THE ART OF INTERNATIONAL NETWORK MANAGEMENT

MANAGING INTERNATIONAL POLICY AND BUSINESS NETWORKS AS A DEVELOPMENT STRATEGY: THE MALAYSIAN EXPERIENCE

Fabienne Fortanier* and Rob van Tulder**

Themes: General Networks; Policy Concerns

Status: workshop paper

Key words: network management, multinationals, development model

---

ABSTRACT

Developing countries are increasingly integrated in international business and policy networks. National development becomes the outcome of international network management - the management of a complex combination of multilateral, bilateral, regional and other policy networks between nation-states, which can imply intensification, but also de-intensification of particular relationships. This 'network perspective' may be the outlook for a pragmatic development strategy, which is able to deal with the increasing importance of multinational companies on the one hand, and on the other hand sustains a national growth path. Traditional development theories focus on national models and usually ignore the importance of both <u>*inter*</u>*national non-multilateral institutions and the strategic choices of multinationals. This paper aims to bring both networks together, and studies the way in which the management of international policy networks influences the type of FDI attracted and its consequent impact on the national economy. Malaysia provides an interesting case study of the way both types of networks can be pragmatically and simultaneously managed. This paper focuses on four different networks the Malaysian government was confronted with since the 1980s: OPEC, the WTO and the IMF regime, ASEAN and bilateral investment treaties. Malaysia does not seem to fit into any orthodox developmental model, but is more instructive than most models previously considered to be best-practice examples of developmental states – such as Japan or Korea – or export models – such as Taiwan or Singapore.*

---

* Fabienne Fortanier – consultant at the OECD, Directorate for Financial, Fiscal and Enterprise Affairs. The views expressed in this document are the authors' and are not necessarily shared by the OECD.

** Rob van Tulder – professor of International Business-Society Management, Erasmus University Rotterdam/Rotterdam School of Management

Thanks to Geoffrey Jones for extensive commentary on an earlier version of this paper.

1. INTRODUCTION: NETWORK MANAGEMENT AS A DEVELOPMENTAL PERSPECTIVE

Today's world seems to be structured and governed through networks. The Network Society is said to have taken hold (cf. Castells, 1998ff), and some have proclaimed the age of 'alliance capitalism' (Dunning, 1997; Gerlach, 1992). The increased attention for network structures is reflected in the literature on the internationalization strategies of big multinational enterprises. In recent years, firms cluster (Porter, 1998), engage in strategic alliances (Hagedoorn, 1995) and in international outsourcing relationships (Kotabe, 1992), or exchange technology and patents on a non-equity basis (Kuemmerle, 1999). MNEs' international location and alliance decisions form the linking pin in an increasingly interdependent world.

At the macro-level, this interdependence is illustrated by the growth rates of both trade and foreign direct investment (FDI), which have been higher than those of world Gross Domestic Product (GDP) since the early 1980s. At the moment, 23 per cent of all production is traded across national borders, and total FDI stock as percentage of GDP has risen to 14 per cent (UNCTAD, 1999). Private flows now take the lions' share of international resource flows, and in the case of many developing countries, FDI has become larger than Official Development Assistance and other international capital transfers taken together.

It is therefore not surprising that most developing countries are looking for ways to reap the benefits of increased inward FDI and see MNEs as possible means to support their development policies. Multinational corporations can be major sources of capital, but are also important as providers of ideas, technology and people, which gives them a significant impact on countries' own production systems and economic development. MNEs can contribute to employment, increase tax-income, provide foreign exchange through their exports, and promote a country's general economic growth through the creation of linkages with local suppliers and buyers. However, MNEs can also crowd out local firms, export capital by manipulating transfer prices, create or maintain hazardous working conditions and disrupt a host country's culture by promoting values and lifestyles incompatible with local customs and believes. The relationship between economic growth and MNE behaviour in the form of FDI and trade is all but unambiguous (cf. Lall, 2000; Vernon, 1998).

One of the intervening variables in the relationship between network strategies of firms and economic development, are development policies of host country government. Parallel with the rise of the network approach in International Business, a growing number of scholars from political science is addressing network formation in policy areas as well (cf. Kickert et al, 1997). But their approach primarily focuses on networks *within* the nation-state, and only grants limited attention to the *inter*national dimension in which countries operate.

This international dimension of host government development policies has usually been addressed through the simple dichotomy of a country being 'open' or 'closed', or 'outward' versus 'inward' oriented. Since the 1980s, the open, outward or export led growth strategy has been hailed by scholars and international institutions as superior to the inward, import-substituting approach (Bhagwati, 1977, Krueger, 1985). In response, Rodrik (1999)[i] has suggested that policies of import substitution might not have been so detrimental to developing countries as often suggested by the so-called 'Washington consensus'.

On the one hand, the dichotomy of 'open' versus 'closed' recognises that host country governments are seldom passive institutes that let MNEs move in and out of their territory, but instead seek to regulate –both promote and prohibit – certain types of FDI, trade and technology transfer or other aspects associated with MNE behaviour, trying to reap the benefits while minimising the harmful impacts of MNEs. On the other hand, it has not been taken into account that government polices are increasingly formulated at, or at least influenced by, international co-operative agreements and institutions, including the regime set by the WTO, various RIAs, and bilateral investment treaties concerning trade or the protection of FDI.

These agreements are supposed to bring benefits to both the signing countries and MNEs. Institutionalist theorists (Cf. Keohane and Martin, 1999) suggest that international agreements and institutions can overcome collective action problems of states by providing the participating countries with information about the other countries' preferences, intentions and behaviour, hereby reducing the transaction costs of co-operation, while making the increased revenues of co-operation – the prisoners dilemma – available. MNEs on the other hand benefit from these agreements through the harmonisation of national rules they bring, which reduces barriers of entry to foreign markets (Preston et al,1997).

The differences in barriers of entry to markets that are inside a network (formed by treaties and membership of institutions) and those outside it, will influence MNE behavior and trade and investment patterns accordingly. Since nationality of firms is still an important factor in the type of internationalization strategies they pursue, it does make a difference for countries in which networks they are included, and in which ones not. A country's membership of networks can be both part of deliberate development strategy, or be more like an 'emergent strategy' (i.e. unintended; Mintzberg and Waters, 1985). In both cases, the way a country 'manages' its' network – making decisions as to which ties to maintain, which to intensify and which to *de*-intensify (van Hezewijk, Metze, 1996:14) – is an important aspect of a country's development trajectory.

This paper illustrates that international network management for developing countries represents a delicate balance in which non-membership of certain policy networks can be as relevant as membership. Temporarily opening up the national economy to international links can be as important as variants of close-ness of the economy. In bringing both Business and Government networks together in a more systemic and balanced way, this paper shows that the management of international policy networks influences the networks created by firms, reflected in the type of FDI attracted and its impact on the national economy.

Malaysia provides an interesting example in this respect. Since its independence in 1957, Malaysia has shown extremely high annual GDP growth rates of almost 7 per cent annually. It successfully changed its' economic structure from mainly agricultural-oriented towards an industrialised society. During this same period, FDI and associated exports have increased significantly. Currently FDI inward stock is 42 % of GDP, and more than 80 per cent of total production is exported (MIDA, 2000). But Malaysia is far from an open economy. Partly as a result of a pragmatic network position in international institutions (including non-membership as well as membership) Malaysia proved to be relatively resistant to the effects of the 1997-98 Asia Crisis –thereby outperforming leading countries such as South-Korea. The Malaysian case shows the rationale for entering into thoughtful international network management, implying both the timely intensification as well as de-intensification of international links both with regard to business networks as to policy networks.

The remainder of this paper first tackles the early Malaysian experiences with FDI and development. Can the national policy be considered to be either import substitution, export orientation or combinations of both, and what where their effects on its inclusion in networks of multinational corporations. The second part of the paper deals with Malaysian experiences with the role of foreign investment in development since the 1980s, which – parallel with the rise of international institutions (Kahler, 1995) - can be formulated in terms of (non) membership to policy networks and network management. All of the networks described relate to trade and investment and therefore with MNE activities: the non-membership of OPEC, the pragmatic membership of WTO and IMF, the leading role in the formation of ASEAN, and the pragmatic formation of networks of Bilateral Investment Treaties. Each of these strategies represent different types of network management open to a relatively small developing country. The paper will show that looking at policy formulation in terms of networks can serve as a powerful heuristic instrument, by focussing on the international dimension of policy making without reducing governments to play-balls of the international economic and political system.

2. The early role of FDI in development

At the threshold of its independence in 1957, Malaysia was prosperous in comparison with other Southeast Asian countries. Mild import-substitution (IS) policies were combined with promotion of FDI in both export-oriented agriculture and import-substituting manufacturing, though FDI was still heavily regulated and geared towards nationally set development goals. Malaysia was one of the major recipients of FDI inflows of the developing world (Thomson, 1999). In the 1960s foreign investors contributed to 18 % of GDP growth and accounted for 23 % of gross investments (Hoffman and Tan, 1980). FDI was mainly concentrated in food and beverages, chemicals and petroleum. Tax payments of these foreign companies were a major benefit for Malaysia, though returns diminished when tax allowances were increased during the 1960s. Only a limited amount of employment was created, and foreign companies investing in manufacturing for the local market crowded out some of the local firms. But foreign MNEs had an overall positive influence on the balance-of-payments of Malaysia, compensating the net outflow of investment capital with high exports, of mainly rubber and tin (ibid.). These policies of (moderate) import-substitution, high exports, and a competent managing government contributed to relative high growth rates of GDP in this period and a first start of industrialisation.

Despite high overall economic growth, a large majority of the people only experienced a very modest growth in income in the 1960-1970 period. Especially the traditional agricultural sector, dominated by the indigenous Malay (*Bumiputra*) majority did not benefit from growth.

Income disparities between the traditional agricultural sector and the rest of the economy widened from 1:2.5 in 1960 to 1:3 in 1970 (World Bank, 1980), which increased tension, polarised politics along ethnic lines and caused racial riots to break out after the 1969 general elections.

In response, the government proposed its New Economic Plan (NEP), with two main goals: (1) to eliminate poverty and (2) to reduce racial imbalances in income, employment or ownership of assets. Since the possibilities of ISI for growth were exhausted, due to the relative small size of the Malaysian market[ii], limited possibilities of economies of scale, and unavailability of better skilled labour and higher technology needed for industrialisation, the main means to reach the goals of the NEP was export-led growth. The strategy of growth-through-exports, in combination with the NEP goal of increased *Bumiputra* participation in the modern sector, led to two the set-up of two phenomena which each attracted considerable amounts of FDI. The first was the creation of Export Processing Zones (EPZs), second the set-up of State Owned Enterprises (SOE) which entered in joint ventures with foreign firms to reduce risks and to benefit from foreign technologies.

The creation of the EPZ and the SOEs resulted in the inflow of considerable FDI in to Malaysia, resulting in an FDI to GDP ratio of more than 20 % of GDP in 1980[iii] (UNCTAD, 1999). Especially in non-metallic mineral products and electronics foreign firms started to become important. Major investors were from the United Kingdom, mainly active in natural resources, and from Japan and the USA.

The results of the export promotion policies was a five-fold increase in exports during the period of 1970 to 1980 and exports as share of GDP increased from 42 per cent in 1970 to 58 per cent in 1980. This growth of exports significantly contributed to high GDP growth rates, which even exceeded the high projection of the NEP (World Bank, 1999). However, besides the exports, the foreign firms concentrated in the Malaysian EPZs have contributed little more. Though a study by Lim in 1978 found that EPZs did created employment on a large scale, especially on the part of the creation of linkages, performance was disappointing. Large parts of the inputs for exports were imported. Firms had also been offered tax holidays and transfer of technology, knowledge and skills was very limited.

From the early 1980s onwards, Malaysian development policies can be seen in terms of network management. It will be shown in the following part of this paper that the way Malaysia – whether part of a deliberate strategy or less pronounced - has managed the networks its economy is included in has affected the flows of FDI coming to Malaysia, and their effects on the country's development.

3. Non-membership: OPEC

The first interesting example of Malaysian policies towards international economic policy networks can be found in the early 1980s, when the non-membership of OPEC had significant impact on Malaysian development. Because Malaysia had chosen – in contrast with Indonesia – not to join OPEC, it also did not have to obey the various production quota rules OPEC installed. While OPEC countries increased oil prices during the second half of the 1970s, this created lucrative market possibilities for non-OPEC countries, including Malaysia. From 1978 to 1986, Malaysia was able to increase its net crude oil exports with an annual average percentage of as high as 17%, which was never shown afterwards (Malaysia Energy Centre, 2000). At the same time, the OPEC countries' combined crude oil production decreased from 31,8 million barrels a day in 1980, to 17 million barrels a day in 1985, in terms of world market share from almost 50% in the late 1970s, to 30% in 1985 (Williams, 1999), since lowering their own production was the only way for OPEC countries to maintain the stable prices they aimed for.

Malaysia's non-membership of OPEC gave it the possibility to export large amounts of crude oil, using the scarcity created by OPEC and the consequent high prices. With the large funds which became available a second phase of import substituting policies was launched (OECD, 1998). The rationale behind it was to decrease the vulnerability of Malaysia on the great fluctuations of commodity prices in the 1970s and change the structure of exports towards manufactures. Policies aimed to develop heavy industry and to reduce reliance of manufacturing industries on imported machinery. Especially cars, cement and steel were protected (Bowie and Unger, 1997). The ISI program attracted different types of FDI than in preceding years. First of all, Joint Ventures with the State Owned Enterprises (SOEs), which were set up to implement the heavy industrialisation program, became a favourable mode of entry. HICOM (Heavy Industries Corporation of Malaysia) was one of the most important partners. It was an investment company that developed a series of joint ventures with foreign corporations, like with Mitsubishi in automotives, and Honda, Suzuki and Yamaha in small engine manufacturing. Secondly, though ISI policies attracted some FDI in the protected sectors, it deterred investors in other sectors due to e.g. the higher prices of steel. Table 1 illustrates that the main sector to which the increase in foreign investment was located was indeed the ISI sectors, in which growth of foreign fixed assets has been highest.

FDI inward stock as percentage of GDP only increased with 2.6 % to 23.7% between 1980 and 1985. In 1980, FDI constituted still more than 30 % of total investment, by 1984 this had decreased to 16 percent (Bank Negara, 2000), due to extremely high government expenditure. The foreign subsidiaries which were set-up remained highly import-dependent, generated few backward linkages and hardly exported. On top of that, the capital-intensive nature of the industries made they generated little employment. The ratio between total capital investment of foreign projects and the potential labour created by the project almost tripled

Table 1. Fixed foreign assets in Malaysia, in Million RM and % of total fixed assets

	1980		**1986**		**Increase 1980-1986**	
Sector	RM mill	% of total	RM mill.	% of total	In RM mill.	%
Food	469	31.80	761	25.68	292	62.3
Beverages	242	76.34	429	70.21	187	77.3
Textiles	346	53.81	376	52.51	30	8.7
Leather products	11	47.83	19	47.5	8	72.7
Wood products	95	13.48	76	8.47	-19	-20.0
Furniture	9	31.03	9	16.36	0	0.0
Paper & printing products	24	9.96	100	19.08	76	316.7
Chemicals	209	53.05	548	21.22	339	162.2
Petroleum, coal products	82	78.10	1160	37.01	1078	1314.6
Rubber products	152	46.06	196	41.35	44	28.9
Plastic products	19	11.66	46	14.7	27	142.1
Non-metallic minerals	147	18.61	718	30.67	571	388.4
Basic metal products	72	34.78	418	32.61	346	480.6
Fabricated metal products	84	26.17	195	22.75	111	132.1
Machinery	49	42.24	116	38.93	67	136.7
Electronics	536	79.64	1331	76.58	795	148.3
Transport equipment	96	31.58	235	21.52	139	144.8
Scientific equipment	25	92.59	49	92.45	24	96.0
Miscellaneous	29	43.94	65	46.1	36	124.1
Total	**2696**	**38.91**	**6847**	**34.05**	**4151**	**154.0**

from 0.05 (Million Ringgit per employee) in 1980 to 0.14 (million Ringgit per employee) at the high tide of ISI policies in 1983 (Bank Negara, 2000).

Without staying out of OPEC, which generated large funds, Malaysia could not have implemented their ISI strategies. These strategies led to the changes in inflows of FDI towards the protected industries, with their consequent impact of FDI on the Malaysian economy.

4. Pragmatic membership: WTO and IMF

Malaysia has always been a 'pragmatic proponent' of both the World Trade Organisation (WTO) and the International Monetary Fund (IMF). Though the Malaysian government has generally adhered to IMF and WTO standards and regulations, it tried to stay in an independent position in policy making. Malaysia's critical stance towards these multilateral institutions becomes clear in both the rhetoric speeches of its' president[iv] as well as in practice, during meetings of the WTO and IMF[v]. The effects this position has on investment flows is discussed below: firstly, during the liberalisation period at the end of the 1980s; and secondly during the Asian financial crisis at the end of the 1990s.

5.1 Liberalisation at the end of the 1980s. Liberalisation of trade, and a selective liberalisation of investment, started when a severe recession ended the second-stage ISI around 1985. This liberalisation of trade and investment differed however from the kinds of liberalisation in many other developing countries. As Okamoto (1994) notes, the two main distinctive characteristics of Malaysia's liberalisation policy were its gradual implementation and the combination of both export promotion and import liberalisation. Malaysian investment policies were open to those firms in export oriented industries, directing foreign firms to Export Processing Zones with subsidies and other incentives. But firms aiming to supply the local market faced high barriers. These barriers also existed in certain 'strategic' industries, like the automotive industry in which Malaysia tries to promote its own car, Proton. Up until today none of the big American, European or Japanese automotive firms has invested in Malaysia (MIDA, 2000). The special policies of Malaysia were possible because the Malaysian government was not dependent on the international institutions, with only limited, and before 1985 completely repaid loans (IMF, 2000). Other developing countries which had to liberalise under pressure of IMF did so more quickly and less selectively than Malaysia, with overall negative effects (Przeworski and Vreeland, 2000).

The controlled and selective opening up of the country was followed by the large FDI-induced export-led growth boom of the late 1980s and the 1990s, with most FDI located in Export Processing Zones. Not only did the absolute FDI inward stock increased eight fold from 1980 to 1998, also the relative importance of foreign direct investment in total GDP doubled (UNCTAD, 1994 and 1999). The new inflows of FDI were mostly seeking to use Malaysia's low labour costs for export oriented assembly. Investment flows hence became increasingly labour intensive, which is illustrated by the number of workers per million Ringgit invested, which was 7.8 in 1986, and increased to 15 in 1989 (Bank Negara, 2000). Whereas FDI used to be concentrated in the natural resource sector, in the late 1980s manufacturing -especially the electronics sector- attracted huge parts of the total FDI inflows. Most of the FDI was oriented towards exports, again especially the electronics sector, which has driven Malaysian exports to reach almost 90 % of its GDP (World Bank, 2000).

The simultaneous liberalisation of both exports and imports in especially the EPZ, made them very attractive for MNEs. This did not bring large positive effects on the balance of payments, since though exports were high, at the same time large parts of outputs were imported. In the electronics sector as much as 80 per cent of exports was imported. If then repatriation of profits and other capital transfers are considered, concerns can rise as to the real balance of payment effect of these foreign firms in Malaysia. A study of Fry (1993) suggested that the long-term effects of FDI on both the trade and the current account balance have been positive. UNCTAD studies (1997) seem to confirm that though on the short run MNE activities are negative for a country current account, they do attract new flows of FDI and have an overall positive contribution to the balance of payments. Despite the positive net balance of payment effect of the foreign investors, also large parts of total production are imported points to low local linkage creation, decreasing the opportunity for spill-over effects significantly.

5.2 The Asia crisis. The experience of Malaysia with the Asia financial crisis additionally shows that the position in and policy towards international networks can have significant consequences for national development options. The Asian financial crisis of 1997 affected Malaysia severely – though it did not hit as hard as in Indonesia or Thailand. From the start of 1998, economic growth rates turned negative, only to become positive again in the mid of

1999. To address the effects of the Asian crisis, the policy response constituted partly of (temporarily) further liberalisation of investment rules and the promotion of exports. But what is important is that Malaysia did not turn to the IMF for financial assistance, and not all policies followed technical advice provided by the World Bank and the IMF (Wee, 1999). Malaysian measures (ibid.) included the prevention of trading of the Malaysian currency: individuals and corporations were not allowed to take more than RM 1,000 out of the country. Also, Malaysia increased tariffs on imports (temporarily) and introduced a 12-month restriction on the repatriation of portfolio capital, one of the sources of the crisis, with a system of exit levies, with the levy decreasing with the duration of the investment. Other Malaysian guidelines on portfolio investment continue (since 1974) to discourage Mergers and Acquisitions by foreign but also by Malaysian interests (UNCTAD, 2000:20). The policies followed by Malaysia – a partial closure of the economy – could not have been possible when Malaysia was not independent from WTO, which disapproved of the Malaysian measures which were in contrast with the its principles of free trade. The Malaysian method seems to have worked, with FDI flows not so severely affected by the crisis. Recent economic growth rates picking up the high levels of before the Asian crisis, of 7 to 8 per cent, which make Malaysia's growth among the fastest in the region (McNulty, 2000).

Pragmatic allegiance to the IMF and WTO regime, made that Malaysia had considerable space to formulate its own policy as regards liberalisation of exports and imports, which could be much more moderate and selective than in other developing countries. This policy has led to considerable inflows of FDI, especially in the EPZs, which had overall positive impact on development. Also, Malaysia was free to formulate its own responses to the consequences of the Asian Crisis, which – though a long term assessment is difficult to give - seems to have been more successful than those of surrounding countries.

5. Leading membership: Regional Integration

One of the most significant networks which influenced type, origin and effect of FDI in Malaysia has been the Association of South East Asian Nations, ASEAN. Despite the relatively shallow nature of ASEAN co-operation in comparison with the European Union, NAFTA and Mercosur, regionalism is a major component of Malaysian (trade) policy (WTO, 1997). Malaysia attached strong importance to regional co-operation and is one of the active members of ASEAN, proposing further and deeper regional integration. Founded in 1967, ASEAN now consists of ten members together forming a Free Trade Area (FTA). ASEAN was a very early attempt to make use of the loopholes in the GATT regime (spelled out in Artcile XXIV) and can be considered to have been a weak alliance of states by design (Cf. Ruigrok and Van Tulder, 1995: 295ff). The FTA established allows firms to export and import goods within the region without paying import duties. This increases opportunities to integrate production in the ASEAN region and creates a very large market. Though the real FTA will only be established in 2003, current import duties between the ASEAN countries are already very low and decreasing. Negotiations have started on the ASEAN Investment Area (AIA), which aims to liberalise national investment rules and to grant intra-ASEAN investment national treatment by 2010.

But even without the AIA in place, ASEAN has been of high importance in determining investment flows to Malaysia, as Bende-Nabende et al. (1997) show through regression analysis. The major investors in Malaysia throughout the 1990s have been the Asian countries (see table 2). Also before that period, Asia and especially Japan has been principle investors in Malaysia (MIDA, 2000).

The high inflows of FDI in the 1980s and 1990s are not only due to Malaysian policies, but also stemmed from developments in the surrounding region. This further illustrates the importance of Malaysian membership of ASEAN. First of all, the 1985 world-wide currency

Table 2. origins of FDI inflows into Malaysia in the 1990s, mill. RM

	Total	USA	Europe	Japan	Other Asia	Others
1991	8.776	1.223	1.512	2.507	3.269	265
1992	14.195	2.984	2.358	2.843	5.727	283
1993	17.062	3.402	3.536	3.053	6.905	166
1994	28.864	7.226	3.165	4.131	12.491	1.851
1995	26.871	7.276	1.776	2.645	13.565	1.609
1996	31.081	10.134	4.026	2.709	13.301	911
1997	35.967	10.912	2.815	3.593	17.451	1.196
1998	27.757	5.697	4.005	5.637	11.185	1.233

Source: Bank Negara

realignments made the Japanese yen, the Taiwan dollar, the Korean won and the Singapore dollar more expensive in comparison with Malaysia, and drove firms producing in the former countries to set up lower cost production sites in Malaysia (Lim and Siddall, 1997). Second, many of the forerunners of the Asian dragons - Singapore, Taiwan, Taipei and Korea - lost their position in the General System of Preferences which granted their exports preferential access to the developed world. Third, Singapore had become one of the regional major hubs, particularly in the electronics industry. These three developments all resulted in a shift of especially labour-intensive production towards Malaysia, who's proximity and trade regime made it an optimal location vis-à-vis other developing countries to relocate that kind of production to.

Regional integration made it possible for industry to vertically integrate production. Especially the Japanese firms and the ones in the electronics industry (not always –though often- the same) have made use of this. Firms like Sony, Matsushita and Aiwa treat the region as an economic integrated unit, having located plants to service Asian and western markets in the region's economies according to their comparative advantage. Non-Asian multinationals, particularly US firms, also made linked investments in the region, generating new trade and capital flows among host countries (Fong, 1995). This regional vertical integration of production on the one hand increases trade within the region, but on the other hand decreases local linkage creation in favour of regional linkages. Firm strategies have located the 'clever stuff' in Singapore, which is superior in infrastructure, communication and transport-facilities, and the cheaper and lower tech assembly in Malaysia. But with the increase in Malaysian development, higher value added activities have relocated to Malaysia, and low labour seeking investment is directed to other less developed parts of ASEAN, like Vietnam and Cambodia.

This regional division of labour is used and further enhanced on a 'sub-regional' level, in the Asian so-called growth triangles, in a number of which Malaysia participates actively. These growth triangles complement comparative advantages of each of the countries involved. The most widely known and fully developed growth triangle is the SIJORI, between Singapore, Johor (Malaysia) and Riau (Indonesia). With Johor offering the abundance of land, skilled and semi-skilled labour, Singapore the high quality human capital and infrastructure, and Indonesia the low cost land and low skilled cheap labour (Athukorala and Menon, 1995). This growth triangle has attracted large inflows of investment and it has already been argued that not only the sites involved in the growth triangle have benefited, but also the surrounding areas (Lee, 1991).

Malaysia's position in, and pro-active policies towards ASEAN resulted in a relocation of production from the frontrunners in Asian development towards Malaysia when the former were forced to do so by *inter alia* currency realignments. The surge of regional investment made possible by the ASEAN FTA tariff cuts, has had significant effects on Malaysian development. On the one hand, regional linkages were created instead of local ones, on the other hand, the increases in trade between vertically integrated MNE affiliates has contributed to economic growth in Malaysia.

6. PRAGMATIC NETWORK FORMATION: BILATERAL INVESTMENT TREATIES

The final network discussed in the one formed by Bilateral Investment Treaties (BITs), which are still the main means to regulate international investment flows. The signature of

BITs is usually meant to reassure investors by establishing strict norms and conditions as to expropriation, nationalisation and compensation (OECD, 1993), and the absence of BITs serves more as a deterrent to investors than the presence of BITs serves as a trigger. Malaysia has been one of the most active signers of BITs in Asia, as table 3 shows. 45 BITs have been concluded up to the end of 1998.

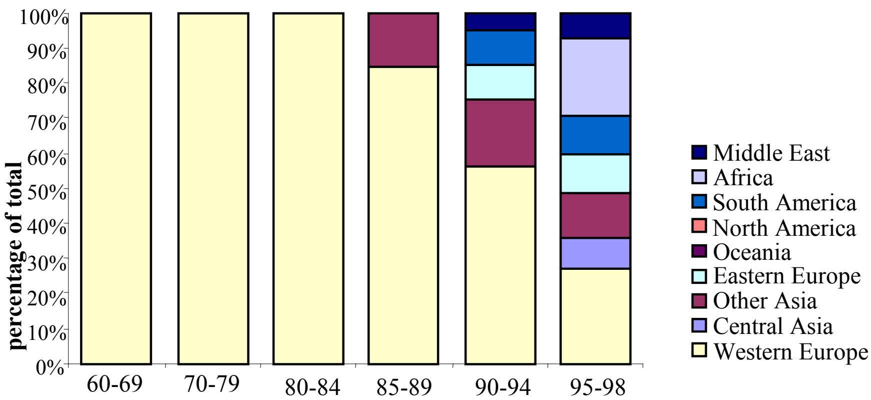
Table 3. Total number of BITs signed by selected Asian countries, 1960-1998

	60-69	70-79	80-84	85-89	90-94	95-98	Total
Malaysia	1	5	2	5	8	24	45
Thailand	1	2	0	4	8	6	21
Philippines	0	1	1	2	5	13	22
Indonesia	4	4	0	0	18	21	47
Japan	0	1	1	1	1	4	8
Hong Kong	0	0	0	0	5	9	14
Singapore	0	6	1	1	3	7	18
Taiwan	0	0	0	0	2	5	7

Source: compiled from UNCTAD.

The first wave of BITs to which Malaysia was a partner occurred in the end of the 1970s, and included mostly European partners; in the second phase, starting in the early 1990s, developing countries were the main co-signatures (UNCTAD, 1999; Mida, 2000). As figure 1 shows, these recent BITs are signed with countries in Asia, Africa and the Middle East. The

Figure 1 Malaysian BITs, cumulative, as percentage of total at the end of time period



trend of signing treaties with less developed countries corresponds not with FDI inward flows, but instead with the increase and pattern of Malaysian FDI <u>out</u>flows. Malaysian FDI outward stock consisted only 1.8 per cent of GDP in 1980, but has risen to 13 per cent in 1997. The size and importance of outward FDI for Malaysia becomes even stronger when this figure is compared with the same percentage world-wide (8.0%) and those of the European Union (14.8%), the USA (9.4%) Japan (2.2%), and the rest of Asian countries, of which only Singapore and Hong Kong show higher numbers (UNCTAD, 1999). Other Asian countries have not shown this high levels of outward FDI, and have not signed BITs with less developed countries.

Malaysian outward investment flows have mainly been aimed at acquiring foreign technology. This has not only been a corporate strategy, but is also an explicit policy of the government. A similar strategy was initially used in resource-based industries, such as rubber and tyres. The government has not only encouraged outward FDI for its role in technology transfer but also for its contribution to Malaysian exports[vi].

So far outward investments have mainly concentrated in textiles, wood products, rubber products, transport equipment and the oil industry. Malaysian textile plats have been established in Mauritius, palm-oil refineries in Egypt, and rubber product plants in China[vii]. Petronas, the national oil company, is also aggressively investing in oil field development in Iran and Vietnam. In this respect it is interesting to note the amount of BITs signed with oil-producing countries in Africa and the Middle East.

Another major Malaysian company investing abroad is Sime Darby, a diversified company active in (amongst many other things) plantations, property development, heavy industry equipment and motor vehicle distribution and forestry. Sime Darby has acquired assets in the UK and Australia, indeed aiming to acquire technology. The state-owned automotive firm Proton did the same when purchasing Lotus, a British sports car maker. Both Petronas and Sime Darby are in the top 50 of MNEs from developing countries (UNCTAD, 1999) and listed in the 1999 Fortune Global 500 ranking.

Malaysia's way of building a network of BITs has been part of an active policy of promoting outward investment, and indeed outward FDI had been oriented to those developing countries with which BITs have recently been signed. These outward investment contributed to technology transfer.

7. CONCLUSIONS

With the growing importance of international production networks, trade and international finance, government development policy is also increasingly formulated at, or influenced by, international institutions and agreements. Using the example of Malaysia, this paper has shown that looking at national development policy formulation in terms of the management of (international) networks can be a powerful heuristic instrument in examining the effect of MNEs and consequent FDI and trade on national development. A small country like Malaysia needs to be extremely pragmatic in managing its international networks. Sometimes the country can be leading, sometimes it has the opportunity to be a formative force behind networks, but often policy makers should be pragmatic and take care of sustained independence from too much reliance on international networks. Examples of the rational behind the intensification as well as the de-intensification of network interrelations have been given. Since the start of the 1980s, the position of Malaysia in, and Malaysian policies towards various international networks have been important in determining the type and effects of FDI inflows. Without staying out of OPEC, Malaysia could not have financed its ISI strategies of the 1980s. Without being independent from the WTO and IMF – or in other words: due to pragmatic membership of these institutions - Malaysia would have had to deal much less pragmatic with liberalization of trade in the end of the 1980s, or with the consequences of the Asian Crisis. Regional integration in Asia, of which Malaysia has been a active supporter, has been a key factor in attracting FDI to Malaysia, with also ASEAN sub-regions becoming of increasing importance to the national development strategy. Finally, the network of Bilateral Investment Treaties, of which Malaysia has been an active (de)signer, has shown remarked resemblance as regards timing and direction of Malaysian outward FDI. Effective development policies (increasingly also for developed countries) evolve in the interaction between international policy and business networks. The present paper has illustrated that thinking about development in terms of (international) network management has at least heuristic value. A network approach linking business and government networks, should be able to link insights from development theory, institutionalism, international business and international political economy. In any case, regarding open and closed development strategies and the role of FDI and trade without orthodoxy seems to represent a prudent framework for strategists who want to become effective network managers.

---

i Besides drawing attention to the importance of well-developed national institutions

ii 10 million inhabitants in 1970 and a average annual GDP per capita of around 1000 US$

iii Compare this with 5.0 % as the world average and 9.9 % for Southeast Asia

iv See for example the speech delivered at the 6th Nikkei Shimbun conference on the future of Asia.

v See for example the responses of Malaysia issued to the WTO's 1997 trade policy review, or its position in APEC regarding the start of a new round of trade negotiations within the WTO.

vi Financial Times, 3 December 1996. 'Malaysia sees high tech partners'.

vii Financial Times, 19 March 1991. 'Foreign investment in Malaysia surges ahead'.

REFERENCES

ASEAN. 2000. *Statistic of Foreign Direct Investment in ASEAN*. Jakarta: ASEAN.

Athukorala, Premachandra and Menon, Jayant. 1995. Developing with Foreign investment: Malaysia. *Australian Economic Review*. Vol.109(1):9-22.

Bank Negara (2000) Statistics Malaysia. Website: www.bnm.gov.my, 10 may 2000.

Bhagwati, Jagdish. Editor. 1977. The New International Economic Order: the North South debate.MIT Press.

Bowie, Alasdair. and Unger, Danny. 1997. *The politics of open economies, Indonesia, Malaysia, the Philippines and Thailand.* Cambridge: University Press.

Castells, Manuel. 1998. *The rise of the network society*. Oxford: Blackwell.

Dunning, John. 1997. Alliance capitalism and global business. London: Routledge.

Fong, Pang Eng. 1995. in: NRI.

Fry, Maxwell. 1993. *Foreign direct investment in Southeast Asia: differential impacts.* Singapore: Institute of Southeast Asian studies.

Gerlach, Michael. 1992. *Alliance capitalism. The social organisation of Japanese Business*. Berkeley: University California Press.

Hagedoorn, John. 1995. *Technological change an the world economy: convergence and divergence in technology strategies*. Aldershot: Elgar.

Hoffmann, Lutz. and Tan, Siew E. 1980. *Industrial growth, Employment and Foreign investment in Malaysia*. Kuala Lumpur: Oxford University Press.

Kahler, Miles (1995) *International institutions and the political economy of integration*. Washington: The Brookings Institution.

Keohane, Robert O. and Martin, Lisa L. 1999. Institutional theory, endogenity, and delegation. Paper prepared for Progress in International Relations Theory: a Collaborative Assessment and Application of Imke Lakatos Methodology of Scientific Research Programs, January 15-16, Scottsdale Arizona, USA.

Kickert, Walter; and Klijn, Erik-Hans & Koppenjan, Joop. Editors. 1997. Managing complex networks: strategies for the public sector. London: Sage publications.

Kotabe, Masaaki. 1992. *Global sourcing strategy*. New York: Quorum Books.

Lall, Sanjaya. 2000. *Promoting industrial competitiveness in developing countries. lessons from Asia*. Economic paper no.39. Commonwealth publications.

Lee, Tsao Y. 1991. *Growth Triangle: the Singapore-Johor-Riau experience*, ISEAS: Singapore.

Lim, Linda.Y.C. and Siddall, Nathaniel .S. 1997. 'Investment dynamism in Asian developing countries', in: Dunning, J.H. and Hamdani, K.A. *The new globalism and developing countries*, Geneva, UN University Press.

Lim, Linda.Y.C. (1978) *Multinational firms and manufacturing for export in less-developed countries: the case of the electronics industry in Malaysia and Singapore*, Unpublished PhD dissertation in economics, University of Michigan, Ann Arbor.

Krueger, Ann. 1985. Import substitution versus export promotion. *Finance and development*. June1985.

Kuemmerle, Walter 1999. The drivers of foreign direct investment into research and development: an empirical investigation. Journal of international business studies, 30(1): 1-24.

Malaysia Energy Centre. 1989. *National Energy Balance Malaysia*. Kajang Selangor, MEC.

McNulty, Sheila. Malaysia bids to attract investors. *Financial Times.* 15 august 2000.

MIDA, 2000. *Malaysia: Investment in the manufacturing sector. Policies, incentives and facilities*. Website: www.mida.gov.my 15 may 2000.

Mintzberg, H. and Waters, J.A. 1985. Of strategies: deliberate and emergent', *Strategic Management Journal*, Vol. 6(3):257-272.

OECD. 1993. *Foreign direct investment relations between the OECD and the dynamic Asian Economies, the Bangkok workshop*. Paris: OECD.

OECD. 1998. *Foreign investment in Malaysia.* Paris: OECD

OECD/DAC. 2000. *International development statistics*. Paris: OECD.

Okamoto, Yumiko. 1994. Impact of trade and FDI liberalisation policies on the Malaysian economy. *The developing economies*. Vol.22(4): 460-478.

Porter, Michael E. 1998. *Michael Porter on competition*. Boston: Harvard Business School Press.

Preston, Lee E. And Windsor, Duane. 1997. *The rules of the game in the global economy: policy regimes for international business*. Boston: Kluwer.

Przeworski, Adam and Vreeland, James R.2000. The effect of IMF programs on economic growth. *Journal of Development Economics*. Vol 62(2) 385-421.

Rodrik, Dani. 1999. *The new global economy and developing countries: Making openness work*. Washington: Overseas Development Council. Policy Essay no.24.

Ruigrok, Winfried and Van Tulder, Rob. 1995. *The Logic of International Restructuring*, London/New York: Routledge.

Thomson, Stephen. 1999. *Southeast Asia: the role of FDI policies in development,* Paris: OECD.

UNCTAD. 1994. *World Investment Report, Transnational corporations, employment and the work place.* Geneva: UNCTAD.

UNCTAD. 1997. *World Investment Report, Transnational Corporations, Market Structure and Competition Policy.* Geneva: UNCTAD.

UNCTAD. 1999. *World Investment Report, Foreign Direct Investment and the Challenge of Development.* Geneva: UNCTAD.

UNCTAD. 2000. *World Investment Report 2000. Cross-border M&As and development.* Geneva: UNCTAD.

Van Hezewijk, Jos and Metze, Marcel. 1996. *Je kent wie je bent. De verborgen kracht van relatie-netwerken*. Amsterdam: Uitgeverij Balans.

Vernon, 1998. *In the hurricane's eye. The troubled prospects of multinational enterprises*. Boston: Harvard University Press.

Wee, Victor. 1999. Malaysia: Responding to the Economic Crisis. In: OECD. *Structural aspects of the East Asian Crisis*, Paris: OECD.

Williams, James L. 1999. *Market share within OPEC*. WTRG Economics. Website www.wtrg.com, 7 September 2000.

World Bank. 1980. *Malaysia. growth and equity in a multiracial society*, New York: World Bank.

World Bank. 1999. *World Bank Development Indicators*. New York: World Bank.