2005

Europe, Spain, and the Future of Spanish Multinational Firms

Mauro F. Guillén
University of Pennsylvania

Recommended Citation (OVERRIDE)
Guillén, M.F. (2005). Europe, Spain, and the Future of Spanish Multinational Firms. In Guillén, M.F. *The Rise of Spanish Multinationals: European Business in the Global Economy*, 224-232. Cambridge University Press.

Europe, Spain, and the Future of Spanish Multinational Firms

Abstract

The last fifteen years or so have witnessed a major transformation of Spanish businesses. After decades of protectionism and isolation, virtually all of them are now exposed to the winds of international competition; nearly a thousand have invested abroad in order to exploit the opportunities inherent in operating across borders. As a result, Spain has become one of the ten largest foreign direct investors in the world, with key consequences for the country's economy, financial system, diplomacy, image and society, as well as for Europe.

Disciplines

Business Administration, Management, and Operations | Business Law, Public Responsibility, and Ethics | Corporate Finance | International Business | Management Sciences and Quantitative Methods | Marketing | Organizational Behavior and Theory

10 *Europe, Spain, and the future of Spanish multinational firms*

That they invent things? Let them invent!
The electric bulb illuminates here as much
as where it was invented.

Miguel de Unamuno (1906)[1]

It suffices to take a look at a map to see that
the natural strategic advantages of Spain are
so formidable that if the country is strong
then it will play a major role in global
affairs, but if weak it will attract the
attention of the strong.

Salvador de Madariaga (1931)[2]

THE last fifteen years or so have witnessed a major transformation of Spanish businesses. After decades of protectionism and isolation, virtually all of them are now exposed to the winds of international competition; nearly a thousand have invested abroad in order to exploit the opportunities inherent in operating across borders. As a result, Spain has become one of the ten largest foreign direct investors in the world, with key consequences for the country's economy, financial system, diplomacy, image and society, as well as for Europe. Moreover, this process of foreign expansion is applauded by the population and by the labor unions. Unless jobs are destroyed in the home country, Spanish multinational firms can continue to rely on a considerable amount of social goodwill in support of their quest for international competitiveness (see chapter 9).

[1] "¿Que ellos inventan cosas? ¡Invéntenlas! La luz eléctrica alumbra aquí tanto como donde se inventó." From a letter to philosopher José Ortega y Gasset (Robles 1987: 42).

[2] "Basta una ojeada al mapa para mostrar que las ventajas estratégicas naturales de España son tales que, si fuerte, ha de representar en el mundo un papel de primer plano, y, si débil, ha de ser constante objeto de atención por parte de los fuertes" (quoted in Rubio 2003: 557).

Looking towards the future, Spanish multinational firms face three distinct challenges which also affect the country and Europe as a whole. These have to do with the sustainability of their foreign expansion, the need to improve their image, and the implications for Spain's and Europe's roles in the world. Let me analyze each of them in turn.

The sustainability of foreign expansion

How sustainable is the foreign presence of Spanish firms, focused as it is on a few industries and a few parts of the world? The answer to this question can be broken down into two interrelated issues. The first has to do with the extent to which their current foreign operations will continue to be profitable, while the second with whether Spanish firms will continue to be "Spanish" in the sense of keeping their centers of decision-making located within the country. As analyzed in chapter 6, one-third to one-half of the profits of the large Spanish multinationals come from Latin America. Those streams of profit are subject to wide fluctuations. Although Spanish firms with operations in the region have managed recent crises rather well, their long-term well-being is under constant threat. From my perspective, the best way for Spanish firms to manage this exposure is to reduce the relative weight of their Latin American operations by expanding in other parts of the world, especially Western and Eastern Europe.

The issue of managerial control is linked to the dependence on Latin American growth and profits in a paradoxical way. On the one hand, growth in a profitable albeit risky part of the world militates against takeovers or even makes the Spanish firms more capable of launching takeovers themselves due to their greater size. On the other, if those investments turn sour, Spanish firms could see their share prices plummet and they could become easy prey. I find the geographical concentration of Spanish foreign direct investment more problematic than its industry focus. I am not concerned about the importance of foreign investments in service sectors. Quite the contrary, services hold the key to the future because Spain is a service economy. Having said that, manufacturing remains an important part of Spain's economy, but I am confident that many Spanish firms have made the necessary investments to remain competitive. The geographical concentration, however, is problematic because Latin America represents no more than 8 percent of the global economy (Spain, 2 percent). If the largest Spanish multinationals remained strong in just Spain and Latin America, they would be missing from 90 percent of the global economy, hardly a desirable prospect.

Among all the peculiarities of the foreign expansion of Spanish firms perhaps the most salient has to do with its relatively small presence in the rest of Europe, which accounts for about 20 percent of the global economy. Spain has been a member of the EU since 1986, a bloc that guarantees the free movement of goods, capital, and people. Spain also is a founding member of Economic and Monetary Union (EMU). British, French, Dutch, German, Italian, and Swedish firms have long invested in Spain. They are active in service as well as manufacturing industries. Spanish firms, with only a few exceptions, do not enjoy a comparable presence in those European countries. As analyzed in chapter 5, part of the problem lies in the fact that the largest Spanish multinationals operate in highly regulated, and hence highly politicized, industries such as banking, telecommunications, and energy. In several cases, nationalism has stood in the way of the Spanish multinationals making acquisitions in Europe. I suspect that it is only a matter of time before a wave of mergers and acquisitions in the leading European service sectors takes place. If Spanish firms are not ready for it, others will be.

I fully realize that if Spanish firms do acquire a presence in Europe as well as in Latin America, they will only be strong in about one-third of the global economy. However, it takes time for firms to expand internationally, and Spanish firms need the time to acquire the requisite skills. If they join forces with their European counterparts, they will be in a much better position to pursue growth in other parts of the world. Their present organizational and managerial capabilities are perhaps appropriate for expansion in the United States and Canada, which account for almost 25 percent of the global economy. The biggest challenge will be Asia, which accounts for over one third. The three largest economies – China, Japan, and India – pose unique problems for foreign firms. Medium-sized Spanish firms in manufacturing and in services have a small presence in China, but almost none in Japan or India. The greatest stumbling-block lies in managerial personnel. It is unclear whether large Spanish firms will be in a position to expand in Asia within the foreseeable future; unless, that is, they merge with other European firms.

In the case of the large Spanish multinationals, I see expansion in Europe through mergers and acquisitions as a necessary step toward further expansion in the United States, Canada, or Asia. Without the skills and managerial personnel of their European counterparts, it is likely that Spanish firms will remain strong in the 10 percent of the world represented by Spain and Latin America, and largely absent from the rest. A different scenario might encounter the medium-sized multinationals analyzed in chapter 3, many of which are family-owned or -controlled. Some of them already have a presence on four continents. Their biggest challenge will be to find an ownership and governance structure than enables them to continue growing.

Intangible assets and Spain's international image

The sustainability of Spain's foreign investment also depends on the ability of companies to develop intangible assets such as brands, technology, and managerial know-how. It is well known that Spain allocates meager resources to R&D – no more than 1 percent of GDP – much less than most countries in the OECD except for Portugal, Greece, Hungary, Poland, Turkey, and Mexico. Countries such as Japan, Germany, Finland, South Korea, and the United States spend three times as much as Spain; France and the UK twice as much (MCT 2003). Spain is the only "advanced" country that spends more on lotteries than on R&D. In fact, lottery expenditure (which excludes casinos and slot machines) stands at nearly twice R&D expenditure: 1.8 percent of GDP (Garrett 2001).

Another peculiarity of the Spanish case is that business firms are relatively less involved in R&D than their European, Japanese, Korean, or American counterparts. While in the OECD as a whole businesses contribute two-thirds of total R&D expenditure, in Spain they only contribute about half. The reasons why Spanish firms do not spend enough on R&D are not well understood. At first sight, it seems like a lack of vision with negative consequences for their long-term competitiveness. The reality, however, is complex. One cannot generalize to the entire spectrum of Spanish firms. As observed in chapters 1 and 4, two-thirds of Spanish foreign investment has been undertaken by firms in service sectors such as banking, transportation, telecommunications, electricity, water, hotels, mass media, and security services. In these activities companies tend to buy the technology rather than create it. Their international competitiveness derives from their marketing, managerial, and organizational skills. For instance, Spanish high-technology manufacturing firms devote 11 percent of value added to R&D, compared to 5 percent for high-technology service firms (MCT 2003: 73). Still, Spanish service-sector firms compare relatively well with their foreign competitors. For instance, Telefónica devotes 1.8 percent of total revenues to R&D, an amount that, while low for manufacturing firms, is appropriate for its industry given that Deutsche Telekom spends 1.7 percent and British Telecom 1.5 (*Actualidad Económica*, 1 August 2003). As discussed in chapter 3, large Spanish firms are not the most active in R&D. Rather, it is medium-sized firms, often family-owned, which invest the most. Foreign firms established in Spain do not stand out for their R&D activities either.

The consequences of the gap in resources allocated to R&D translates into a situation in which, during 2001, for every patent filed by a Spanish resident in order to secure protection in Spain, non-residents file forty-six patents, up from nineteen in 1990. Spain imports 60 percent more high-technology products than it exports (MCT 2003: 71–3). The country's technological dependence is on the increase.

It seems rather obvious that spending on R&D must be raised, as the new head of the government has promised, and that businesses need to contribute more to that effort. There is another aspect that requires attention. According to the Heritage Foundation, the US Chamber of Commerce, the National Patent Protection System and the US Trade Representative Watch List, Spain is among a large group of countries – mostly developing – with weak protection of intellectual property rights (Zhao 2004). This may be an important reason why foreign firms prefer not to do R&D in Spain, thus depriving local firms of spillover effects.

I also believe that much of Spain's image problem, as analyzed in chapter 8, is inextricably related to the perception that Spanish companies and products tend to be low-tech and lack sophistication. The central and autonomous regional governments in Spain can spend money improving the country's image through advertising. Countries like South Korea and Taiwan, by contrast, have focused on allocating money to R&D and not to public relations. That is the example for Spain to follow. Aside from this, Spanish companies do need to work on projecting a better, more accurate image with international financial journalists. They also need to facilitate the job of equity analysts and business school faculty so that more research reports and teaching cases are written about Spanish firms.

Spain's role in the world

The writer, historian, and diplomat Salvador de Madariaga (1886–1978) put it succinctly in the quote that appears at the beginning of this chapter. Because of its strategic relevance, Spain either plays a major role on the diplomatic chessboard – as it did during the sixteenth and seventeenth centuries – or becomes a pawn in global affairs. Madariaga was an astute observer from afar of his country's predicament. A world traveler, educated in Paris at the Ecole Polytechnique and the Ecole des Mines engineering schools as well as at Oxford, and the Spanish Republic's ambassador to the US just before the Civil War of 1936–9, he was a liberal who yearned for the return of democracy to Spain, and who cared about his country's international stature. He formulated his prescient argument a few years before the Civil War, which would be proved correct: the conflict was prolonged and intensified by the intervention of Nazi Germany and the Soviet Union.

It is sad to realize that the aftermath of the horrific 11 March, 2004 terrorist massacre in Madrid also illustrates his point. With José María Aznar (1996–2004) Spain became more attuned – the critics would say subservient – to US policy. After Rodríquez Zapatero's surprise win, the country has ostensibly oscillated towards the Berlin–Paris axis. Leaning on the former or the latter is no guarantee that Spanish economic and financial interests will be observed, although I would consider the European option more compatible with them, as I explained in chapter 7. Still, because of the zigzags in foreign policy, Spain is now farther away from the goal of being a respected country in the world than it was ten years ago. The reality is more of a comparatively weak country with a fluctuating foreign policy: the worst of all possible scenarios. Spain yearns to participate in the global diplomatic tennis match as a key player, but, if it fails to commit itself to a sustainable and popular foreign policy, it runs the risk of becoming merely the ball hit back and forth by more powerful countries.

The foreign investments of Spanish firms are both a constraint and an opportunity for foreign policy-making. They are a constraint because foreign policy needs to keep them in mind so as to advance, or at least not interfere with, the international activities of Spanish companies. They represent an opportunity because they infuse bilateral relationships with substance and meaning. The analysis of Spanish foreign policy in chapter 7 suggested that Spain must use Europe as leverage in its pursuit of vital cultural and economic interests around the world. Let me turn to this most important topic.

Implications for Europe

Spain is a country fully integrated with Europe in terms of trade and foreign investment. Although Latin America has been the most important destination for Spanish multinationals, their process of international expansion has repercussions not just for Spain but also for Europe. These fall into three categories. First, within the European context, Spain is no longer a relatively poor country with powerless firms. Second, Spanish financial and economic interests outside Europe are not necessarily the same as those of other European countries, hence further complicating the pursuit of a common European relationship vis-à-vis third countries. And third, while two decades ago Spanish firms were not, or could not be, active actors in the European mergers and acquisitions landscape, the situation is today much changed.

Spain has closed almost half of the per capita income gap that separated it from the EU when it joined as a full member in 1986. In that year Spain's per capita GDP at purchasing power parity was 72 percent of the EU-15 level; in 2003 it was roughly 85 percent. Given that the Spanish economy continues to grow faster than the EU average, the country is likely to bridge the gap even more. True, part of this superior performance is owing to the generous EU transfers from richer members, which have fueled infrastructure investments. A thriving Spanish economy has come hand in hand with ever larger and more internationally oriented service-sector firms, as analyzed in chapters 4 and 5. Thus, Spain and its firms have gained economic weight within the EU, something that brings both opportunities and risks. The opportunity is for Spain to become a more important player in key decisions and to participate in the probable Eastern European boom. The risk is to fail to defend the country's interests. As Leopoldo Calvo-Sotelo, the head of government in 1981–2, famously stated, the

EU is not a "love machine," but a "measuring machine." Europe might expect a more assertive Spain, but Spain needs to play its cards carefully and tactfully, especially in an expanded Union, because it is large enough to be influential but too small to accomplish anything by itself.

Perhaps the main reason why Spain needs to exercise caution in its European policy is because its global cultural and economic interests do not overlap much with those of the large EU countries, let alone the new Eastern members. In addition to the interests inherited from the past, Spain has acquired new ones, especially in Latin America and North Africa (the Maghrib). No other European country has so much at stake in these two regions as Spain does, with the only possible exception in the Maghrib of France, a country that is often a competitor of Spain's. The EU's expansion to the East offers little help in this regard, unless Spain can forge other types of ties with the newly admitted members.

In the area of European mergers and acquisitions, Spanish firms in several service sectors are likely to become important players. As I suggested in chapters 4 and 7, Spain's role in Europe could benefit from cross-border mergers in at least two ways. The first would be to make it possible for the large Spanish multinationals to enhance their stature and consolidate their chances of remaining viable competitors. The second would be a way out of Spain's difficult predicament as a country with vital cultural and economic interests in two parts of the world – Europe and Latin America – that often seem to contradict each other. If half a dozen large Spanish firms were to acquire, or merge with, some of their European counterparts, then Spain would find it easier to make both sets of interests compatible with each other. This "Europeanization" of Spain's Latin American economic interests might be attractive to other countries like Italy, France, or Germany, given that their manufacturing (though not service) firms are already major investors across the Atlantic. In this way, Europe would benefit from an enhanced presence in Latin America, and Spain from increased embeddedness in one of the world's largest and safest economic areas. Naturally, the Spanish government and public – and the companies themselves – should be ready to accept the need, in some cases, to relinquish national control of the firms in whole or in part. It will be very hard indeed for all of the Spanish multinationals to play a role globally without becoming part of greater European entities. Thus

Spanish companies stand the best chance of expanding furthest around the world as "European" firms, perhaps controlled and managed not only by Spaniards.

While during the last fifteen years Spanish firms of all sizes have grown to become serious international competitors, their future is far from assured. Medium-sized multinationals – often family-owned or -controlled – face formidable hurdles in the global economy, especially because they compete in manufacturing industries in which their foreign counterparts are much bigger and possess a longer history of innovation and international growth. The future of the large Spanish multinationals is not certain either. They have a well-established presence only in Spain and Latin America. Their next step should be to consolidate their European positions, perhaps as a springboard to further expansion in North America and Asia. This analysis also applies to Spain as a country. Although its Latin American interests are substantial, the country needs to work hard to forge a set of relationships in Europe that make it possible to pursue its overall agenda. A Spain firmly rooted in Europe will help improve both its international stature and Europe's leadership in the world.

The Rise of Spanish Multinationals

European Business in the Global Economy

MAURO F. GUILLÉN

CAMBRIDGE
UNIVERSITY PRESS

CAMBRIDGE UNIVERSITY PRESS
Cambridge, New York, Melbourne, Madrid, Cape Town, Singapore, São Paulo

Cambridge University Press
The Edinburgh Building, Cambridge CB2 2RU, UK

Published in the United States of America by Cambridge University Press, New York

www.cambridge.org
Information on this title: www.cambridge.org/9780521847216

First published 2005
Reprinted 2006

Printed in the United Kingdom at the University Press, Cambridge

A catalogue record for this book is available from the British Library

Library of Congress Cataloguing in Publication data
Guillén, Mauro F.
The Rise of Spanish Multinationals: European Business in the Global Economy / Mauro F. Guillén.
p. cm.
Includes bibliographical references and index.
ISBN 0 521 84721 4
1. International business enterprises – Spain. 2. Spain – Foreign economic relations.
I. Title.
HD2887.G84 2005
338.8'8946 – dc22 2004057107

ISBN-13 978-0-521-84721 - 6 hardback
ISBN-10 0-521-84721 - 4 hardback