian School of Economics and Business Administration (NHH) and Foundation for Research in Economics and Business Administration (SNF) for first helping me to choose both theme and company, and thereafter for giving me feedback and support throughout my work. I will also thank Jotun, both in Norway and Thailand, for giving me the opportunity to write about this interesting company, for all the interviews and meetings, and especially to Mr. Bjørn Naglestad, managing director of Jotun Thailand, for all his help and inspiration in writing this thesis.

I want to thank the following persons, with whom I had some very interesting interviews and conversations:

Jotun Thailand:

Mr. Bjørn Naglestad, *managing director*

Mr. Per Arne Nilsen, *Technical director (Former Corporate Project Director)*

Mr. Chaiyaporn Wejnaruemarn, *Sales and Marketing Manager - Dealers*

Ms. Suchada Chuensuksawadi, *Sales and Marketing Manager - Projects*

Ms. Nittaya Sae-Liew, *Senior Sales Admin Executive*

Jotun Malaysia and Jotun Norway:

Mr. Stein Petter Lunde, *managing director, Jotun Malaysia*

Mr. Odd Gleditsch jr., *chairman Jotun A/S Norway*

Mr. Bjørn Granerød, *former managing director Jotun Thailand and his wife*

Ms Elisabeth Granerød

Others in Thailand:

Mr. Prapoth Sawankhathat, *Investment Promotion Officer, Investment Services Center, BoI*

Ms. Nantiya Peapteesut, *Norwegian trade chamber, Thailand*

Mr. Haakan Skoglund, *Managing director, Connector Asia*

Others in Norway:

Mr. Hans Jarle Kind, *Norwegian School of Economics and Business Administration (NHH)*

Mr. Guttorm Schjelderup, *Norwegian School of Economics and Business Administration (NHH)*

Introduction

This thesis is written both as an independent thesis in the area of economic analysis, and as part of the project "The multinational activities of Norwegian shipowning companies", led by Hans Jarle Kind.

I was given the opportunity to write my thesis as part of the "Operasjon Eksportoppdrag" (Operation export-assignment) which is supported by the Norwegian Ministry of Trade and Industry (NHD), Aiesec and the company that I have written for. This gave me the opportunity to go to Thailand for a period of fourteen weeks to experience and learn more about the kingdom, and to meet persons who could answer my many questions.

Jotun has been present in Thailand for more than three decades and has gained experience from different economic stages. Jotun Thailand has performed well, and is today present in several countries in the Southeast Asian region.

From the start, I wanted to put a major focus on the theory, but I realized early that the family-owned Jotun Company has a unique and interesting history, and that it is important to learn about this to understand the path and strategy chosen. In addition, Thailand, like other Southeast Asian countries, has a culture and history dramatically different from what we are used to in Europe.

I have split the thesis into five parts. These are:

- *Thailand in general*, with a view on its history, economic situation, and cultural aspects.
- *Jotun in general*. -to get an understanding of the spirit of the Gleditsch family, and the strategy that was chosen already decades ago.
- *Jotun Thailand* and how it fit into the OLI-theory. I want to test whether we today can say, according to Dunning, that Jotun did the right thing or not when Jotun decided to establish themselves in Thailand.
- *Theories on Multinational Enterprises and Foreign Direct Investment.* I will here take a closer look at Dunning's Eclectic Paradigm, and apply the theory on Jotun to explain how and why the Norwegian paint producer established themselves in Thailand.
- *Conclusion and Summary*

Part I
Thailand

History of Thai Economy and Trade

In the early seventeenth century Western traders set up trading posts in the former capital of Thailand, Ayutthaya. The monarchy saw an opportunity and a valuable source of revenue and started a royal trade monopoly. This monopoly lasted almost two hundred years. Chinese merchants were called to the kingdom to organize the trade. These Chinese became warehouse men, accountants, customs officials, captains and so on and, in short, they ran all aspects of the trade.

At the end of the seventeenth century, the Thai king expelled the European merchants and closed Thailand to Western trade, and focused commerce on China. About one hundred years later, Bangkok became the new capital. In the early years of Bangkok, Thailand was close to bankruptcy, and the monarchy decided to give up its trade monopoly, and trade was again opened to Western merchants. The contacts with the West inspired strategies for both investment and administration, and Thailand turned into a modern country. Chinese merchants and craftsmen were attracted to come to Thailand to promote commerce. The king still remained a leading merchant, but now shared the commercial activities with officials, members of the royalty and with Chinese merchants.

In 1824, when Rama III acceded to the throne, he abolished royal trading and several trade monopolies. The free trade benefited the rural population as the Chinese merchants visited remote areas never exposed to commerce before. The villagers were encouraged to produce various goods for exports, and were secured regular supplies of merchandises. The Thais grew wealthier and they began commuting a specific labor tax. The free trade did not include Westerners. The king claimed the right to exclusively trade with the Westerners and imposed high duties on them.

After many years of negotiations, Rama IV in 1855 ratified the Treaty of Friendship and commerce (The Bowring Treaty) to avoid a military confrontation with the West. The treaty lowered the taxes on Western traders, and replaced the measurement fees by a three percent import tax. This cooperation is claimed to be one of the reasons why Thailand never was colonized. In addition, Rama V embarked on an ambitious program of modernization to avoid colonization. He implemented political and economical changes, developed infrastructure and organized a modern army. These reforms probably helped Thailand to avoid colonization, but as a result it overthrew the monarchy. The administration and the army became the new elite, which later challenged the monarchy's power.

Rama VII enthroned in 1925 and was the last absolute monarch in Thailand. After a coup in 1932, the king became a constitutional leader allowed to reign but not to rule. The executive power rests on the prime minister and his cabinet and the legislative power on a bicameral parliament. In the beginning of the new regime, men and women were granted the right to vote for representatives in the legislature, and expenditure on education were increased. However, publications and radio speeches were censored and creation of new parties was prohibited. This semi-democracy gave way to dictatorship and after 1939, when Luang Pibul became Prime minister, nationalism was intensified. On May 11, 1949, an official proclamation declared that the country would henceforth be known as Thailand. The word "Thai" means free, and Thailand means "Land of the Free". The government managed to increase its control over the economy by introducing countless regulations, most of which proved to be ineffective or impracticable. The military officers got into top civilian post in the administration and in public enterprises. The generals joined hands with Bangkok Bank, and became board members and rich thanks to director's fees, dividends and presents. This happened also with other banks, and the politico-financial axis dominated until mid 1970s. The bankers obtained privileges and favors, which favored them in business competition. These favors could be very simple, but highly effective: The generals could for example command that cars, machines etc. should be of a certain brand. Later, the military officers also gained influence in the private sector as they joined the boards of private businesses and set up their own businesses.

The US encouraged General Sarit (1957-63) and his colleagues to adopt a free-world model of development and to provide state backing for the growth of private business. Sarit and his men were already board members of Thailand's leading firms, and agreed with the

Americans. They were then helped by US money and expertise, and both the businesses and the generals boomed. Schools and colleges were built to educate and train the coming workforce, the existing infrastructure was upgraded and new infrastructure was built. On US advise Sarit established tariff protection to protect infant enterprises, and Thailand introduced investment incentives and welcomed foreign capital. The urban economy grew rapidly, but at the same time, agriculture promised quicker and surer returns than a difficult leap towards industrialization.

The King

King Bhumipol Adulyadej was born in 1927, and is the ninth ruler of the Chakri dynasty and widely respected. The king acceded to the throne in 1946, was officially crowned in 1950, and is the world's longest-reigning monarch. The monarchy has become the single strongest force that unites the people. The king's powers are theoretically no greater than those of European monarchs. He is the head of the State, head of the armed forces and the upholder of the Buddhist faith and of all religions in Thailand. The King plays little part in the day-to-day government operations, but he represents national tradition and serves as a powerful symbol of Thai national identity and unity.

The Deputy Foreign Minister said in one interview that the king provides the bridge between traditional politics and democracy. He has used this authority on occasion to resolve internal crises or to draw the government's attention to social problems. The king has initiated several projects, like crop rotation, irrigation, reforestation and road building. The Thais themselves rarely speak about their king officially, and they are unwilling to discuss the present or the future of the monarchy. On the other hand, American and European consultant agencies as well as all the foreign businessmen in Thailand with whom I have spoken, say that King Bhumipol commands enormous respect and moral authority. In an article in Far Eastern Economic Review[2], it was said, "King Bhumipol's steadying role has been critical to Thai economic development". There is actually concern in Thailand today, that the political system has become too dependent on king Bhumipol's guidance. There has been, and still is, an absence of well-functioning, impartial democratic institutions in Thailand, and it is hard to say what will be the political and social situation when he is gone.

Politics

Although nominally a constitutional monarchy, Thailand was ruled by a series of military governments interspersed with brief periods of democracy from 1932 until the 1992 elections. Since the 1992 elections, Thailand has been a functioning democracy with constitutional changes of government. The traditional balance between the monarchy, the bureaucracy, the politicians, the military, and the private sector is changing. The military has less to say as the society has become increasingly more pluralistic and complex, and demands for political reform are strong among Bangkok's middle class and elite, and the financial crisis in 1997 actually was a stimulus to political reform.

The today existing party politics and coalition governments will probably continue to be shaky. One reason for this is that more than sixty percent of the population lives in the countryside where patronage and vote buying prevail, a Thai that sells his vote to a politician, will not later try to "re-sell" the vote to another politician. Thailand has many political parties, and as a result civilian government has been a multi-party coalition and inherently unstable. No elected government has yet completed a four-year term! Thai political parties, maybe with the exception of the Democratic Party, tend to be centered on individual personalities rather than ideologies. All parties accept working within a framework of democratic principles and free enterprise economics.

However, the unpredictable political system and the frequent changes in government generally have not affected the country's overall stability. To make a short comparison between Singapore, Malaysia and Thailand when it comes to business environment and production costs, one might say that Singapore has an advantage of good infrastructure, personnel support and an "easy-to-orientate" system. The overall business atmosphere in the country is good. In addition, Singapore does offer competitive tax benefits and incentives for investment, the country has a sound government, good communication facilities, skilled manpower, and strong support facilities. In Malaysia, input factors are cheaper than in Singapore, but the system and economic politics are to some extent unpredictable. A very attractive regulation today may be removed at any time, and there exist certain regulations

[2] Politics & Policy-sector, Far Eastern Economic Review, December 16, 1999.

considering ownership and whom to employ. As an example, all companies that want to supply the shipping sector (=the governmental company Petronas) need to have a Petronas-license. Until 1998 the requirement was to have a minimum of 30 % bumiputras (ethnic Malaysian) in the management, but this requirement was suddenly changed in 1999 to demand a minimum of 30% in the top management.

Thailand has a perfect location in Southeast Asia, with two coastlines and borderlines to Malaysia, Myanmar, Laos and Cambodia, and it is therefore in terms of distance, easy to export to, and import from, its neighboring countries. It is still cheaper to produce in Thailand than in Malaysia and Singapore, but the kingdom has, however, a weak state administration, and experiences problems with corruption, shortage of skilled labor and has still a low level of secondary education. Ratings made by The Political and Economic Risk Consultancy in Singapore in 1999 put Thailand below Indonesia, Malaysia, the Philippines and Vietnam when it comes to potential for social unrest. The rating was based on scores by 600 regional businessmen. (See table 1, where 0 is best and 10 the worst).

Table 1
Rating: Corruption, transparency and potential for social unrest

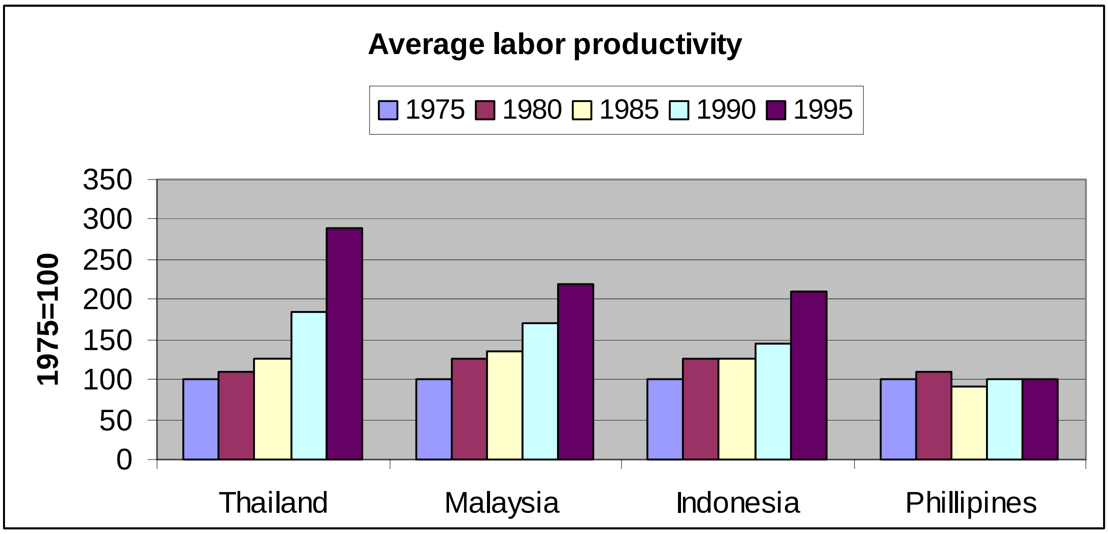
Country	Corruption	Transparency	Potential for social unrest
Indonesia	9.91	8.00	9.64
Malaysia	7.50	6.50	4.88
Philippine	6.71	6.29	4.43
Singapore	1.55	4.55	1.18
Thailand	7.57	7.29	3.86
Vietnam	8.50	9.50	5.00

Source: The Political and Economic Risk Consultancy, Singapore 1999

Further, both the growth in average labor productivity and in total factor productivity has been higher in Thailand than in Malaysia and Indonesia:

Figure 1

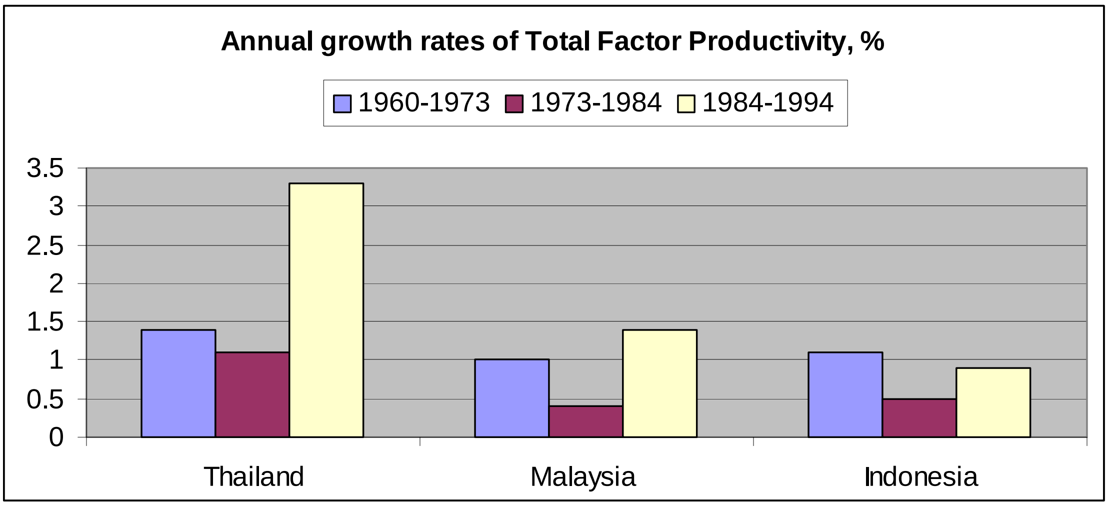
Average Labor Productivity



Source: Austria, 1998

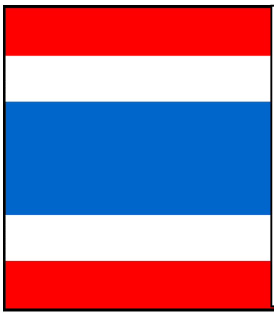
Figure 2

Annual growth rates of total factor productivity



Source: Austria, 1998

Demographics



Total area: 514,000 square km
Population: 60,1 mill (1996)
Labor force: 54,5% (1996)
Land boundaries: 4,863 km
(Burma 1,800 km, Cambodia 803 km, Laos 1754 km and Malaysia 506 km)
Controls the only land route from Asia to Malaysia and Singapore
Coastline: 3,219 km

The Thai population is mostly rural, concentrated in the rice-growing areas of the central, northeastern, and northern regions[3]. However, as Thailand continues to industrialize, its urban population is steadily growing. More than 10 million of the country's 62.9 million people (1999) live in the capital, Bangkok[4].

Most people in Thailand speak Thai, the official national language. Dialects are spoken in rural, but the Standard Thai, the dialect of the Central region, is the national language. The Thai language may prove difficult to learn as it has little in common with Western languages and is built up of many similar words but with different sounds and tones that indicate completely different words. Other common languages are Chinese and Malay. English is spoken and understood to some degree in Bangkok and in the major tourist areas, but it might be hard to have good communication or complex negotiations.

Thailand is known as a Buddhist country and 95 percent of Thais describe themselves as Buddhists. Most Thais practice Buddhism jointly with other beliefs, which often relate to luck and eviction of evil spirits. It is often not distinguished between the various religious practices and many Thais therefore assume that they are all part of Buddhism. The rest of the population embraces Islam, Christianity, Hinduism, and other creeds. There is absolute religious freedom in Thailand, and the king is patron of all major religions.

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[3] See also appendix I and II for Key economic Indicators and Sectoral Shares of GDP
[4] Numbers are from Bangkok Bank 1998 and Bank of Thailand June 1999

The major ethnic group is Thais, who count for about 75 percent of the population. Besides them, other ethnic groups are Malays, Chinese, Cambodians, Vietnamese, Indians and different hill-tribe people. Thailand has for centuries absorbed a stream of Chinese immigrant. Today the Chinese form a sizeable community and it is estimated that the ethnic Chinese count for some 14 percent of Thailand's population. Thailand was the only country among its neighbor countries that never was under colonial rule. This made it easier for the Chinese society to survive in Thailand than in the neighbor countries during the late 1930s when nationalist politicians became stronger. Even as the Chinese grew wealthier on the business opportunities in the 1940s, they did not become enemies of the nationalist politicians, but actually more attractive friends and partners. In the late 1930s, politicians set up state enterprises and invited successful Chinese businessmen to run them and make them profitable. The same politicians used the wealth from the state enterprises to strengthen their own position. Their business partners were repaid with government contracts, monopolies and other privileges.

Social behavior

Thais are often described as a respectful, mild-mannered, hospitable and fun-loving people[5]. They have a good sense of humor, like to be entertained, and laugh whenever possible. The main goal of most people seems to be enjoying life. All work, study or religion should have some element of fun to be undertaken. The Thais strive to keep even moods and they refrain from showing emotions. They dislike impulsiveness, impatience, high temper and display of anger. Rural Thais might have difficulties to understand the differences between their own and western culture and norms, and therefore they might react quite strongly to certain "misbehaviors".

A western businessman that wants to do business in the kingdom has to learn the very important guidelines for conversation and negotiations with Thais. When it is necessary with discussions, they must remain totally private and tactful, as public discussions are considered taboo. Thais try to keep interactions amicable because verbal fights may damage relationships permanently. On the other side, the Thais are very direct concerning comments

[5] Information and personal opinions from interviews with Ms Elisabeth Granerød, Mr. Bjørn Granerød, Mr. Chaiyaporn Wejnaruemarn, Ms. Suchada Chuensuksawadi and Mr. Bjørn Naglestad.

on looks and clothes, which from a western point of view might be rude. Body movements and position of the head and feet conform to certain accepted norms.

Thais have a strong sense of hierarchy, and ranks are meritorious. Inheritance has hardly any effect on people's position in society. This hierarchy also prevails in business. The decision-making rests exclusively with top officials and managers of companies and administrations. The concept bears heavily on human relations. It normally takes a long time to build an open relationship and to become a trusted friend or partner, but long-term relationships can get very open. Doing business in Southeast Asia requires a lot of experience, contacts and resources, financial as well as human. It is of major importance when conducting business in Thailand that foreign companies tailor their market strategies to the oriental tradition, which is premised in trust and relationships. Thai government agencies and companies contract first to those with whom they are already familiar, so it might be very challenging to establish a local presence and make the right connections. It has been a common practice for foreign firms to form strategic alliances with local firms, as the import climate has then has tended to become friendlier and more open. There also exists a so-called Alien Business law, which regulates the foreign ownership in all companies established in the kingdom.

The workforce

Only 6 percent of the population is more than 65 years. The size of the work force now exceeds 34 million, with the majority of the work force under 30 years of age, and approximately 30 percent are under the age if 15. Each year about 800,000 people, with a literacy rate above 90 percent, join this force. The population growth rate is about 1.3 percent per year.[6]

It is a common fact that there is a shortage of educated and experienced staff in Thailand, which has led to competition for educated employees. Thai blue-collar workers were previously not known for being loyal to their company; if any company offered a higher salary than the present one, the Thais could leave at short notice. This changed a bit after the economic downturn in 1997, when several companies had to close down or reduce their work force, and the unemployment rate rose. The situation today is back where it was in

1996, which means that the ability of a company to attract and retain staff depends on how well the companies manage to tailor compensation packages to meet individual employee needs. Today, not only the wage, but also factors such as work job security, environment, organizational policies, relationships with superiors, and possibility for career influence the Thais when they make a decision whether to join, or remain with, a company. Admission to training programs to upgrade skills also helps to motivate staff and is from a Thai point of view seen both as a reward for good performance and as part of the total compensation package.

The Association of Southeast Asian Nations (ASEAN)

ASEAN was established in 1967. The member countries are Thailand, Brunei, Indonesia, Malaysia, the Philippines, Vietnam, Myanmar, Laos, Cambodia and Singapore. The members have developed increasingly close ties with each other, and the foreign and economic ministers hold annual meetings. The 3rd ASEAN Informal Summit was held in Manila, Philippines in the end of November 1999. The member countries there showed that although their economies were weakened by the Asian financial crisis, the work to reduce barriers to trade is continuing even more determinedly. Leaders from China, Japan and South Korea were also present at the summit. There has actually been a move towards cooperation with Northeast Asia as well. The 13 countries (called ASEAN-plus-three) agreed to work together in the future in the areas of trade, investment, monetary and financial coordination, technology transfer and scientific exchanges[7]. Rodolfo Severino, the secretary-general of ASEAN says[8] that the prospects for a common East Asian currency may be thirty years off, but that it seems to be on the way. There are, however, many historic animosities to overcome. The northeast Asian countries together account for 40 percent of the world's population, and their total GDP is approximately $ 8 trillion. Regional cooperation is progressing in economic, trade, banking, political, and cultural matters. Thailand is a major force in ASEAN and plays an active role in other economic organizations such as the Asia-Pacific Economic Cooperation forum (APEC), the World Trade Organization (WTO).

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[6] Numbers and information from Bank of Thailand June 1999
[7] FEER, Dec 16th 1999
[8] The Economist, A Survey of Southeast Asia, Feb 12th, 2000

ASEAN Free Trade Area (AFTA)

In 1992 the ASEAN-members decided to create a free trade area in Asia – AFTA. The purpose was to reduce tariffs on intra-ASEAN trade and among other things to attract foreign investment. The ASEAN countries want to integrate their economies in a huge common market place. The EC-system is used as a model, but the political and economical differences in the region might mean that the integration will take some time. The implementation of the AFTA accelerated after the regional crisis in 1997 and 1998, with the ASEAN countries adopting a number of measures to attract investments from abroad in order to reduce the negative impact of the crisis. The rising trade demand has transmitted expansion rather than contraction across borders, and the interdependence of the region's economies has begun to work in favor of recovery. AFTA changed the requirements for lower import duties to be completed already by the year 2002, and to include all agricultural and industrial imports. The tariffs for 90 percent of all products produced in -and traded between- Singapore, Malaysia, Thailand, Indonesia, Philippines and Brunei have already been reduced to a maximum of 5 percent. The member countries are also working towards zero tariffs for all products by the year 2015.

The Asia (ASEAN+3) are among the most economically integrated regions of any major developing area with trade performance that is highly correlated, and highly integrated exchange rates and financial markets. AFTA is expected to make it easier to achieve free trade with capital, technology and educated labor in the region. While Thailand will lose revenues as a result of lower duties on imports from other ASEAN countries, it also benefits from lower duties imposed on its exports by other ASEAN countries. Thailand stands to gain more than lose from AFTA. Within ASEAN itself, Thailand's trade competitiveness remains strong, and the kingdom’s share in the overall ASEAN export market rose from 12.7 per cent in 1992, the year before joining AFTA, to 21.1 per cent in 1997.

The adjustments that have to be made as part of the AFTA requirements are a first test for the Thai industrial sector. Thai industries will have to face up to a much stronger impact from global trade liberalization under WTO later on, and how they fare under AFTA in the next few years will be crucial. Thailand will probably experience that foreign-made goods quickly will flood the domestic market, but on the other hand, trade liberalization will create new opportunities for Thailand's industries. Additional markets for Thai exports will open up and imports of raw materials needed for manufacturing will become cheaper. Analysts believe that the AFTA will be expanded to include other countries in the region (China, South-Korea and Japan).

Thailand's exports of paints, varnishes and similar products total around 1,000 million Baht a year. The export markets are small and fragmented, and mostly Asian: Japan, China, Malaysia, Indonesia and Taiwan. The ability to compete in the paint industry will be decided by raw material costs, the size of the market and the energy factor. Today, paint makers import raw materials and technologies from non-ASEAN countries. Thai makers of industrial paints are relatively experienced and enjoy higher production capacities than other ASEAN paint makers.

Part II

The Jotun Group[9]

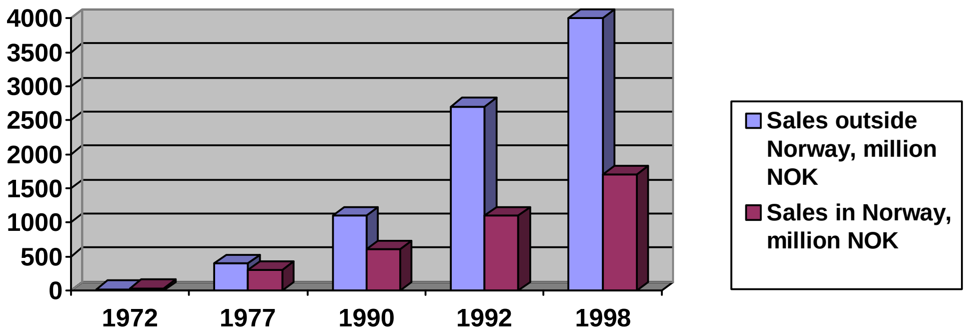
Introduction

Jotun is an international producer of paints, coatings, varnish and powder coatings. Jotun has approximately 4 000 employees worldwide, is present in 50 countries and has factories in 20 countries. The sales in 199910 were NOK 4,871 million, which was an increase of 580 million on 1998. The profit for 1999 and 1998 was NOK 241 million and NOK 44 million, respectively[11].

Jotun has its products sailing on all seas, and is among the Norwegian companies with the largest international market. Jotun enjoys a strong presence in its three selected international markets; Europe, the Middle East and the Far East (Southeast Asia). The markets are chosen both for business opportunities, and for spreading risk to different geographical markets. In 1998, the Group generated 69 % of sales from overseas operations, which consist of an extensive network of production and sales subsidiaries, distributors, agents and licensees.

Figure 3

Sales income Jotun Group, 1972-1998



Source :"The Story of Jotun"

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9 Information in this part is taken, Jotun 1999 Annual Report and from interviews with Mr. Odd Gleditsch jr., Mr. Bjørn Naglestad, Mr. Per Arne Nilsen, Mr. Bjørn Granerød, and from the book "The Story of Jotun"
10 Press release, March 2000. Sales for 1998 were NOK 4,300 million (from Jotun 1999 Annual Report).
11 See appendix V, Key Figures Jotun Group 1999 and appendix VI Jotun Group assets and equity

History

The history of Jotun is quite unique in the Norwegian and even the European industrial history. Not many family-owned Norwegian companies have had such an impressive development as Jotun. Today Jotun is one of the biggest industrial groups in Norway, with the original owner family, Gleditsch, a major (53.5%) stakeholder in the company.

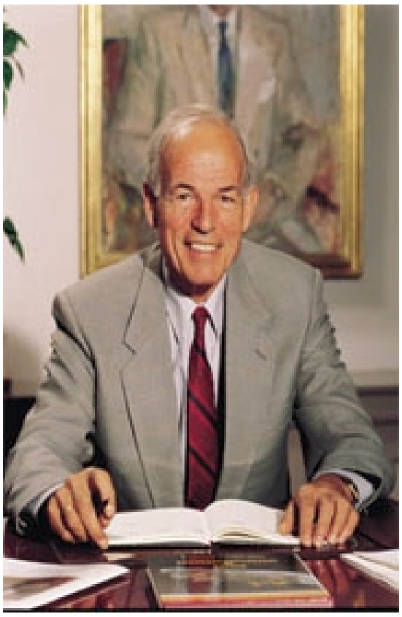
Odd Gleditsch started to distribute paints to the whaling fleets in Southern Norway in 1920. After a few years, he saw the potential in the paint business and decided to manufacture the paints himself, he therefore established Jotun Kemiske Fabrik A/S in Sandefjord, Norway in 1926. Production began the year after, in 1927; mostly supplying marine paints to the local whaling fleet and merchant ships in Sandefjord. Gleditsch was a salesman by heart, and traveled round the Norwegian coast to visit customers - old and potential new ones.

From the very beginning, Odd Gleditsch placed great emphasis on quality. Norwegian ship-owners demanded high level on quality and service, and Jotun has collaborated with the ship-owners and worked continuously to meet the demands. Odd Gleditsch played a very essential and special role in Jotun, both for the development of the company and the market, as well as for the company culture. Jotun mostly supplied the local whaling fleet and merchant ships with marine paints, and had its commercial breakthrough with Arcanol in 1931. Jotun had operational contacts and supplied soon the marine industry with marine coatings in most of the world. Even today, Jotun is ranked as one of the world's biggest producers of marine paints.

In the early 1950s, technology at the decorative paints marked had its breakthrough with the product Fenom. This paved the way to the private market, to the homeowners. The technical advantage of Fenom was that ordinary people could paint their homes themselves with a professional result. The decorative paints for the interior and exterior markets then became an important part of the company's growth.

Jotun settled abroad as early as 1962, when it opened a factory in Libya. The reasons for choosing Libya were that the country was active in oil exploration, and there were indications that the economy would develop very fast. Odd Gleditsch jr. considered the future potential paint market as big, and established Libyan Norwegian Industrial Company, Linoco. After having exported to Thailand for years, Jotun established themselves in Bangkok and started to produce powder coatings in 1968. The valuable experience from establishing the factory and producing in Libya helped Jotun in establishing a factory in Thailand, and further on, the problems in Libya taught Jotun about the importance of considering risk and unpredictable conditions in foreign countries. Jotun gradually lost its shares in Linoco, and in the mid 1980s Jotun was out.

Picture 1.
Odd Gleditsch jr.



The competition in the Norwegian paint industry had become tough in the 1960s. The manufacturers cut prices to gain market shares, and there was little profit to be made. Odd Gleditsch was the driving force behind the Norwegian paint manufacturers' merger when the Jotun Group of Companies was formed in 1972 by a merger of the four largest Norwegian paint manufacturers: Alf Bjercke A/S, A/S De-No-Fa and Lilleborg Paint & Varnish Factory, Fleischers Chemical Factory A/S and A/S Jotun Odd Gleditsch. The new company could focus on quality and was better prepared to increase activities abroad. Under the supervision of the Jotun's Chairman, Odd Gleditsch jr., resources were concentrated, a high technical standard was achieved, and Jotun turned out to be a front figure of the internalization of the Norwegian business environment.

Strategy

The expanding route has always been one and the same to Jotun: to rush slowly, and to move only one stone at the time, putting them calmly on top of each other. Jotun has expanded internationally in a very successful way, and has gained important experience from most of the world. The decisions and investments have always been for a long-term approach. Odd Gleditsch jr. puts it this way : "To build up a business, you need good products, good staff, capital and earnings. Each brick rests on the other bricks, and the company must respect the culture of the other countries". Long before the slogan "Go global, act local" gained a foothold in the business world, Jotun has emphasized the importance of finding suitable persons to go abroad, and tried to act locally even if the firm and thinking are global. Jotun says that the paint industry needs to generate higher earnings if the industry is to develop and produce forward-looking products that can combine quality with better health and environmental features.

Picture 2

Jotun Worldwide

Jotun is divided into three divisions: Jotun Decorative, Jotun Paints and Jotun Powder Coatings.

For Jotun Group in total, all three divisions had progress in 1997. The largest division, Jotun Paints had enjoyed strong growth and greatly improved profits, despite increasing international competition. The division has secured an even stronger position in the international shipping market, and has seen major increases in sales of corrosion protective coatings for industry and offshore installations.

Jotun Decorative

Jotun Decorative produces decorative paints and lacquers for indoor and outdoor use in Scandinavia. Jotun has a market share in excess of 70% in Norway, and enjoys a solid position in the Swedish and Danish market. The market share in Scandinavia was increased again in 1999. Jotun chose to put a focus on Scandinavia instead of other big European countries like Germany, France and England, to avoid markets where strong competitors were already established, and where competition was tough. In addition, Jotun is a Norwegian owned company, and Norwegians are per capita, the world's most paint consuming people.

Jotun Decorative has focused on brand building, and is putting more emphasis on those areas where it is the market leader. The customers demand more value for their money, both regarding service and product quality. This makes Jotun improve its performance constantly. Jotun's market position is supported by a proprietary system of in-store tinting machines called the Multicolor System. The machine is capable of producing more than 10,000 colors at the retail shop level. The system reduces stocking requirements for both Jotun and dealers as it allows tinting bases to be mixed in-store to the customers' specifications.

Jotun Paints

Jotun Paints is the group's largest and most international division, and has a significant share of selected markets in the Middle East and South East Asia. Jotun Paints is divided into three subdivisions: *Jotun Decorative paints*, *Jotun Marine Paints* and *Jotun Protective Coatings* . Jotun provides a full-range of protective and marine coatings for all kinds of steel structures, from barges to super tankers and industrial constructions. The products extend both the lifetime and the safety of steel structures, and reduce the maintenance costs. The competition among the biggest producers of marine paints and protective coatings has tightened and the mark-ups have got smaller the last years. The Paints division in total reported higher volumes and sales in 1999, but its margins is under pressure. *Jotun Decorative paints* in the Middle East and Southeast Asia has the last years shown progress, despite the economic crisis in these regions.

Jotun Marine Paints

is among the world's leading suppliers of marine paints. The marine coatings and systems for cathodic protection aim to keep the protection at a high level throughout the lifetime of ships. Jotun has experienced that customers consider the long-term aspect and the long-run costs when they are to choose protective systems. Jotun has created a complete system, called "Single Source Solution", which is a combination of paint and cathodic protection, and has also put emphasis on further development of products and paints for inside and outside protection of ships. Jotun has from research and constant testing acquired knowledge about fighting corrosion, and did recently launch a tin-free antifouling, Sea Quantum, that was well received in the shipping markets world-wide. Jotun has managed to establish as a major supplier of marine coatings in the US. Jotun have acquired a production plant in Louisiana, to ensure that American customers can benefit from better service and greater delivery reliability.

Jotun Protective Coatings

delivers corrosion-protective systems to the offshore industry. When demand for corrosion protection grew, Jotun established Jotun Cathodic Protection A/S, which combined the paint systems and cathodic protection. Building on its original franchise in marine paints, the protective coatings business area today markets paints world-wide for offshore and general industrial applications as well as its line of anti-corrosive marine paints, for example paints for maintenance of fishing trawlers and of ships and super tankers. The subdivision has among other things made large deliveries to Russia and Singapore and has earned a strong foothold in markets like Malaysia and Indonesia and in all the Middle East. Both the oil-producers in the North Sea and the Norwegian Petroleum Directorate have approved the paints systems that Jotun delivers for use on offshore installations. Jotun also sells paints for maintenance of industrial equipment and buildings on shore, and customers from various industries choose protective systems from Jotun. This market has experienced great growth lately in Egypt, Turkey and Australia, while the market growth has been negative in Asia as a result of the financial crisis.

Jotun Powder Coatings

Jotun Powder Coatings develops and produces powder coatings for use in heavy rust protection, cathodic protection, and electrical industry producing electric products as microwaves and refrigerators. Jotun has a 20 percent world market share in this area, and wants to become one of the world's leading actors in this market. The powder coating is an environment-friendly product for the treatment of surfaces, because it is produced and applied without the use of organic solvents. Further, the powder coatings are dry industrial paints, which have significant advantages to paint in terms of adhesion and ease of application.

Total sales reached USD 103 million in 1998. In 1999 Jotun Powder Coatings reported higher sales volumes, but lower sales values and earnings. The competition has got fierce, and this put a pressure on the overall prices. Powder Coatings seems to strengthen its position in the market, but the growth of this market lead to a shrinking market for traditional (wet) paints.

Part III

Jotun Thailand[12]

Introduction

Jotun is, besides Thoresen, the biggest Norwegian actor in Thailand. Jotun and Corro-Coat (both owned by Jotun Norway) employ 245 and 106 persons, respectively. I will in the following say ”Jotun Thailand” when I talk about Jotun Thailand Ltd. and/or Corro-Coat NOF Co.

In Libya, Jotun learned how to build up an industrial enterprise in a country completely different from Norway. Jotun encountered many problems, e.g. with respect to choice of business partner, and to how to handle investment in alien countries. Jotun acquired experience, related both to technological problems, cultural differences and how to cooperate with the foreign local authorities. Jotun learnt that before it could make a final decision to establish themselves in a foreign country, it is important to understand the local culture and politics. Further, when a decision on an investment was made, Jotun emphasized the importance of sending the right persons to the new affiliate, persons who could understand the local culture and at the same time communicate Jotun’s organizational culture and values. It was also communicated that the Norwegian way to do thing not necessarily has to be the best.

The history of Jotun Thailand

Jotun established themselves in Thailand long before the Southeast-Asian countries started their impressive growth. When Jotun made the investment decision, it had already for years been exporting paints to a large Chinese-owned agency, Seng Fah, in Bangkok. Odd Gleditsch considered the market-potential in Thailand to be present both for paints and protective coatings. At the same time, the competition in the country was not as hard as in established European markets. In 1967 Tore Lundh, the man who helped Jotun turn things in the right direction in Libya, was sent to Thailand to look at the possibilities of establishing

[12] Information about Jotun Thailand is from interviews with Mr. Chaiyaporn Wejnaruemarn, Ms. Suchada Chuensuksawadi, Mr. Bjørn Naglestad and Mr. Bjørn Granerød, and from the book “The history of Jotun”

a factory in Bangkok. With respect to the experiences from Libya, Jotun wanted to understand the local culture and politic before Jotun took the final decision to establish themselves in Thailand. A Norwegian shipping company, Thoresen & Co that had been in Thailand since the end of the 19th century helped Jotun with knowledge and its already established network.

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In 1967 there were already some good quality paint producers in Thailand, and there was only one license left for a foreign paint producer. Tore Lundh realized early that it would be difficult to fight against other, bigger, foreign companies in terms of money, and that Jotun needed to establish relationship with people that had importance in the Thai system. He therefore systematically got in contact with persons, who were all educated at one particular school and spoke English. Lundh talked about Norway, the nature, and the monarchy and about the importance of the family. The tactic seemed to work, and Jotun obtained the last license.

Fortunately, even if Jotun did not allow themselves too much time to consider the investment, Jotun has fared better in Thailand than in Libya. After Jotun got the license, the investment decision was made relatively quickly, and in March 1968 Jotun opened its factory in today's Bangkok, in Samut Prakarn. Jotun was actually the first international paint producer to invest in Thailand as a Board of Investments (BoI)-promoted project. The license gave Jotun exemption from tax for a period of five years. The license given had the same goal as today: to develop Thai industry and commerce through foreign capital and the introduction of new production techniques and technology. The Alien Business law demanded that a maximum of 49% of the share capital could be on non-Thai hands. However, the license allowed Jotun to be a 100 % non-Thai enterprise, but the shares had to be on a minimum of 6 hands. Thoresen & Co. bought 20 percent of the shares and the first manager came from Thoresen & Co. Jotun bought all its shares back in 1992.

Tore Lundh left Thailand and went to Malaysia in 1968 to look at the opportunities there. Kaare Kleive, a paint chemist, became Jotun’s first manager in Thailand. He was soon accompanied by Bjørn Granerød, who took over as manager in 1974. Granerød believed in the market for protective coatings, and in the importance of being first at the marketplace. The competition in the protective coatings market was also less intense. He changed the direction somewhat and put focus on protective coatings for steel constructions, industrial projects and marine paints, which gave better profit per unit sold, and Jotun Thailand experienced profit every year from 1974 onwards.

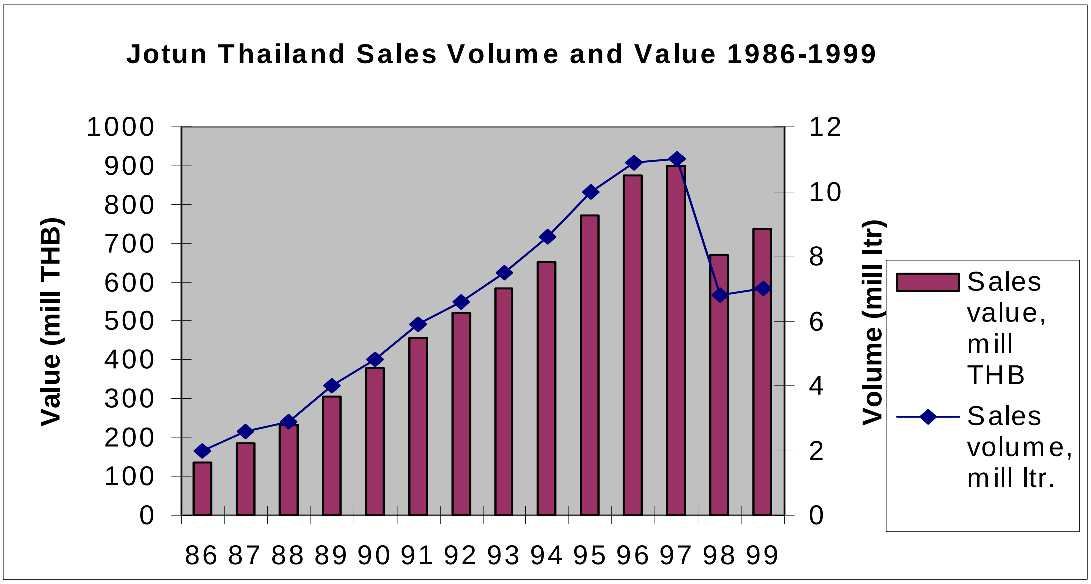
The Chinese agency continued to serve the paint dealers, and Jotun’s own sales people took care of the big projects and industry segments. Jotun realized early on that there were both technical as well as cultural differences between Norway and Thailand, and little by little Jotun learnt not only how to live with the differences, but also how to perform well with them. On the sales side, it was important to learn how the Thai system functioned, who decided what, and what a great role relationships play in Thailand.

In 1978 Jotun established Corro-Coat Nof (Thailand) Ltd. This factory was the first powder-coating factory Jotun established outside Norway, and the factory was the first in its category in the world. Jotun perfected some of the technological steps, adjusted the powder coatings to better fit the tropical climate. It took some years to earn the first profit from Corro-Coat, but every year since 1982, the results have been positive and, according to Jotun, satisfying.

In 1990 Jotun Thailand changed strategy. Now it was Knut Overgaard, a marketing man, who turned the effort to the decorative market, which is about six times bigger than the total of the protective and the marine market. Jotun Thailand entered the decorative paint market with products already developed in Norway, but with adjustments to the warmer and more humid climate in Thailand. Today Jotun Thailand has earnt a 6 per cent market share of the total decorative market, compared to a 25 per cent share on the protective and marine market (the industrial paint segment). The domestic market for industrial paint in Thailand was, in 1997, still growing at an attractive rate of 12-15% per year. The produced volume for Jotun Thailand is 60 per cent decorative paints and 40 per cent protective and marine paints, with the value equally divided, 50/50, between them.

Figure 4

Jotun Thailand Sales Volume and Value 1986-1999



Source : Reports from Jotun Thailand February 2000

For the first time in years, Jotun Thailand experienced stagnating sales and lower earnings in 1998. In Thailand, one of the results from the crisis in 1997 was that the entrepreneurs on big projects on order from their customers had to cut costs wherever possible. This meant that they bought less-quality paints, probably thinking more about short-term expenses than long-term benefits like quality and future durability. The reduced construction activity and the reduction on quality demands resulted in negative operating results in 1998.

Jotun's position in Thailand

The first really big product in Thailand was Coal Tar Epoxy, a paint that is used to paint and protect river barges. The paint is very well known up-country as high-quality paint at an affordable price. To people in Thailand, Jotun is known for selling high quality paints to boats, ships and pipelines that last even with tough weather conditions, and the brand name Jotun means high quality and expensive paint.

Jotun is the fourth biggest supplier of decorative paints in Thailand. The market segment is upper and middle class, which counts for about 10 million people. Jotun claims a 25%

market share in the industrial paint segment. Demand is especially high for paints used on air conditioners, lighting fixtures, metal furniture, auto parts and marine manufacturing. The overall economic rating for Thailand has improved, and for Jotun this has resulted in an increase both in volume and sale of about 20 percent compared with the same period last year. This is an impressive growth, when one take into consideration that Jotun in March, as the first paint company, decided to raise prices, because of an expected price increase on raw material.

Jotun Thailand has divided its sales organization into two : projects and dealers. The former one concentrates on bidding for projects, and on establishing relationships with entrepreneurs, architects and real estate owners. The latter is directed towards the dealers, who are the ones who get in contact with the end users. As a rule, paint dealers in Thailand have all different paint brands in stock, and promote the brands with the highest mark-up potential. Jotun therefore has to give high revenue to sellers and distributors so that they promote and sell its products. The long-time value and benefit of a high quality paint very much depend on the correct treatment of the surface before application, Jotun therefore puts a great effort into educating its sales & marketing people – and in teaching the architects, entrepreneurs and dealers how to prepare the surfaces before application, and how the application should be done.

Marketing effort

Jotun was first with the multicolor system in Thailand, and is still today the only actor that both produces the paints and provides service and maintenance on the system. Jotun has started marketing for the decorative paints through national TV-channels. One of the major goals of the advertising campaign from 1999 and 2000 has been to create awareness and to inform people of the advantages of Jotun’s multicolor-system. The slogan ”More than ten thousand colors” has told people that they have an almost unlimited choice of colors, and on the other hand, the dealers see the advantage of only keeping the white base-paint in stock. One of the world’s leading advertising companies, Lowe Lintas & partner, which is the biggest advertising company in Thailand has been hired to do the marketing for them.

The feedback on the television commercial has been very positive, and dealers and outlets have been thankful for the extra advertising, paid by Jotun, and have given Jotun more space and better shelves in their stores. The reason for doing marketing through TV divided; first, Thais love pictures, motion and funny stories, which are easier to communicate on TV than through newspapers and magazines. Second, almost everybody in Thailand has access to television, and when bought, it is always on. Third, the use of TV is almost for free, in contrast to newspaper and magazines, which are charged per copy.

New factory

In 1996, Jotun decided to build a new factory in order to be able to produce enough to satisfy expected future demand. Jotun had already bought land for a new factory in Amata Nakorn Industrial Estate in Chonburi when the financial crisis in Southeast Asia appeared in 1997. However, Jotun did not give up the new factory, and the official opening took place in December 1999, with the Norwegian Princess Märtha Louise present. The financial crisis in Thailand and Asia caused some setbacks and problems, but now, in 2000, when all arrows are again pointing upwards for the region, Jotun is present with a new modern factory, which can handle production growth.

Picture 3
Jotun's new factory

The new factory has replaced the former plant in Samut Prakan. The cost, USD 25 Millions, is Jotun's largest single investment, and enough for the factory to be equipped with the latest manufacturing technology. The factory fulfills Jotun's high demands regarding job security, environmental issues and quality. The quality control is strict, both when it comes to the quality of the raw material as well as the quality of the finished goods. Jotun was actually the first multinational paint producer that received the two ISO certificates, ISO 14001and ISO 9002. The first was given for environmental performance in terms of emission control, the working environment and waste handling. The latter was given in 1996 for implementing the ISO 9002 quality system.

The Board of Investment (BoI)

Jotun Thailand has during its 32 years in the kingdom applied for four approvals and has relocalized and built new factories twice. Bjørn Naglestad says that the Thai authorities have provided excellent support and that the relations have been good during the more than 30 years Jotun has been present in Thailand. Jotun values the relationship with the Board of Investment highly, and has on two occasions invited key members of the BoI to Norway; in 1996 and 1997. Tax laws, regulations and the criteria for tax holiday connected to Jotun's relocalization were very uncertain, but Jotun was granted BoI privileges in 1997 for relocating its factory to an industrial estate outside Bangkok. The secretary-General of the Board of Investment, Staborn Kavitanon said with the opening of the new factory that "Jotun benefits the country (Thailand) by providing hundreds of jobs to Thai workers in the region, and by training them in the use of the latest technology".

Normally the BoI does not accept invitations from companies. The reason why they accepted the invitation from a Norwegian company was that Thailand's former king, King Sulaonkhorn visited Norway in 1907 and wrote a travel letter that is obligatory reading in primary school. The king wrote warmly about his visit to North Cape, and the BoI representants accepted the invitation on the condition that they also were taken to North Cape. The BoI deputee enjoyed the 1996 trip so much that the BoI director asked Jotun if he could come to Norway on a trip too. In addition to the cultural arrangements, the visitors saw some important parts of Norwegian industry, and were introduced to Norwegian business life.

Part IV

Theories on Multinational Enterprises (MNE) and Foreign Direct Investment (FDI)

Introduction

Theories about international trade are one of the oldest parts of economic theory. Countries have for centuries earned money on international exchange of goods. Adam Smith said already in the 18thcentury that the gains from international trade are not only from the export income, but also in terms of a greater supply of consumer goods. Multinational Enterprises[13] have since WWII had an importance on the development of the world's economies. The MNEs have integrated the world economy with linking economic activities in home and host countries, and have an impact on the home country[14] as well as the host country.

The international business research is concerned with firm-level business activity that crosses national boundaries. The activities may include transfer of goods, capital and people, as well as knowledge and relationships.[15] Further, the research looks at the interrelationships between the operations of the firm and foreign environments in which the firm operates[16].

The historical evolution of MNEs have by researchers been divided in four major periods[17]:

- The early internationalization (1200 to 1945)
- The golden age of internationalization (1945 to 1973),
- The new internationalization (from 1973 to 1990s), and
- The ongoing period.

13 A multinational enterprise is a firm that controls assets (factories, mines, sales offices etc.) in two or more countries (Definition by UNCTAD)

14 Home country in this context means the country where the firm originates. Further, Host country is the expression used for the country(ies) where the firm extends its business operations.

15 Mira Wilkins "Multinational Corporations: An Historical Account", 1998

16 From lecture on International Business and Economic Development, Torben Pedersen, professor at the Department of international Economy and Management, autumn 2000

17 From lecture on International Business and Economic Development, autumn 2000. For more information about each period, see appendix VII

Theories

The theories made on international trade in the 20th century have put focus on what it is that decides the extent and the composition of the exchange of international goods. Norman[18] argues that the most important contribution is the Hecksher-Ohlin-theory[19], which is a theory on the connection between relative access to input factors and the international trade. The theory says that a country will export the goods that are intensively in the use of the input factors, with which the country is relatively well equipped, and import other goods, and that it therefore will be an equalization of factor prices internationally and a specialization in production.

Stephen Hymer, wrote his Ph.D. thesis in 1960, and put focus on the fact that there was a growing need to create theories on FDI. His theory was quite simple, and he meant that firms become multinational because they want to expand their monopoly advantages to foreign markets. The earlier contributions were mainly concerned about the two questions "Why do firms go abroad" and "Why locate abroad". The contributions were not taking into considerations the changing trade patterns in the world economy, but were still used by trade economists until the 1990s.

Herbert Grubel and Peter Lloyd published a study in 1975 that showed that more than 50 per cent of all international trade is exchange of similar goods (cars for cars, clothes for clothes – but with different brand names and models). The reason for this is product differentiation and economies of scale, but might also be that there exist differences in technology and transaction costs (tariffs, taxes, transport costs, technical requirements). This means that factor prices will differ among different countries, and there will be countries with advantages in labor-intensive production and other countries with advantages in capital-intensive production. Industries that are intensive in the use of labor will then have incentives to invest in a country with low wages. An example on this is that the labor-intensive manufacturing industries often are located in Southeast Asian countries, where the wages are relatively low.

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18 Norman, Victor D. 1997

19 Heckscher-Ohlin Theory by Eli Heckscher and Bertil Ohlin, often called the "Free Trade Theory"

In 1976 Buckley & Casson gave birth to the internalization theory, which implied that there existed certain costs of using the market. These costs existed because of market failure, and were called transaction costs. The year later, Dunning presented his eclectic paradigm, which combined the different existing theories on international trade. I will in this part apply the eclectic paradigm on Jotun in Thailand.

The trade theories from the 1990s have focused on more complex problems in the international trade, and also on the interrelationship between companies and governments.
Dunning has been in the game for a long time, and has been a very important contributor to the theories on international trade. In 1995 Dunning wrote an article "What's wrong –and right- with trade theory" and put focus on the enormous changes that have been in international trade pattern the last two or three decades. He has also changed and expanded his eclectic paradigm as the world economy has changed and demanded other theories and explanations[20]. Dunning also tries to look into the future, and predicts a more complex and daunting world. This, according to Dunning, is for four reasons[21]:

- First, the difference between the territorial space open to corporations and individuals, and under the jurisdiction of governments, has increased.
- Second, the boundaries of the leading institutions for organizing economic activities are gradually being destructed.
- Third, standards of living have improved especially among wealthier nations, and this has led to an increased demand of quality-of-life-improving goods and services, which governments can strongly influence by their actions or non-actions.
- Fourth, today's alliance capitalism seems likely to demand an increasing and more deepened economic role of sub national and supranational authorities.

Market failure

When there exists market failure, some of the market transactions cannot be undertaken. Two of the main causes for market failure are asymmetric information and firm specific public goods. An example of the former is when the seller of a good, e.g. a car, knows more about the good than the buyer. With most products, it is the seller that knows the product

[20] Dunning, John, "What's wrong –and right- about trade theory", 1995
[21] Dunning, John, "Alliance capitalism and global business", chapter 14, 1997

best. The buyer has less possibility to get to know the product before he buys it, and needs to be convinced that the product works and is worth a certain price. The name ”market for lemons” is commonly used on the second-hand car-market, where the car-owner knows the history track of the car, and how it has been driven, what kind of accidents that have occurred to the car, how well it has been maintained, and so on.

The problem with imperfect information and ”market for lemons” can easily be transferred to transaction costs in most markets, and the main reason for international production is probably transactional market failure[22]. With specialized products or services, it is really difficult for a buyer to know whether the product or service is worth the price. For the seller to sell the product, he has to convince the buyer that his product is better than the alternatives and worth its price. This works for many products that can be examined and tested before sale, but certain services and added quality on a specialized product will lose its value if the seller has to disclose all the specifications.

These failures lead to the establishing of firms, and also multinational firms, because a firm can more effectively transfer the information and the services inside the organization. Foreign Direct Investment accounts for an increasing share of international financial flows[23]. FDI is typically industry specific investments that integrate horizontally or vertically. The horizontal integration is when a firm establishes a new affiliate[24] in a foreign country, either through building a new factory or buying an existing firm. The advantage of buying an existing firm is that the existing local management and staff know the local market, and it demands less time before production can start, in addition, there is one local competitor less. The vertical integration is when a firm buys a foreign firm that either is a supplier or a customer. This is often done in industries where the input prices might fluctuate a lot, or where it is of major importance to have access to a specific market.

[22] Teece 1986, ”The modern theory of TNC”
[23] International financial flows include in addition to FDI, funds that firms borrow from foreign banks and raise from other sources in foreign financial markets, as well as official flows, primarily official development assistance. (UNCTAD)
[24] An affiliate is an enterprise in which an investor, who is resident in another country, owns a stake that permits a lasting interest in the management of that enterprise. An affiliate must have at least 10% foreign ownership. An affiliate is called a subsidiary if the foreign parent has at least 50% ownership. (UNCTAD)

Has there been any change in the world trade?

Hirst and Thomson[25] mean that there have been no particular change in the world trade: they say that the current trade situation is very much alike the situation before WW1. Kobrin, on the other hand, argues against Hirst and Thomson, and says that there is a quantitative and a qualitative new situation now compared to earlier internationalization.[26] Kobrin argues that the trade today quantitatively is "broader in terms of markets encompassed, deeper in terms of density and velocity of transactions and based on international production rather than trade". Qualitatively, "nation based economy is undermined, because of network based economic relations across borders and a rapid growth in information based relationship across borders." According to Dunning,[27] the globalization of the world economy has affected the pattern of trade in three main ways:

- The increasing mobility of assets has widened the options of firms in how they engage in international trade and production.
- The importance of arm's length transactions has declined relative to transaction conducted between related parties, and this part of trade has become increasingly more integrated in the multinational firm.
- National governments and supranational regimes have become increasingly more important in the management of trade and the competitiveness of immobile resources and capabilities.

Multinational Enterprises and Foreign Direct Investment

There are today more than 60.000 MNEs worldwide[28]. These MNEs have more than half a million affiliates and control foreign assets worth $15 trillion (1998) Almost 70 per cent of world trade is controlled by MNEs, and 35 per cent of the total trade is between MNEs and between MNEs and their affiliates. The typical industries with a high degree of MNEs are industries with advanced technological production equipment, industries with high research and development (R&D) costs, knowledge-based industries and so on. Firms with immaterial firm-specific assets will also tend to be multinational.

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[25] Hirst and Thomson, "Globalization in question", Polity Press 1999

[26] Hansen, Michael W., Copenhagen Business School, in lecture about "International business and economic development", 2000.

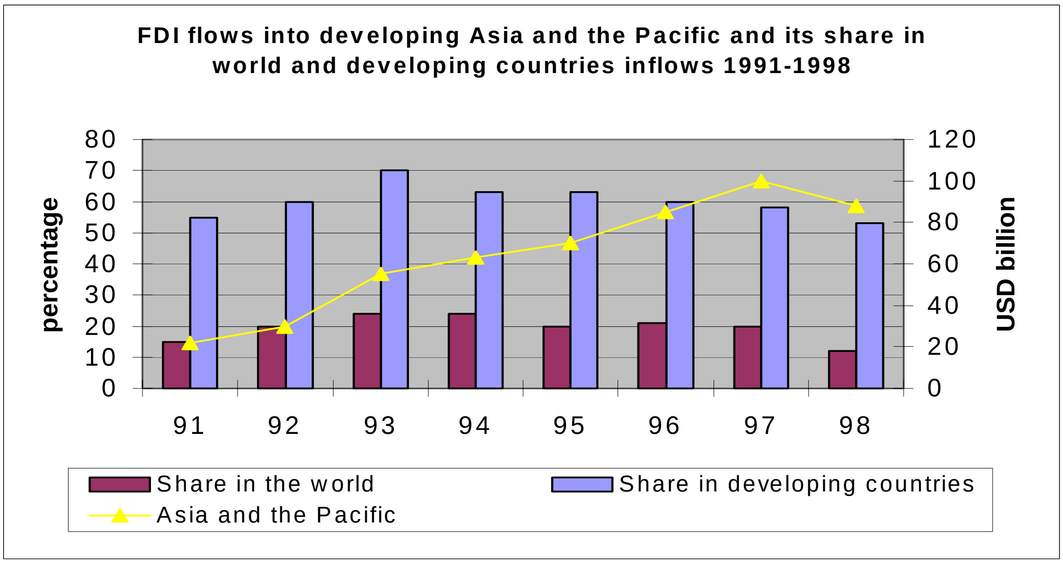
[27] Dunning, john, "What's wrong –and right- with trade theory", 1995

An important question is why companies invest in foreign countries, when there are obvious alternatives to foreign direct investment such as licensing, joint ventures or increased export. It is a common fact that there are certain costs that will be magnified by going abroad, because each country has its own rules, legislations and business culture. These costs may be related to increased uncertainty, transport costs, and the learning of new cultural codes. Other costs are related to language, recruiting new staff from the foreign country, or costs related to understanding the new political, legislative and economical system.

History of MNEs

Most of the FDI are taking place in the industrialized world. The ten largest FDI home countries (that have net FDI outflow) in 1998 counted for 80 per cent of the world total outflow FDI, and the ten largest host countries received more than 70 per cent of the world FDI inflows. The main streams are between USA, Canada, Japan and EC. Approximately 20 per cent of the $650 billion of FDI in 1998 went to developing countries, of which Southeast Asia and East Asia, received about 70 per cent.

Figure 5



Source: UNCTAD, FDI/TNC database, 1999

[28] Numbers and data from World Investment Report 1999

Initially, international production primarily took place in countries where the multinational enterprise could exploit cheap labor and natural resources for export. The multinational enterprises wanted to supply foreign local markets with products similar to those produced in the home country. In the mid-1980s the MNEs role in manufacturing in countries like Singapore and Thailand had become formidable[29]. Singapore has been very successful in incorporating MNEs into its own strategies. The private sector has been dominated by export orientated transnational capital, and Singapore has succeeded in using MNEs as instruments for continually raising living standards for local workers.

Today, markets have proceeded and products have become more specialized. Further, markets have become more integrated (for example the EC and ASEAN), and Multinational enterprises want to take advantage of this and the possibility for economies of scales[30]. Studies also show that the ownership structure of international production has changed, from mainly being fully owned by the foreign (US) company to being minority-owned. Data from the UN Center of Transnational Corporations in 1978 showed that for 41.1 per cent of the affiliates established before 1960 there was 100 per cent ownership, compared with the establishments from 1961 to 1975, where this portion had sunk to 25.3 per cent. The reason for this might be that non-US firms entered the international production-area, but also that the legislation in many Southeast Asian countries has demanded a majority local ownership of all investments, or at least that the shares had to be on a minimum of 5 to 10 hands, e.g. the foreign firm was not allowed to have more than 49 per cent of the stakes in their own affiliate.

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[29] Mira Wilkins ranked host countries by foreign affiliates' percentage of sales in the country's manufacturing sector (1987). Ireland was ranked highest with foreign affiliates that had 65.0% of total sales in manufacturing, followed by Singapore (53.0%), Canada (49.0%), Thailand (48,6%). Peru, Sri Lanka and United States were all at the bottom of the list with 11.8, 11.7 and 11.5%, respectively. Japan was at the very end with only 2,2%.

[30] Economies of scales: the additional cost for producing one extra unit is falling with extended production volume

FDI to Asia

There have been four major waves[31] of Foreign Direct Investment inflows to the Asian countries after 1945, and there has been various degree of governmental intervention. First; in the late 1960s FDI was motivated by the import substitution policies that many Asian countries followed. Foreign firms that wanted to get access to the Asian markets had to establish themselves in the region. In the 1970s, foreign firms were again motivated to invest in Asia because of the good economic prospects and the availability of cheap inputs: capital and labor. In the mid 1980s Japanese firms needed to locate in countries where the wage level was lower, and chose to a great degree to invest in Southeast Asian countries. Today there is a massive amount of Foreign Direct Investment to China. The consumer markets in developing countries and especially the newly industrialized countries have an enormous growth potential, and foreign direct investment is made not only for production, but also because of the importance of being present in a region in order to adapt products and services to consumer demand and needs. It has also become easier and less costly to perform trade, the tariffs in the ASEAN countries have been moved below the double-digit level, and the non-tariff barriers have been reduced.

The foreign companies are encouraged by the potential of Asia. In this dynamic region consumers are becoming increasingly affluent. Producers know that if they want to be serious players in Southeast Asia they need a direct presence in the region. Production facilities will enable them to supply tailor-made products to customers' needs and tap potential. Long term, costs can be controlled by investing in new plants in Asia.

The Thai government promotes foreign investment in Thailand through the Board of Investment (BoI), which was established in 1977. The BoI lists seven categories of economic activities, covering hundreds of types of businesses that are eligible for investment incentives. Potential investors who can show up that they will significantly strengthen Thailand’s balance of payments position, especially through production for export, or support the development of the country’s resources, increase employment, locate operations

[31] Hans Jarle Kind, 1999

in provinces outside the Bangkok metropolitan area, or that simply are considered important and necessary by the government, are eligible for BoI incentives.

Large investments from multi-nationals have helped Thailand to become an important Southeast Asian production center for manufacturers of computers, electronic integrated circuits, automobiles, auto parts and air conditioners. The government's initiatives to promote foreign investments, improved business infrastructures and emerging local entrepreneurs have helped Thailand to expand beyond its traditional export patterns.

Dunning's eclectic paradigm

History

John H. Dunning wanted to offer a framework, which made it possible to identify and evaluate the significance of the factors that influenced the initial act of foreign production and the growth of this production. Dunning presented his paradigm of international production at a presentation to a Nobel Symposium in Stockholm in 1976. He called the paradigm "eclectic", because it consisted of earlier theories made by other economists. Dunning put together theories with market-power perspectives with localization- and transactional theories, and said that the three theories were not competing, but that they all described different aspects of international trade. He tried to explain why there is international production, where the production would take place and how and why multinational firms could earn better profits than national producers in the respective countries[32].

The OLI-paradigm is general in form, and has only limited power to explain or predict particular kinds of international production or the behavior of individual firms. But the paradigm remains still today a useful and robust general framework for explaining and analyzing the economic rationale for international production and the organizational issues that are related to multinational enterprises' activity. The paradigm indicates which internalization theory that will be chosen, dependent on what advantages the specific firm has. Dunning meant that the three requirements: *ownership specific advantages, internalization advantages and localization gains* needed to be present and satisfied at the same time if it should be profitable for a firm to undertake FDI instead of export, licensing or joint venture. Dunning put the options for servicing the foreign markets into the following figure:

[32] Dunning, John H., "The eclectic paradigm of international production: A restatement and some possible extensions", 1988

Figure 6

		Advantages		
		Ownership	Internalization	Foreign location
Route of serving market	Contracts	Yes	No	No
	Exports	Yes	Yes	No
	Foreign Direct investment	Yes	Yes	Yes

This model illustrates what needs to be present in order to participate in international trade, and what kind of route that will be chosen for serving the market. According to Dunning, a firm that consists of ownership advantages, but has no internalization or locational advantages will be better of by contracting (licensing) its international production. Further, a firm that has both ownership advantage and internalization advantages, should not establish a new affiliate abroad if there are no advantages from being localized in the particular country, but serve the foreign market(s) by export. Only those firms that can show ownership, internalization and locational advantages should serve the foreign market(s) through foreign direct investment.

Dunning has changed and expanded his eclectic paradigm throughout the years. The main critic was the superfluity of the O component and the lack of attention given to behavioral variables. In 1993 Dunning came with an updated vision of his eclectic paradigm, where he incorporated asset seeking FDI and where he made a clearer recognition of strategy as a dynamic and firm specific variable, he also suggested that more emphasis should be put on further research on foreign investment and the dynamics and effects of FDI. Two years later, the paradigm was extended to embrace the main features of alliance capitalism. Finally, in the late 1990s Dunning has analyzed how technological developments and globalization are affecting the content and configuration of OLI advantages.

I will in the following explain the three requirements in the eclectic paradigm, and later relate each requirement to Jotun Thailand.

Ownership advantages

The ownership advantages are firm specific and related to the size and the market position that are specific to a particular firm (Dunning 1980). The ownership advantages are often called competitive or monopolistic advantages, and are advantages a specific firm has compared to other firms.. These advantages are the main asset for most firms, because they give the firm market position or cost advantage to other firms. It is of major importance to develop and protect these advantages as competitors might try to copy them.

The competition on the world's paint markets is getting tougher, and Jotun cannot compete in size with its main competitors. Only the best performers will survive, and Jotun therefore has a strategy of finding new market opportunities where Jotun can become the preferred paint supplier and one of the major actors. The major advantage for Jotun is not its products, but the concept of Jotun, which is to provide the customers with paint, training and service. This means that Jotun develops and produces paints for different environments and uses, they educate its distributors, agents and customers how to prepare surfaces and how to apply the paint. All customers involved get training : managers, technicians, officers and painters. Jotun follows up with service whenever needed, guarantees that the colors will not differ between the batches, and always sets quality as the highest priority.

In Thailand and other Southeast Asian countries, long-term relationships are of great importance. In business circles it is very important to know who - which person- who is able to take major decisions. The Asian way of thinking is far more connected to family and trust than the Western way. An elected board of members may be thrown out in one single day, but the family head, the founder, remains what he is. This may have had a positive effect on Jotun's business in Thailand, compared to its major competitors that are mainly big companies, listed on the stock exchange. It is expected that Jotun, as a family-owned company is single-minded and that this is guarantees that they will continue to produce what they are best at: paint and powder coatings. It is hard to say whether it is an advantage to be a Norwegian-owned company in Thailand, but a common saying says that not being American is an advantage in Thailand, whereas the difference between European countries is probably of a less significance.

There are, according to Dunning, three kinds of ownership-specific advantages: standard advantages, benefits derived from belonging to a large organization and benefits from being a multinational enterprise (Schjelderup, 1999).

The standard ownership advantages[33]

The standard advantages are advantages a firm may have compared to other firms in a specific location. These advantages are mainly related to the size and established position an already established firm enjoys, and in some cases, monopoly power. Further, the advantages are often related to product diversification and exclusive access to technology, patents and markets and use of input factors like labor, finance, information and natural resources.,

The standard advantages may lead both to market inefficiency and economies of scale. Brand name and quality are important elements in this category. Jotun's core products are surface treating and cathodic protection. Jotun continually has put a special effort into keeping a high quality product and developing new better products for use in certain industries. Jotun's brand name is strong in Thailand. Jotun has won high-prestige contracts on pipelines and installations that were exposed to different forms of extreme climate, and could then convince "ordinary" customers that they were able to provide paints that protected normal houses and high-houses from harsh weather conditions.

The fact that all business includes some transaction costs can easily lead to the conclusion that MNEs must consist some ownership advantages. The conclusion is based on the assumptions that the transaction costs will be magnified when a firm decides to go abroad, and that the MNEs must compete with local firms that experience smaller transaction costs. The ownership advantages can compensate for the extra costs the MNE has in addition to those indigenous producers face; costs of setting up and operating a foreign affiliate.

[33]Most of the definitions in this chapter are from Schjelderup, Guttorm**,** "Strategic Choices in a Global Environment: The Behavior of the Multinational Firm", 1999

Benefits derived from belonging to a large organization

The benefits from belonging to a large organization are that the affiliate may benefit from economies of joint supply in production, purchasing, finance and marketing, and in addition get access to cheaper inputs like administration, management, R&D, marketing and human capital from the parent company. After more than 30 years presence, Jotun today has earned a position in the Thai paint industry. As Bjørn Naglestad puts it: “In the paint industry references and certificates are important. Being part of a large organization is indeed a benefit. In the world wide marine industry it is a must”. Specific organizational culture and managing practices can count for an important part of the ownership advantages, and the possibility to exploit the parent firm’s knowledge of management, accounting, marketing and finance is of great importance. An already established firm will certainly have some competitive advantages compared to a new firm with no experience in the business.

The organizational culture in Jotun has been quite extraordinary in the Norwegian industry. Gleditsch’s managerial role and his ability to see the importance of all parts in the value chain is probably one of the main reasons for Jotun’s success. The owners have had long-term perspective and have had their vision. Jotun put focus on its core areas, on what Jotun knew best, and realized early that the knowledge related to production, research and marketing it had obtained in Sandefjord and Libya could be used and exploited in Thailand as well as in other countries. As an example, Odd Gleditsch was among the first in Norway to learn about industrial marketing. The experience from Norway probably helped Jotun when establishing in new, unknown countries. Gleditsch realized early that it was of vital importance to understand the major differences when it comes to countries and people, both regarding product demands, cultural and political regulations, but also marketing. The same marketing campaign can easily get a total different welcome in one country than in another, and success in one country will not necessarily mean success in a totally different country.

It is important to possess financial resources to be able to invest in the necessary R&D to keep track with the speed of the technological development. A large organization will typically possess more financial resources than a smaller organization. Also in the paint industry, , it is of great significance to maintain the R&D to be able to maintain a first-class product. Maintaining a high quality has always been a major strategy for Jotun. Jotun invests heavily in R&D, and experiences economies of scale connected to research and development. Some of the components employed in the paint products are also used in the protective coating products. Developments in either of these two product groups can easily be transferred to the other group. Jotun is able to do share the cost and results of R&D with all affiliates, which keeps the R&D costs per unit of manufactured product at a moderate level. Odd Gleditsch Jr. expressed this in this way in 1992: *"I do not believe it is possible for us to operate as an independent company if this is based on the use of technology that other companies have developed. It would be unrealistic for us to continue our research and development operations at their current level on the basis of the turnover that can be achieved in Norway."*

Jotun thinks long-term when it comes to R&D as well as investments. This means that Jotun participate in long-term research and development programs with shipping-, oil- and industrial companies. Jotun Norway has always controlled the group's laboratories. The main part of research and development is carried out in Sandefjord, but regional labs have been established. The regional labs work on projects for the R&D management in Sandefjord, and do also research on certain climate differences and on local construction material. In addition, the different factories have a smaller lab "attached" in order to always being able to check whether the quality on local purchased raw material and the quality on batches do fulfill Jotun's demands. In 1999 Jotun opened a regional development laboratory in South Korea, and made an upgrade for the Malaysian lab.

Benefits of being an MNE

Being an MNE means that a firm is in a better position to take advantage of different factor endowments, factor prices and tax regimes. The firm probably has advantages when establishing abroad as it has experience from managing production, sales and marketing in its "home" country. This means that the firm has the possibility to exploit its technology gains and management gains in several countries, and get access to more markets.

There are certain industries where the ratio of MNEs is higher than the average, and these industries are often characterized by high marketing costs and product differentiating. This means that there are resources based on knowledge rather than physical capital that lead to

FDI. One reason for this is that it is easier and more efficient to transfer knowledge than capital goods. Allowing affiliates to use the knowledge from the mother company or other affiliates has marginal costs close to zero. The multinational firm also has the possibility to get knowledge from their affiliates about local conditions in the foreign country.

Another advantage of being multinational is the possibility to do strategic pricing. When a firm is localized in various countries with different tax policies, the firm can to some extent canalize surpluses from high-tax countries to low-tax countries, so that the total taxes paid by the MNE are reduced to a legal minimum. For a company with high costs related to R&D and marketing, it can be an idea to localize the main research department to the high-tax countries, and charge the affiliates in the low-tax countries as little as legally possible. As a result the company as a whole will earn greater profit[34].

Rugman wrote in 1979 the risk diversification thesis where he said that different firms might have different views on an identical investment opportunity in a particular country. The reason for this it that firms are taking into consideration their existing portfolios and their attitude towards uncertainty. This again means that firm-specific characteristics has to be taken into consideration before it is possible to use the OLI-paradigm to say how a multinational enterprise will response to a specific investment opportunity. Over the years, Jotun has spread risk by serving several sectors. Jotun is divided into three divisions: Jotun Decorative, Jotun Paints and Jotun Powder Coatings. The divisions represent sufficiently diverse segments to enable fluctuating market trends to be contained. Jotun values highly the fact that the markets are within the core areas, i.e. in areas where it has particular expertise and the best chances of success.

Another theory, the risk minimization hypothesis, says that, other things being equal, firms will prefer to spread their investments geographically – firms prefer to diversify their geographical portfolio. Jotun is heavily represented in three geographical areas: Europe, the Middle East and the Far East. The fluctuations in these three areas are not likely to equal another, and this reduces the total and overall risk.

It is an advantage to be multinational when doing business in the shipping industry. The customers are usually big multinational enterprises that demand and expect to get the same products and quality independent of geographical location. Marine paints are produced following global standards, and Jotun is one of the world-leaders on this area and enjoys a good reputation for delivering time and quality. Part of Jotun's strategy has been to get in touch with the shipping companies and to talk with persons in the right positions, both the ship-owners, the captains and the first officers, so that they would understand what Jotun could offer them and which advantages Jotun's coatings might have compared to other competitors' products. About 75% percent of all shipbuilding today is concentrated to Asia. There are, of course, countries and places where it is neither profitable nor favorable to establish a factory or a service center, but in Jotun's strategy it is of importance to be able to *provide their customers with the right products and service where and when they need it.*

In addition, many of the shipping companies in the Southeast-Asian region are Scandinavian or European owned, and Jotun can refer to projects carried out in Europe. Further Jotun can then have an advantage when it comes to language and culture. It has always been part of Jotun's strategy to work with the right people and to value relationships. Norwegians and Scandinavians that are living abroad, will typically keep together, and the relations and contacts between them should not be underestimated. They give each other the opportunity to present their ideas, products and services.

Dunning says today that the future competitive ownership advantages of enterprises[35] between other things probably will be: "the ability to motivate and upgrade the intellectual and creative qualities of the work force, including managers, in a cost-effective way", and "the ability to seek out new and unfamiliar markets, and successfully adapting and promoting the qualities of particular products to meet the specific and localized needs of customers." The former is partly what Jotun has been doing when attracting the best managers to the company, and also when Jotun has showed up a long-term commitment to employees at all levels. The latter is part of Jotun's "old" strategy, but implies that it is necessary to

[34] Schjelderup, 1999

[35] Dunning, John H., "The eclectic (OLI) paradigm of international production: Past, present and future", 2000 and

continuously keep the innovative focus. Firms will in the future need to complement their core competencies with those of other firms. This makes it more important for managers to identify and evaluate potential partners, to make the appropriate agreements with them, and to achieve the results that are in the firms' best interest. The MNE will probably to an even greater extent work with and learn from partner firms, foreign governments and foreign labor unions.

Locational advantages

The second element of Dunning's eclectic paradigm is concerned with the "where" of production. The locational advantages try to explain why a firm should wish to produce and settle in a specific location, and are available to all firms present there. The locational advantages need to be present if a firm should want to locate in a foreign country, if not, the firm will be better off producing in the home country and only exporting to this foreign market. A multinational enterprise will typically engage it foreign production when they find it in their best interest to combine their ownership advantages and certain internalization gains with production in another country. What location to choose for the multinational firm will often be influent by spatial market failure, that is the existence of trade barriers like tax rates, tariffs, environmental legislations or political issues. Further, the advantages might be related to lower factor prices, industrial agglomeration (clusters), barriers to entry and trade costs, strategic considerations, market size, access to skilled labor, the real wage level and lack of local competitors.

One might say that Jotun first was established in Sandefjord, Norway as a result of localization. People from Sandefjord have been used to traveling around the world and to exploiting new markets, ever since man started whale hunting. It was considered normal in Sandefjord to go abroad to work, get some experience and learn about new cultures. One can see a similar pattern between how Jotun first established in Norway and later how new affiliates have been established. Gleditsch first started his career on one of the whaleboats, and from there he realized the market opportunity as a paint supplier, and later on, producer to the marine industry. In addition, it may be said that Jotun went multinational because they wanted to follow its customers abroad. In 1973, Knickerboxer came up with his theory that he called "Strategic actions". He said that companies were forced to go abroad to follow its customers or the industry's leader. Jotun had international customers, and has throughout the years followed and supplied its customers (Norwegian and international shipping companies) abroad. Jotun's products are sailing on all oceans, and its products and service are available in the world's main ports. Thanks to the marine paints, Jotun has established an international network, which has helped them in promoting its other products.

Dunning divided the locational advantage into three groups:

> **Access to and relative cost of production factors that only can be exploited by a firm in a certain area.**

This might be natural resources as well as human made resources. Quality and productivity related to labor, materials, energy and input prices vary a lot between different countries. Language and culture might be vital, and it is important to a firm to consider differences in language, culture, business and customs, before establishing abroad. It is often easier for a firm to invest in a foreign country that in many ways is similar to the home country, as an example in 1998, more than 95 % of all Norwegian foreign investment went to OECD-countries. However, when Jotun has established new factories abroad, it has always been in less developed countries with great growth potential such as the Middle East and Southeast Asia.

It is of course easier to orient oneself in a country similar to one's own, but then again there is a risk that firms don't consider the differences at all. Trading partners in similar countries often take it for granted that the communication and understanding will work out perfectly, but this is often not the case. An illustrative example here is intra-Scandinavian communication, where people can almost perfectly understand each other, but sometimes the very similar languages contain some apparently equal words and sayings that have totally different meanings in the different countries.

On the other hand, trading partners from totally different countries or cultures will expect some differences and potential misunderstandings. It therefore falls natural to everyone every now and then to get things explained one more time in order to avoid the potential misunderstandings. Jotun as a Norwegian firm in Thailand has always known that the cultural differences are present, and Jotun has managed to send people who are good at communicating and to take care of relationship abroad. Jotun has been in Thailand for a long time, and it is now expected from Jotun to know how to handle different situations and what should be respected. Jotun has also learnt how to stay on the right side of Thai values, and has, as an example, earned a reputation for respecting the King, which is very important for the king-loving and respectable Thai people. When Jotun opened the new factory in December 1999, Prime Minister Chuan Leekpai said that "Jotun has been actively involved in the introduction of new production techniques and advanced technology in Thailand", and that "this has helped Thailand to move up the value-added curve and to manufacture higher quality products". The Minister of Industry, Suwat Liptapanlop, added "Jotun has played a major role in Thailand's economy", and that "Jotun has been a part of the ever-changing Bangkok skyline and urban Thailand".

Taxes and trade barriers

These variables are all connected to economic politics, are created by the governments and might be changed or relaxed. Many foreign companies consider these variables, which include are government intervention, tax rates, incentives, investment climate, political stability and control on imports, before they make the final investment decision. Many of the companies that are considering Southeast Asia as a location for expansion have three main options : Singapore, Malaysia, and Thailand. All three countries have come up with innovative programs and incentives to attract foreign investment, and have in different ways affected the MNEs operations. Singapore's Economic Development Board (EDB), Thailand's Board of Investment (BoI), and Malaysia's Ministry of Industry Development (MID) play similar roles in wooing investors. The programs are related not only to market knowledge, legislation and rules, but also to tax specific incentives, as tax holiday or tax deduction. EDB, BoI, and MID ensure access to data and market information and they organize site surveys to help foreign firms (potential investors) identify potential locations.

Many countries try to attract foreign investment by creating certain tax and tariffs policies. The main reason for governments to welcome FDI are between other things the resources (technical, managerial) and spillovers it brings to the host country. A major goal for many foreign governments is that the influence and presence of foreign firms can contribute to the upgrading of existing resources and facilities. With investments, and particularly industrial investments, the mobility of the firm differs before and after the investment is carried out. Before the investment is undertaken, the firm is sensitive to where to locate, and they will consider differences in national tax policy, but it is important to take into consideration whether the tax policy will be sustained or if the policy is just temporary. Given that the policy is reliable and stable there is a good chance that the low tax country will attract FDI.

The reactions from different interest groups and theorists have been two-fold. The arguments from the side that are less in favor of importing resources, are that multinational firms often have a strong bargaining power, and there is a fear for MNE to use this power to capture a high share of the value added or created by the foreign affiliate. On the positive side, emphasis is put on the fact that foreign firms might contribute to a country's development by providing the country with intermediate products that would have been to costly to produce in the host country, and to give access to new technology and ways of production, which can help other local firms and industries to develop. The debate raised on this field has grown very complex, and it is easy to spend a thesis only on the arguments against and for foreign investment. The debate has become increasingly important as production and markets have become internationalized, and that economic activity has become more globally It is impossible to measure the impact of globalization in isolation to the other events and major changes that have changed the structure of the modern world economy. It is however not my intention to give the reader a discussion on this theme, but if the reader is interested in further reading on the controversies, I would recommend further readings.[36]

Tariffs may play an important role, but the effect of a tariff-based policy might be two-fold. High import tariffs make it expensive to a foreign firm to supply a market with export, and therefore counts toward an establishing. An already established firm can enjoy protection

[36] Articles that are positive to MNEs: Hennart, J., "The transaction cost theory of the multinational enterprise", 1991, Dunning many articles, Vernon, R., "International investment and international trade in the product cycle", 1966, Buckley and Casson "The future of the multinational enterprise", 1976, Rugman and D'Cruz "Multinationals as flagship firms", 2000, Blomstrom and Kokko, "Multinational corporations and spillovers", 2000, and "How foreign investments affects host countries", 1997

from other firms that try to supply the market through export. On the other hand, being established in a high tariff country can lead to high production costs if the raw material and inputs need to be imported at a high price. In addition, a high tariff-country can easily earn a reputation for not being investment friendly.

When Jotun was established in Thailand in 1968, it got the last license for foreigners to produce paints in the Kingdom. The Thai government prevented for some time other foreign firms from entering the Thai paints market. Being located in the market protected Jotun not only from new foreign companies that wanted to enter the country, but also from the tariffs on imported goods, which used to be very high in Thailand. Jotun's strategy has, however, been based more on "feeling" than numbers, and important decisions like where to locate have never been taken on a pure tax-related basis[37], Jotun has always chosen to establish themselves in promising markets with above-average growth potential.

The Board of Investment has developed a scheme where existing activities will be promoted if they relocate from central to regional areas[38]. The main purpose is to encourage industrial development in regional areas and to move some of the industry out of Bangkok. Thailand is divided into three zones according to the level of industrial development and distance from the capital. In order to obtain one or more of the relocation benefits, the firm has to relocate from its present zone to a less developed industrial zone (from zone 1 to zone 2 or 3, from zone 2 to zone 3). Dependent on the location the firms benefit from tariff reduction (50 to 100 %) on import of production machinery for the new factory, exemption or reduction of import duty on raw or essential materials for a period of up to eight years and tax holidays for a period from three to seven years. There exist some extra benefits for relocation to zone 3, for example that after the seven-year tax exemption period, the firm pays 50% less corporate income tax for five more years.

Articles with a critical view on MNEs: Hymer, S., "The international operations of national firms", 1976, Caves, R., "Multinational firms and economic analysis", 1996, and "Multinationals in developing countries", Lall, S., "Transnational corporations and economic development", 1993

37 Odd Gleditsch jr. in interview

38 See appendix III for exact numbers and applicable benefits

Jotun's new factory is located in tax zone 2, and Jotun Thailand benefits from rules of relocation matter and enjoys seven years tax holiday. Jotun could have obtained greater benefits if it had located the new factory in zone 3, but Jotun considered the benefits to be less than the potential negative sides like long distance from the market and a potential loss of experienced workers. Besides this, Jotun's strategy has, as mentioned before, always been to establish themselves where it finds it best, not in order to obtain the greatest incentives and tax benefits.

Transportation cost and access to market

In many industries, like production of food or construction material, where the quantity and volume are high and the ratio "sales price / transportation cost" is relatively low, distances and transportation cost are of importance. In industries, where the main product is either knowledge or high technology (small units at high price) the transportation cost is of minor interest. The goods often have to be produced by people with specific skills on specially designed production equipment. Firms that produce goods that have high transportation costs will typically try to locate close to their market. These goods are unlikely to be very capital intensive in terms of advanced technology and well-educated labor.

Most Asian markets are big compared to Scandinavian or European markets. Some of the world's most populated countries and cities are in Asia, and the consumer markets in the newly industrialized countries (NICs) have an enormous growth potential. FDI is made not only for production matters, but also to show commitment in promising regions. The MNEs know that a firm established in a market is able to adjust its products and marketing towards local demands and conditions, and this is of course of major importance if they want to become serious players in Southeast Asia.

When Jotun first established themselves in Thailand, the country was less developed. But, there was an established shipping industry in the kingdom and Gleditsch and Lundh saw the business opportunity both for paints and protective coatings. At the same time, the competition in this kingdom was not as hard as in established European markets. The international customers require that they get the same product and standard worldwide for their ships. The reason for Jotun to establish in Singapore was that the shipping industry was present, and the international customers demanded the products and services that they also got in Europe. To ensure that the concept of Jotun was brought through, Jotun decided to invest in a plant and to open an affiliate in Singapore.

The transportation costs from Norway to Thailand, the lower labor cost[39] in Asia and the possibility for utilization of local raw materials made the decision of establishing in Thailand and setting up a manufacturing facility. As has been usual for Jotun, no fancy investment analysis was made prior to the investment decision. When Jotun set up the factory in Thailand with limited funds, it was more than anything the entrepreneurial approach to a business opportunity. Jotun realized early that it was important to concentrate on its core areas, on what it knew best. For Jotun, this means that the knowledge related to production, research and marketing was brought from Sandefjord could be used and exploited in Thailand as well as in other countries. The reputation Jotun has earned in the market for protective and marine paints makes them competitive in most countries.

With AFTA it is possible to produce different types of paint in great volumes and export intra-Asian. There are, however, two main reasons for not doing so: the decorative paints are adapted to local factors and the enormous volumes creates a need for huge warehousing capacities. This is one of the reasons for Jotun having chosen to build local production facilities in Singapore, Malaysia and Thailand. The leading time might be a crucial element when Jotun bids for contracts in construction projects. If the decision were to be taken today, Jotun would probably not have established factories in Thailand, Singapore and Malaysia. Even if the production costs are higher in Singapore than the two other countries, there are still some benefits from producing in Singapore. The political stability in Singapore is by far better than the southern parts of it neighbor country, Malaysia. In Malaysia, as an example, there exist several restrictions on who you may employ and what percentage of the employees that have to be origin Malays (Bumiputra), and if these requirements are not full-filled, the company is not allowed to deliver any products or bid for projects in government-owned companies. One problem is that the restrictions and regulations are changed every now and then and it is hard to predict what is to come. This problem is present also in other

[39] See appendix IV for Cost of Doing business in Thailand and Tax rates.

Southeast Asian countries, and Singapore is considered the less risky one, with a ”clean” system almost like no other country.

A more modern definition of locational advantages

Another definition of the locational advantages is “the ability of locations (regions, countries or sub-regions) to offer immobile assets necessary for the mobile assets (….) to be used most efficiently – both to add value to those assets; and to create (through innovation or tapping into indigenous capabilities) new assets.”[40] Dunning means that there are several new factors that are likely to get increased significance in the future. One of these are the availability and quality of a skilled labor force. Another factor is the creation of regional markets - we have already seen the expansion of the European Community (EC), and the growing cooperation among the ASEAN countries. This factor will probably continue to favor foreign production in the future. Further, market-facilitating policies by governments and partnerships for growth will probably get more importance. Further, countries will need to sustain and upgrade the competitiveness of their own firms and indigenous resources, and therefore need to attract knowledge-related assets. In addition, the globalization has lead to concentration of some kinds of value-added activities, and these clusters have become an important locational benefit to firms.

Internalization gains

The internalization gains are related to how organizing activities within a firm rather than at a market place might be more effective. Dunning meant that a firm needed to effectively internalize its advantages if they should be better of by establishing an affiliate abroad. A firm must believe that the benefits from internalization in the market, less the extra transaction costs involved, are greater than the benefits the firm would have achieved through some other way of entry. Dunning says that if other firms can easily get access to and internalize the ownership advantages of a firm, the firm should consider selling or licensing these advantages. I have in the following illustrated which choices of commitment

[40] Dunning, John H., “The eclectic (OLI) paradigm of international production: Past, present and future”, 2000 and

a firm need to consider if it wants to sell its products abroad, and what entry mode that should be chosen if the firm decides not to supply the foreign market through export. Several of the contents that are related to internalization gains have already been discussed in the ” Market failure” on page 35, and in the ”Ownership advantage” and ”Location advantage” parts, and will therefore only be briefly mentioned here.

Dunning tried to explain what kind of international production would be chosen by a multinational enterprise by looking at all three components and the interplay between them. Dunning meant that the ability to internalize a firm’s ownership advantages is the competitive advantage of the firm. It is the possible gains from internalization that are the reason for multinational enterprises to exist. This in combination with both the ownership advantages and the localization advantages makes the firm choose establishment of an affiliate instead of (continued) export, licensing or joint venture.

Theories on internalization

Some of the theories on internalization are Vernon’s Product lifecycle theory, the Principal-agent-theory and Buckley & Casson’s internalization theory.

The product lifecycle theory

Ray Vernon developed the product lifecycle theory (PLC) in the mid 1960s. Vernon was interested in explaining the process of deepening internationalization of US firms. He started off with trade theory, but the assumptions of perfect competition and product homogeneity did not give a good picture of the real world, and Vernon wanted to find a better approach[41]. Ray Vernon used a micro-marketing concept, the product cycle. The theory treated trade and investment as part of the process of exploiting foreign markets, and the relationship was explained as dynamic. Vernon tried to answer both the “why” and “where” questions of production, and added “when”.

Vernon found that US firms in the 1960s had a comparative advantage in innovating particular products, and other countries had comparative advantage in adding value to these innovations. He meant that firms in developed countries were rather much alike, in terms of access to technology and capacity to comprehend scientific principles[42]. This means that much of the development will take place in developed countries with large markets, and from there on be produced in other developed countries. In 1974, Vernon said that foreign production might bee seen as a strategy made by the multinational firm to protect –or even to gain- an ownership advantage vis-à-vis their competitors. Vernon meant that when demand grows, production becomes more or less standardized, and with a stable and solid home market, the demand from other countries will grow as well. The product will be exported at the initial stage, but as the product becomes standardized, one might assume that the production becomes more labor intensive. This might result in production being moved to less developed countries.

There are several factors that make it reasonable to develop a strategy based on foreign production. These factors are the menace of local imitations, lower production costs in some countries, transportation costs and trade barriers, non-tradable firm specific assets, competition strategies and so on (Schjelderup, 1999). We can apply this theory on Jotun, but with some exceptions. Jotun has always first started to export the existing paints either from Norway, or from another affiliate close to the "new" country. Only after some time, when Jotun has earned a foothold, it has either established a joint venture, or established in the foreign country. The production of paints has do some degree become more standardized; most of the production are done by machines, but it is a need for experienced people. The management, R&D and marketing effort is of course harder, and probably not desirable to standardize.

The Principal-agent-theory

The Principal-agent-theory says that it is hard if not impossible to write a complete contract, and the unwritten words can lead the other firm or an employee to go in certain directions. If the principal wants to monitor the agent –the other firm or the employee - this can be done, but at a high cost. It is always of interest to make a contract that leads the principal and the agent towards the same goals. The problem with incomplete contracts exists in all firms, and includes the commitment and behavior of management, employees, customers

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[41] John Dunning, Globalization and the Theory of MNE activity.
[42] Schjelderup, 1999

and vendor, and what kind of incentive systems and regulations that a firm has to live after to in a best possible way live with this.

When going abroad, this problem arises for example when a firm decides to license its production or enter into a joint venture. Two common disadvantages with joint venture have been that the mother firm does not have the control needed over the “affiliate” and that there exists opportunism, that is that the local firms or agents often see the potential to gain a little more from the cooperation, at the foreign firm’s expense. The local firm knows the market better than the foreign firm and can therefore adjust to the regulations and the local business culture. The local firm often has something that it wants to optimize, and this does not always fit in with the multinational enterprise’s goals and strategy. This might lead to moral hazard, as the licensing firm tries to gain on behalf of the multinational firm.

Jotun has some joint ventures or partnerships in the Middle East. The local firms have the market knowledge needed in the region, and there exist certain regulations that have made this choice the best option for Jotun. The local firms run the production, but all management, shared services and R&D are led from Jotun Norway. The Middle East Jotun firm then pays a royalty to Jotun Norway. Jotun has reduced this problem, as it run both management and R&D.

Buckley & Casson’s internalization theory

In 1976 Buckley & Casson gave birth to the internalization theory, which implied that there existed certain costs of using the market. These costs existed because of market failure, and were called transaction costs. These market failures lead to the establishing of firms, because a firm can more effectively than the market transfer information and services. The internalization gains depend on to what extent a firm finds it profitable to by-pass markets. This is also the reason for MNEs; a multinational firm gets value from affiliates in more than one country, and there has to be a reason why these activities should be coordinated or to some extent regulated from one firm instead of the market.

All business and information exchange include some transaction costs, and from this we can easily make the conclusion that MNEs must consist some ownership advantages. The conclusion is based on the assumptions that the transaction costs will be magnified when a firm decides to go abroad, and that the multinational enterprise must compete with local firms that experience smaller transaction costs. The ownership advantages can compensate for the extra costs the MNE has in addition to those indigenous producers face; costs of setting up and operating a foreign affiliate. When a firm is establishing abroad, there is a risk that they may lose some of their ownership advantages, it therefore has to be able to effectively internalize the ownership advantages, if not the firm will be better of by selling or licensing the advantages to other firms.

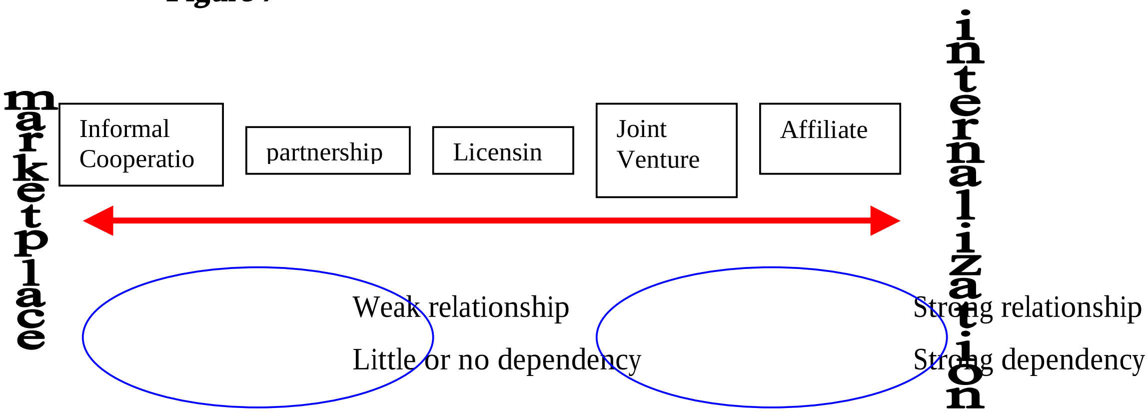
The reasons and motives for internalization can also be that the MNE will ensure the quality of end products, or safeguard the supplies of important inputs to protect the core assets of the firm. Other reason can be that the firm wants to spread some overhead costs (administration, marketing, R&D). High transactional costs are likely to lead to a higher degree of international production, whereas high costs of operating a foreign affiliate is likely to lead to contractual agreements with local foreign firms.

Some of the internalization gains an MNE experiences are from market failure and from the fact that the firm is multinational. The firm can avoid or exploit government intervention, choose the best possible system for pricing of intra-firm-trade to reduce taxes, and adjust prices to local markets. Further, risk is reduced if the firm is exposed to different markets. A firm that manages to internalize its core assets and (newly gained) knowledge on R&D, production and management - even across borders - will have a possibility to keep the knowledge inside the firm.

Entry mode

When a firm decides how and to which degree they shall internalize, they can choose anything between export and establishment of affiliates. In between lie informal cooperation, partnership, licensing and joint venture. The various kinds of entry modes represent various levels of economic commitment, risk and control. The possibilities for Jotun have been either to continue to export, licensing, joint venture or internalization.

Figure 7



Source: Haugland, 1996

This figure illustrates that the further firms are to the left, the less dependent they will be on each other. On the very left, we have the market-solution. The closer to the right, the more dependent will the firms be on each other. On the very right, we have full internalization. Three factors that point toward establishing an affiliate and internalization of the tasks are; first, the possibility for increasing economies of scope –which includes products that require similar inputs, distribution or marketing needs, second, the increasing importance of tacit knowledge, teamwork and face-to-face communication and third, the closer integration of innovation and production processes along value chains.

Export

Export is often the solution for a firm with too little capital to be able to establish themselves in a new country, but it is also the first step many firms take when they want to take a look at new possible markets. Jotun had for several years served the Thai market through export when it first established in Thailand in 1968. However, there was, and still is, high transportation costs from Norway to Asia, and the production costs are significantly higher in Norway than in Thailand. In addition, Thailand used to have high tariffs on imported goods, and all these factors counted towards establishing an affiliate close to the market.

Licensing

The second option, licensing, means that a firm with a certain product or technology lets another firm use the knowledge and possibly also the brand name and receives a royalty for the use. The major advantage from licensing is that the firm do not have to invest any capital, and the overall risk is reduced. The potential difficulties with cultural problems can also be avoided, and the local production can typically start sooner. . On the downturn-side, it is difficult for a firm to monitor the effort of the licensee, and the problems with asymmetric information can make licensing risky and costly. Further, profit from licensing is also normally lower than with own production of the product.

Jotun could have licensed its production to a local firm in Thailand. But Jotun wanted to keep the Jotun concept with education, R&D, high quality and service at a high worldwide level. A licensing agreement would normally not have given Jotun the control it would need to fulfill this strategy, because a firm normally encounters difficulties if they try to tell another firm exactly what to do. As a supplier to the shipping industry, it is of major importance to be able to deliver the products at the same level of quality and service worldwide. Jotun is not only selling paint, but also the education and service that are needed to keep the paint long lasting and at a high quality level.

Joint venture (JV)

Joint venture is when two or more firms establish a new firm together and run the new firm together. This is as close as one can get to internalization without actually being there. The advantage of Joint Ventures is the access to new markets and avoidance of trade barriers. The product can get into the new market faster. Further, the firms involved in the JV can share the R&D costs and knowledge, and they possibly have different market segments that they can easily approach with the new product.

The disadvantages of JV are the problems with intern pricing, and that there is a lack of incentives for the involved parts to make any extra effort, as the potential gain has to be divided between all parts involved. Joint ventures have typically been a popular variant in Thailand, because the government put a requirement of Thai majority on foreign firms. The advantage of having a local partner that knows and understand the business environment and the cultural codes has also led many foreign firms to choose Joint Venture as entry mode.

Establishing an affiliate

When a firm decides to establish an affiliate, it can mainly choose between buying an existing plant or building a new plant. The advantage of buying an existing firm is that the firm gains access to local knowledge if it keeps the local staff. It takes a lot of knowledge and understanding of foreign rules to set up a new factory, and it is therefore of importance that the management and staff know the legislations and the local market. In addition, when acquiring an already existing firm, production can normally start earlier, and in addition, there is one local competitor less. It is, however, often of importance to use the latest technology, and the existing organizational culture might not fit into the overall organizational culture in the MNE, and this can favor the building of a new factory.

Jotun has in Thailand built new factories. First, when Jotun established in the late 1960s, Thailand was less developed, and there existed no local firms that Jotun considered acquiring. Second, when Jotun relocated its factory in 1998, it wanted to build a new, high-quality factory that can hardly be found in any part of the world. Some of the old equipment and machines for production of powder coatings was easily transferred to the new factory, but most of the wet paint equipment replaced with new technology and machines.

Part V
Conclusion

I have in this last part taken a look at and explained all three requirements that Dunning says need to be present if a firm wants to establish itself abroad. It is however, difficult, to foresee and explain the international profile of a multinational enterprise. I wanted to see whether the Dunning OLI-paradigm could explain Jotun's investment in Thailand 32 years ago. I have tried to illustrate each requirement with examples from Jotun, and have in this connection showed that that Dunning's eclectic paradigm can be used for explaining and analyzing many of the organizational issues that Jotun has faced in Thailand. What I realized after working both with the theory as well as the history and advantages of Jotun, was that has fulfilled the three prerequisites for foreign direct investment.

Jotun actually followed a highly recommended line in the business world; first export to a new market, in order to win market acceptance and market shares, and to learn about the country and the business culture. Jotun has first established a network and relationships and thereafter established themselves in the country, either by buying an existing firm or, like in Thailand, building a new factory. Jotun has managed to keep a long-term strategy and a continued focus on quality and service, meaning that it has been able to differentiate its products at the same time as competition in the world paint market has become tougher. This is probably the right way to go, and it is hard to see a better choice for Jotun, with its increasingly more demanding customers.

Summary

I have in this thesis given an introduction to Jotun and Thailand. I decided to tell more than anticipated from Jotun's history, as both the history and business culture of this family-owned Norwegian paint manufacturer to a great degree has inflected on its worldwide investments and strategies taken. I found Jotun an interesting company, and it feels good today to see a family-owned company that to this great degree has succeeded with its global strategy, and has won both market share and respect in a country that in some many ways differ from that of Norway, Jotun's home country. Further, Jotun has since long before human capital became a common word, believed in the ability of its employees and managers and given several persons the opportunity to develop themselves and the firm through foreign experiences and exposing. Jotun has had the ability to listen to customers and employees, and in the capacity of family-owned has had the ability to choose and follow new directions whenever it has been necessary.

Jotun has been established in the Kingdom of Thailand from the late 1960s, and opened last year a new factory, the biggest single-investment for the company worldwide. Jotun has taken part in the economic growth and has seen and lived with the changing environment in the kingdom. Thailand proved to be one of the fastest growing economies from 1985 to the economic crisis in 1997. After a couple of years with slower economic growth from these years to come back, but I believe the region has a strong growth potential, as the consumer markets are growing rapidly.

During more than 30 years of presence, Jotun has established a solid and extensive network, and enjoys today a solid position in Thailand. The mixture of a family-owned company with selected managers that worked on long-term basis, a jovial staff, and the understanding of local adjustments have turned out to be good for Jotun, and I am happy to have learnt some of its history and experience.

The changes in the global economy has already led to firms searching globally for assets. A large part of today's FDI is made in form of acquisitions and mergers, and profits are being reinvested in the host country. In addition, more attention is now being paid to gains that might arise from being part of a complex or cluster of firms. As mentioned in this thesis, about 75% percent of all shipbuilding today is concentrated to Asia, and in my opinion, that makes a cluster, with a continued demand for marine paints and protective coatings

Dunning[43] has suggested that the future path of the eclectic paradigm might be that economists will build more elegant models, and work with more interdisciplinary theories. He says that the motives and determinants of the modern MNEs have increasingly been widened to embrace social considerations, and that it therefore may be needed to further reformulate the paradigm in close future. Until now, no particular focus has been placed on the dynamics of OLI, but as Dunning sees it, more attention should be put on the cross border innovating actions of corporations.

[43] Dunning, John H., “The eclectic (OLI) paradigm of international production: Past, present and future”, 2000

Appendix

Part I: Thailand

Appendix I

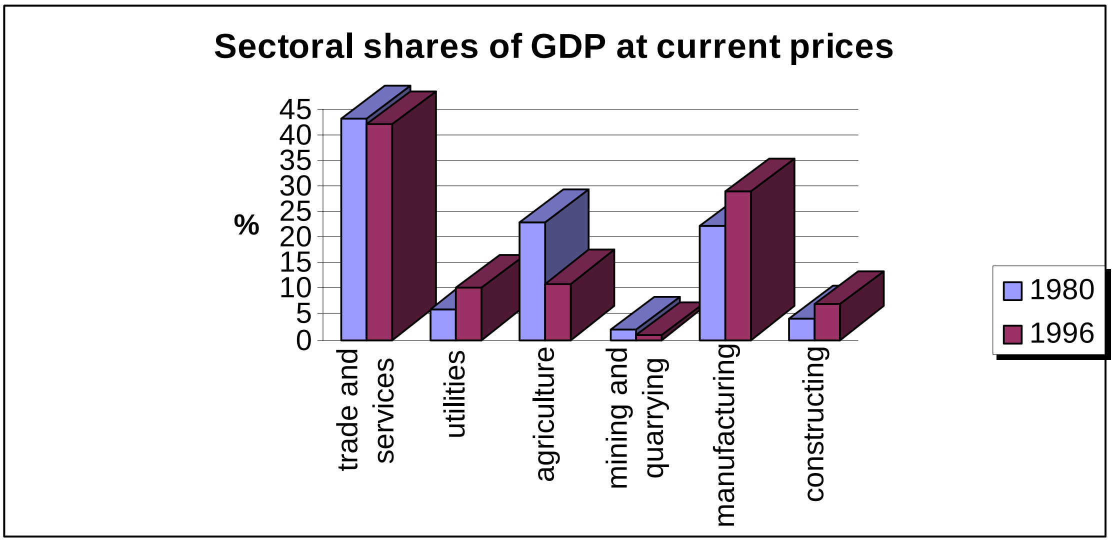
Thailand's Key Economic Indicators

	1996	1997	1998	1999
Population (million)	60.1	60.8	61.5	62.1
Unemployment Rate (%)	1.5	1.9	4.0	4.2
Nominal GDP	181,417	150,445	112,767	119,070
Real GDP Growth (%)	5.9	-1.8	-10.4	4.0
Consumer Price Inflation (%)	5.9	5.6	8.1	0.3
Money Supply (M2) (%)	12.7	16.3	9.5	2.1
Deposit Rate (%)	9.4	9.3	8.9	4.9
Exchange Rate (Baht/US dollar)	25.4	31.4	41.6	37.8
Total Exports	54,287	56,997	52,932	55,277
Total Imports	70,728	59,697	40,723	46,210
Trade Balance	-16,441	-2,710	12,209	9,067
Current Account Balance	-14,654	-1,283	14,359	10,949
Foreign Exchange Reserves	38,700	27,000	29,500	34,800

Figures in millions of U.S. Dollars unless otherwise indicated

Appendix II

Sectoral shares of GDP at current prices, 1980 and 1996.



Source: National Economic and Social Development Board and Bank of Thailand

Appendix III

BoI Incentives

The BOI offers two kinds of benefits: Tax-based incentives, such as tax holidays or tariff exemptions, and non-tax privileges, such as guarantees, protections, permissions, and services.

The non-tax privileges are available to all BOI-promoted projects, regardless of location, industry, or condition.

Tax-based incentives, on the other hand, depend on several factors. All projects will receive certain benefits; however, additional incentives are available for locating in Special Investment Promotion Zones, producing for export, or engaging in industries identified as Priority Activities.

Industrial Estates Focus

Thailand has created a network of Industrial Estates, which operate almost as free trade zones, in order to promote exports, foreign investment and economic decentralization from Bangkok. The Industrial Estate Authority of Thailand (IEAT), which is attached to the Ministry of Industry and whose objective is to ensure orderly planned industrialization, administrates the numerous estates in the kingdom.

There are mainly two categories of estates with the first being General Industrial Zone (GIZ), which is the area reserved for the location of industries manufacturing for domestic and/or export consumption. The other is Export Processing Zone (EPZ), which is the area reserved for location of industries manufacturing for export only.

Firms located in an EPZ or GIZ receive benefits that include:

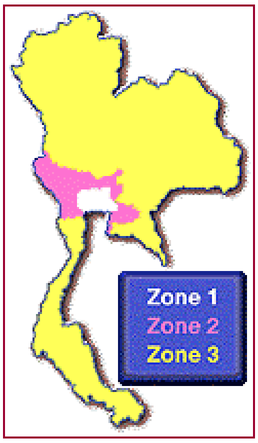
- Corporate tax exemptions
- Reduction or exemption of import duties on machinery or materials used in factory manufacturing.
- Permission to own land
- Permission to use foreign consultants, skilled technicians and experts
- EPZ's will usually contain a customs clearing house for fast clearance of goods

Privileges by location

Investment privileges have long been used to support government goals in decentralizing Thailand's industrial base.

In line with the government policy of decentralization from the Bangkok Metropolitan Area, the BOI announced new "Policies and Criteria for Investment Promotion" in **April 1993,**creating three **Investment Promotion Zones** throughout Thailand.

Promoted projects locating in these Zones may receive additional incentives, including further tax and duty reductions, as well as allowances for infrastructure investments



Zone 1: includes Bangkok, Samut Prakan, Samut Sakhon, Nakhon Pathom, Nonta Buri and Pathum Thani (Bangkok and 5 provinces)

Zone 2: includes Samut Songkhram, Ratchaburi, Kanchanaburi, Suphanburi, Angthong, Ayutthaya, Saraburi, Nakhon Nayok, Chachoengsao, and Chonburi (10 provinces)

Zone 3: encompasses the remaining 61 provinces plus Laem Chabang Industrial Estates The extent of the benefits granted to a company operating in an EPZ or GIZ depends upon the area of the country it is located in. Thailand's Board of Investment (BOI) created three Investment Promotion Zones in the country with projects in each zone receiving additional incentives, tax and duty reductions as well as allowances for infrastructure investments

For projects in Zone 1:

- No tax exemption or reduction on machinery, except projects which export not less than 80% of total sales or locate their factories in industrial estates or promoted industrial zones. Such projects will receive a 50% import duty reduction on machinery which is not included in the tariff reduction notification of the Ministry of Finance (Notification C 13/2533) and which is subject to import duty greater than or equal to 10%.
- No corporate income tax exemption, except for projects which export not less than 80% of total sales and locate their factories in industrial estates or promoted industrial zones, in which case a three-year exemption will be granted.
- Exemption from import duties on raw or essential materials used in export products for a period of one year.

For projects in Zone 2:

- 50% import duty reduction on machinery, which is not included in the tariff reduction notification of the Ministry of Finance (Notification No. C 13/2533) and which is subject to import duty greater than or equal to 10%.
- Corporate income tax exemption is given for 3 years, extendable up to 7 years, for projects, which locate their factories in industrial estates or promoted industrial Zones.
- Exemption from import duties paid on raw or essential materials used in export products for a period of one year.

For projects in Zone 3:

- Exemption from import duties paid on machinery.
- Corporate income tax exemption for 8 years.
- Exemption from import duties on raw or essential materials used in export products for a period of 5 years.
- 75% reduction of import duty on raw and essential materials used in production for domestic sales for 5 years, renewable on an annual basis, provided that raw or essential materials comparable in quality are not being produced or do not originate within the Kingdom in sufficient quantity to be acquired for use in such activity.

Special privileges are granted as follows:

- A reduction in corporate income taxes paid by 50%, available for 5 years after the exemption period.
- Double deduction from the taxable income of water, electricity, and transport costs for 10 years from the date of first sales.
- Deduction from net profit of 25% of the costs of installation or construction of the project's infrastructure facilities is given.

Relocation

Benefits for Factory Relocation - The Board of Investment developed a scheme where existing activities will be promoted if they relocate from central to regional areas. The primary purpose is to encourage industrial development in regional areas. In order to evaluate the regional promotion, Thailand has been divided into 3 zones according to the level of industrial development. These criteria are applied on a policy basis without strict legal definition. In order to obtain a benefit from the government, a company needs to meet the following criteria:

1. The operation must relocate from Zone 1 to Zone 2 or from Zone 1 or 2 to Zone 3.
2. The type of activity and size of investment must be in accordance with those specified by the Board of Investment Promotion List.
3. For projects facing environmental problems and required by Thailand's Ministry of Industry to relocate: the factory must relocate to an industrial estate or promoted industrial zone; the former factory must be closed down and all machinery moved to the new location; the new factory must be ready for operation within two years of receiving the promotion certificate.
4. For other types of operation: the existing operation must employ no fewer than 50 people; main production machinery must be moved to the new location and the new factory must be ready for operation within two years of receiving the promotion certificate.

A company that fulfils the conditions will obtain income tax exemption for a 3 to 8 year period (3 years for relocation to zone 2, 7 years for relocation to an industrial estate or a "promoted industrial zone" and 8 years for relocation to zone 3). Relocation to zone 3 involves additional benefits: 50% reduction of corporate income tax for 5 years after the exemption period, double deduction from taxable income of water, electricity and transport costs for 10 years and deduction from net profit of 25% of the costs of installation or construction of the project's infrastructure facilities.

Appendix IV

Cost of doing business in Thailand and Tax rates:

Selected Salaries

Position	Monthly	
	Baht	US $
Executive Secretary (Good English skills)	31,000	819
Entry Level Office Staff (Computer literate in English)	16,000	423
Research/Marketing Staff	29,000	766
Personal Manager, HRD Director	65,000	1,718
Office Manager/GM	40,000	1,057
Administrative Staff	15,000	396
Driver (Including overtime)	11,000	291
Housekeeper	6,000	159
Messenger	7,000	185

Note: Bonus conditions vary from business to business, although one month's extra salary a year is closest to the average.

Source: These figures are based on the results of an informal survey conducted in October 1999 of selected businesses in Bangkok.

- **Note: All US$ conversions are calculated at a rate of US$1 = 37.84 baht (Average full year rate for 1999).**
- **Source: Bank of Thailand.**

Tax Rates and Double Taxation Agreements (1999)

Corporate Income Tax

Corporate Income Tax	Rate
A. Tax on net corporate profits	30%
B. Withholding tax on remittances of profits	10%
C. Withholding tax on remittances of dividends	10%
D. Tax on gross income of foundations and associations	2%

Structure of Import Tariffs

Structure of Import Tariffs	Tax Rates
Basic raw materials, necessary raw materials, and materials subjected to special treatment	0-1%
Primary goods and machinery	5%
Intermediate goods	10%
Final goods	20%
Commodities requiring specially high protection	>30%

Note : Source: Revenue Department, November 1999

Double Taxation Agreements

Thailand has Double Taxation Agreements exist with the following countries: Austria, Australia, Bangladesh, Belgium, Canada, China, Czech Republic, Denmark, Finland, France, Germany, Hungary, Indonesia, Ireland, Israel, Italy, India, Japan, Laos, Luxembourg, Malaysia, Mauritius, Nepal, the Netherlands, Norway, Pakistan, the Philippines, Poland, Romania, Singapore, South Africa, South Korea, Spain, Sri Lanka, Sweden, Switzerland, United Kingdom, United States and Vietnam.

Labor Costs (1999)

Entry Level Salaries for Select Jobs, per month		
Position	baht	US$
Manufacturing Sector		
Engineer	16,307	431
Technician	10,379	274
Designer	10,000	264
Electrical engineer	20,000	529
Industrial engineer	17,000	449
Junior secretary	10,487	277
Private Sector		
Computer staff	11,116	294
Economist	40,000	1,059
Accountant	10,500	277
Systems analyst	21,500	568
Auditor	8,000	211
Service Sector		
Junior secretary	7,000	185
Translator	15,600	412
Receptionist	5,217	138
Sales clerk	7,172	190
Salesman	8,988	238
Retail manager	18,800	497

Minimum Daily Wage Rates	**Baht**	**US$**
Bangkok, Samut Prakan, Nonthaburi, Pathum Thani, Phuket,Nakon Pathom, and Samut Sakhon	162	4.28
Phangnga, Ranong, Chon Buri, Nakhon Ratchasima, Saraburi and Chiang Mai	140	3.70
Other Provinces	130	3.44

Overtime Regulations	
Overtime performed on regular working days	- time and a half
Regular work on public holidays	- double time
Overtime performed on public holidays	- triple time

Part II: Jotun

Appendix V

Key Figures, Jotun Group 1999

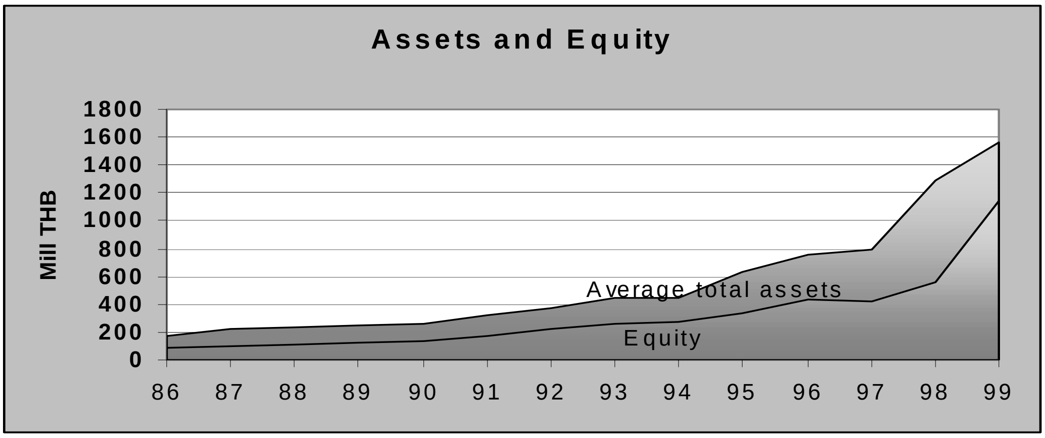
Key figures

(In million of NOK)	**1999**	1998	1997	1996	1995
SALES					
Sales external	4 871	4 290	5 166	5 236	4 816
Export ratio (%)	66	69	74	72	71
Profit					
Operating profit	251	259	462	372	280
Profit on ordinary activities	241	197	367	268	199
Profit before tax	241	197	1 112	268	226
Net cash inflow from operating activities	100	345	484	250	24
PROFITABILITY					
Return on assets (%)	7,5	8,4	14,1	11,3	9,7
Return on capital employed (%)	10,1	11,0	19,2	15,9	14,2
Operating margin (%)	5,1	6,0	8,9	7,1	5,8
Return on equity (%)	7,4	7,0	13,2	14,1	11,1
YEAR-END FINANCIAL POSITION					
Total assets	4 234	3 825	3 535	3 564	3 387
Capital expenditure	366	445	240	220	214
Equity (incl minority interests)	2 251	2 285	2 127	1 249	1 088
Equity/assets ratio (%)	53,2	59,8	60,2	35,0	32,1
Group employees at year-end, including employees at joint ventures	3 623	3 321	3 331	3 562	3 337

(1 USD= approx. 8,5 NOK June 2000)

Appendix VI

Jotun Group Assets and Equity 1986-1999



Source: Jotun group report for 1999/2000

Part IV: Multinational enterprises

Appendix VII

The historical evolution of MNEs.

The early internationalization (until 1945)

The early internationalization started in the thirteenth century with the Italian bankers' establishment in England and the Hanseatic league, and lasted until the end of World War II,

was mainly based on *exploitation of primary resources* in developing countries, and existed mainly among colonial powers. In the first part of this period the MNEs were characterized by trading outposts and non-resident controlled investments across borders (e.g. the mining industry). The second part of this period started with the transportation and communications revolutions in the early 1800s, and a greater variety of companies made investments across borders, but still they maintained control from their home country.

The Golden Age on internationalization (1945 to 1973)

The second period, The Golden Age, is the name used for the period when a formidable expansion of MNEs took part. In this period, governments started to intervene with import substitution policies, and firms that wanted *access foreign markets* had to establish themselves in the foreign country. In the 1950s it was mainly American MNEs that invested abroad and spread technology globally. One reason for this was that almost fifty per cent of the worldwide manufacturing was within the United States, and when large developing countries adopted import-substitution policies, the transnational (American) corporations invested behind the barriers to be able to trade. In 1960 US accounted for 60 percent of the total Foreign Direct Investment stake of market economies, and accounted for more than eighty percent of all new investment directed at the manufacturing industry. During this period more countries became active players in the area of Foreign Direct Investment, and this lead to a drop in US' share of the total direct investment stock.

The new internationalization (from 1973 to 1990s)

Governments in most parts of the world liberalized the trade policy somehow and allowed privatization. MNEs have been increasingly welcomed as a means of establishing and strengthening an industrial base for economic development[44]. The increased openness in trade and the change in attitude by governments towards multinationals have possibly three major reasons:

First, the pressure from international organizations (WTO, IMF and the World Bank) to provide freer trade, second, the increased prosperity of countries that have been open to multinationals (Singapore), compared to in some cases almost stagnating economies of the import-substitution countries, has raised the question of whether the latter strategy was an appropriate one, and third, the end of the cold war made multinationals turn to Eastern Europe, and developing countries had to make themselves more attractive towards foreign investment.

MNEs seeking efficiency and the creation of global production networks characterize this period. A major change in this period was that developing countries that had been the most successful in attracting FDI in the 50s and the 60s, had earned some bargaining power. According to Evans[45], the actual states used this bargaining power to get more back from the MNEs:

More local investment in productivity-enhancing assets,

The MNEs had to increase the exports so that they could cover their rising demand for imported goods

The MNEs to become more involved in the domestic industrial establishments.

The Japanese had worked hard to recover; they had borrowed the foreign (American) technology and improved on it. The Japanese developed new theories on management, and knew that they had to produce quality products at low cost to be able to compete against the US companies. In the 1980s Japanese innovative firms had become a strong rival for the American MNEs.

The ongoing period

Today, we see more alliances in the world market. MNEs are seeking strategic asset for their Foreign Direct Investment[46], trying to organize the production globally. The global network has made it possible to supply

[44] World Investment Report 1999, ch.1

[45] From Peter Evans "Transnational Corporations and Third World States: From the Old Internationalization to the New", 1998

[46] Foreign direct investment is "Investment made to acquire a lasting interest in an economy other than that of the investor, the investors purpose being to have an effective voice in the management of the enterprise." (IMF)

sophisticated markets from remote locations. Governments cannot only use tax-deductions as incentives to attract MNEs, but also have to provide these companies with a more educated workforce, stable politics and modern infrastructure.

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