The evolution of internationalization
Towards a new theory?

ANTÓNIO CARRIZO MOREIRA

ABSTRACT: The theories of internationalization encompass a wide variety of explanatory elements that follow the firms' responses to distorted, imperfect markets. Whilst traditional theories were concentrated on foreign direct investment and on how multinationals enlarged their involvement in international markets, recent theories have focused their attention on small to medium businesses following either a staged model or a networked approach. There has been wide disagreement regarding all theories of internationalization. This paper provides a brief literature review on the main theories of internationalization and concludes that due to the emergence of a new polycentric economic world a new theory encompassing new important factors is in strong demand.

Key words: Theories of Internationalization, Internationalization, Multinational Firms, SMEs

TÍTULO: A evolução da internacionalização: a caminho de uma nova teoria?

RESUMO: As teorias da internacionalização agregam uma ampla variedade de elementos explicativos das respostas que as empresas têm dado a mercados imperfeitos. Embora as teorias tradicionais se tenham concentrado no investimento directo do estrangeiro e as multinacionais tenham alargado o seu envolvimento em mercados internacionais, as teorias mais recentes têm focalizado a sua atenção nas pequenas e médias empresas, seguindo, principalmente, duas abordagens: o modelo sequencial e o modelo em rede. A discussão em torno das teorias da internacionalização tem sido ampla. Este artigo fornece uma breve revisão da literatura das principais teorias da internacionalização e conclui que, devido à emergência de um novo mundo policêntrico, uma nova teoria que envolva tanto as pequenas e médias empresas como o novo policentrismo é necessária.

Palavras-chave: Teorias da Internacionalização, Internacionalização, Multinacionais, PME

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There have been a variety of different approaches to explain the internationalization of business activities. They normally concentrate on distinct aspects of the reasons for, and results of, enterprises operating in more than one environment and have changed dramatically throughout the last decade.

Whereas traditional theories have focused their attention on the internationalization of production and foreign direct investment (FDI) where the multinational enterprise (MNE) played a central role, recent theories have approached internationalization as a process in which firms increase their involvement in international operations adapting their strategies, resources and structure to new investments. The focus of recent theories has centred on small and medium-sized firms (SMEs).

The internationalization of firms, the liberalization of the world economy and the globalization of business have brought about new interdependencies among firms along the value chain as well as among countries. With the pervasive changes imposed by this new international environment, the literature about internationalization has remained partially scattered focusing different non-related topics. Clearly, there is almost no general theory of internationalization of a firm. As a consequence, the main objective of this paper is to assess the evolution of the main theories of internationalization in order to pave the way for a new theory of internationalization that takes into account SMEs, MNEs, Nation-State interests, a process view of internationalization and the eclectic paradigm.

This paper is divided into eight sections. The first is the introduction. The second examines neo-classical theories of FDI. The third section deals with the approaches studying the international production: the market power approach and the internalization approach.

The macroeconomic approaches to FDI are addressed in the fourth section of the paper. The fifth section stems from the notion of absorptive capacity and the cumulative process of technological development.

The sixth section deals with a synthesis of the other theories of international production: the eclectic paradigm, which attempts to analyze the *whys* and *wherefores* of firms' decisions in terms of ownership, locational and internalization advantages.

Section seven addresses the internationalization of SMEs following two main strands: the Uppsala model and the network approach, which are concentrated on SMEs. Finally, section eight summarizes the different theories put forward throughout the paper and concludes with a proposal for a new theory incorporating Nation-

States, SMEs, a new blend of the eclectic paradigm and a networking view of the relationship of SMEs-MNEs in the value chain.

NEO-CLASSICAL THEORIES OF INVESTMENT

Hymer's (1976) presented the first theory of foreign direct investment. A considerable amount of literature existed on foreign investment but no difference was made between portfolio investment and foreign investment.

According to neo-classical theories, FDI is the consequence of comparative advantages held by host countries. Therefore, the differences in production factor-prices are seen as one of the main motives for the localization of MNEs in developing countries. Like the neo-classical theory of trade, the neo-classical theory of foreign investment also assumes that countries are differently endowed in abundance of capital and labor.

In the traditional neo-classical approach, economically advanced countries tended to export goods requiring capital-intensive production methods to less-advanced labor-abundant countries. It was also assumed that salary differentials between home and host countries were the main motives for attracting FDI, which was afterwards dismissed not only because the productivity/salary cost relation proffers a more appropriate explanation of the location of MNEs in several countries (Andreff, 1995), but also because most MNE salaries are higher than local firms in host countries (Rainelli, 1979).

Due to the assumptions of the neo-classical approach (perfectly competitive markets, identical production functions in different countries, and perfect knowledge and certainty), it is unsuited to explain today's activities of the MNEs: they neglect production functions, firms and product and service differentiation. Consequently, as technological mastery allows firms to evolve from their initial factor-endowments, comparative advantages should not be regarded from the static viewpoint because they are dynamic in nature.

THEORIES OF THE FIRM

The Market Power Approach

One of the first theories addressing the issue of international production is Hymer's (1976). The theory was the first to leave behind the articulation of international production with international trade and capital movements. The theory suggests that a firm's main motivation to locate production facilities abroad involves the pursuit of market power and not the desire for technological advance. According to Hymer (1976) the objective of locating production abroad is to extend collusive networks, to decrease the level of competition and to increase the entry barriers to outsiders, i.e., to take advantage of the restrictive and anti-competitive nature of MNEs' impact on market structure.

In considering what differentiates FDI from a portfolio investment, Hymer (1976) and Kindleberger (1969) assume that direct investment abroad is costly and risky and therefore the firm decides to engage in it because it gives the investor the control over the investment.

The most important of the motivations to exploit market imperfections by FDI is that it allows the firm to exploit collusion abroad and therefore weakens competition in the expectation that it will lead to larger profits. This advantage, based on financial, innovation, cost, or marketing aspects, is specific to ownership and is very important because it will allow the firm to successfully compete with indigenous firms in their own market. This type of market imperfection is the kind of "ownership" advantage that a firm undertaking FDI must possess in order to counterbalance the relative advantages of native firms. The second motivation is the firms' advantage to operate, produce and/or market in any industry. The third motivation mentioned by Hymer (1976) is the drive of large firms towards diversification. Clearly, market imperfections not only alter the behavior of firms, but must also counterbalance the high costs of direct investment abroad.

Both Kindleberger's (1969) and Hymer's (1976) messages are very clear: perfect competition must be avoided for direct investment to succeed and this creates conflicts. Market imperfections can be created in four different ways. Firstly, in the goods markets, especially due to marketing skills, product differentiation, pricing, etc. Secondly, in factor markets, especially due to access to capital markets, superior management, "proprietary" knowledge or better technology. Thirdly, through the creation of internal and external economies of scale (which are directly linked to market imperfections). Finally, through the governments' intervention in the production and trade, namely restricting output and entry.

Internalization Approach

The internalization approach is closely associated with transaction costs economics that draws from Coase's work (1937) on the efficiency with which transactions between agents of production are organized. As transactions might be organized both internally and externally, the concern of the internalization theory is to identify the mode of transfer in which its effective cost is minimized.

When the transaction costs of a cooperative exchange are lower than those of a market exchange, the market must be internalized in order to increase the collective efficiency of the group.

Buckley and Casson's (1976) theory of MNE postulates that:
- firms maximize profit in imperfect markets;
- due to market imperfections, there is an incentive to internalize markets; and
- internalization of markets across national boundaries generates MNEs.

The basic assumption behind the internalization approach is the existence of market imperfections. Therefore, the firm is the direct organizer of non-market transactions, and is concerned with the most effective position of the boundary between the internal and external environment. The firm might be defined as the controller and coordinator of a network of transactions (Cowling and Sudgen, 1987). In this sense, transactions are of an external market kind, but production may be controlled and coordinated by its own administrative center.

The internalization approach has two important strands that must be considered. The first is that internalization can substitute external arm's-length contracts for internal markets, due to lower transaction costs. The second strand comes about when a market is created within the firm when the external market is absent. These two strands are especially important in the transaction of intermediate products – in the first case – and intangible assets as knowledge or technology – in the second case.

The advantages of internalization stem from market imperfections, especially when (Buckley and Casson, 1987):
- there are long time lags to access unsatisfactory future markets and to implement alternative production processes;
- discriminatory pricing is needed to exploit market power efficiently;
- bilateral market power might be generated;
- there are uncertainties in the transfer of knowledge between parties;
- there are imperfections deriving from government intervention by devices such as tariffs, taxation and restriction of capital movements.

The main problem with the internalization approach is that it may explain the growth of the firm but surely does not explain why firms decide to take the multinational route. Another drawback is the relevance given to R&D and to the fact that MNEs tend to operate in knowledge-base industries.

Buckley and Casson (1987) argue that knowledge is cheap and riskless when transmitted internally but not externally, which makes it easy to transmit across internal borders but not externally. Although this might explain why some firms generally prefer direct production abroad to licensing in their foreign operations, it certainly does not explain why firms prefer to serve foreign markets through international production rather than by exports.

The rationale behind both the internalization and the market power approaches lies with the firm's current state, the advantages it possesses *vis-à-vis* other firms and its attempts to maximize returns from foreign markets. The main difference between the internalization and the market power approaches is that the motivation of the latter is perceived as a desire to increase the firm's market power whilst the motivation of the former is perceived to be the minimization of coordination costs between national boundaries.

MACROECONOMIC APPROACHES TO FOREIGN DIRECT INVESTMENT

Technological Gap Theory

Posner's (1961) analysis on how an initial product innovation in one country led to both cumulative technological and trade advantage resulted in the development of a set of theories around the concept of "technological gap". Posner (1961) proposed the technological gap theory based on different propensities of firms for learning and innovating, which led to the development of dynamic economies of scale. For Posner, trade advantages were the result of cumulative advantages of innovating firms that managed to gain experience in international production.

Hufbauer (1966) modified Posner's technological gap theory of trade by introducing two important points: a) the length of time to produce a new product as the relevant variable and not just the volume of past production in order to modify the learning function and its related lag and b) the differences in relative wages in the trading companies.

A new approach was explored by Hirsch (1965) that tried to relate the growth of the demand during the product's life cycle from invention to maturity. He analyzed the phases of the product's life cycle in relation to the technology and scale of production, the type of labor skills needed, and the countries' comparative advantages.

According to Hirsch (1967), developed countries have an advantage in the first phase of the product's life because they can provide the engineering and scientific capabilities required, which are not likely to be present in developing countries. In the growth phase of the product, the developed countries still have advantages over developing countries because of the managerial and organizational skills, and financial capabilities needed to produce on a very large scale. In the last phase of the product's life developed countries are, in general, likely to favor developing countries where labor costs are lower and thus tend to lose competitiveness.

Product Life Cycle Model

Hirsch, Posner and Hufbauer analyzed the trade effects of the technological gap between countries. At about the same time Linder (1961) suggested that trade flows were greatest between countries with similar factor endowments due to the similar levels of income and demand.

The Product Life Cyde (PLC) approach attempted to combine ideas from Posner (1961) and Linder (1961) in order to explain trade patterns in the post-war period. Vernon (1966) used a microeconomic concept to explain a macroeconomic phenomenon: the growth of the USA FDI in Western European countries in the post-war period. The main argument used by Vernon was that the high level of income and demand fostered innovation, which gave American firms an advantage to increase exports and then through import-substituting investments in Europe.

Vernon's PLC model underpinned its theory in the location of production. In its initial phase, production would take place in the home market. This is based on the fact that all activities necessary for creating a new product are likely to be based in the firm's own market for its own market. In a later phase in the cycle, as demands spread at home and abroad, the advantages of the firms are likely to be most fruitful in countries with similar high-income demand patterns. This will give the firms an impetus to export to "similar" countries. Later in the cycle, as the product becomes more and more standardized, it is more easily imitated by competitors. Competitiveness is likely to depend less on the uniqueness of the product and more on cost--cutting activities. The importance of low labor costs relative to total costs, the increasing elasticity of demand, the broadening of competition and the expansion of foreign markets are factors that might lead to a strategy of locating production overseas. As the product matures, trade would return to a cost-based comparative advantage pattern. In this situation MNEs would have to rely more on barriers to avoid activities from competitors and less on technological advantages.

The main inadequacy of the PLC approach to explain FDI has been questioned by several authors: Yamin (1991), Cantwell (1995), Kojima (1978).

Yamin (1991) argued that with increasing international integration and with the change of perspective in the internationalization of firms, more and more firms are likely to encounter each other in the international arena and therefore the degree of unrivalled technological leadership will no longer be enjoyed by American firms.

Cantwell (1995) questioned Vernon's model hypothesis (innovators are virtually always generated in a firm's home country and technological leaders are predominantly international investors). He not only demonstrated the geographical dispersion of the innovation within MNEs, but also restated the second hypothesis arguing that the internationalization of technological development is led by firms with the strongest records in innovation.

The PLC model suffers from a preoccupation with FDI as an import-substitution vehicle. In his criticism of PLC approach Kojima (1978) considered the distinction between import-substituting (trade-displacing) and export-platform (trade creating) types of investment.

Kojima and Ozawa (1985) claim that global welfare is increased where international production helps to restructure the industries of each country in line with dynamic comparative advantage. Their argument is extremely useful in contexts of rapidly expanding economies that may be both able and willing to relocate less advanced activities in LDCs and upgrade their domestic production activities in their home countries.

THE TECHNOLOGICAL ACCUMULATION APPROACH

The central idea of the technological accumulation approach is that technological development is a cumulative process, i.e., it is seen as a gradual and a continuous improvement of existing techniques that take place through adopting, testing and implementing new ideas either in the production process or in the technology creation phase.

The technological accumulation approach rests upon the notion of absorptive capacity and maintains a dynamic character. It suggests that the interaction of production and technology creation leads to similar paths of technological development. Although firms in a similar industry tend to employ similar production techniques and encounter similar technological problems, each firm follows a unique path.

Cantwell (1989) and Pavitt (1987) have been notable in the development of the technological accumulation approach. They suggest that the generation of innovations and the international production reinforce and spark off each other.

The technological accumulation approach considers technological competition to be a major driving force for firms competing in oligopolistic international industries. Competition makes firms aware of the creation of new skills and competencies that will allow them to compete for a better market position and to improve their competitiveness. The technological accumulation approach compels firms to foster the creation of the basis of the exploratory potential to compete in different environments and in different industries, and not to be focused merely on the creation of new products.

If technological development is cumulative and unique for every single firm, problems will be encountered every time a firm tries to acquire brand new technologies instead of developing them internally. Costs of adapting external technologies to the firm's requirements may be high vis-à-vis to the possibilities of the seller of the technology extending its own network.

Kogut and Zander (1993) studied the difficulties of inter-firm technology transfers and argued that MNEs arise because intra-firms transfers of tacit knowledge are more efficient than inter-firm ones.

Following Kogut and Zander's (1993) work, it might be argued that technological development is organizational in nature, unique and path-dependent. Therefore, it might be considered a potential entry barrier for the transfer of technology across organizational boundaries. The existence of a broad international network in the international business arena is just a reflection of the nature and consequences of a technological development, its uniqueness and its path dependency.

Several points can be highlighted as contributions of both the technological gap approach and the PLC model (Ietto-Gillies, 1992):

- technological advantages lead to competitive advantage;
- technological advantages are cumulative in nature. Among the reasons behind cumulativeness are the dynamic economies of scale, learning-by-using, doing and implementing and a tendency towards the accumulation of inventions;
- the change of comparative advantages during the life product phases, i.e., the country with advantages in the initial phase of the product is likely to lose the advantage when the product reaches maturity;
- imitation effects are likely to be stronger in countries with high incomes. The mechanisms and speed of imitation in production are linked to the market structure in which firms operate.

The PLC theory is very interesting for several reasons. Firstly, it is very dynamic. There is a strong interplay between the role of consumers, the role of producers and the market structure. Secondly, it relates production with market elements: technology and know-how are endogenous and are linked to the economic environment of countries and to market conditions.

The main weakness of the PLC model is its excessive concentration on the product and its life. Vernon's theory loses important elements linked to multi-product firms, diversification strategies, normally related to multinational strategies and to accumulation of technological advantages.

THE ECLECTIC PARADIGM

The eclectic paradigm, proposed by Dunning (1977) is basically a synthesis of other theories of international production. Dunning considers two types of investment. The first is related to economic activities that take place within national boundaries but related with goods and services directed towards foreign markets. The second is related to the activities of national economic agents that use resources located in a variety of countries to produce goods and services in order to supply foreign markets. The former involvement falls within the conventional trade theory, the latter within the international production and FDI approaches.

Dunning's approach is an attempt to analyze the *whys* and *wherefores* of the firm's decisions in terms of *Ownership, Location and Internalization* advantages. Ownership advantages are those that are unique to a particular firm and enable it to take advantage of investment opportunities abroad. Locational advantages are those which are specific to a country. These types of advantages are especially attractive for foreign investors. Internalization advantages are the benefits that derive from internal markets and that allow firms to bypass external markets and the costs associated with them.

The eclectic paradigm contends that MNEs possess ownership advantages *vis-à-vis* their competitors, which can be further exploited by locating production in countries with locational advantages. According to Dunning (1977), there are three types of ownership advantages; the first is due to the ownership of particular, unique intangible assets, e.g., firm-specific technology, knowledge of markets, R&D, etc. over other firms in the market. The second is attributable to the collective ownership of complementary assets, e.g., joint ability to create new technologies, usage of raw materials, access to market, monopoly power and size. The third type of ownership advantage derives from the firm's multinationality, i.e., a firm operating in many countries is likely to be in a better position than a national firm to take advantage of different business situations.

It is argued that an international network control is retained by MNEs due to the internalization advantages, which stem from the ability of the firm to appropriate full return on its ownership of specific assets as well as from the coordination of the use of complementary assets. It is recognized by Dunning that the internalization advantages result from the transactional market failure. Three reasons for this market failure are given: the first is risk and uncertainty of transactions carried out across national boundaries. The second is the existence of externalities that may not be exploited in an arm's-length transaction. The third is from the economies of scope generated through the coordination of the interrelated activities.

Dunning (1993) identifies three conditions for FDI to take place:
1. the firm must have ownership-specific advantages (O) vis-à-vis other competitors of other nationalities in the particular market it serves;
2. the firm must have benefits from internalizing the use of resources in which it has an (O) advantage rather than selling them. These advantages are the internalization advantages (I);
3. the global interests of the firm are served by creating (O) advantage in a particular foreign location, assuming that (O) and (I) conditions are satisfied. This will confer the firm with an (L) advantage.

The incentive to internalize derives from the existence of market imperfections. They might be structural, as e.g. barriers to competition, or cognitive, e.g. imperfect knowledge. As mentioned above, the eclectic paradigm is a synthesis of other approaches that concentrate on trade or international production, on the possession of superior technology or on imperfect market structures.

The eclectic paradigm has strong points which make it very successful. Nevertheless, it cannot explain the case of European countries (Ietto-Gillies, 1992), which: a) are heavily involved in both inward and outward FDI and b) where the largest share of FDI is directed towards developed countries.

THE INTERNATIONALIZATION OF SMES

Although abovementioned theories have been used to explain the determinants of firms' internationalization they have been criticized for their focus on:
- FDI, with little regard for other modes of entry in foreign markets,
- large multinational firms.

The great advantage of these two models is that they underpin the explanation of the behavior of those firms in the early stages of internationalization whilst the theories focused on former points are more suited to explaining the behavior of large multinational firms.

As the importance of small and medium-sized firms has been explicitly exposed for most of the world's economies because they represent around 61% of total turnover and 73% of total employment (OECD, 1997c), it is not strange that academia, public policy makers and businessmen have turned their attention to the internationalization of SMEs. Accordingly, the theories of internationalization would not be complete without addressing their importance in SMEs.

A Process View of Internationalization

The international process perspective grew from the seminal work of Johanson *et al.* (1975) on the internationalization of four Swedish firms. They realized that those firms followed an evolutionary four-stage internationalization process known as the establishment chain. Initially, the firm has occasional exporting activities. In the second stage, the firm exports regularly through agents due to its growing knowledge of the foreign market. In the third stage the firm has a deeper involvement abroad and exploits the market through a sales marketing subsidiary and, finally, the firm engages in international production in the fourth step. Clearly, FDI only occurs in the third and fourth stages.

This process is based on a linear cumulative path in which the absence of international experience reduces the propensity of the firm to engage in unknown markets. As a consequence, the firm initially focuses its activities on the national market in order to avoid unnecessary risks (Johanson *et al.*, 1977). As soon as the firm gains experience in foreign markets and manages to internalize the knowledge gained, it is willing to underpin its subsequent stages committing more resources and controlling its operations abroad (Loustarinen, 1979; Johanson *et al.*, 1977).

In order to explain the progression of the firm's activities to foreign markets, Johanson *et al.* (1975) used the concept of *psychic distance* which involves differences in culture, languages, education, industrial development, political systems, among other things. They found that SMEs normally internationalize to low psychic distant markets in the first movements abroad and once they gain experience in these markets they expand their activities to more psychic distant markets.

Despite their linear point of view, Johanson *et al.* (1977, 1990) claim that not all firms must go through all stages. Firstly, some firms are resource intensive or large enough to short-circuit stages (mergers and acquisitions are typical examples). Secondly, when foreign markets are as stable as local markets or when firms have a strong stock of knowledge gained in other markets, firms are expected to skip some stages as a consequence of their former experience.

This model lives in a permanent dilemma confronting the dynamic and static perspectives of internationalization. While the static perspective focuses on the operations, commitments and knowledge the firm holds in the market, the dynamic perspective deals with the evolution of the international activities, namely with the decision of committing the firms' resources *vis-à-vis* the risk of the several markets and the lack of experience in those markets.

Some criticisms have been put forward on several grounds. Reid (1983) and Andersen (1993) question the model asserting that while it describes the international expansion process it does not explain the reasons why firms embark on each stage of the model. Turnbull (1987) criticized its deterministic perspective defending that internationalization does not necessarily follow a linear path. Sullivan *et al.* (1990) have questioned the influence of geographic distance in the internationalization process in their research. Vahlne *et al.* (1990) and Dunning (1995) assert that the distance to the market loses a great part of its significance with the on-going globalization process in which the liberalization of trade, the Internet and the diffusion of English as a common business language have made the world shrink.

Leonidou and Katsikeas (1996) have also criticized the Uppsala model on structural, methodological and conceptual grounds. They defend that casting away other business activities besides those being assessed clearly undermined the operationality of the model. Another criticism advanced is the lack of extensive support of the psychic distance which was totally different at the time the model was presented and the international, more open business environment we find nowadays.

Forsgren (1989) advances two criticisms on conceptual grounds defending that the Uppsala model does not only explain why the firm starts its internationalization process and does not include acquisition as a means of entrance in their markets.

Although the model has been extensively validated (Bilkey and Tesar, 1977; Czinkota, 1982; Reid, 1981) in its evolutionary progression it ignores two important aspects: (a) how the inward internationalization process has underpinned the firm's outward posture (Stahl, 1999); and (b) how firms manage the intricacies of de-internationalization in its outward internationalization process (Wech and Loustarinen, 1988).

More recently, the emergence of the *born-globals* (Rennie, 1993; Madsen and Servais, 1996; Rasmussen *et al.*, 2000) has also questioned the traditional pattern of the internationalization process which has been affected by the globalization process and the development of new communication and information technologies.

The Network Approach to Internationalization

The importance of the relationship between all agents of the value chain was popularized by Håkansson (1987) with his interactive approach on the Industrial Marketing and Purchasing Model.

The participants (suppliers, buyers, competitors or other institutions) in the process and the environment of an interaction affect the way in which firms interact. The complementarities of the participants enable the creation of a network of relationships in which the internationalization takes place when the network is extended abroad. This network-based internationalization should be based on the context in which participants operate and on the condition in which they operate (Madsen *et al.*, 1997) and on the interdependent, non-hierarchical exchanges (Coviello *et al.*, 1999) that lead to the emergence of the concept of business networks.

The network approach to internationalization was put forward by Johanson *et al.* (1988), who concluded that the degree of the firm's internationalization depends on both the networks established by the firm and the position of the firm in that network. As a consequence, the network in which the firm operates affects its international position.

Johanson *et al.* (1988) claim that traditional models are biased when both the firm and the market are strongly internationalized because the degree of market internationalization affects the factors that lead firms to internationalize. Despite the networked approach, Johanson *et al.* (1992) recognized that the internationalization is a cumulative process that depends on the result of the firm's interaction and on the long-term perspective of the relationships.

Coviello *et al.* (1997) concluded that firms' internationalization is more based on opportunities as a result of previous contacts than on strategic decisions. They claim that the incremental process view should be merged with the networked perspective in order to address how the lack of resources of most SMEs does not inhibit firms in their search for foreign markets.

Clearly, internationalization approaches are far from a unique solution. As Loustarinen (1994) and Welch *et al.* (1993) claim, the process perspective should encompass the inward, outward and cooperative phases from a holistic point of view.

Accordingly, the internationalization process should not be seen as a one-way street and should include the de-internationalization of the firm (Loustarinen and Welch, 1988).

From the firm's resources point of view, internationalization should be based on the firm's competencies. Accordingly, due to resource differences, all firms should not only have different internationalization processes but should also emerge in different strategies and relationships. As a consequence, there should not be any definite sequence pattern in the internationalization process and the network approach should be interpreted as a search for dynamic complementarities between firms belonging to markets with different growing and economic potentials.

Another important point that deserves a more consistent approach is the relationship between the need for cooperative agreements and its relationships with the R&D investment strategy. Although the entrance in any form of cooperative agreement presupposes that the firm has core competencies in particular areas, it is not clear how distributed is the cooperative network and how all participants complement each other dynamic complementarities.

The growing number of firms that are internationally involved from their beginning (Coviello and Munro, 1997; Madsen and Servais, 1997) challenge the traditional approach followed by the Uppsala model. Based on research on the pattern of the international expansion of new technology-based firms (NTBFs), it was clear that those NTBFs relied on a significant number of cooperative agreements to underpin their international agreements and did not follow the gradual pattern of the Uppsala model. These *born-global* firms, as Rennie (1993) called them, represent a new challenge for the internationalization of firms.

Finally, the emerging multinationals of the new economy or *metanationals* (Doz, Santos and Williamson, 2001) overcome their competitors by sensing, mobilizing and integrating their resources at international level.

According to Doz, Santos and Williamson (2001) metanationals have three levels of competition: (a) the identification and assessment of new competences, innovative technologies and leading market knowledge; (b) the integration of scattered capabilities and knowledge in order to pioneer new products and services; and (c) the optimization of efficiency of their distributed operations. The particularity of the metanationals is that all new challenges and new opportunities of the three levels of competition happen at a global level, and the winners are those that manage to tap the potential of technology, capabilities and market potential scattered around the globe.

For metanationals to succeed in this new knowledge economy, they need to augment their existing capabilities instead of relying on the clones of today's multinationals.

As in the case of born-globals, the metanational questions the gradual pattern of the Uppsala model and emphasizes the importance of networking activities that seek the complementarity of the firm's resources.

TOWARDS A NEW THEORY?

The aforementioned theories attempt to explain the international production phenomenon and the existence and growth of the MNEs. Most of the FDI theories can be seen as a different response by the MNEs to imperfect markets.

The theories of FDI outlined in this paper are centered on the explanation of responses by MNEs to imperfect markets. They generally tend to explain the phenomenon of international production and the existence of the growth of MNEs.

The theories of FDI have focused on factors that give the firm the capability to move from being predominantly domestic to operating in foreign countries. There was a general lack of interest in the generation and transfer of technology which is considered exogenous to the firm, or implicit in operative terms. Once the firm operates in a truly international environment, all the conditions and considerations related to the exercise of technology power remain either exogenous or implicit.

When compared to the technological accumulation approach and to the eclectic paradigm, the classical theories seem to be losing importance especially when technological change is increasing and international competition is more intense.

The technological accumulation approach considers that technological development is cumulative and unique for every single firm. Although problems are foreseen every time a firm tries to acquire a new technology instead of developing it internally, the technological accumulation approach does not explain why firms operating in foreign countries and competing in different environments tend to rely more and more on collaborative agreements and on sourcing policies.

The change in nature of international and technological competition reflects the changes in emphasis of most of the theories of FDI from a narrower concern to a wider dimension, i.e., towards a more balanced approach recognizing exploitative aspects.

Although the eclectic paradigm is seen as a synthesis of theories of international production, it remains microeconomic in nature. Kojima (1990) criticises the eclectic paradigm for abandoning the macroeconomic approach and for neglecting the country as a variable of analysis. Mucchelli (1990) asserts that the eclectic paradigm also neglects the sectoral influences, the alliances between firms and the global strategies followed by MNEs.

Mucchielli (1985) argues that the internalization approach gives way to eclectic approaches in which "anything can happen" based on situational and suboptimal advantages. Accordingly, it is only of advantage to those MNEs that maximize profits at a global scale and prejudicial for most national and international markets due to creating more imperfections.

The market power and the internalization approaches, very popular during the seventies and eighties, remain valid despite the more liberal economic involvement found since the nineties. What is new in this polycentric world is that economic functions of the State are being transferred to MNEs and most of the world's countries struggle to attract FDI (Lemeire, 1997; Michalet, 1999); this confirms Hymer's (1972) assertion on how MNEs organize the world by imposing a hierarchy on national economies as a consequence of the exercise of the economic power of their organizations and strategies.

A new world capitalism is emerging not only due to the accumulation of capital and profits, but also derived from the concentration of strong bargaining power in large MNEs. On the other hand, SMEs around the world are also expanding internationally as a consequence of two dynamics: firstly, they are exploiting the new opportunities opened by the globalization process playing the rules of the game imposed by MNEs. Secondly, they are expanding their activities as a response to the interest of Nation-States that seek to stimulate the multinationalization of their firms.

The abovementioned theories are being questioned due to the polycentrism of the international economic power: though they remain valid, they are being shaken due to epistemological issues that posed by globalization. In this regard, a new globalization theory that includes the following topics is on the rise: (a) Nation-States as major players with specific interests at local and global level; (b) SMEs willing not only to play active roles in local markets, but also globally, as new opportunities scattered around the world can be sensed and exploited; (c) the process of SME-MNE involvement in global value chains, which is a mixture of the Uppsala and the process model, taking into account their relationships along the value chain and Nation-States influences; and (d) a new blend of the eclectic paradigm that involves the three above-mentioned topics.

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