

## 2. Foreign Direct Investment in Egypt, India, South Africa and Vietnam: Comparative Empirical Results<sup>5</sup>

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### INTRODUCTION

In this chapter, we compare and contrast the characteristics, determinants and performance of foreign direct investments (FDI) in the four emerging markets of our study – Egypt, India, South Africa and Vietnam. The findings emerge from a large scale survey project which was designed to study the business environment; the mode of entry of FDI; the subsequent performance of investing firms; and the broader impact of FDI on the host economies (see Chapter 1). Our analysis in this chapter is primarily comparative and draws on findings from the survey of around 600 firms, comprising 147 from Egypt, 147 from India, 162 from South Africa and 170 from Vietnam. Detailed discussions of the findings from each country are contained in subsequent chapters.

The underlying conceptual framework for our analysis has been outlined with reference to Figure 1.1 in the previous chapter, which draws on the work of Meyer and Estrin (2001). Our approach is to model the strategic choice by a multinational firm about where and how to place their overseas investment as being driven by the various elements of the business environment in the host economy to complement firm and industry specific issues explored in the strategic management literature. This includes a large number of facets, including the level of institutional development, the legal structure, the policy framework and the physical infrastructure. A crucial question for each investing firm concerns the balance of advantage and disadvantage resulting from these factors in each alternative host location. The investing firm needs to be able to purchase or obtain sufficient resources in order to function successfully, and the factors determining where these resources are obtained will depend in part upon the character of the investing firm itself. For example, a firm with considerable multinational experience and rich in intangible assets may be in a position to provide many resources itself, and

*ceteris paribus* is more likely to enter as a greenfield operation. Firms with less experience, smaller or less well endowed in intangible assets, may instead choose to purchase a higher proportion of these assets from the host economy. But there remain a number of important choices to make. The resources could be obtained by outright acquisition of an existing firm. This could be done in totality, or only partially. Alternatively the potential entrant could create a new venture jointly with an existing firm. From this decision tree, we identify the four main “modes of entry” available to investing firms: greenfield entry, acquisition, partial acquisition and joint venture.

In the following section, we describe the characteristics of the four-country enterprise sample in terms of sectoral distribution, size, and parent firm location. We go on in the third section to contrast the modes of entry in the different countries, which we link to the motivations for FDI and to the resources available to the investing firms and from the host economies. Managers’ perceptions of the business environment in the host economies are compared and evaluated in the fourth section, which considers input markets and infrastructure as well as political and institutional arrangements. The comparative performance of foreign subsidiaries in the four host economies is the subject of the fifth section, and conclusions and implications for the remainder of the study are drawn in the sixth.

## HOST AND SOURCE FIRM CHARACTERISTICS

In this section, we compare the characteristics of the sample in each of the four countries in terms of the sectors, the size of enterprises and the regions from which the parent firms originate. In Table 2.1 we report the distribution of industries by country of the FDI projects. The data refer to the number of firms, not to value of investments. The primary sector investment is found to be everywhere only a small proportion of the foreign investment, representing around 3 per cent of the total. As our sample covers only developing economies one might have expected a high proportion for example in mining. As this is a capital-intensive sector, we find that the primary sector represents a slightly higher proportion of investment to South Africa, measured in terms of capital value (4 per cent). There are also important inter-country differences in terms of the sectors receiving FDI. Investment into Vietnam conforms to a more traditional view of FDI into developing countries, being in manufacturing industry, and within this sector, to basic consumer and intermediate goods. In contrast, investment in manufacturing in India and South Africa has been directed towards the machinery and equipment sector and, to a lesser extent, into intermediate goods. In all four countries, the service sector, (especially finance), is important but South Africa and Egypt have higher proportions of foreign

affiliates in this sector than do India and Vietnam. Indeed, more than a fifth of all firms entering South Africa go into the financial and business service sector, as against only 7 per cent in Vietnam and 13 per cent in India. Egypt and Vietnam also have considerable entry into the trade and tourism sector, in excess of 10 per cent of the total in both cases; and entry into infrastructure and construction is also comparatively high in Egypt (18 per cent). Finally, it is worth underlining the high proportion of investment into the IT sector in India in recent years. Since 1991, we find almost 20 per cent of the total number of Indian foreign affiliates enter that industry, which is consistent with the public awareness about the rapid growth of the Indian software industry (see Commander (2004)) and Desai (2003)).

*Table 2.1 Cross Country distribution of affiliates by sector (% of affiliates)*

Sector	Egypt	India	South Africa	Vietnam
Primary	3	3	3	4
Basic consumer goods	13	12	13	36
Intermediate goods	15	16	14	27
Machinery & equipment	10	26	19	8
Infrastructure & construction	18	6	12	2
Trade, tourism & recreation	15	1	5	13
Financial & business services	18	13	21	7
Information technology (IT)	5	19	8	1
Pharmaceuticals	3	5	5	2

In Table 2.2, we report the size distribution by employment of foreign subsidiaries in each country, using five employment categories ranging from 10 to 50 workers to companies with more than 1000 workers. Our sampling strategy excludes firms with fewer than 10 workers. We also provide information on the growth of the foreign affiliates by showing employment at the date when the company commenced operations (start of business) as well as in 2001.

Contrary to common perception, most FDI projects in all our sample countries are relatively small, employing fewer than 100 workers on average. This could represent either a lack of comparative advantage in heavy industry or the existence of barriers to entry, for example government regulations or powerful domestic incumbents. The finding suggests that governments should not look immediately to FDI as a motor to create employment in emerging markets, especially in India and Egypt where median employment at the time of entry was only 30 and 40 workers respectively.

Table 2.2 Cross country distribution of affiliates by employment (% of affiliates)

Employees	Egypt		India		South Africa		Vietnam	
	Start of business	2000	Start of business	2000	Start of business	2000	Start of business	2000
10-50	58	38	65	46	40	31	33	24
51-100	9	19	12	18	16	23	27	24
101-250	15	18	18	19	22	16	21	20
251-1000	12	18	5	16	14	20	17	27
More than 1000	6	6	0	1	9	10	2	5
Total	100	100	100	100	100	100	100	100
Median no. Employees	40	73	30	56	76	90	85	127
Median size of fixed capital stock (US\$ million)	-	1.45	-	0.69	-	1.67	-	1.20

However, employment in foreign owned subsidiaries in all our countries is growing rapidly. Everywhere except Vietnam, the majority of affiliate firms started with fewer than 100 employees and only in South Africa did more than 25 per cent of firms start operations employing more than 250 employees. This is probably associated with the higher proportion of acquisitions in South Africa. On average, foreign affiliates are somewhat larger in Vietnam than in all the other countries, and this was true from the start of operations. This reflects the more labour intensive production that results from the relative factor endowment of Vietnam, as well as the sectoral distribution, with a higher proportion of basic manufacturing industry.

Looking at the size distribution of foreign affiliates in terms of capital stock paints a similar picture. The median values in 2000 are also reported in Table 2.2. In all the countries, fixed assets of foreign affiliates are valued at less than US\$ 2 million for the majority of firms. The proportion of “small investments (valued below US\$ 2 million) is the largest in Vietnam and India (67 per cent), though these differences could merely reflect variation in cross-country purchasing power and the sectoral distribution. However, one fifth of all investments into South Africa had fixed assets valued at more than US\$ 10 million in 2001, as against between 10 and 13 per cent in the other three countries. The data on median capital stock is consistent with that on median employment, with South African subsidiaries significantly larger than in the other three countries, especially than in India and Egypt.

In Table 2.3 we compare the distribution of parent firms’ home countries. For ease of comparison, we have grouped the enormous numbers of source countries (more than forty) into five. Though the leading source economies are common to all countries, regional factors have significantly influenced the pattern of FDI.

Thus we find the largest proportion of investing firms is almost always from Europe and North America. These two regions account for 80 per cent of total FDI into India and South Africa and 63 per cent into Egypt. However, 78 per cent of investment into Vietnam derives from its “own” region of East Asia; this is a region which only provides 14 to 15 per cent of foreign affiliates into India and South Africa and a mere 2 per cent in Egypt. Moreover, in Egypt, around one third of total numbers of investments come from the Middle East and North Africa, but this region invests virtually not at all in the other surveyed countries. Regional investors appear to play little or no role in investments to South Africa and India – perhaps because they are not so closely integrated into their regional rather than into the global economy, and because of the size of the home market, especially for India.

*Table 2.3 Cross country geographic distribution of parent firms (% of parent firms)*

Home region of parent firm	Egypt	India	South Africa	Vietnam
North America	19	31	23	5
Europe	44	50	57	15
East Asia, inclusive Japan	2	14	15	78
Middle East and North Africa (MENA)	33	4	0	1
Other (including Australia)	2	2	6	2

## ENTRY STRATEGIES

We have argued that firms decide how to enter foreign markets according to the balance of advantage between the alternative ways of creating overseas subsidiaries: greenfield entry, partnership with a local firm (joint venture (JV)) or by acquiring part or all of an existing organisation (partial or full acquisition). As the entry mode varies, one would expect the investing firm to be purchasing differing amounts and forms of resources from the domestic markets of the home and host economies and using differing quantities of its own resources. Investing firms might therefore rely on greenfield modes of entry relatively more if resources were more easily available in host economy markets and could be more easily transferred from the investing firm, or if there were fewer opportunities to equip firms in the host economy. On the other hand, acquisition might be used relatively more frequently if there was an abundance of suitable firms available in the host economy, and these had appropriate brands, supply networks, distribution networks and so forth which would be expensive for the entering firm to replicate for themselves.

We report the distribution of entry modes by country in Table 2.4. As we show in the later chapters, entry mode choices in our sample countries are not always unconstrained. In particular, regulations limited full ownership or acquisition in India and Vietnam for some of the period in some sectors. While acquisition is the most significant mode of entry in developed countries (see for example UNCTAD (2002)), it is less common in less developed economies and also in our sample. Thus greenfield and joint venture are found to be the dominant modes of entry in Egypt, India and Vietnam. Taken together, these represent around 80 per cent of all FDI entry in the past decade in these three countries. However, there are some interesting differences in the pattern between these countries. For example, we find relatively more entry via joint venture in India and more greenfield in Vietnam. South Africa is very different to the other three, however, with around one third of all entry by acquisition, and less than a third being

greenfield. This contrasts especially with Vietnam, where more than half of all entry is greenfield, or Egypt, where the proportion is 46 per cent.

This seems to suggest that, compared to developed economies, in emerging markets as a whole, foreign entrants rely relatively more on their own resources than on what can be purchased in the local market place, either unbundled or as a bundle of resources (that is through acquisition).

South Africa differs from this pattern, perhaps because it has a more developed network of incumbent firms and a more developed market, both of which facilitate entry by acquisition. India has more entries by joint venture than any of the other four countries (54 per cent) and this probably reflects the heritage of legal requirements – and the peculiarities of the host business environment.

*Table 2.4 Cross country distribution of affiliates by mode of entry (% of affiliates)*

Mode of entry	Egypt	India	South Africa	Vietnam
Greenfield	46	35	31	56
Joint Venture	37	54	23	32
Acquisition	5	4	31	2
Partial Acquisition	12	6	14	11 <sup>7</sup>

The literature (see for example Dunning (1993)) categorises the motives for FDI into “efficiency-seeking”, for example for skilled labour, “resource-seeking” (for raw materials) and “market-seeking”, for example producing for the local market. Our survey yields a categorisation of motives that partially maps into this framework. Questions in our survey allow us to identify the two standard entry motives, and additionally permit us to subdivide the market-seeking category into a further three groups which might be relevant to an emerging market. We report in Table 2.5 data on the share of output exported, at the time of entry and currently, to distinguish between market and efficiency or resource-seeking entry modes. If the primary objective is exporting (in which case the motive for entry was efficiency or resource-seeking), the new subsidiary could have been created either to serve the global market; or a regional market, with the new entry as a hub; or as a source of inputs for the global firm itself, in an integrated vertical supply chain. Given the small share of the primary sector in our sample, we can interpret export-oriented entry as primarily efficiency-seeking. If the primary objective for the new entrants is to serve the host domestic market, the motive for entry is probably market-seeking. We allow for all these categories in Table 2.5.

Perhaps surprisingly, we find efficiency-seeking to have been the dominant motivation for entry in only one of four economies, Vietnam,

though it was also important in India. This contrasts with the findings in UNCTAD (2002), which stresses the role of efficiency and resource-seeking FDI in developing economies as a whole. Perhaps the modest FDI performance of our sample countries noted in the first chapter may in part be explained by the fact that efficiency-seeking entry is relatively less advantageous in them. It also appears that firms made and stuck to the strategic decision about whether production is primarily destined to be exported or for the home market prior to entry, since the proportions of sales exported do not alter greatly between the date of entry and 2001.

If we look first at South Africa and Egypt, the bulk of firms in our survey were set up primarily to serve domestic markets; only around 20 per cent of sales were exported at the start of operations, though this had risen in South Africa by six percentage points by 2001. This focus on domestic market by foreign affiliates is probably associated with the sectoral pattern of FDI: for example, in Egypt, with the concentration on tourism and services. Even in 2001, only around a quarter of FDI in Egypt and South Africa could be viewed as “efficiency-seeking”.

When we consider the categories of efficiency-seeking entry, a significant proportion in Egypt (nearly half) is found to be serving the regional market, but in South Africa we find relatively more exports are destined for the global market. However, interestingly, we find that in recent years the regional market is also becoming more important, at least relative to when firms first entered in South Africa. Perhaps this suggests that South Africa is beginning to become more integrated into the broader African market since the collapse of the apartheid regime in the mid-1990s.

Surprisingly, given the size of its domestic market, India has a higher share of FDI focused towards exports than Egypt or South Africa, though more than 60 per cent of sales by foreign affiliates remained destined for the home market. Of the 36 per cent that is exported, on average, nearly half of exports by Indian firms are directed into the global economy, while the regional market is much less important. But the survey suggests that India also serves as a relatively important location for production along the supply chain for some multinationals, since around one quarter of the exports by subsidiaries in India are destined for other affiliates of the parent firm. The export orientation to other affiliates is unsurprisingly particularly concentrated in the IT sector, suggesting a lot of investment probably represents relocation of back office and software development activities.

We find investment into Vietnam to have been motivated by rather different factors from those in the other three countries; efficiency-seeking is the majority objective. The average proportion of product exported is 50 per cent, and has been at this level for firms since the start of operations. This orientation towards efficiency-seeking investment perhaps helps to explain



*Table 2.5 Market focus of affiliates (% of sales)*

Market focus	Egypt		India		South Africa		Vietnam	
	Start of business	2000	Start of business	2000	Start of business	2000	Start of business	2000
% of sales exported	23	26	36	37	19	25	51	50
Of which:								
Regional market	10	12	6	7	4	10	25	24
Global market	10	10	20	20	11	12	20	20
Other affiliates	3	4	11	10	4	3	6	6

the sectoral distribution, which is concentrated on basic manufacturing. It may also be explained by the geographical distribution of parent firms, located largely in the South East Asia. Policy has been focused to promoting exports as well. This interpretation is strengthened when one notes that almost half of exports are destined for regional markets and a further 12 per cent to parent firms<sup>6</sup>.

The questionnaire asked firms to rank the resources they regarded as important for their competitiveness. Though we offered fourteen choices, only eight were consistently reported as being critical by our respondents. These fell into five categories: financial (provision of equity financing); technological (technology); intangible assets (brands, business and distribution networks, marketing); tangible assets (machinery) and management. In all four countries, we find that brands, management and technology are always considered to be the crucial resource underlying the success of foreign investments, though the exact ranking differs somewhat from country to country. Brands are seen as the most important resource for success by foreign affiliates in Egypt, India and South Africa, while equity is ranked as the most significant resource for success for foreign affiliates in Vietnam, second most important in India, and third in Egypt and South Africa. Indian respondents rank technology as the critical resource for success, as do Egyptian managers, but it is ranked only third in South Africa and Vietnam. Interestingly, factors that one might expect to be contributed by a host economy partner – for example networks, machinery or marketing – are rarely seen as the critical factors for success in the survey.

One obtains a richer picture by focusing on the leading three rather than the single critical resource for success identified by our respondents. In this case, we see from Table 2.6 that technology is ranked above all other resources in Egypt and India, and it is ranked in second and third places in South Africa and Vietnam respectively. Management, which is rarely considered to be the leading single resource for success, is most frequently included as one of the most important factors, using this criterion, in South Africa and especially in Vietnam, where more than half of our respondents list it in their top three resources. Management is also ranked second in Egypt (where 47 per cent of respondents place it in their top 3 resources) and South Africa. Other important factors listed in the top three resources include intangibles (marketing and brands). In Vietnam, machinery is also considered important. It is mostly provided by foreign investors and entails embedded technology transfer.

This perception by the managers of key resources for success appears in line with what one might expect given the observed motives for investment and the sectoral distribution of foreign affiliates. For example, in Vietnam, FDI entrants have concentrated relatively more on industrial commodity production for export, so it is not surprising that we find the critical resources

to be perceived by managers of subsidiaries as being management, technology and fixed assets; brands have played less of a role. However for the market-seeking investors into Egypt and South Africa, technology and brands as well as management have proved to be the source of competitive advantage. The importance of technology in India as a critical resource for success probably arises because there is relatively more high-tech investment there.

*Table 2.6 Cross country evaluation of the three most important resources for success (% of affiliates)*

Resource	Egypt	India	South Africa	Vietnam
Brands	32	31	36	20
Business networks	30	27	34	23
Distribution networks	13	20	25	22
Equity	11	30	14	25
Machinery	19	13	19	36
Management	47	34	40	52
Marketing	33	26	32	29
Technology	50	48	39	29

In Figures 2.1 to 2.3, we investigate how firms obtain the resources that they regard as critical for the success of their investments, based on the three most important sources. As one might expect, we find in Figure 2.1 that local firms do not in general supply technology, equity or brands. Though they typically provide distribution and business networks and marketing skills. In Egypt, local firms supply relatively more of the key resources in marketing, management, business and domestic enterprise and distribution networks than in any other country, perhaps reflecting the character of investing firms into the Middle East and North Africa. Local firms supply relatively less of everything in Vietnam, presumably indicating the weaker business environment. The relatively more developed state of the South African business sector is illustrated by the relatively greater local provision of machinery and management, though in fact South Africa and India prove to be quite similar in terms of the local firm contributions over a wide variety of resources. Figure 2.2 provides information on the contribution of the foreign parent firms. Here, we observe the converse picture to Figures 2.1. The foreign firms supply equity, brands, technology and management, but usually rather less in terms of marketing, distribution and business networks. In Figure 2.3 we look at the role of the local market as a source of resources, and observe that these do play an important role especially in the more developed economies of our sample - Egypt, India and South Africa in terms

of the business and distribution networks and to a lesser extent of management.

## EVALUATION OF THE HOST BUSINESS ENVIRONMENT

Our approach highlights the potential impact of the business environment on foreign investment decisions. We have focused on foreign affiliates' managers evaluations of the quality of the host country's labour force; the quality of the local inputs; and on the institutional environment. Their perceptions measured on a scale from 1 to 5 are summarised in Tables 2.7 to 2.9. Overall, we find considerable within-country variations relative to between-country variations, with standard deviations for most of the below reported indices in the range of 0.9 to 1.2. Differences thus should be seen only as indicative of underlying patterns in the environment.

Table 2.7 reports managers' evaluation of labour markets for four categories of labour ranging from skilled manual workers through to executive management. Perhaps surprisingly for emerging markets, these are all evaluated relatively highly on average, frequently above a level of 4.0.

Moreover, despite the differences in development level and educational attainment, there is surprisingly little variation of these managerial assessments of the business environment across countries and over time. This suggests that foreign firms are either sufficiently small or pay sufficiently high wages to avoid fundamental constraints on the supply side of the labour market. However, Vietnam was rated somewhat below the other countries at the date of starting operations, and it had not closed the gap by 2000. The difference is particularly marked with respect to executive management. It is possible that the Vietnamese scores are affected by the transition from central planning to a market economy, which acted to exacerbate existing shortages in management by creating a demand for market economy based managers and leadership skills.

Considering Table 2.7 in more detail, we find that labour markets are evaluated at around 3.8 to 3.9 in three of the four countries at the start of operations, with Vietnam substantially lower at 3.3, primarily because of weaknesses in the availability of executive managers. The situation is perceived as improving markedly up to 2000 in Egypt, India and Vietnam, with Egypt and India rated on average at that time well above 4.0 in each sub-category (except for executive management in India at 3.9). However, despite considerable improvement in all four categories, labour availability in Vietnam in 2001 is still rated below the levels attained in the other three countries up to a decade earlier.

Though labour availability is rated quite highly in South Africa at the time when foreign affiliates commenced their operations – the levels are comparable to India and slightly below Egypt – the situation did not improve

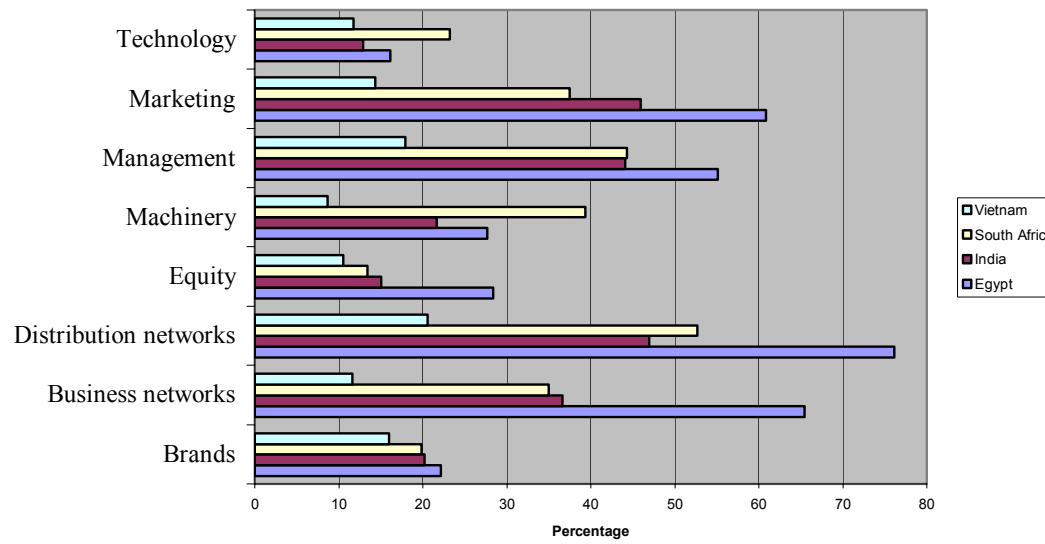


Figure 2.1 Local firms source of three most important resources

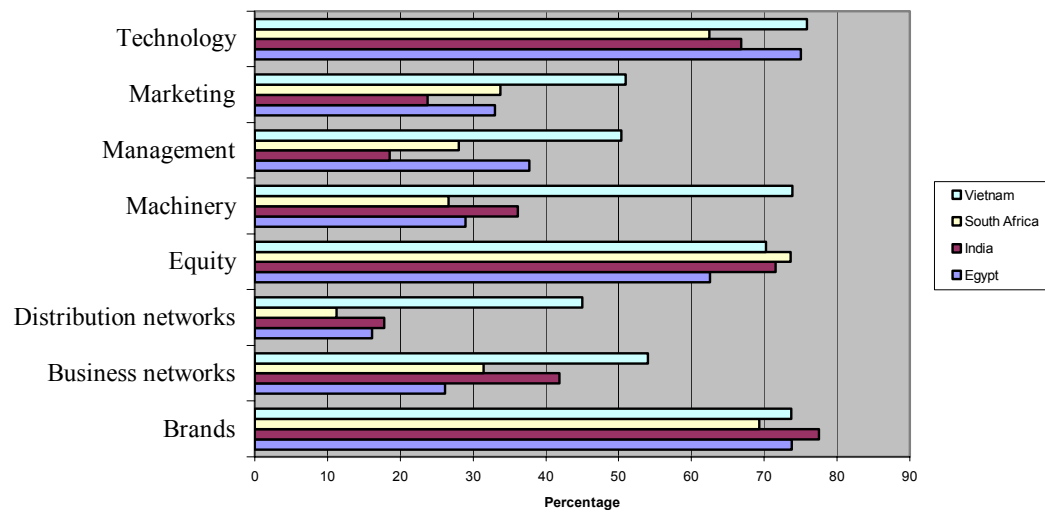


Figure 2.2 Foreign parent source of three most important resources

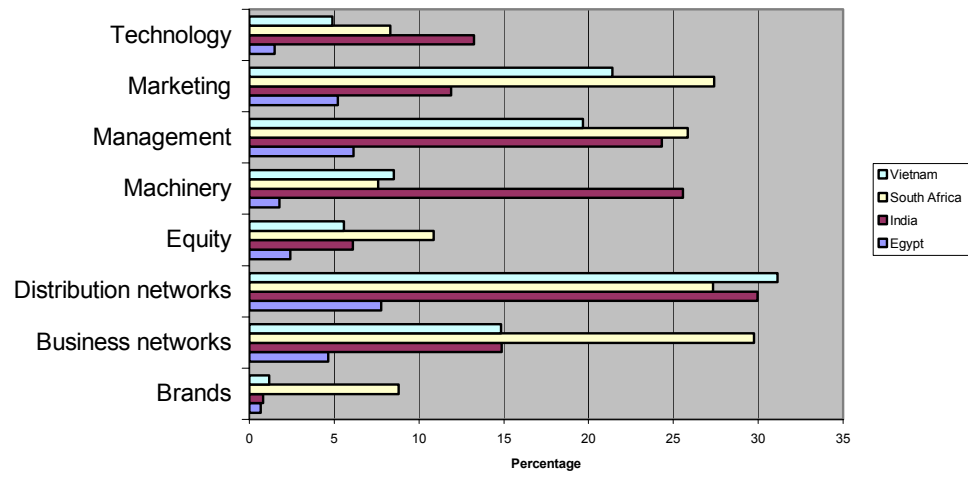


Figure 2.3 Other local source of three most important resources

from then until 2001. This has led to deterioration in South Africa's relative position in terms of labour availability by 2000. In all four countries, executive management is evaluated as being the hardest to obtain both at the start of operations and in 2000.

Turning to local inputs in Table 2.8, we find South Africa to be perceived by managers of foreign affiliates to provide a better business environment across the board in terms of the six indicators reported: quality of raw materials and machinery; the ability to obtain real-estate; the quality of professionals; the reliability of information technology and the telecommunications network; and finally, the reliability of utilities, such as electricity. This is true at both the start and the end of the period, though, as in Table 2.7, we observe considerable improvements in the evaluations of local inputs in Egypt, India and Vietnam but very little in South Africa. Hence, by the end of the period, the most advanced other country, India, is attaining evaluations comparable to South Africa at the start.

The most serious problems in the local environment noted by managers of foreign firms in Table 2.8 at the start of operations concern machinery and components in Egypt, telecommunications and IT in India and, raw materials, components and machinery in South Africa and Vietnam. Real estate is also a source of difficulty to inward investors in Egypt, India and Vietnam. The greatest perceived improvement from the date of entry to the current time is perceived to be in IT and telecommunications, especially in India, and Egypt. Problems of machinery and components persist in Egypt and Vietnam, and are exacerbated slightly in South Africa, but we observe some slight improvement in India.

In Table 2.9 we report managers' perceptions about another crucial set of issues for investors into emerging markets – the institutional and policy environment. This is evaluated in three categories: the quality of government at the local, provincial and central level; the predictability of the policy framework; and the quality of the institutional structure. In the latter category we include the legal framework and environmental regulations as well as several important specific issues concerning visas, property and business licensing.

Managers' evaluations of the host economy business environment are somewhat lower on average than we observed in the previous two tables. The average evaluation of the institutional environment in every country is around 3 on a 1-5 scale, and, in fact, a high proportion of observations average in the 2's ("not very conducive"). Moreover, except in Vietnam, there is little real evidence of improvement in these crucial areas for foreign investors; indeed the situation is perceived as deteriorating very slightly in South Africa and is more or less unchanged in Egypt between the time of entry by foreign affiliates and 2000.

When we dig deeper into the detailed questions, we find interesting institutional differences across the four countries. In some aspects the quality



of the institutional environments are seen to be reasonable (that is above 3.5), for example in Egypt (environmental regulations) and South Africa (real estate and environment). Indeed in all four countries, one or another indicator of the institutional environment group is ranked above 3.0 (that is visas and environmental regulations in India and Vietnam). However, the general legal framework is perceived to be not conducive (less than 3.0) in Egypt and Vietnam, and only in South Africa does it approach a satisfactory level (nearly 3.5). Moreover improvements to the institutional environment have at the very best been modest, and often non-existent. The only exception is Vietnam, where things had improved somewhat by 2000 in terms of business licensing, real estate and visas. Interestingly, at the time when most of our sample of foreign affiliates started operations, Vietnam ranked very poorly in terms of the institutional environment, but by the end of the period it had overtaken all the other countries in this regard except for South Africa. The same period saw South Africa perceived as deteriorating slightly in terms of the institutional environment, particularly with respect to visas and work permits.

Turning to predictability of the business environment, this was also perceived to be poor by managers of affiliates at the time when operations began in three of the four countries; only in South Africa was predictability above 3.0 on the 1-5 scale and in no countries did it exceed 4.0. Moreover, predictability of the business and policy environment has not been perceived by foreign investors as improving over the period to 2000 in any country but Vietnam. Indeed we find there has been a slight deterioration in the evaluation of the predictability of policy in Egypt and South Africa, though it is found to be improving slightly in India. Even so, the evaluation there remains low - only 2.79 on the 1-5 scale.

Finally, we report the evaluations of the quality of government. Once again, this is found to be very poor in Egypt and for local government in India, but somewhat better in Vietnam and South Africa. India in particular appears to have considerably improved foreign business perceptions of the quality of its central government, but not of its provincial or local government. The perception of quality of all levels of government has improved sharply in Vietnam between the start of its operations of the foreign affiliates and 2000, and interestingly the quality of Vietnamese government is now perceived to be highest of our four sample countries. It might be that the Vietnamese government at all levels has been striving to become more "business friendly" and open to foreign investors, leading also to the improvements in policy related aspects of the institutional environment (for example visas and real estate) as well as predictability. We find a slight decline in the evaluation of government quality in Egypt and South Africa over this period, paralleling the previously noted decline in predictability.

Our findings in Table 2.9 are symptomatic of the institutional weaknesses perceived by foreign investors into emerging markets and

Table 2.7 Cross country labour market evaluations

Type of personnel	Egypt			India			South Africa			Vietnam		
	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change
Executive management	3.66	4.01	0.35	3.51	3.91	0.40	3.48	3.56	0.08	2.59	2.87	0.28
Professionals	4.08	4.37	0.29	4.04	4.37	0.33	4.15	4.11	-0.04	3.57	3.82	0.25
Operational management	3.85	4.25	0.4	3.77	4.23	0.46	3.75	3.76	0.01	3.42	3.65	0.23
Skilled non-managerial labour	4.17	4.42	0.25	4.01	4.36	0.35	3.95	4.03	0.08	3.79	4.03	0.24
Mean	3.94	4.26	0.32	3.83	4.22	0.39	3.83	3.87	0.03	3.34	3.59	0.25

Note: 1=never available, 5=readily available

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Table 2.8 Cross country local input evaluations

Local input	Egypt			India			South Africa			Vietnam		
	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change
Utilities	4.07	4.45	0.38	3.52	3.80	0.28	4.55	4.63	0.08	3.43	3.86	0.43
IT and telecoms	3.66	4.42	0.76	3.17	4.14	0.97	4.06	4.27	0.21	3.35	3.87	0.52
Professional services	4.03	4.15	0.12	3.94	4.44	0.50	4.44	4.48	0.04	3.69	4.04	0.35
Real estate	3.98	4.16	0.18	3.83	4.20	0.37	4.47	4.51	0.04	3.68	3.83	0.15
Machinery	2.86	3.19	0.33	3.68	4.21	0.53	3.77	3.85	0.08	3.11	3.45	0.34
Raw materials and components	2.87	3.08	0.21	3.40	3.91	0.51	3.51	3.46	-0.05	3.09	3.42	0.33
Mean	3.58	3.91	0.33	3.59	4.12	0.53	4.13	4.20	0.07	3.39	3.75	0.35

Note: 1=never available, 5=readily available

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Table 2.9 Cross country institutional environment evaluations

Institutional factor	Egypt			India			South Africa			Vietnam		
	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change	Start of business	2000	Change
Business licenses	3.06	3.12	0.06	2.92	3.38	0.46	3.70	3.80	0.10	3.21	3.75	0.54
Real estate	3.40	3.59	0.19	3.09	3.41	0.32	4.04	4.10	0.06	2.91	3.32	0.41
Visa and work permits	3.36	3.40	0.04	3.12	3.42	0.30	3.00	2.77	-0.23	3.21	3.62	0.41
Environmental regulation	3.60	3.62	0.02	3.11	3.13	0.02	3.63	3.56	-0.07	3.30	3.47	0.17
General legal framework	2.95	2.92	-0.03	3.03	3.14	0.11	3.49	3.33	-0.16	2.88	3.27	0.39
Predictability	2.87	2.67	-0.20	2.71	3.79	0.08	3.65	3.58	-0.07	2.80	3.15	0.35
Central government	2.89	2.87	-0.02	3.07	3.33	0.26	3.32	3.26	-0.06	3.23	3.59	0.36
Local government	2.97	2.91	-0.06	2.93	3.05	0.12	3.39	3.27	-0.12	3.11	3.40	0.29
Mean	3.14	3.14	0.00	3.00	3.19	0.20	3.51	3.44	-0.07	3.10	3.46	0.36

Note: 1=not at all conducive, 5=very conducive

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probably explain the relatively poor overall FDI performance in our sample countries, relative to the “stars” of emerging markets such as China.

## PERFORMANCE OF FOREIGN INVESTMENTS

We asked several questions to our respondents about the performance of their subsidiaries, all of which were perceptual and ranked on a scale from 1-5. We explored performance in terms of productivity, profitability and growth in revenue of the subsidiary, and the findings are summarised in Table 2.10. The average scores are fairly high in every country. This may be encouraging news for foreign investors into developing countries but such conclusions must be treated with caution since there may be a selection bias; firms that were relatively successful in their FDI entry are the ones more likely to have responded to the questionnaire. Moreover the firms best positioned to succeed in the difficult business environment of emerging markets may be the ones that chose to invest in our sample countries. However, the variations across countries and by sector and entry mode are of interest.

Performance in productivity was on average ranked highest among the performance measures, being evaluated above 3 in all countries and in three of the four countries above 3.5. The only other performance indicator to score above 3.5 in Table 2.10 was the evaluation of revenue growth in South Africa. Interestingly, performance in profitability everywhere is seen on average as quite disappointing, being evaluated below 3.5, though this may reflect gestation periods. These rankings suggest performance is not quite as good as the raw data suggests, and that perhaps *a priori* assumptions about the business environment in emerging markets are too optimistic, especially if firms are inexperienced. The cross-country variation persistently gives a ranking in which Vietnam is at the bottom in terms of performance, but different countries are at the top, depending on the performance criteria used. India dominates in terms of productivity and South Africa in terms of profitability and revenue growth. This indicates that despite recent improvements in the environment it remains hard to make profits in less developed economies like Vietnam, but is easier in more developed countries like that of South Africa. However, it is interesting that, on average, the cross-country differences are not found to be very great. We also find little variation in performance by sector or entry mode, and these tables are not reported.

A second indicator of the performance of FDI from the perspective of a government in the host economy would be spillovers from the investment. To address this issue, we consider the extent of training, which is potentially of great significance in emerging markets because the training offered to the labour force by foreign owned firms could be an important source of

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improved labour quality and productivity across the entire economy, as labour flows from the foreign subsidiary to other firms.

*Table 2.10 Comparative company performance, cross country*

Performance indicator	Egypt	India	South Africa	Vietnam
Productivity	3.82	3.90	3.84	3.43
Profitability	3.26	3.28	3.46	2.64
Revenue growth	3.42	3.28	3.77	3.02
Mean	3.50	3.49	3.69	3.03

*Notes:* 1=performance expectations not met at all, 5=performance expectations entirely fulfilled

The comparative findings are reported in 2.11, which show the share of training over the per centage of sales in the four countries in four categories - total, management training, non-management training and internal training. We find training expenditures to be very modest, in terms of the share of sales, in all the countries, though far from insignificant. Training in all categories represents a higher per centage of sales, and therefore potential for spillovers, in South Africa, followed closely by India and Egypt. There is less training undertaken in Vietnam in all the categories. Thus, interestingly, Vietnam, which attracted a high proportion of resource-seeking FDI, displays weaker performance of the foreign subsidiaries and in one of the possible spillovers to the Vietnamese economy.

*Table 2.11 Value of training expenditure, cross country (% of sales)*

Training indicator	Egypt	India	South Africa	Vietnam
Total training expenditure	2.32	2.13	2.54	1.89
Management training	1.67	1.77	1.74	1.58
Non-management training	1.74	1.73	2.21	1.55
Internal training	1.82	1.76	2.17	1.68
Average	1.89	1.85	2.17	1.68

## CONCLUSIONS

The survey undertaken as part of our project provides a snapshot of FDI's into four comparable emerging markets during the 1990s. The picture that emerges is rather different to expectations derived from the experiences of

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developed economies. Most foreign direct investments to these emerging markets are small, sometimes very small, and surprisingly high proportions are in the financial and service sector. There is a significant regional pattern to the distribution of donor firms' countries – it is clear that local familiarity, experience with emerging markets and integration into regional trading blocks, plays some role in the FDI process to developing economies.

Contrary to expectations, most FDI to our sample countries is motivated for market rather than efficiency-seeking reasons. This is especially true for South Africa and Egypt. Investments into India follow a split pattern, with most FDI being of a market-seeking character but with a small yet very significant efficiency-seeking sector oriented to export and often integrated into company supply chains in the IT sector. In contrast, Vietnam has a much larger efficiency-seeking FDI sector, representing a majority of all investments. This is reflected in the sectoral distribution of FDI to Vietnam, which is more concentrated in basic manufacturing, and in the regional character of FDI source firms, disproportionately based in South East Asia.

As one might expect in developing countries, appropriate acquisition targets are scarce or capital markets are less well developed and regulations for takeover are more complex. Hence it is unsurprising that the dominant entry modes are greenfield and joint venture in our sample. The only country which looks different in this respect is South Africa, where the industrial and institutional structure is more mature and entry by acquisition is rather more common. The combination of majority greenfield entry, efficiency-seeking motivation, predominant manufacturing and regional integration make the case of Vietnam more comparable to the earlier models of rapid growth through FDI and exports in China, Thailand and Malaysia, than to any of the other countries in our sample.

The survey presents a consistent picture of what the managers of foreign subsidiaries perceive to be the resources crucial to success in emerging markets – brands, management and technology. In general, foreign firms provide the bulk of these inputs, while local firms provide distribution, business networks and marketing skills. Moreover, the perception of the business environment of the host economy is for the most part quite good, though there may be sample selection issues here. The quality of the labour force is found to be fairly good in all four countries, though some problems are noted in the availability of executive management, especially in Vietnam. This is probably because foreign subsidiaries use expatriates, pay efficiency wages or are too small a sector to suffer from economy-wide skill shortages. In terms of the quality of local inputs, most host economies in our sample are again evaluated quite highly by our sample of managers, and perceptions are improving everywhere except in South Africa. The most serious problem with respect to the business environment is perceived to be in the area of the institutional and policy environment. This is evaluated as being significantly worse than the other aspects of the business environment noted above, and is

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not seen as improving anywhere except in Vietnam during the 1990s. Indeed the situation in South Africa is seen as deteriorating slightly. Predictability of government policy and the quality of central and local government are highlighted as particular problem areas.

Despite this, the bulk of our respondents are relatively satisfied with the performance of their foreign affiliates, especially with regard to productivity and revenue growth. Performance in profitability was evaluated rather less well however, perhaps because of the inevitable gestation lags. Despite the rapid improvement in the institutional environment, it has so far proved particularly hard for foreign firms to meet their profit and other performance targets in Vietnam.

In the remainder of this book, we explore findings of the survey in more detail for each country, and we illustrate many of our major themes – institutional environment, entry mode, source of crucial resources, and performance – with a number of case studies from each country. The country chapters also discuss in greater depth the institutional and policy environment in each country and country specific findings from the survey. In the final chapters, we bring together the material in separate policy and managerial conclusions.