Linkages and resource flows to local firms: Danish firms in Argentina

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Abstract: *The study addresses the direct linkages between affiliates and local host country firms and look at the impact on competitive advantages. The analysis is based of a model of the relationships and resource flows between parent company, the affiliate and the local partner firms. Empirically it builds on information collected from the total population of Danish firms established in Argentina. Because the firms a mainly locating in Argentina for market seeking reasons this study provides an insight to the linkages and resource flows to downstream distributors and customers that have a more significant importance than suppliers and subcontractors.*

Key words: *Linkages, Multinational corporations, Affiliates, Competitive advantage, Developing countries and emerging markets.*

INTRODUCTION[1]

Globalization has led to profound changes in the ways and forms under which cross-border firm cooperation takes place. Increasingly such cooperation takes place between firms in developed countries and firms in developing and emerging market economies. Much research interest has been given to cooperation with firms in Asia, and significantly less to cooperation between firms in Europe and in Latin America. This paper focusses on the cooperation between Danish affiliates and their local partners in Argentina.

An important development in economic globalization has been how different parts of the value chain are being dispersed at various locations and how the chain can be managed in different ways. When companies in non-hierarchical and non-ownership relations are cooperating, questions arise related to the division of value chain activities, to the governance and management of the chain and to the effects of the linkages and resource flows between the firms. These questions have been addressed in various sub-themes in the international business (IB) literature.

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The focus of this paper is on the cooperation between Danish affiliates in Argentina and their local partners; the linkages and the transfer of resources between them. The overall research questions guiding the paper are:

Why do Danish invest in Argentina, how do the affiliates cooperate with local firms, and what is the impact of the cooperation on the partner firms?

To answer these questions the paper leans primarily on the IB literature dealing with effects of direct linkages between the affiliate of the multinational corporation (MNC) and its business partners in the host country, but as a background to understand the formation of linkages we need first to look at why the MNC invests drawing at the location motives (Dunning 1993; Lasserre 2003). The knowledge of the investment motives provides input to analyse the sort of linkages with upstream and downstream partners.

The study contributes to new knowledge in the following ways: (1) Much of the recent offshoring/outsourcing debate has been concerned with the strategies of the offshoring firm and the impacts in the home country (Sako 2005). Less attention has been paid to the forms of cooperation, the linkages and the impact on the local firms cooperating with the affiliate of the MNCs (Giroud and Scott-Kennel 2006; Rocha, 2006). (2) Furthermore, studies have focused on outsourcing in the supply chain of upstream manufacturing value added activities (supplier and subcontractors) and on offshoring of business service support activities. Much less attention has been paid to offshoring of downstream activities including marketing, distribution, sales and after-sales services (Scott-Kennel and Enderwick 2005:115; Giroud and Scott-Kennel 2006:8). This form of firm cooperation is related to knowledge of host country markets, marketing, distribution networks and customer knowledge. (3) Finally, because the main debate on offshoring has been on the upstream supplier linkages, the geographic focus has been on business relations with firms in Asia. European not to say Danish firm cooperation in Latin America has attracted much less attention.

LITERATURE REVIEW

The basic questions addressed in this paper are how foreign affiliates and local firms cooperate and exchange resources through their direct business linkages, and thereby exploit the possibilities to access resources they have not internalised, and develop capabilities and improve their competitive advantages. These questions have been looked at under various headings in the literature: international business alliances (Dunning 1993, 1997); cross-border firm linkages (Hansen and Schaumburg-Müller 2006; Scott-

Kennel 2004; Giroud and Scott-Kennel 2006); global value chains (Porter 1985; Gereffi et al. 2005); and outsourcing (Kakabadse & Kakabadse 2000; Doh 2005; Kuada 2006).

The mainstream IB literature has a rich contribution to the study of the impact of foreign direct investment on the host country economy and companies, but most of these studies are confined to the study of spill-overs or unintentional effects from studies at the macro or industry level (Blomström and Kokko 2000). There are fewer studies at the firm level of the direct linkage effects and resource transfers coming about as a result of a strategic cooperation between foreign and local companies be it in supplier/subcontractor, agent/buyer or in horizontal alliance relations. The global value chain literature has provided insights to the governance modes lead firms and the upgrading effects on suppliers in the chain (Gereffi et al. 2005). The methodology and modelling of this study has, however, been more inspired by the relatively few IB studies focusing on the direct inter-firm linkages and resource transfers (see Giroud and Scott-kennel 2006). Recently this literature has been significantly developed by Joanna Scott-Kennel, based on her large sample study of foreign companies operating in New Zealand (Scott-Kennel 2006 and 2007). Her basic model has also been used in linkage studies of foreign firms in East Europe (Scott-Kennel and Enderwick 2004). This paper aimss at making her basic linkage model more explicit and include the impact aspect measured as importance for firm competitive advantage.

FDI in Argentina

Except for shorter periods of economic crises foreign direct investment flows into Argentina have played an important role in the economy. The investment location motives have however been relatively diverse, FDI being both attracted by natural resources and energy endowments, and the market potentials of the country. The economic crises and the following liberalization of the economy in the beginning of the 1990s with the dramatic wave of privatization attracted foreign investors into massive investments in public utilities and in the financial sector (Chudnovsky et al. 1997; Petrecolla and Lousteau 2001; Toulan 2002).

In general inward FDI activities in Argentina are presently growing and so are their impacts in the local economy. Studies of the FDI impacts in Argentina find important technology spillover interactions between MNC affiliates and domestic firms even after the inflow of FDI has grown more in the resource-processing industries after the economic liberalization (Bell and Marin 2004; Marin and Bell 2006). Despite the recent trade liberalization, the FDI inflow has in recent years continued to surge with the result that Argentina’s manufacturing industry has become heavily dependent on foreign firms (Narula and Marin 2003).

Danish firms in Argentina

Danish companies are increasingly investing in the emerging market economies but most of these investments are focused on manufacturing in the business-to-business markets, and not in natural resource extraction or public utilities. The share of the Danish stock of foreign direct investments in developing countries increased to 18% by the beginning of the 2000s. Half of the Danish companies investing abroad offshore activities previously conducted in Denmark, and the offshoring has primarily taken place to developing and emerging economies (Hansen et al. 2006). The stock of Danish FDI in Latin America was by 2003 close to 5% of the total Danish FDI stock abroad, and closing in on the FDI stocks located in Asia and Central and Eastern Europe (Hansen et al. 2006). Until now Danish firms moving to Asia have mainly been doing so for resource seeking motives attracted by low labour costs. But the trend is changing with globalization and increasing purchasing power in a growing number of emerging economies, and therefore the location is increasingly market seeking and strategic motivated.

For Danish firms locating in Latin America's larger economies like Argentina and Brazil the motives are more mixed as the main drive historically has been to overcome the trade barriers and establish production within the protected markets of these relatively large markets.

By 2009 there were 32 Danish affiliates located in Argentina representing both large Danish companies operating globally and smaller ones. There are no specific studies of Danish investments and their impacts in Argentina. A survey of Danish investments in developing countries shows that only a little more than 30% of the Danish affiliates in Latin America exported more than 30% of their turn over and very few exported internally to other entities of the multinational corporation – contrary to the firms established in Asia (Hansen et al. 2006). The survey found that "following the client" was an important motive for Danish investments in Latin America, and that local sourcing was even more important than for the FDIs in Asia. Both of these results indicate that we should expect a high degree of both forward and backward linkages to other firms in Argentina. This is confirmed by the findings in the survey that each Danish investment project in Latin America on average had more than three collaborations with local firm, which was higher than for investment projects in Asia and Eastern Europe.

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MODEL AND PROPOSITIONS

In the modelling there are three units of analysis; the parent Danish MNC; the affiliate in Argentina and its business partners in Argentina. The business partners include three categories:

- Vertical – upstream suppliers or subcontractors to the affiliate. They are local companies from which the affiliate buys goods and services or local subcontractors to which the affiliate outsource production of goods and services;
- Vertical – downstream distributors (agents) and buyers. They are firms to whom the affiliate sells products and services either for distribution or for directs consumption (for reasons of simplicity it also includes relations to franchisers and licensors under agents and buyers).
- Horizontal – alliance partners. They are business partners with whom the affiliate work together without the partner being a supplier or a buyer but cooperate for purposes related to research and developments, production technology, markets research and studies, developing complementary and strategic business opportunities and sharing assets etc.

The analytical framework is a further development of Scott-Kennel 2006 and 2007 basically using her concepts on linkages, transferred resources and competitive advantages. It has in its general forms four sets of independent variables; governance, investment motive, forms of relationship and linkages. Resources transferred in the relationships are both an dependent variable and an independent variable for the measure of the perceived impact on competitive advantage; the main dependent variable.

The overall framework is summarised in Table 1

Table 1: LINKAGE MODEL FRAMEWORK

Unit of analysis **Variables**	**Parent MNC company**	**Affiliate**	**Local Partner**
Governance	International Corporate Strategy (Typology from Bartlett & Ghoshal: global; multidomestic; transnational)	Affiliate typology (partly based on Enright & Subramanian 2007)	Type of transaction with affiliate (transactional; contractual; collaborative)
Investment motive	Foreign entry strategy motive	-	-
Relationship	Foreign entry strategy mode (wholly owned/JV)	Affiliate autonomy	Relationship to affiliate (three types)
Functional activities	Industry	- Industry - Functional activity of affiliate	- Industry
Linkages		Linkages to local partners - strong/weak - number of partners	-
Resource transfer content (independent and dependent variable)	- Parent company resource transfer to affiliate	- Resource transfer from parent company - Resource transfer to local partner - Resource transfer from local partner	- Resource transfer from affiliate - Resource transfer to affiliate
Impact (dependent variable)		Competitive advantage	Competitive advantage
Control variables	Size	Size Cluster location Business environment	Size Cluster location

Drawing on the literature of the international direct investment strategies (Dunning 1997; Lasserre 2003); cross-border firm linkages (Altenburg 2000; Hansen & Schaumburg-Müller; Scott-Kennel 2006; Scott-Kennel and Enderwick 2005); global value chains (Porter 1986; Gereffi et al. 2005); and outsourcing (Kakabadse & Kakabadse 2000; Doh 2005; Kuada 2006), five propositions are developed for Danish firms locating and operating in Argentina: two propositions on the location motives and three on the flows and importance of the resource transfers.

For Danish companies with ownership advantages to operate globally Argentina is a distant market with limited comparative location advantages besides the size of its market, which has its specific institutional arrangements and a certain degree of protection. Argentina also has a location attraction from its specific natural resources, but few Danish firms besides part of the agro-business industry have ownership advantages in natural resource industries. We therefore suggest the proposition:
P1: *Danish companies locate in Argentina mainly market reasons (no other location advantages are considered highly important).*

Looking more specifically at the manufacturing firms they may invest in sales and distribution activities only, where trade barriers are low and access to local resources do not constitute a main motive. For those manufacturing firms that locate production in Argentina we expect that market seeking location motives to be combined with other resource seeking motives. However, access to low cost labour is not expected to play a major role. The second proposition is:
P2: *Danish manufacturing companies locate production functions in Argentina for market and other access reasons other than low cost labour.*

Since proposition 1 and 2 suggest that low cost factors are not the main investment motive and, given the Danish affiliates have to compete with local and other foreign firms in Argentina, we will expect that the parent company to counterbalance the liability of foreignness transfer resources that are important for the affiliates' competitive advantage – therefore:
P3: *Danish parent companies transfer resources that are important for the affiliates' competitive advantage.*

Operating in a distant country with specific institutional arrangements for organizing production activities and servicing customers, the affiliate will rely on vertical partners and often transfer important resources to them. When the affiliate sees the linkages to be close with vertical partners, the transfer of resources will be seen more important for the competitive advantage of the local partners. This leads to the following two propositions:
P4: *Resources transferred by the Danish affiliates to (vertical) partners are considered important for local partners' competitive advantage.*

P5: *Danish affiliates with strong linkages to local partners transfer resources important for the (vertical) local partners' competitive advantage.*

METODOLOGY

This paper approaches the answer of its research questions on an exploratory basis. As it will be explained below, the total population of Danish affiliates in Argentina is 29 and 22 valid responses were obtained from the total population. Although the response rate is very high (75%), it does not allow running regression analysis given that the minimum required number of data points for such an analysis is around 30 (cf. Rocha and Sternberg, 2005).

This section describes the characteristics of the population, the data collection process and the survey scheme.

Population characteristics and data collection process

From the information provided by the Danish Embassy in Buenos Aires and the Argentinean-Danish Chamber of Commerce and Industry 32 Danish affiliates located in Argentina were identified. The Danish companies established in Argentina are in many cases affiliates of highly internationalized Danish companies like Maersk, Grundfos, Danfoss, Vestas, Novo Nordisk but there are also affiliates of very small and less experienced Danish firms. Almost all of the Danish affiliates are operating in the business-to-business markets and they are almost all wholly owned by the Danish parent company; there are very few joint ventures.

A questionnaire with mainly closed questions was developed to be answered by the affiliate mangers. The core questions related to different resource flows between parent company and affiliate and between the affiliate and its local partners upstream, downstream and horizontal. The questionnaire was tested and then distributed to the total population of Danish affiliates in Argentina. The design of the questionnaire was partly inspired by Scott-Kennel's FDI linkage publications from her study of FDIs in New Zealand (Scott-Kennel 2005; 2007). Conceptually the impact measurement of the effect on competitive advantage was added, and the grade of impact was specified for each type of resource transfer flow using a Likert scale on the perceived grade of importance of the different types of resource transfers on competitive advantage. For the resource transfers from parent company to affiliate eleven types of resource transfers were specified; for transfers from affiliates to suppliers/sub-contractors and to distributors/buyers there were fourteen types and from affiliates to horizontal alliance partners there were eight types of resource transfers. In addition we also introduced a question on the reverse transfer of resources from vertical and horizontal partners to the affiliate with tens types of resource flows.

All the 32 affiliates listed were contacted and asked to fill out the questionnaire. One affiliate was not operating any longer, and two affiliates informed that their parent company had changed ownership and were not any longer Danish companies. From the remaining 29 affiliate companies, 22 questionnaires were returned.

Looking at the main sector composition of the parent corporations we have the following distribution (Table 2):

Table 2 Distribution of Danish parent companies

Sector	Number total population (responding affiliates)
Manufacturing	23 (16)
Services	4 (3)
Construction /engineering	2 (2)
Total	29 (21)

Almost none of the Danish corporations are selling consumer goods but are operating in the business-to-business market if we in that include products sold to farmers and pharmaceutical products. Ten of the parent corporations in manufacturing are operating in the agro-business industry dealing with inputs and ingredients or agricultural products, and five corporations are operating in the health industry.

PRELIMINARY RESULTS

Given that we are not running regressions because the total population is small (n=22), the analysis is based on the actual numbers resulting from the survey.

The first proposition relates to the motives of Danish firms for locate activities in Argentina where we suggested that it was mainly for market seeking reasons. This is confirmed by the data where 77% or 17 out of 22 affiliated said that access to the Argentinean market was the only or major reason to locate, and 41% answered that access to the Mercosur market similarly was the only or major reason. It is not surprising that Argentina is an attractive market for some Danish corporations. However, this market potential can be exploited by either exporting directly to the market or by locating production in the country. We pursue this issue further in the analysis below of the second proposition.

Our second proposition looks only at the Danish corporations in the manufacturing sector which have offshored production activities to Argentina. The data shows that among the sixteen manufacturing corporations only five have located production activities; four of them are relatively large corporations. The reasons for the location appears mixed as indicated in Table 3 but although the number is small the market reasons both with respect to the Argentinean and Mercosur markets appear important as well as following clients and customers. Access to cheap labour and other assets play a less significant role.

Table 3: Manufacturing corporations who located manufacturing activities in Argentina

Motive for investment:	**Number of manufacturing firms**	**Number with 1-3**	**Number with 4 and more**
Access to the Argentinean market	**5**	**2**	**3**
Access to the Mercosur market	**5**	**2**	**3**
Access to low cost labour	**4**	**3**	**1**
Access to inputs and natural resources	**5**	**4**	**1**
Access to other cost reduction (tax; subsidies)	**4**	**3**	**1**
Access to know how, technology, strategic assets	**4**	**4**	
Following customers and clients	**5**	**2**	**3**
Locate before competitors (first mover)	**5**	**5**	
Other:	**1**	**1**	

Note: 1-3 no, minor and moderate reason; 4-5 major and only reason.

To analyse our first proposition on what type of functions Danish companies locate in Argentina we first look at the resource transfers between parent company and affiliate as shown in Table 4 that shows a high degree of transfer of resources from the parent company important for the affiliate's competitive advantage. The resource transfer is important for the affiliate to operate but its does not mean that the affiliate has less autonomy.

Table 4: Resource flows from the parent company to the affiliate and the importance for competitive advantage

Number of resource flows	**Number of firms**	**Number of firms with at least one flow of definite or major importance**
0-4	2	1
5-9	16	15
More than 9	4	4

The figures in Table 4 support our third proposition that the MNC parent company transfer many resources to the affiliates and that these resources are considered important for the competitive advantage by the affiliates.

If we look at the affiliates' relation to local partners Table 5 shows the number of partners in the three categories 1) suppliers/subcontractors; 2) distributors and buyers, and 3) alliance partners.

Table 5: Number of alliance partners

Number	Suppliers/subcontractors	Distributors/buyers	Alliance partners
None	8	6	6
One	2	6	4
2-9	5	5	1
More than 9	3	2	0
n=	18	19	11

Four affiliates (n=20) have answered that they don't have partners of any type in Argentina with which they have linkages and transfer resources, which means that they operate on pure market terms in Argentina with no relations to local firms. Otherwise around 45%, 66% and 45% have one or more partners in the three respective partner categories.

When we then look at the affiliates' transfer of resources we have in Table 6 measured how many types of resources are transferred and the perceived importance for the partners competitive advantage.

Table 6: Resource transfers to vertical partners and competitive advantage importance

Number of resource transfer to upstream activities (14 flows)	Number of firms (strong linkages)	At least one resource flow of major or definite importance
0-4	12 (1)	1 (0)
5-9	8 (2)	5 (2)
More than 9	2 (2)	1 (1)
Number of resource transfer in downstream activities		
0-4	8 (1)	2 (0)
5-9	10 (3)	9 (3)
More than 9	4 (2)	4 (2)

Note: 1=Not important; 2=Minor importance; 3=Moderate importance; 4=Major importance; 5=Definite importance.

Here we see that the transfers to local suppliers and subcontractors only include a relatively small number of resources and that these resource flows are not perceived important for the partners' competitive advantage. When there is a larger number of resources transferred, one or more are most often considered important for the competitive advantage of the partner. The transfers of resources that are considered important are product/service specification, technical assistance and training of partner staff for both upstream suppliers and subcontractors, and distributors and buyers. However, when the importance is measure at the Likert scale the importance for downstream partners seems larger than for suppliers and subcontractors upstream.

This picture changes when we look at the transfer of resources downstream to distributors and buyers. Here a smaller proportion of affiliates transfer a low number of resources (four or less), while the majority of affiliates (67%) transfer 4 or more types of resources, and this type of transfer include in almost all case resources considered important for the partners competitiveness.

We will consider proposition four only partly supported in the sense that only the Danish affiliates operating in Argentina appear in particular to transfer resources of importance to their down stream partners of distributors and buyers while the flows to their suppliers and sub-contractors are fewer and less important.

In the questionnaire the affiliates were asked if they among their local partners had some with which they would considered having strong linkages defined as linkages where there is frequent interaction with the business partner and the partnership is of strategic importance to the affiliate. Nine out of the twenty-two answered positively. In Table 6 we have indicate the numbers of strong linkage partners in parentheses. The number is small but the results tend to support our expectation that these linkages have a transfer of resources more important for the competitive advantage of the local partners.

CONCLUSIONS AND FUTURE RESEARCH

The study asked the questions of why Danish firms locate in Argentina and how they cooperate with local firms and what is the impact of this cooperation on the partner firms? To answer these questions five propositions were developed on why Danish firms located activities in Argentina, what types of activities they locate and the extend and importance of resources transferred by the parent company to the affiliate. On this background it was proposed that the transfer of resources from the affiliates was important for the competitive advantage of the local partners, and in particular for those where there were strong linkages between the partners.

A framework was developed to analyze the competitive importance of the resources flowing from the partner company to the affiliate and from the affiliate to its partners.

Based on an analysis of 77% of the total population of Danish affiliates it was found that market seeking was the overall motive for location and that few manufacturing companies had established production activities. Most affiliates were sales subsidiaries to serve firstly the Argentinean market and secondly Mercosur. Following the nature of the location motive, it was found that the affiliates had more linkages with downstream partners and the resources transferred to the distributors and customers were considered more important for the competitive advantage of the partners. There were fewer partners where the linkages were considered strong but in these cases the resources transferred were considered more important.

The preliminary results from this research indicate how investments coming from Danish companies with a market seeking profile in particular transfer resources considered to have a competitive advantage to downstream partners while linkages to upstream suppliers and sub-contractors are fewer and less important.

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