Multinationals and Performance: Policy Implications [*]

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Executive Summary

Governments in emerging economies are supporting the transformation of their firms into multinationals. This policy has generated a debate because, unlike related policies such as export promotion or the attraction of inward foreign direct investment which have direct influences on employment and investment in the home country, the support of outward foreign direct investment (OFDI) in some cases is seen as supporting investment and employment abroad. Nevertheless, it appears that outward foreign direct investment has positive spillovers in the home economy.

In this report we take a different approach from the traditional analysis of spillovers and instead analyze the relationship between multinationalization and performance to understand under which conditions firms need for government support to become multinationals. We propose that if managers find it profitable to expand their firms abroad, the government may not need to provide support as managers already have incentives in place and the spillovers would happen. Thus, government support for OFDI can be directed at helping firms become multinationals by reducing constraints on and facilitating the process of OFDI rather than at directly subsidizing the investments.

We analyze this relationship in a panel of publicly traded Thai firms in the period 1990-2012. We find that internationalization appears to have a positive impact on profitability and may follow a curvilinear relationship. We also find that there is no clear relationship between the location of international expansion and profitability, except for investments in offshore financial centers that appear to have positive relationship.

From these findings we recommend caution on public support for OFDI. Managers appear to have the incentive to engage in foreign investment and thus may not need government support to continue expanding their firms abroad. Government policy can be directed at lifting constraints to investments in the home country and in host countries that will reduce the cost of expanding, allowing managers to choose the destination countries they consider to be better for the success of their firms.

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