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The Changing Multinational Corporation—A Nation State's Relationship: The Case of IBM in India

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The Changing Multinational Corporation--A Nation
State's Relationship: The Case of IBM in India

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The Changing Multinational Corporation--A Nation State's Relationship:

The Case Of I.B.M. in India

Abstract

During 1977, IBM was asked to withdraw from India due to their unwillingness to comply with the Foreign Exchange Regulation Act (FERA) of 1973. However, with (1) the recent signing of a Memorandum of Understanding between the U.S. and India, (2) the easing of trade restrictions by the Government of India against foreign firms, (3) the declining value of the U.S. dollar, (4) the slump in the U.S. computer market, (5) the rapid growth in the Indian computer market, and (6) changes in other environmental factors, IBM is again actively seeking and securing new business. In recent months, IBM has secured a number of large contracts, and is on the verge of reentry into the burgeoning Indian computer market.

The purpose of this study is to examine the underlying factors that influence both the divorce and reunification between host governments and the multinational corporation. The study, conducted through personal interviews with the chief executives of IBM, government officials, and other knowledgeable persons, examines the socio-political aspects of FERA and its implications for the multinationals in India and elsewhere in developing countries.

The Changing Multinational Corporation--A Nation State's
Relationships: The Case of I.B.M. of India

Introduction

Conflict between multinational corporations and host-country governments has attained an added dimension in recent years. Changes in the international business environment have led to significant alterations and, in some instances, reversal of past policies by both multinational corporations and host-country governments. Studies of multinational corporation-host country government conflict, therefore, need to reflect the significance of change as an underlying explanatory factor in predicting the policy-response modes of multinational corporations and host country governments.

The major players during the early stages in the evolution of multinational corporations were U.S. multinational corporations and host country governments. However, since the 1970s, European and Japanese multinational corporations and state-owned enterprises have entered the international business arena. These newcomers to the international business scene provide host country governments with alternative means to secure managerial and technological know-how, capital, and market network. The availability of alternative methods to fulfill national goals, in line with existing national priorities, has reduced the level of dependence of host country governments on U.S. multinational corporations.

This paper deals with the changing scene in the bargaining position of multinational corporations and host country governments by exploring

the case of IBM's withdrawal from India. The events that led to the withdrawal of IBM from the Indian market in 1977, the changes in bargaining positions, and the reinstatement of a close working relationship in recent months, are classic illustrations of the pervasive impact of the international business environment on both the multinational corporation and the host country government.

Increasing Potential for Conflict

Since the 1970s, multinational corporations have come under increasing fire from various sources. At home, they are accused of exporting jobs and technology. Overseas, they are accused of exploiting local labor, and demanding excessively high royalty payments for obsolete technology and patents. In addition, multinational corporations are accused of using monopolistic power to crush competition, and of gaining favorable rates for large financial credits, thereby competing for scarce capital with the domestic industry.

In response to these perceived abuses of the multinational corporation's monopoly power, host country governments have sought to exercise control over multinational corporations operating under their jurisdiction. While host country governments attempt to create a favorable investment climate in line with their priorities and objectives, they simultaneously impose numerous regulations on the multinational corporations' operations to exercise control and to assert their national sovereignty. Varying degrees of regulations to control the affairs of multinational corporations have occurred in the form of nondiscriminatory interference, discriminatory interference, discriminatory sanctions, or wealth deprivation.¹

Faced with host country government regulations, the multinational corporations' response, in each case, is based on their assessment of the situation and the stakes involved. In certain instances, they comply with the imposed regulations and fall in line with host country government objectives for national development. At other times, they exert their influence and negotiate with the host country government to resolve the potential conflict. In yet other instances, they assert their independence and either prevail over the host country government or close down their operations and withdraw from the host country.

This inconsistent behavior on the part of both multinational corporations and host country governments leads to instability and uncertainty and increases the potential for misunderstanding and conflict. Furthermore, the potential for conflict between multinational corporations and host country governments is magnified by the growing variety and magnitude of host country government regulations on multinational corporations.

This study explores the underlying reasons that influence both divorce and reunification between multinational corporations and host country governments. The study identifies the reasons for different policy prescriptions on the part of host country governments and covers the differing strategic response modes on the part of multinational corporations. A better understanding of the fundamental causes of conflict and the potential for divorce between the multinational corporations and host country governments are necessary to explore alternative policies to reduce the potential for conflict and divorce.

The sources and underlying reasons of conflict between multinational corporations and their external publics, including home- and host-country governments, competing firms, labor, etc., have been the subject of increasing attention.² The literature is replete with references to the political, social, cultural, economic, and legal forces as sources of tension and conflict between the multinational corporations and their external publics.³ Furthermore, the creation of international agencies and international codes of conduct for the multinational corporations have been suggested as possible policy measures to achieve conflict resolution.⁴

A recent study investigated the nature, causes and intensity of conflicts arising between multinational corporations and nation states. The three main conflicting issues were found to be equity participation, control by local nationals, and transfer pricing. Interference with political processes and socio-cultural norms within the host countries were found to be less important. Socio-cultural adaptation by multinational corporations was earlier considered to be of primary importance. The study concluded that the economic issues of equity participation, management control, expansion of exports, reduction of imports, and use of local inputs, have currently assumed primary importance as reasons for tension and conflicts between multinational corporations and host countries.⁵

However, static analysis is no longer sufficient to capture the essence of multinational corporation-host country government conflict which takes place in an international business environment marked by

rapid change. Indeed, the only permanent thing in the prevailing complex, dynamic, and uncertain international business environment is change. Both multinational corporations and host country governments find it necessary to cope with the accelerating pace of change. In certain instances, the changing international business environment has led to the emergence of new priorities and the modification or reversal of past policies. These dramatic changes in host country government policies and/or multinational corporation responses can be captured using dynamic analyses.

Dynamic analysis can highlight the importance of changes in the international business environment as underlying causal variables in understanding multinational corporation-host country government conflict. The framing or revision of policies by host country governments, and the formulation or revision of business strategies by multinational corporations, can be shown to depend upon these environmental changes.

IBM Withdrawal

During 1977, IBM was asked to withdraw from India due to its unwillingness to comply with the Foreign Exchange Regulation Act (FERA) of 1973. Earlier, IBM commenced operations in India in 1952, with long term objectives of growth and increasing market share in the world computer and information systems market through an improved competitive stance. During a period of 25 years, IBM made total profits of approximately U.S. \$5 million on a total investment of \$8 million. Total remittable profits, at the time of phasing out its operations in 1978, were approximately \$10 million. These profits included a net asset value of approximately \$5 million.

This poor performance was largely attributed to several factors, including compensation of approximately \$7.5 million paid to employees and assets sold at less than book value. Other factors included a high rate of effective taxation of 80% to 85% as well as low rates of depreciation on equipment. IBM-India operations constituted only 0.06% of IBM Corporation's total business. IBM's activities in India during this period and the events leading to the IBM-India withdrawal are summarized in Appendix A.

During this period, the Government of India (GOI) alleged that a large number of foreign-owned and foreign-controlled corporations operating in India were making excessively high gross revenues and before-tax profits. Further, the repatriation of large amounts of capital by the multinational corporations constituted a serious drain on India's scarce foreign exchange reserves. The GOI contended that the multinational corporations were using monopolistic power to stifle competition in the Indian market. In addition, the multinational corporations, according to the GOI, gained favorable rates for large financial credits, thereby competing with domestic firms for scarce capital. Finally, the GOI perceived that the multinational corporations were transferring obsolete technology or current technology of minor importance for developmental purposes.

Surveying the industrial scene, the GOI found that most foreign direct investment had occurred in the consumer goods sector. These ventures yielded high rates of profit and required simple technology which could be furnished by domestic entrepreneurs.

Based on these findings, the GOI formulated its own priorities with regard to the country's development. With an abundance of natural resources and a large supply of low-cost skilled labor, India provided the multinational corporations with a large, untapped market and opportunity to enhance their international competitiveness.

Taking stock of its developmental priorities and increased bargaining strength, the GOI formulated its desire to influence the course of foreign direct investment in India. The primary objective was to ensure that foreign direct investment in India would fall in line with the nation's developmental priorities. The means adopted to achieve this objective was the Foreign Exchange Regulation Act (FERA) legislated on January 1, 1974.

Foreign Exchange Regulation Act--The FERA affected all foreign companies with foreign equity exceeding 40 percent. According to FERA, four levels of foreign equity participation were permitted. First, all trading companies engaged in purely commercial activities as well as manufacturing enterprises utilizing "non-sophisticated" technology, were required to reduce their foreign equity to 40 percent. Second, "high technology" companies, utilizing "sophisticated" technology and/or engaging in "special" activities, as designated by the GOI, were permitted to retain a foreign equity holding of 74 percent. A third intermediate level of 51 percent foreign equity was established for multi-activity companies engaged in both sophisticated technology fields and other commercial and trading activities. The fourth level of 100 percent foreign equity was permitted only in those instances where foreign firms were engaged in purely export activities.

The FERA applied to companies already established in India, regardless of the terms and conditions of agreement under which operations had commenced in India. This act was considered very restrictive by foreign firms. The Indian authorities, on the other hand, perceived the FERA as liberal, since it permitted foreign equity of 51 percent and as much as 74 percent in certain instances. These were cases where existing enterprises in India were using or in the process of importing sophisticated technology. The GOI pointed to the tea companies, which were permitted to retain foreign equity to 74 percent as proof of the liberal nature of FERA.

IBM was operating in India as a branch of IBM World Trade Corporation and came under the purview of the FERA. Under the FERA, every foreign company was required to apply to the Reserve Bank of India for a "carry on business license." At this time the foreign firms were required to furnish a summary of the financial details of the business over the preceding few years.

The bulk of resources of IBM's operations in India (70 percent to 80 percent of total revenue) at the time resulted from (1) purely commercial/trading activities such as leasing of data processing machines; (2) operations of IBM's service bureaus, wherein customers utilized IBM machines and were provided with IBM services; and (3) "unsophisticated" technology operations such as IBM's card manufacturing program. However, leasing of IBM data processing machines included maintenance, systems engineering, education, and other services.

Reserve Bank of India Preliminary Determination--The Reserve Bank of India analyzed IBM's activities and past financial details, based upon

the FERA guidelines, and concluded that IBM-India had to dilute its foreign equity to 40 percent. The official notification from the Reserve Bank of India, requiring IBM-India to dilute its foreign equity to 40 percent in two years, was received by IBM in November 1975.

The GOI alleged that IBM was (1) importing second hand machines (IBM 1401 computer systems) into India at extremely low old book values capitalized through the inter-company billing price system, (2) reconditioning these machines, and then (3) either selling them at IBM's standardized worldwide sale prices or leasing them at IBM's standardized worldwide lease rental rates. IBM-India, according to the GOI, was reaping very high profits from the sale or lease of these obsolete machines. Furthermore, IBM was repatriating these profits without providing transfer of any sophisticated technology.

The GOI further contended that additional hidden profits had been repatriated with the parent company. From the standpoint of IBM, however, these hidden profits were called headquarter expenses and were treated by the IBM system as a legitimate expense. These headquarter expenses were apportioned in all revenue earning countries, and reflected (1) administrative overhead expenses, (2) research and development expenditures, and (3) other overhead expenditures incurred by the parent organization. This headquarter expense was based upon revenue of particular IBM affiliates. It was true that India had not directly benefited from the research and development by virtue of its contribution to IBM's headquarter expenses. However, it was equally true that IBM-India had the potential to sell any and all of the new products at the time they were introduced by IBM. Thus the concept for charging

headquarter expenses to IBM-India was for the right to receive and not for what was actually received and sold.

Even though the profits of IBM-India and several other IBM affiliates were poor, the parent company considered long term growth, market share, and a world-wide competitive stance of primary importance. IBM-India's revenue of \$20 million was only 0.1 percent of IBM's worldwide revenues, and to this extent, the loss of IBM-India operations did not constitute a major blow to the health and well-being of the IBM Corporation.

IBM Counter-Proposal--In response to the Reserve Bank of India notification of November 1975, IBM submitted a formal counter-proposal to the Reserve Bank of India in April 1976. IBM's proposal essentially involved the division of its activities in India into two companies--one with a foreign equity holding of 40 percent, and the other with 100 percent foreign equity.

The proposal envisaged segregation of the activities of its four data centers, located in Bombay, Calcutta, Madras, and New Delhi, from the rest of the business activities. The data centers were to be incorporated into an Indian company in which IBM's equity would be 40 percent. These data centers were equipped with IBM equipment and provided facilities and services to a large number of users, whose requirements did not justify the leasing or outright purchase of a data processing system. The employees involved with these data centers were to be transferred to the new company. The proposed 40 percent IBM equity participation would ensure the continuity of business activities and facilitate the transfer

of employees. This aspect of IBM's proposal was in conformity with FERA guidelines.

The 100-percent foreign equity company, proposed by IBM, would engage in exports, the supply of computer systems, and the provision of services. IBM proposed to convert its existing manufacturing activity into 100-percent export by March 1978. In addition, IBM planned to export a contemporary-technology computer peripheral and to diversify the range of its exports of parts, sub-assemblies, and accessories. An export target of \$11.25 million per year was set, and the "added value" in India was expected to exceed 55 percent. IBM intended to continue its local supplier development activities in an effort to maximize indigenous content and technology transfer.

Recognizing considerable software development and computer systems consulting skills in India, IBM proposed to establish a Competence Center in India to undertake such projects for export. IBM planned to develop software and provide high-skill services, such as systems engineering and education to overseas IBM companies and their customers, primarily in South East Asia. An export target of \$1.125 million per year was set. The "added value" in India was expected to exceed 90 percent, owing to significant contribution of professional skills, rather than materials, to such projects. IBM was prepared to sub-contract a substantial part of software development work related to export projects to assist in the enhancement of computer systems in India.

IBM requested permission to sell imported computer systems in India through its Indian subsidiary, where user requirements could not be fulfilled by indigenously manufactured equipment and where a demonstrated

need existed to import equipment. The GOI had evolved comprehensive procedures to procure such equipment. It was expected that imported computer systems would be installed in key sectors of the economy--in priority industries like steel, energy, transportation, and defense. These computer systems were required to assist in the national research and development effort.

IBM's intent here was to maximize the quantum of effort in India. Professionals from IBM-India were to perform tasks such as evaluation of equipment requirements, computer system configuration, software selection, proposal preparation, user education, pre-installation planning, systems engineering assistance, installation, equipment warranty, and post-warranty services. Only manufacture and shipment of the equipment would require overseas support. Consequently, the rupee (Indian currency unit) element of the price would have been significant and scarce foreign exchange would have been saved. Foreign exchange remittances would have been restricted to only that component of the price designed to reimburse the manufacturing plants for the computer system and its spares.

Under the proposed method, foreign exchange remittances were expected to reach approximately 40% of the comparable remittance if the computer system was directly procured overseas. Furthermore, the principal profits from such a system sale would have accrued to IBM-India, and, consequently, would have generated additional tax revenues for the Indian exchequer.

To ensure conformity with FERA, IBM offered to phase out its leasing activity by selling equipment on lease to Indian users at a reduced

price and then to cease leasing equipment. Prior to that time, revenues from leasing had constituted approximately 50 percent of IBM-India's gross revenues. Furthermore, IBM offered to terminate the manufacture of data processing equipment for the local market by March 1978 and to restrict its manufacturing operations henceforth to 100-percent export.

In addition, IBM offered to make available its patents to Indian organizations and to establish facilities for the assembly and computer testing of integrated circuit cards. Moreover, they proposed to establish a laboratory for the measurement and analysis of electrical and electronic components and to establish a Scientific Center. This Scientific Center was to be equipped with a large computer system, provided by IBM, and staffed by scientists from the government, universities, research bodies, and IBM. The proposed Indian Scientific Center would undertake research projects in the areas of flood control or analysis of remotely sensed data transmitted by the earth's resources satellite on geology, mineral exploration, forestation, etc. This would assist the GOI in developing and exploiting natural resources.

Lastly, IBM requested the non-exclusive right to offer maintenance services to existing and potential users of IBM equipment. Maintenance service was considered an important marketing advantage and the most important reason why customers bought IBM equipment. However, this request was in conflict with the Computer Maintenance Corporation, set up by the GOI, to undertake maintenance of all imported computer systems except those maintained by the users themselves. Once the Computer Maintenance Corporation was set up, maintenance would no longer be considered a sophisticated or high technology activity. As a result,

permission could no longer be granted to a 100-percent foreign equity company to undertake this activity.

The IBM proposal was submitted to the GOI in April 1976 and vigorously followed up by the staff of IBM-India during the ensuing months. However, the Chairman of the IBM Corporation did not participate in any of the negotiations. The proposal underwent the scrutiny of the FERA Committee, under the chairmanship of the Secretary of the Ministry of Finance, Department of Economic Affairs.

Reserve Bank of India Final Determination--Initially it appeared as though IBM's proposal was viewed in a favorable light. The first contact with the Prime Minister's office was made in April 1977, when IBM officials received a favorable reception. However, in July 1977, a meeting with Prime Minister Morarji Desai revealed that no exception in IBM's case was possible. The decision was formally communicated to IBM in November 1977. IBM received the final order from the Reserve Bank of India to reduce its foreign equity holding to 40%, as per the FERA guidelines, in order to continue its business operations in India.

Rather than allowing minority Indian shareholding in its manufacturing, sales and maintenance operations, IBM Corporation reluctantly decided to phase out its operations from India in November 1977. In order to ensure continuity of service to its customers, IBM entered into an agreement with Computer Maintenance Corporation, selling it all IBM parts used in maintenance, and all the tools and test equipment. Another group of 200 employees set up a private limited Indian company-- International Data Management Private Limited, and bought all the computing centers and card manufacturing facilities from IBM. IBM ceased operations in India on May 21, 1978.

The Changing Scene

In recent years, the GOI has set new priorities with regard to the development and modernization of Indian industry through rapid development of the electronics sector in general, and the computer industry in particular. The new computer policy, which features import liberalization and other radical measures, was announced on November 19, 1984.⁶

The first objective of the new rationalized computer policy, initiated by the Department of Electronics (DOE), enables the manufacture of computers in India, based on the latest technology, at internationally-competitive prices. The objective is to progressively increase the indigenous content of these computers. The second objective is to simplify existing procedures to enable the computer users to obtain computers that meet their requirements, either from indigenous sources or from overseas. The third objective is to promote the appropriate applications of computers, which are the catalysts for overall economic and industrial development.

Specific measures to broaden the production base include reduction of duty on certain raw materials for the production of peripherals from 75 percent to 5 percent. Imports of know-how and design, drawings for the production of computers, computer-based systems and peripherals, have been liberalized. The duty on peripherals not indigenously available and not likely to be available in the near future, has been reduced from 75 percent to 25 percent. The production of systems and sub-systems, on an OEM basis, has been encouraged to achieve higher scales in production. Restrictions on production capacity have been removed, and up to 40 percent foreign equity participation has been permitted to attract firms with the latest computer technology.

Import procedures have been simplified to reduce delays in the procurement of computer systems not currently manufactured in the country. The duty on computers not available in the country has been reduced from 135 percent to 60 percent. However, a high duty has been proposed for user organizations that wish to import computer systems of a capacity similar to those available in the country.

As a result of this policy, India, which is one of Asia's biggest computer markets, spent approximately \$255 million on data processing equipment last year, and the market is estimated to grow to \$1.4 billion by 1990. Both the current size and future growth prospects of the computer market in India have attracted a large number of overseas manufacturers. Moreover, production in the computer, control and instrumentation sector of the electronics industry has risen from a level of Rs. 3290 million (approximately U.S. \$300 million) in 1983 to Rs. 4270 million (approximately U.S. \$400 million) in 1984, registering a growth rate of about 30 percent.

Estimates of annual production, sharing between public and private sector, and requirement of capital goods investment for electronics during the Seventh Five Year Plan are indicated in Tables 1 and 2. A total outlay of Rs. 1056 million (approximately U.S. \$100 million) for DOE programs has been approved against a proposed outlay of Rs. 2576 million (approximately U.S. \$225 million). A firm step will be taken towards futuristic technology programs through the Fifth Generation Super-Mini Computer Design Program and the Computer Mainframe Program.

The total production of electronics in India in 1984 was of the order of Rs. 18,900 million (approximately U.S. \$1,800 million), compared

to Rs. 13,600 million (approximately U.S. \$1,300 million) in 1983, and Rs. 12,050 million (approximately U.S. \$1,200 million) in 1982. The growth rate of production in the electronics industry climbed from a modest 12.9 percent during the previous year to a substantial 39 percent. Sector-wise production of electronics during the previous three years is given in Table 3.

The electronics industry in India has grown through domestic demand as well as the import substitution effort. However, increasing emphasis is now being placed on creating exportable surpluses and promoting electronic products and services in overseas markets. Details of the number of units approved during 1984 and investments and anticipated exports likely to be generated during the subsequent five years are indicated in Table 4.

Eighty-four proposals for import of computers, costing more than \$50,000, were approved during the calendar year 1984. Major applications for which these computers were cleared for import included process control, data acquisition, computer aided design and management, message switching, research and development, meteorology, railway freight and reservations, defense, and space research.

Some of the major projects supported by the DOE include computerization of passenger reservations and freight information systems for the Indian railways. Suitable computers and computer-based systems have been recommended for the steel information system of the Steel Authority of India and the automation system for the seventh blast furnace of the Bhilai Steel Plant. In the oil sector, the evaluation of the computer system requirement by the Oil and Natural Gas Commission for seismic processing activities has been completed.⁷

Recent events which have triggered IBM's reentry into the Indian market include the signing of a Memorandum of Understanding between the U.S. and India, which has reassured the U.S. government that India would not pass imported U.S. technology on to Russia. Further, the restrictions by the GOI against foreign firms, which led to the withdrawal of IBM from the Indian market in 1978, have been eased.

Other changes that have led to the formulation of new priorities and the modification of past policies include the plunging U.S. dollar, which increases the international competitiveness of U.S. manufactured goods. The saturation and slump in the U.S. computer market and the maturing of some overseas computer markets, have induced computer manufacturers to seek new overseas markets for both offensive and defensive strategic purposes.

The availability of a vast pool of skilled labor and software skills at relatively low wages has led many computer manufacturers to consider setting up manufacturing facilities in India to serve both domestic and export markets in the region.

In response to the above trends, IBM has reentered the Indian market and captured some lucrative contracts. In recent months, IBM, working offshore Australia, has secured contracts for computer systems for the Indian railroads, oil and gas consortium, and set up a national data communications network.

The first contract IBM signed was with the Oil and Natural Gas Commission for the System 4300. This award was made by the Department of Trade and Industry, the same agency that was responsible for IBM's withdrawal from India in 1978.

Three IBM-4300 host computer systems have been selected for the INDONET project, India's largest integrated data network, in view of the high priority assigned to INDONET for software export. These three machines have been ordered for centers in Bombay, Calcutta, and Madras. This network is expected to stretch out over another 27 nodes and a possibility of further contracts for IBM.

IBM has also finalized contracts for India's train reservation system, which is being developed by the Computer Maintenance Corporation and is based on IBM-4300s. One system has already been delivered and another seven are on order.

Other organizations have opted for IBM equipment. The private-sector computer company Tata Burroughs and Computer Maintenance Corporation have each ordered a System 4300. An IBM System 38 is being installed at Bombay's National Hospital, and a System 3083 is being delivered to the Fireman's Fund Insurance Co. in Madras.

Finally, the computerization of Indian banks, all of which are nationalized, is another vast project that IBM is pursuing vigorously. IBM is bidding on all three levels of the envisioned system--branch, regional, and head office. About 6,000 branches are involved, and the GOI has already issued implementation deadlines and encouraged banks to buy equipment tailored to a common specification. Here too, IBM has a head start since the tender calls for twenty-five main frame "IBM 4381-type machines."⁸

Despite speculation to the contrary, at the present time IBM insists that its activity in India is limited to off-shore marketing, and that

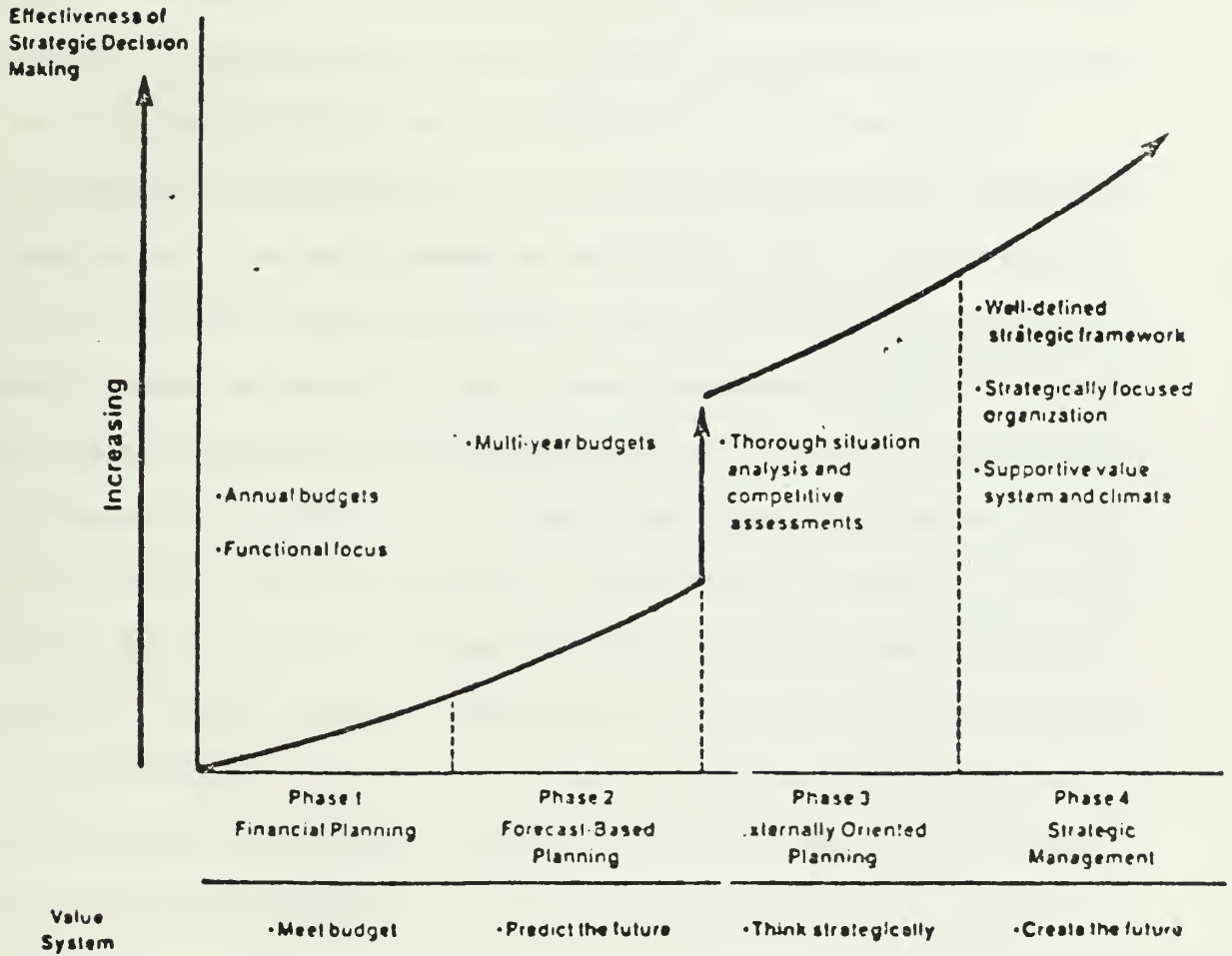
it has no plans to change its mode of operation. However, IBM has certainly responded to what it perceives to be changes in the policies of the GOI, which seeks to develop indigenous computer expertise while maintaining self-reliance and control over its resources. The declining value of the U.S. dollar has increased the international price competitiveness of IBM and other U.S. manufacturers. The slump in the computer industry in the U.S. and the maturing of the computer industry in Western markets, have motivated U.S. computer manufacturers to search for new, large and rapidly growing computer markets. Only time will tell whether the present reunification process will culminate in IBM resuming manufacturing operations in India.

Summary and Implications

The withdrawal of IBM from India in 1977 and the reinstatement of a close working relationship in recent months are a clear illustration of the changing relationship between multinational corporations and host country governments. The relative bargaining position of both multinational corporations and host country governments and their policy and strategic response modes are affected by changes in the international business environment. This study of the IBM withdrawal from India in 1977 and its reentry in recent months stresses the importance of change in the international business environment in explaining the policy and strategic response modes of multinational corporations and host country governments.

The increasing complexity of business problems and the pace of change in the international business environment should induce multinational corporations to move up the strategic planning continuum, set

FIGURE 1
 PHASES IN THE EVOLUTION OF STRATEGIC DECISION MAKING



Source: F. Gluck, S. Kaufman and A. Walleck, "The Four Phases of Strategic Management," The Journal of Business Strategy, Vol. 2, No. 3, Winter 1982, pp. 9-21.

forth by Gluck, Kaufman, and Walleck.⁹ The four phases in the evolution of strategic decision making are depicted in Figure 1. As indicated there, the purpose of financial planning (phase 1) is to meet the budget, and that it involves annual budgeting and a functional focus. The purpose of forecast-based planning (phase 2) is to predict the future which involves multi-year budgets, strategic gap analysis, and a "static" allocation of resources. Strategic thinking is the purpose of externally oriented planning (phase 3). This stage requires a thorough situation analysis and competitive assessment, evaluation of strategic alternatives, and "dynamic" allocation of resources. Finally, the purpose of strategic management (phase 4) is to create the future through a well-defined strategic framework, a strategically focused organization, widespread strategic thinking capability, a coherent reinforcement of management processes, and a supportive value system and climate.

Much of the strategic planning of American, European, and Japanese multinational corporations is concentrated on phases 1 and 2.¹⁰ Only to a limited extent do Japanese multinational corporations undertake planning at phase 3, involving environment scanning and a competitive assessment.¹¹ By and large, planning has been used as a control device rather than as an assessment of the future.¹²

Overall, multinational corporations have not paid much attention to environmental scanning. For example, Keegan, in his interviews with 50 executives of 13 U.S. multinational corporations, reported that very few companies were using systematic methods for information scanning. "Computer-based systems were not found...and even traditional manual systems of information retrieval were hardly significant as factors in

day-to-day information gathering." The majority of the companies used personal sources ("word of mouth"), for gathering environmental information.¹³

Similarly, Fahey and King's study of 12 large American firms revealed that environmental scanning was not a well-established corporate function. Their other conclusions were (1) environmental scanning was not a well-established corporate function; (2) very few companies gathered useful information on political regulatory conditions; and (3) most of the firms relied on ad hoc methods.¹⁴

Given the dynamic international business environment we face today, multinational corporations need to make a quantum leap from financial planning (phase 1) and forecast-based planning (phase 2) to externally-oriented planning (phase 3), and move towards strategic management (phase 4). Strategic planning in multinational corporations should begin with a thorough situation analysis of the business environment, the competitive situation, and competitive strategies. The strategic plans of multinational corporations should include in-depth analysis of these factors while keeping track of trends and changes in the international business arena through environmental scanning.

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APPENDIX A

IBM's Activities in India

<u>Date</u>	<u>Activities</u>
1955	IBM first opened offices in India.
October 1967	Industrial license (IL) for 1401 series computers received.
April 1968	Application for IL to manufacture 67 System 360 computers submitted. GOI questioned IBM's policy of operating on wholly-owned basis.
May 1968	IBM Vice President explained IBM's policy to GOI. IBM offered to have Advisory Board in IBM-India operations. IBM volunteered to retain 40% of ATN profits for reinvestment in India during the IL period.
September 1968	Modified proposal for Systems 360, submitted in line with customer demands for equipment. Proposal covering specialty electric motors, wire contact relays, cables and cable harnesses submitted. IBM VP explained that capital participation is not possible because of implications of its worldwide activities. IL for Systems 360 not forthcoming.
January 1969	IBM offered to submit a phased manufacturing program within six months of receipt of Industrial License. IBM offered to re-export all 360 equipment and manufactured goods in the event the manufacturing program is not accepted. IBM World Trade Corporation's Chairman offered two overseas research scholarships per year to Indian nationals. Two research scholarships granted in 1969. Indigenous content in 029 punch machine, manufactured for export, rose to 57%.
October 1969	IBM VP offered complete technical data, diagrams, and possible indigenous content specifications to Indian vendor nominated by GOI. IBM offered to manufacture special air defense computers in India by sub-contracting activity to Bharat Electronics, Ltd., a GOI undertaking. IBM offered to reduce its export utilization and to contribute 15% thereof to India's foreign exchange reserves.

IBM's Activities in India
(continued)

<u>Date</u>	<u>Activities</u>
January 1970	IBM offered to manufacture specified ancillary computer units for sale to Indian organizations for incorporation in computers manufactured by them. IBM advised GOI it was exploring manufacture of typewriters in India for export. Despite repeated offers, clarifications, supplementary offers, IL for Systems 360 did not materialize.
January 1, 1974	GOI introduced Foreign Exchange Regulation Act (FERA). All trading companies engaged in purely commercial activities and manufacturing enterprises using "non-sophisticated" technology required to reduce foreign equity to 40%. "High technology" companies, using "sophisticated" technology and/or engaged in "special" activities as designated by GOI, permitted to retain foreign equity holding of 74%. Multi-activity companies, engaged in both sophisticated technology fields and other commercial and trading activities, permitted to retain foreign equity holding of 51%. Enterprises engaged purely in export activities permitted to have foreign equity holding of 100%. FERA only applied to firms already established in India. GOI rendered decision on nature of technology used solely on basis of India's capabilities and needs.
November 1975	IBM received official notification from Reserve Bank of India (RBI) requiring it to dilute its foreign equity to 40% within 2 years.
April 1976	IBM submitted formal counter-proposal involving the division of its activities in India into two companies, one with a foreign equity holding of 40%, and the other with 100% foreign equity.
April 1977	First contact with the Prime Minister's office made by IBM officials. Favorable reception.
July 1977	Meeting with Prime Minister Morarji Desai. No exception to FERA possible in IBM's case.
November 1977	IBM received final order from RBI to reduce foreign equity holding to 40% as per FERA guidelines to continue business operations in India. IBM reluctantly decided to phase out its operations in India.
May 21, 1978	IBM ceased operations in India.

TABLE 1

Estimates of Yearwise Electronics Production Envisaged
During the Seventh Plan 1985-90 (in Rs. million)

S.No.	Sector	1985-86	1986-87	1987-88	1988-89	1989-90	Total
1.	Components	4800	8700	9700	14000	21000	56200
2.	Consumer Electronics	7300	9000	12000	15500	20000	63800
3.	Communication	6000	9000	13300	20500	31000	80000
3.1	Broadcasting	800	1000	1400	1900	2400	7500
4.	Aerospace & Defense	3750	4150	4800	5100	5400	23200
5.	Central Instrumentation & Industrial Electronics	6000	7800	10600	14600	20100	59100
6.	Computers & Office Equipment	2000	2900	4300	6500	8700	24400
Total		30650	40550	56300	78100	108600	314200

Source: Department of Electronics, Government of India. Annual Report 1984-1985.

TABLE 2

Estimated Production/Investment Sharing Between
Public Sector and Private Sector 1985-90 (in Rs. million)

S.No.	Sector	Public			Private		
		Percent- age	Produc- tion	Invest- ment	Percent- age	Produc- tion	Invest- ment
1.	Components	40	22480	3200	60	33720	4800
2.	Consumer Electronics	20	12760	400	80	51040	1100
3.	Communication	80	64000	6000	20	16000	1500
3.1	Broadcasting	90	6750	450	10	750	50
4.	Aerospace & Defense	90	20880	2400	10	2320	300
5.	Central Instrumenta- tion & Industrial Electronics	40	23640	2230	60	35460	2230
6.	Computers & Office Equipment	30	7320	1100	70	17080	1100
Total			157830	15800		156370	11100

Source: Department of Electronics, Government of India. Annual Report 1984-1985.

TABLE 3

Production of Electronic Equipment and Components
(in Rs. million)

S.No.	Sector	Calendar Year Production		
		1982	1983	1984
1.	Consumer Electronics	3370	3300	5870
2.	Communication & Broadcasting Equipment	2550	2700	3205
3.	Aerospace and Defense Equipment	1085	1260	1490
4.	Computer, Control and Instrumentation	2420	3290	4270
5.	Electronic Components	2140	2300	3030
6.	SEEPZ	485	750	1035
Total		12050	13600	18900

Source: Department of Electronics, Government of India. Annual Report 1984-1985.

TABLE 4

Investment In Capital Goods and Estimated Export Earnings
in Next Five Years (100% Export Units Approved During 1984)

S.No.	Sector	No. of Units	Investment in Capital Goods (in Rs. Millions)	Estimated Export in Five Years (in Rs. Millions)
1.	Consumer Electronics	2	5.25	130.47
2.	Computer Control and Instrumentation	5	22.00	1502.74
3.	Communication and Equipment	1	2.68	1266.50
4.	Components	15	171.21	2914.59
5.	Computer Software	13	204.25	1484.37
Total		36	405.39	7298.67

Source: Department of Electronics, Government of India. Annual Report 1984-1985.

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