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The Economic Impact of MNCs in Developing Countries: A Case study of Zambia.

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ABSTRACT: Multinational corporations (MNCs) are enterprises that have business operations in two or more countries. They deliver services or manage production establishments in more than one country. MNCs conduct a significant proportion of their operation in developing countries and thus, they can have an impact on the economies of these countries. The debate of whether MNCs help or harm the economies of developing host countries is as old as the existence of multinational corporations and will be discussed in this paper. To acquire a better understanding of the subject matter, a definition of MNCs has been given. The paper will discuss the historical evolution and characteristics of MNCs, their theoretical framework, and their structure. It will also evaluate the positive and negative impacts of MNCs on the economies of developing countries. Additionally, the case study of Zambia is discussed to observe the pattern of economic impact brought about by MNCs.

Keywords: Multinational corporations, developing countries, positive impact, negative impact, economy.

1. INTRODUCTION

Multinational Corporation (MNC) is a term synonymous with world trade today, and it refers to an enterprise whose business activities are spread in more than one country (Ghani, 2015), having their original base in more developed countries like Britain, USA, China and Japan. Examples of MNCs include Nike, Sony, Apple, Toyota, Coca-Cola and all these have investments and operations in developing economies (Rahman, 2009). The goal of MNCs in expansion into developing countries is profit maximisation and the developing economies have favourable conditions to facilitate this. MNCs venture out into developing economies because of various advantages such as cheap labour and production costs, availability of natural resources, lower tax rates and tax exemption that are offered for specified periods (Ghani, 2015). Additionally MNCs also recognise the increase in consumer demand for various products and services and move into developing economies to increase their market base.

The developing host countries also seek to attract investment from MNCs as these countries have insufficient funding to drive holistic economic development. Host countries benefit from FDI, job creation, skills development and technological transfer brought about by MNCs.

However, the operations and benefits of MNCs in developing countries have been questioned owing to the negative impact that some MNCs have had on developing countries. These corporations have been seen to exploit developing nation's workforce, natural resources and exert undue political influence over governments (Jiboku, 2018). A country's economic development is measured using various economic indicators such as Gross Domestic Product (GDP), employment, Capital inflow and outflow, Skills development technological advancements among others. We will thus use various economic indicators to assess the impact of MNCs on developing economies. The paper through a selective analysis of a few MNCs operating in Zambia will determine the impact of MNCs in developing countries.

1.0 Objectives of the Study

The main aim of this study is to find out the Economic impact of MNCs in developing host countries. The paper will assess the positive and negative economic impact of MNCs on developing countries. The study will analyse the impact of MNCs on various economic indicators such as Gross Domestic Product (GDP), employment, capital inflow and outflow, and

technological development. To gain a better understanding of the impact of MNCs on developing countries, a case study of Zambia is discussed. Additionally, the paper will highlight the role of Governments in mitigating or eliminating the negative effects of MNCs.

2 LITERATURE REVIEW

2.1 Developing Countries

Developing countries are defined as nations having low levels of industrialization, high unemployment, minimal capital equipment in addition to simple production technology (Muthon, 2012). According to (Kuepper, 2021), a developing country is one that has low human development index and an underdeveloped industrial base, in comparison to other countries. Developing countries have low levels of economic development, which leads directly or indirectly to economic, political, social, and environmental challenges that significantly impede quality of life in that country.

According to (World Population Review, 2021), a total of 137 countries are categorised as developing economies. The United Nations uses a metric known as Human Development Index (HDI) to determine whether a country is developed or is developing. The HDI takes into account a number of factors, including economic growth, education, health, life expectancy, and quality of life. The highest possible HDI score is a 1.0 and a nation that scores less than 0.80 is considered developing. Another criteria that can be used to ascertain if a country is developed or is developing, is the Gross National Income (GNI) per capita. The GNI is used to estimate a country's standard of living. Zambia is one such country that meets the criteria of a developing nation.

Developing countries have insufficient funding to finance economic development in their countries, and thus the need for foreign direct investment. Foreign governments can only provide little of this funding. Therefore, developing countries seek to obtain private foreign investment via MNCs, so as to improve their economic wellbeing and increase the standard of living for its citizens.

2.2 Multinational Corporations (MNCs)

Multinational corporations (MNCs) are defined as firms which are incorporated in one country but which own, control, or manage production and distribution facilities in several countries (Ayesha, 2021). Many multinational corporations are based in developed countries and have extended their business operations to developing countries. MNCs may acquire financial capital from one country, raw materials from another, produce goods and services in another and sell their outputs to various countries (Nyirongo, 1995).

The history of MNCs is traced back to the history of colonialism. Many of the first MNCs were formed at the will of European monarchs in order to conduct expeditions. A number of the colonies that were not held by Spain or Portugal were under the administration of some of the world's earliest MNCs (Ferdausy, 2009). One of the first MNCs was the British East India Company (1600 – 1874), which ventured into international trade and exploration, and run trading posts in India (ECI, 2021).

In today's era, examples of current leading global MNCs include Walmart, Sinopec group, China National Petroleum and Royal Dutch Shell (Fortune, 2021). MNCs are generally larger and more productive than local companies, and are usually willing to invest in local markets (Resnick, 2014). A significant number of MNCs began their operations in developing countries by the 1990s.

2.3 Positive Impacts of MNCs

MNCs facilitate foreign direct investment to developing countries which is essential for economic growth. Foreign direct investment provides surplus funding to compensate for the insufficient foreign aid and government local savings (Ferdausy, 2009). MNCs also bring with them the wealth of knowledge and skills to host countries. Employees from host countries get to learn from highly experienced staff from MNCs. MNCs ensure that its workers in foreign countries are well trained so as to increase productivity (UKEssays, 2018). Similarly, MNCs facilitate technological transfer to developing nations. MNCs allow developing countries to benefit from huge research and development funds that go towards technological advancements.

MNCs create employment in developing countries and thus increase the standard of living for workers in that country. According to (Ferdausy, 2009) MNCs tend to pay even better wages than local firms. For example a study in 2001, found that MNCs paid 70% more for white-collar

workforce and 33% more for blue-collar workforce than locally owned companies in Indonesia. Additionally, MNCs support exports of the developing countries and lessen import dependence as the host countries are able to produce needed goods and services. This promotes industrialization and efficiency and consequntly reduction in the cost of goods and services. Thus an increased number of people are able to access the needed good and services (UKEssays, 2018).

2.4 Negative Impacts of MNCs

Since the inception of the year 2020, the world has faced a global pandemic 'corona virus' which has impacted numerous countries worldwide. In an effort to contain the spread of this pandemic, lockdown measures between borders have been enforced (Lora Jones, Daniele Palumbo & David Brown, 2021). Consequently developing countries and MNCs that depend on commodity exports and tourism have been negatively impacted. Imports and exports for MNCs in these developing countries has been restricted thus affecting business operations and causing loss of jobs for workers in these countries.

Some MNCs have been criticized for their labour practices in foreign countries. For example, South Africa has recently taken Huawei's local unit to court over employment rule breeches. According to (Nqobile Dludla , 2022) China's Huawei employed approximately 90% foreign nationals against 40% as permitted by regulations.

MNCs because of their sheer size have caused environmental damage in developing nations (Ferdausy, 2009). Multinational oil companies have been criticised for widespread pollution in developing countires such as Nigeria and Indonesia. In a bid to attract foreign investors, developing nations have lessened their regulations. Consequently MNCs have been exempted from certain legal obligations which may control or stop their activities which could be environmentally destructive. (Ferdausy, 2009) states that MNCs in developing countries also cause an outflow of capital through profits, debts, royalties and through manipulation of export and import prices. Critics argue that MNCs may have return flows that are unjustifiably high.

2.5 Theoretical Framework of MNCs

The structure and operative orientation of MNCs is dicussed using the following theories:

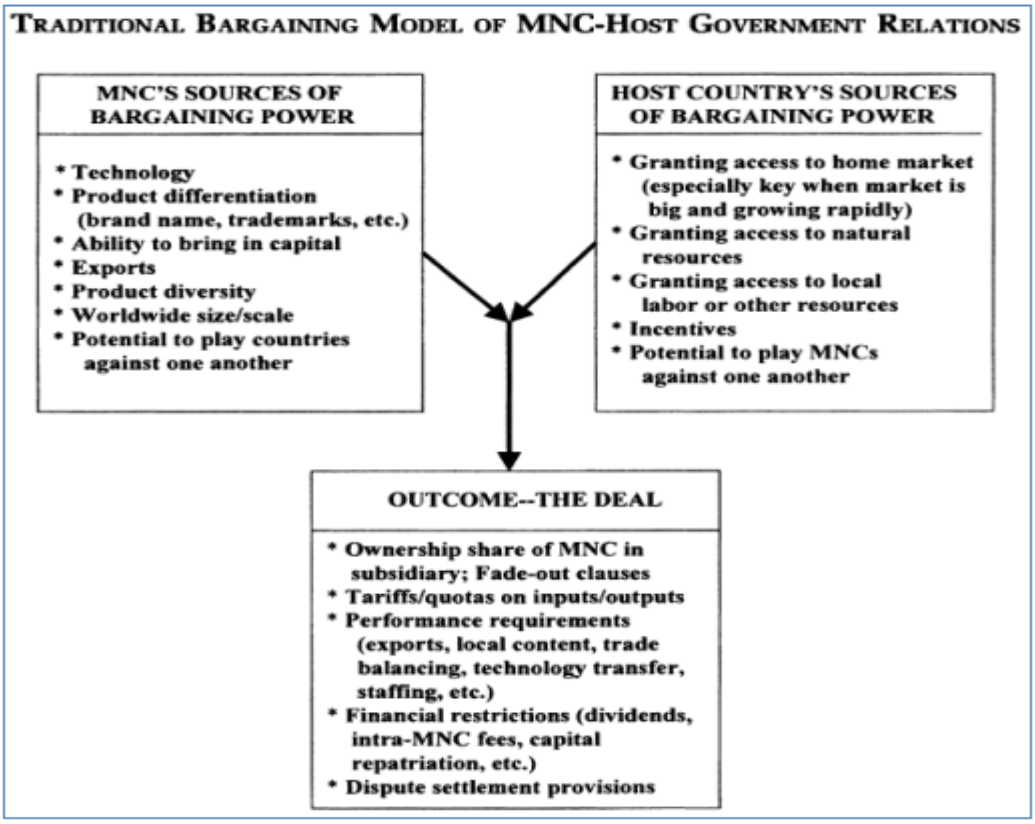
2.5.1 Oligopoly Theory

The Oligopoly theory seeks to explain why compannies transform into multinational corporations. Any firm through its technology, market expertise, managerial and production skills can venture abroad to exploit the power of monopoly. This theory asserts that few producers through extensive marketing and advertising strategies can monopolize their goods (Ghani, 2015).

2.5.2 Obsolescing Model

This model was developed in 1977 by Raymond Vernon and it explains the shift in bargaining relations between the host country and the MNC. The model states that the initial bargaining power sits with the MNC but gradually it then favors the host country. At the starting point MNCs due to its advanced technology, expert employees, and ready access to markets have an upper hand; but as the investment is made the bargaining advantage shifts towards the host country (Ghani, 2015). The figure below shows the traditional Bargaining model of MNC-Host Governement Relations.

Figure 1: Traditional Bargaining model of MNC-Host Governement Relations.



Source: (Zulu, 2014)

2.5.3 The Product Cycle Theory

This theory developed by Raymond Vernon seeks to explain the partern of international trade. The product life cycle refers to the stages of a product's life span, that is, the length of time a product is introduced to consumers into the market until it's removed from the shelves. This theory asserts that newer, more successful products push older ones out of the market (Ghani, 2015).

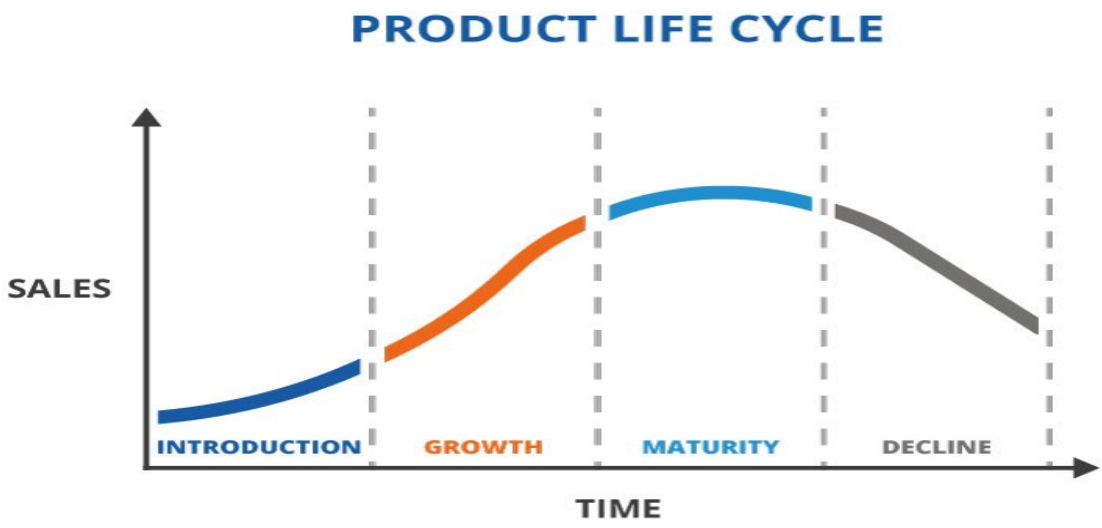
According to (Indeed, 2021), the Product Cycle Theory can be illustrated by the following stages of production:

1. First stage of production is the introduction stage when new product is introduced that is exported abroad to economies which have local needs and demands.
2. Second stage of production is the growth stage. A product manufactured in the country of origin after the maturity tends to move the production centers to other countries with cheaper cost of production.

3. Third stage is the saturation stage where the sales of the product reach a limit where there is no or little possibility to increase sales.
4. The last stage is the decline stage which is evident in underdeveloped and developing and countries where goods are exported abroad due to lack of consumers and markets.

The diagram below stages of the product life cycle.

Figure 2. Product Life Cycle (TWI, 2022)



Soruce: https://www.twi-global.com

2.5.4 The Tariff Jumping-off Hypothesis

This hypothesis asserts that MNCs use FDI as a tool to jump over tariff or nontariff barriers of the host countries. This trend was observed as the Japanese and US MNCs invested in UK and Ireland to jump over tariff barriers and to get ready access to western European markets.

2.6 Structure of MNCs

The various structural patterns of MNCs are highlighted below:

- **Horizontally Integrated MNCs:** MNCs that manage production sites located in several countries producing same or similar products.

- **Vertically Integrated MNCs:** MNCs that manage production sites in several countries to manufacture products that are used as inputs in other production sites of the world for producing finished goods.
- **Diversified MNCs** MNCs that do not manage production sites located in several countries that neither falls in the category of vertically nor horizontal integrated MNC (Ghani, 2015).

2.7 A Case Study of Zambia

2.7.1 MNCs in Zambia

A large number of multinationals, over the years, have extensively invested in Zambia. Some of largest companies operating in Zambia are MNCs. These include Lafarge (manufacturing), Shoprite (retail group), Standard Chartered Bank, Airtel (mobile telephony), ZCCM Investments Holdings plc (copper mining) and Konkola Copper Mines, a subsidiary of the international mining group Vedanta (Network, 2020). Historically, MNCs focused on extractive and primary industries such as Copper minning undertaken by ZCCM and plantation activities. Currently MNCs are investing in other sectors: Manufacturing, Technology industry and Banking among others.

2.7.2 Investment Climate

The Zambian economy is an an era of economic liberalisation. The government has been creating a conducive environment to attract investment opportunities. One push for MNC investment stems from the fact Zambia in the recent years has faced budget deficits annually (O'Neill, 2021). The presence of budget deficits implies that the government does not have enough funding to support economic development in the country, and thus the need for FDI. Consequently, Zambia has resorted to sale of some government assets (privatization) to MNCs as they possess skills and capital required to efficiently run them.

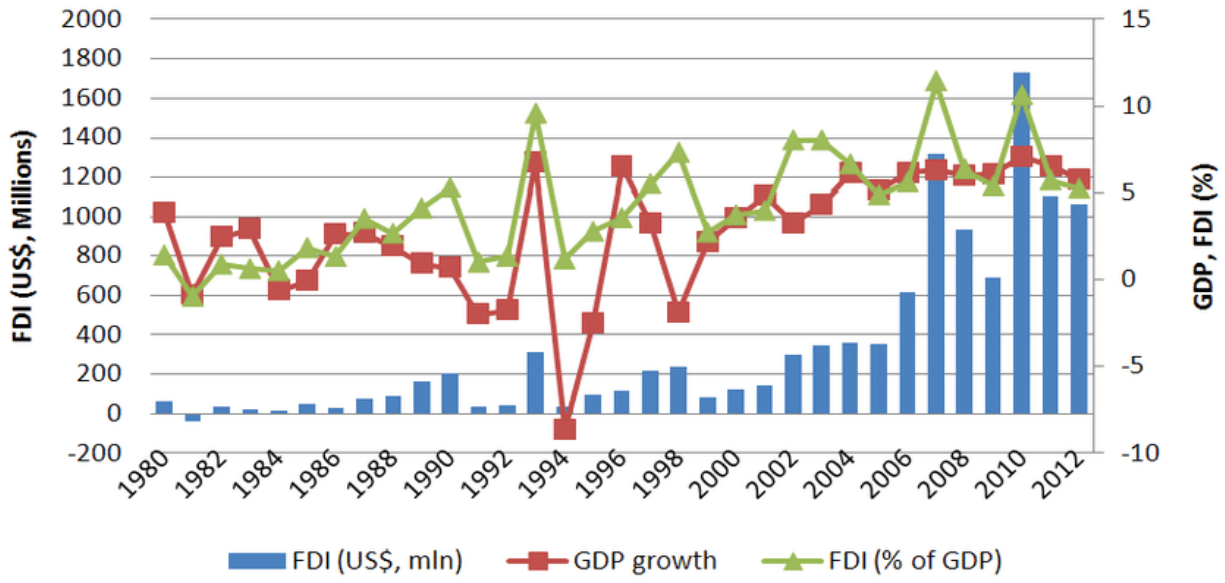
The country Zambia is particularly attractive for investment as it has no tight regulations and unncessary redtapes on the flow of capaital in and out of the country. The developing country also has availabilty of cheap labour. Additionally, there is a good market base for MNCs in the developing country Zambia, owing to increase in consumer demand for various goods and services. The favourable market base also stems from the multinational company mindset' that the elite and the upper middle class have. With this mindest they prefer purchasing products with an attached 'foreign product' due to perceived durability or quality. The availability of the

country's resources such as copper minerals also attracts MNCs. The MNCs seek to use the natural resources as raw materials in the manufacturing plants, or to produce goods and generate huge revenue from these investments (Ghani, 2015).

2.7.3 Impact of MNCs

The figure below illustrates that over the past years from the period of 1990 to 2015, Zambia's FDI generally, has been directly proportional to the to GDP growth. Gross domestic product (GDP) is the total market or monetary value of all services and goods produced within a country's borders in a specific time period, and thus an economic indicator of economic power (Statista, 2022). Thus, it can be concluded that MNCs contribute to economic development via GDP growth. More specifically, foreign investment enables developing countries to buy imports. The figure below shows the GDP and FDI trends in Zambia from 1980-2011.

Figure 3: GDP and FDI trends in Zambia from 1980-2011



Source: (Mahembe, 2022)

However, FDI through privatisation has been seen as an obstacle to development by some. For example, Technological institutions may be denied the opportunity to invest and grow in research when high capital MNCs take over technological research and development. Privatisation effectively transfers some of the developing countries capital resources to an MNC. This relinquishes government roles in a country, as MNCs are left to continue with their activities with little or no control (Nyirongo, 1995).

The presence of MNCs in Zambia has facilitated technological development in the country Zambia. The state has benefited from the research and development carried out by the multinationals. Huawei is an example of a Chinese multinational technology corporation that has invested and spearheaded technological advancements in the Information and Communications Technology in the developing country Zambia (NGWATO, 2020). A technological milestone the giant Tech Huawei has facilitated in the country Zambia is the introduction of 5G Mobile Network. This New generation of Technology would not have been made accessible at this particular time without the presence of the MNC in the country.

MNCs have also provided employment in the country Zambia. For example one of the biggest MNCs in Zambia Airtel currently has 319 employees. This number excludes the workers indirectly employed by Airtel via subcontractors (Airtel Zambia, 2022). Although wages seem very low by Western standards, people in developing countries prefer these new jobs as compared to working as a subsistence farmer with even lower income.

MNCs in the country Zambia have been known to negatively impact the environment. This can be seen from an occurrence in 2015, where citizens of the country called for scrutiny of MNCs operating in the mining industry. According to (Pollitt, 2019) “Villagers from the Chingola District of central Zambia have been allowed to pursue their case against UK-based Vedanta Resources in the London courts, after alleging their water supply was polluted by the company’s Zambian subsidiary. The 1,826 citizens of Zambia’s Copperbelt Province claim toxic materials were discharged from the Nchanga Mine into watercourses providing their only source of crop irrigation and drinking water.

3 RESEARCH METHODOLOGY

3.1 Study Design

The primary method for conducting this research is based on the qualitative exploratory method that will explore the existing literature on this topic. There is currently a lot of existing literature pertaining to the subject matter, but to make it unique to the Zambian economy, the case method is applied. Various MNCs operating in Zambia and other developing countries are analsyed to assess the impact of MNCs on developing economies. Additionally, Various economic indicators

or variables such as GDP, capital inflow and outflow, employment and technology development have been used to asses the ecvonomic impact of MNCs in developing countries.

3.2 Data Sources

This study is analytical in nature which is solely based on secondary data. Secondary data has been collected from several sources including relevant books, journals, government reports, newspapers, and websites.

3.3 Data Analysis

To effectively analyse the data obtained, the following theories: Obsolescing Model, Oligopoly Theory, Product Cycle Theory and the tariff jumping-off hypothesis were used to assess the relationship between the various economic indicators or variables, and the presence of MNCs in developing countries. The economic variables used include Capital inflow and Outflow, GDP, Employment and Technological development. Evidence from the case study of the developing country Zambia was also used to provide evidence of the impact of MNCs in Zambia.

4 FINDINGS, DATA ANALYSIS AND DISCUSSIONS

4.1 Findings of Study

A Multinational corporation is defined as an enterprise which controls and manages assets in at least two countries. Typically, such companies consist of separate companies known subsidiaries in different countries, and typically have a centralized head office where they coordinate global management. The majority of large multinational corporations are Japanese, American, or Western European, such as Wal-Mart , Exxon Mobil ,Nike, Coca-Cola, Toshiba, BMW and Honda. Many MNCs are large enough that have annual sales volume that exceeds that of entire GNP of the host countries they operate in (Nyirongo, 1995).

The desire to control resources, in addition to secure access to overseas markets has driven some firms to expand their businesses to developing countries. Other reasons for the expansion of MNCs into developing countries such as Zambia include availability of cheap labour and production.

In their host countries MNCs have been condemned for exerting too much control over local economies and politicians. Developing countries had to compete to attract investment from corporations by eliminating taxes and easing regulations. Additonally local politicians have been seen to often cater to MNCs at the expense of local citizens. Governments of developing countries seek FDI through MNCs with a view of developing their economies, but sometimes at the expenses of natural resources which have been exploited. A case study of Zambia also shows evidence of water pollution from a minning MNC company ZCCM (Shalala, 2017). MNCs have also been found to have poor labour practices such as poor working conditions for its workers and low wages.

However , MNCs have also been benefical to developing countries as they increase the capital inflow through foreign direct investments. Apart from that a great deal of employment opportunities have been created by MNCs. Skills Transfer and Technological Development and positive GDP growth has also been witnessed from the operation of MNCs in the developing country Zambia.

4.2 Data Analysis and Discusson of Results

The drive for firms to expand into developing countries such as Zambia is explained by the Oligopoly theory. This theory explains why firms transform into MNCs and it asserts that a firm through its technological expertise, market expertise, managerial and producton skills can move abroad to exploit the power of monopoly. Another theory that explains the expansion of MNCs into developing countries is the Product Cycle Theory. This theory refers to the length of period a product moves from being introduced into the market until it's taken off the shelves. The Product Cycle Theory is used by firms to make informed business decisions including pricing, cost cutting and promotion to expansion. Company’s are able to predict the results of expanding into a developing country at a particular time of the product cycle (Ghani, 2015).

Obsolescing Model explains why multinationals seem to exert undue political influence over governments and local politicians tend to cater to the needs of MNCs. The model asserts that the initial bargaining power sits with the MNC but gradually it then favors the host country. At the starting point MNCs, due to the advanced technology, expert employees and ready access to markets have an advantage; but as the investment is made the bargaining advantage shifts

towards the host country. Critics assert that although MNCs have influence over politicians, this is counterbalanced by governments' abilities to regulate them. Governments have the power to set the terms according to which the MNCs should operate.

This occurrence of MNCs evading taxes, tarrifs and barriers is supported in the tariff jumping-off hypothesis. This hypothesis asserts that MNCs use FDI as a tool to jump over tariff or nontariff barriers of the host country. MNCs do this with a view of generating more profits. The above theories discussed explians or validates the beahaviour of MNCs in developing host countries.

As can be seen from the findings, MNCs have both positive and negative impacts on the economies of developing host countries. On one hand, MNCs are beneficial to the development of host countries as they facilitate for capital inflow, GDP growth, Job creation, Infrastructure development, technological development among others. On the other hand, MNCs hinder the development of developing countries by channeling excessive returns (capital outflow) outside of the country. Poor labour practices such lower wages also slow down economic development. MNCs have also been found guilty of environmental pollution. Additionally MNCs prevent autonomous development by preventing local companies from participating in dynamic sectors of the economy that have been occupied by them.

As can be seen the impact of MNCs in developing countries varies from country to country, and depending on what economic variables that are being observed. The government of the developing host country has a responsibility to implement policies and regulations that ensure the MNCs do not impede economic development.

5. CONCLUSIONS, AND RECOMMENDATIONS

5.1 Conclusion

In view of the research findings and data analysis, it can be concluded that the economic impact of multinational corporations can either be positive or negative depending on the developing host country and the economic variables being observed.

MNCs play an important role in the developing countries. They facilitate job creation, Skills development and training, and technological transfer. MNCs also contribute to positive GDP growth, capital formation and reduction of poverty.

Nevertheless, MNCs can be guilty of environmental pollution and exploitation of human resource and natural resources. Critics of MNCs allege that MNCs in a bid to lessen their production costs, look for developing countries with flexible environmental regulations, and execute productive activities in those countries that worsen the local environmental problems. The right operating environment for MNCs in host countries is generally difficult to find because of their different objectives. MNCs seek to maximse profits and competiveness, whilst host developing countries seek economic development. Thus host governments need to be proactive and prudent enough to ensure that MNCs operate with little or no negative impact on the economy.

One study established that the impact of MNCs is notably positive in “open” economies, and notably negative in “closed” economies. Other studies show that impact of MNCs is dependent on the effectiveness of domestic industry policies, tax and macroeconomic policies. A World Bank study established that the impacts of MNCs depend on the industry, as well as host country policies (Ferdausy, 2009). It is thus logical to assume that the characteristics of the developing country's industry and policy environment are important determinants of the net impacts of MNCs.

5.2 Recommendations

As an open economy that can not operate in isolation, Zambia will continue to attract capital inflows through Multinational investments. It is thus prudent the state’s government develop policies that will not only attract MNCs but also regulate them to operate according to desirable set standards.

Government should ensure that labour laws which facilitate workers to have acceptable working conditions are strictly adhered to by MNCs. MNCs which fail to adhere to these laws should face heavy fines, which act as a disincentive to breaking the rules. However, a legal system of control is likely to be more effective in a developed, rather than a developing country. More economically developed countries are likely to have greater influence on MNCs, than less

economically developed countries. This is because developing countries may not want to control MNCs because these corporations could be a useful source of FDI. They fear that they might lose out on FDI, and thus an opportunity for economic development, if they control MNCs (Impact-of-Globalisation-on-Local-and-National-Economies, 2021). Nevertheless the the responsibility still remains with state governements to ensure transparency and accountability in their operations with MNCs.

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