1 *Spanish firms come of age*

> Spain is not so different, so special as it is manipulatively said to be. We must stamp out once and for all the idea that Spain is an anomalous country . . . a case apart, an exception that justifies any action.
>
> Julián Marías, philosopher and sociologist (1965)[1]

DURING the last decade of the twentieth century a number of Spanish firms catapulted themselves to worldwide visibility. In banking, BBVA and Grupo Santander became the largest financial institutions in Latin America, within the top five in the eurozone, and among the twenty-five largest in the world, while Telefónica became the world's eleventh-largest telecommunications provider (the top firm in Latin America) and Repsol-YPF the ninth-largest oil company. In consumer goods, Freixenet became the largest producer of sparkling wines, and Inditex (the owner of the Zara brand) one of the leading apparel designers, makers, and marketers. In industrial goods, Ficosa International and Grupo Antolín led the world in the production of certain automobile components, and several of the worker-owned cooperatives of Mondragón Corporación Cooperativa expanded throughout the world as if they were regular capitalist enterprises. And in security services, unfortunately a key industry for the twenty-first century, Prosegur became one of the two or three top global firms. Since 1993, Spanish firms have invested abroad nearly \$200,000 million (€180,000 million). As a result of this remarkable process of international expansion, the Spanish economy, the financial system, foreign policy, the labor market, and society have been transformed in profound ways.

[1] "España no es tan diferente, tan 'especial' como interesadamente se dice. Hay que deseterrar de una vez para siempre la idea de que España es un país anómalo . . . que constituye siempre un caso especial, una 'excepción' al amparo de la cual puede hacerse lo que convenga." I thank William Chislett (2003) for calling my attention to this quote.

The rise of multinational firms from Spain poses a number of questions, because their process of international expansion is, to a certain extent, paradoxical. Spain is not among the most advanced countries in the world in terms of per capita income or technological development. Virtually no Spanish firm has global brand appeal. Yet hundreds of them are making formidable inroads into the global economy. This book aims to tell and analyze the story of the opportunities and problems produced by the enhanced stature of Spain in global economic and political affairs as a result of foreign direct investment (FDI) by Spanish firms.

After decades of international isolation, backwardness, and dictatorship, Spain entered the twenty-first century as a relatively "normal" country, boasting a relatively high degree of integration with the rest of the world, a vigorous economy, and a consolidated democracy. Since about 1980, the country and its firms have undergone a quite extraordinary process of change, including deregulation, privatization, enhanced competition, and increasing exposure to imports and inward foreign investment. In 1987, just one year after becoming a member of the European Union, the stock of cumulative inward foreign investment in Spain started to exceed the level for the average country in the world, adjusting for the size of the economy. Spain had become more attractive than the average country as a destination for foreign investment. Starting in 1992 Spanish firms responded to the growing arrival of foreign firms and to the creation of the European single market by stepping up their own foreign investments, a process that led to a unique situation in recent history: by the end of 2000, just as the twentieth century was drawing to a close, the cumulative stock of foreign direct investment by Spanish firms exceeded that of foreign firms in Spain for the first time in recent history (see figure 1.1). In 2002 Spain's stock of outward FDI reached the equivalent of 35 percent of GDP, up from less than 1 percent in 1980. Tellingly, Spanish firms have invested abroad more than those from the average high-income country. While in 1980 Spain was the twentith-largest foreign direct investor in the world in absolute terms, by the end of 2002 it had become the tenth-largest, behind the United States, the United Kingdom, France, Germany, the Netherlands, Hong Kong, Japan, Switzerland, and Canada, after having surpassed several countries that had been more important investors in 1980 (Belgium, Denmark,

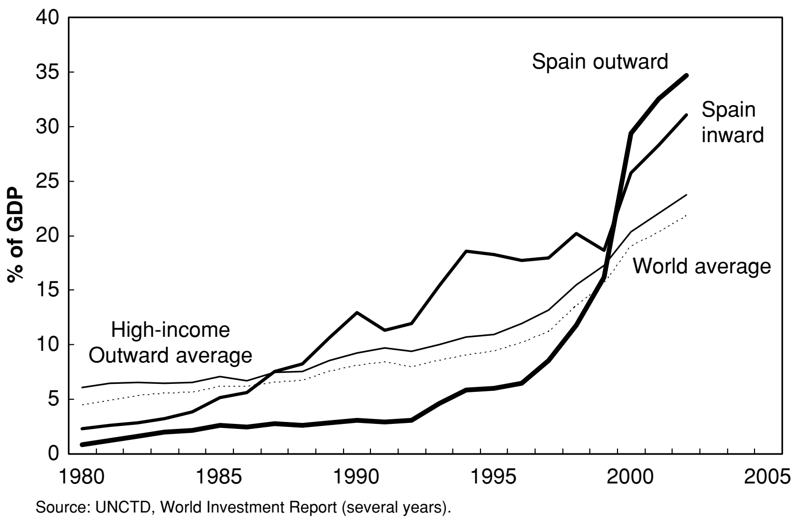

Figure 1.1. Spain's foreign direct investment stock position, 1980–2002.

Greece, Italy, Sweden, Australia, South Africa, Argentina, Brazil, Mexico, and Singapore).[2]

While Spanish multinational firms have been rather idiosyncratic in terms of the industries (mostly public utilities and financial services) and geographical regions (mainly Latin America and the European Union) in which they have expanded internationally, the reasons why they proceeded to invest abroad can be readily explained by established theory. I will make systematic use of economics, management theory, sociology, and political science to demonstrate that the logic underpinning the process of international expansion of Spanish firms has been, for the most part, sound, and in several instances simply brilliant.

[2] UNCTAD (2003: 262–5). The figures reported in figure 1.1 do not take into account the effect of "transit capital," i.e. when instrumental security-holding companies (entidades tenedoras de valores en el extranjero, in Spanish) are used to take advantage of certain tax incentives in Spain. When foreigners set up these companies, both inward and outward direct investment flows are artificially inflated. The companies were allowed after a 1995 reform of the Corporate Tax Law (Fernández-Otheo 2003). The timing around 2000 of the moment when outward investment stock exceeded inward stock is not affected by this effect.

However, I will also point out that many Spanish multinational firms are still far from the global frontier in terms of financial, organizational, managerial, and technological capability. Similarly, the country and its government seem relatively lacking and unprepared when it comes to coping with the economic, financial, diplomatic, political, and social consequences that increased outward foreign investment entails. The international financial community, the media, and business schools have increased the amount of attention they devote to Spanish firms, though not as much as one would predict given the growing importance of Spanish foreign direct investment. Thus, my main argument is that, while Spain has indeed become a "normal" country from the point of view of its integration with the global economy, it continues to be a second-rate country, aspiring but unable to join the club of the most advanced and powerful countries in the world. I argue that the gap separating Spain from the elite club of countries is not merely quantitative, as such simple statistics as gross domestic product per capita reveal (see figure 1.2). Spain finds itself behind the truly advanced countries in a *qualitative* way: one that has to do with power and influence. I shall offer some cardinal ideas as to how to close this other kind of gap.

Three myths about the Spanish multinationals

There are three widely held, albeit somewhat inaccurate, beliefs about the remarkable process of internationalization of Spanish firms over the last decade: (1) the process was driven by the adventurous investments of a small cadre of "new conquistadors"; (2) Spanish firms have invested mainly in Latin America, the reason being the shared language and culture; and (3) Spanish foreign direct investment is "anomalous" (and perhaps doomed to ultimately fail) because Spanish firms lack the requisite technological and managerial skills to succeed in the global economy. One of the purposes of this book is to address these myths. Let me preview the reasons in turn.

The myth that the Spanish multinationals are merely brave conquistadors who did not know what they were getting themselves into, but nonetheless managed to strike gold, is completely inaccurate. First of all, most people forget that there are nearly one thousand Spanish firms with investments abroad (UNCTAD 2003:222), and while some may have made wild investment decisions, it would be

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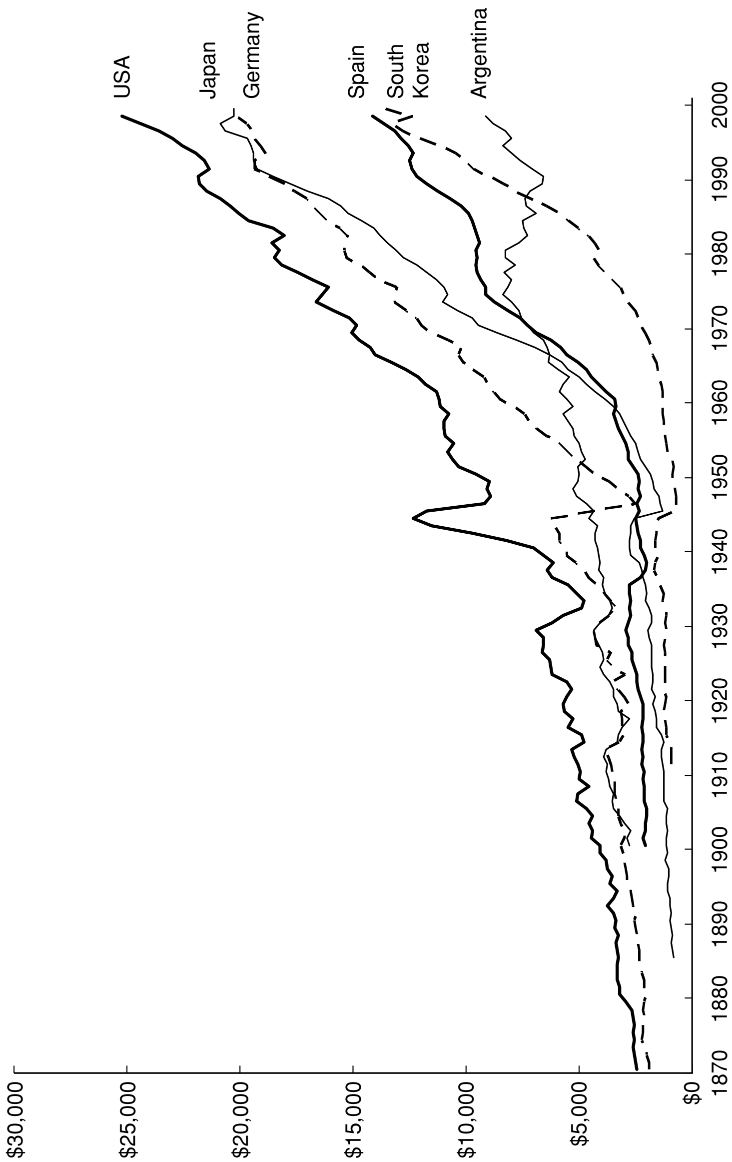

Sources: Maddison (1995, 2001).

Figure 1.2. Gross domestic product per capita, 1870–1999.

hard to believe that *all* of them were equally careless. Neither have all Spanish multinationals been able to strike gold. A second fact that undermines this myth is that dozens of articles and several books published over the last few years by Spanish and foreign scholars demonstrate that patterns of Spanish foreign investment can be readily explained with theories that also happen to account for the patterns observed for other, richer countries.[3] Thus Spain is hardly any different as far as the foreign investment decisions made by its firms are concerned.

The second belief, that Spanish foreign investment was to be expected as a "natural" projection of its firms into a linguistically and culturally similar region, such as Latin America, is simply fallacious. If that were the only, or the main, reason why Spanish firms invested abroad, why did they wait until the mid-1990s to do so? Why was Spanish investment south of the Rio Grande negligible during the period between the loss of Cuba and Puerto Rico back in 1898 and the early 1990s? There is, in addition, another fallacy related to this myth, namely, that most Spanish foreign investment has had Latin America as its destination. In fact, only 43 percent of net investment since 1993 has had Spain's former colonies as its destination, 60 percent if one excludes holding companies from the data (Fernández-Otheo Ruiz 2003:74; see also Fernández 2003). The European Union accounts for another 43 percent of net investment. (Moreover, since 1997 more than one third of Spanish investment in Latin America has arrived in Brazil, a *Portuguese*-speaking country that represents 40 percent of the region's economy. Far more Spanish entrepreneurs and managers speak English than Portuguese.) Clearly, a common language and culture help in managing foreign subsidiaries, transferring products and services, and relocating expatriate executives and their families. Language and culture can be *facilitators*, but they can hardly be the main reason, or a prime cause, why Spanish firms invested some $90,000 million over ten years in the region. It is also worth considering that the reaction of the stock market has been more

[3] See, among others: Alguacil and Orts (2002); Campa and Guillén (1996a, 1996b, 1999); García Blandón (2001); García Canal (1996); García Canal, Valdés Llaneza, and Ariño Martín (2003); García Canal and Valdés Llaneza (1997); Guillén (2001c); López Duarte and García Canal (1998, 2001, 2002a, 2002b); and Molero (1998).

positive in the case of investments in OECD countries other than in Latin America (López Duarte and García Canal 2003), probably because of the higher risk associated with operating in emerging economies.

The third myth strikes at the heart of a major problem looming large over Spain's future: the relatively weak technological capabilities of a country that nonetheless aspires to be rich and influential on the global stage. It is indisputably true that Spanish firms account for a tiny fraction of worldwide patents, and that the country devotes meager resources to R&D (less than 1 percent of GDP). However, more than half of Spanish foreign direct investment is in banking, public utilities, telecommunication services, and construction, activities in which managerial know-how and "project-execution capabilities" are more important than technology, which can be readily acquired in the marketplace (Amsden and Hikino 1994). Besides, successful multinationals tend to possess proprietary assets, of which technology is just one. Another important source of proprietary competitive advantage is brands, and Spanish firms do have valuable trademarks (see chapter 8). Lastly, it is important to remember that aggregate figures are always misleading: there are Spanish firms at the leading edge of technological innovation, especially in metals, industrial machinery, and transportation equipment and components, as identified by an OECD study published just before the beginning of Spain's outward foreign investment boom (Archibugi and Pianta 1992). Like any "normal" country, Spain has specialized in certain technological areas, although the process is still in its infancy.

Dunning and Narula (1994) proposed that the relationship between foreign direct investment, on the one hand, and the ownership, location, and internalization (OLI) factors that underpin foreign investment decisions, on the other, changes according to the country's stage of economic development and sophistication. In other words, the relative weights and roles of the three elements of the OLI or eclectic approach to international production vary as countries (and their firms) become richer, shift from natural to created assets, and become more embedded in the world economy (Dunning 1979, 1981, 1988).

In 1996, José Manuel Campa and I stated that "the case of Spain may be taken as representing a group of middle-income countries that, in spite of being early industrializers and having achieved relatively high standards of living, have not moved far in what has been termed the 'investment development path'" (Campa and Guillén 1996a:207). At the time, Spain was still receiving more FDI than it was sending to the rest of the world. Spain's attractiveness to foreign investors up until the mid-1990s had to do with what Dunning and Narula (1994) call natural assets, such as relatively cheap labor and a large domestic market. The very scarcity of created assets such as brands and technology was said to be preventing outward FDI from reaching higher levels. However, the phenomenal increase in foreign investment by Spanish firms since the mid-1990s does not seem to fit the predictions of the investment development path in that Spain has become a fully developed country from the theory's point of view, while lagging seriously behind other major countries in terms of technological and marketing expertise.

The (recent) history of Spanish foreign direct investment

As is true of many other countries, the FDI cycle in Spain has historically been affected by domestic political events and upheavals as well as by economic developments.[4] Liberal trade policies in the mid-nineteenth century set the stage for the arrival of French, Belgian, and (after 1870) British investments in railways, mining, wineries, banking, insurance, and public utilities. The return of protectionism and legal restrictions to foreign investment after 1891 slowed down the inflows. Meanwhile, Spanish investments abroad paled by comparison, with Cuba and Argentina as the major destinations (Tortella 1994:128–34; Nadal 1975:25–53, 87–121).

The 1920s witnessed the rise of American, German, and French investment in electrical machinery, chemicals, autos, and telecommunications despite growing restrictions on foreign investment and trade (Campillo 1963). Over this early period of industrialization, Spain attracted foreign investment at increasing rates, albeit with many ups and downs dictated by political financial, or economic crises. Most of these early inflows of FDI had to do with the exploitation of either natural assets such as mineral deposits and unique agricultural products (wines in particular), or the development of the markets for

[4] This section relies heavily on Campa and Guillén (1996a).

transportation, communication, banking, insurance, and basic industrial goods. During the first two decades of the century, Spanish investment abroad was negligible except for the mostly speculative flows during World War I.

The Great Depression was shallower in Spain than elsewhere in Europe or America, but nonetheless devastating for FDI. The Civil War of 1936–9 represented a further setback to foreign investment and trade. After the war, the authoritarian government of General Franco became dominated by a group of populist and staunchly nationalist economic policy-makers who implemented a series of foreign-exchange controls and protectionist measures, and encouraged import-substitution investments in industry, while the Allied powers imposed a trade embargo that remained fully in place until the late 1940s. A restriction of foreign ownership to a maximum of 25 percent, the overvaluation of the currency, the intricate system of multiple exchange rates, mounting inflation, and economic stagnation provoked capital flight and close to zero inward FDI. However, Spanish firms did invest abroad in mining and construction projects, especially in Morocco and some Latin American countries.

From liberalization to EU membership, 1959–1986

The liberal economic reforms of 1959 assigned foreign capital several roles to play: supplementing the meager level of domestic savings, generating much-needed hard currency, and facilitating technology transfers (Varela Parache et al. 1972; Muñoz et al. 1978:45–60). The reformers also introduced changes into the protectionist regime: very steep tariff barriers were substituted for non-tariff barriers to trade. The punitive taxation of imports of industrial and consumer goods in a domestic market of considerable growth potential attracted inward FDI during the 1959–73 period. During the 1960s and early 1970s, annual inward FDI flows ranged between 0.15 and 0.59 percent of GDP, while outward FDI stayed under 0.10 percent of GDP, i.e. twenty-five to thirty times smaller than inward FDI. By the mid-1970s, and despite the reduction in foreign activity in Spain, inward investment was still about four times higher than outward investment.

Spanish investments abroad during the 1960s had to do with: (1) the access to raw materials (uranium, paper pulp, petroleum, various metals, fisheries), (2) the creation of distribution channels for Spanish fish, beverages, and food products, (3) construction and engineering projects (especially in Latin America and the Arab world), and (4) banking. Manufacturing FDI based on firm-specific advantages was not significant until the early 1970s. While manufacturing investments were initially worth 20 percent of total outward FDI, by the mid-1970s they represented nearly 40 percent. Firms in the chemical, paper, mechanical, electro-mechanical, textile, and beverage industries invested in manufacturing activities abroad (COCINB 1973:25; Muñoz et al. 1978:352–3). Most analysts agree that the government did little to facilitate outward FDI during this period. Exchange controls were too tight and state subsidies to help create distribution channels abroad were not very effective (Varela Parache et al. 1972; Moreno Moré 1975:106–7). One destination of intense Spanish outward FDI in the early and mid-1970s was the relatively depressed French department of the Pyrénées Orientales (the historic Roussillon), to the north of one of Spain's most developed industrial regions, Catalonia (Castellvi 1973; Raurich et al. 1973). Catalan firms in the textile, clothing, appliance, chemical, beverage, and food-processing industries invested there to secure access to the European Common Market, given that the 1970 Preferential Agreement with Spain failed to significantly reduce tariffs for labor-intensive manufactured goods. This specific location was selected for its geographical proximity and relatively lower labor costs than in other European areas.

The world economic crisis of 1973 and the Spanish transition to democracy after 1975 slowed down FDI. By the late 1970s, however, both outward and inward flows resumed their upward trend, albeit with significant annual ups and downs until the mid-1980s due to the second oil shock, the 1981 world recession, and the initial uncertainty over the Socialist Party's electoral victory in 1982. In 1985 outward and inward flows represented 0.16 and 1.00 percent of GDP, respectively, more than three times the rates for the early 1970s. This upward trend since the mid-1970s was in part facilitated by regulatory changes. The agencies that had tightly controlled foreign transactions since the 1940s were dismantled as the Ministry of Commerce assumed the authority over foreign investment authorization and control (De Erice 1975). In 1973–4 and 1976–7 procedures for inward FDI were clarified and simplified (Muñoz et al. 1978:45–60), while similar changes were introduced for outward FDI beginning