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POLITICAL OBSTACLES TO GLOBALIZATION: THE DAEWOO-THOMSON AFFAIR

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This paper examines some political contstraints which limit the process of globalization. While economic theory would predict that firms locate the various stages of production of their products in those countries demonstrating clear comparative advantages, and while intra-firm trade data shows that multinational firms do, by and large, try to globalize their production, there are occasional political obstacles to such strategies. Many Korean firms have expanded into Europe for economic reasons, but the case of Daewoo Electronics ill fated attempt to purchase Thomson shows that analysts must take political, as well as economic conditions into account before the process of globalization can be understood.

If this were the world economists imagine, there would be no barriers to trade, flows of capital, or movement of the factors of production. In such a world, production would be governed by the relative rarity of factor endowments and the behavior of firms would converge to "best practice."[1] Such a world exists, of course, only in the mind's eye and the academic imagination. It is a fantasy world that is convenient for the construction of theories and the instruction of students. It is useful for the simplification of abstractions and for the purpose of argument. Sadly, those interested in theories of trade sometimes forget the fanciful origins of their constructs and occasionally use their theories as the basis of policy recommendations. This is, of course, not only the sin of economists, but of other social scientists as well. Political scientists, are equally guilty of such hubris and often as much to blame when simplistic models form the basis of policy suggestions. Fortunately, theories which are inadequate when taken singly, are better when combined. Thus, theories of globalization offered by economists are often inept descriptions of the real world, but so then are those of political scientists who reduce all behavior to the interests of the state.[2] If we look more

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[1]For a discussion of the convergence to "best practice" thesis, see Suzanne Berger and Ronald dore, eds., *National Diversity and Global Capitalism* (Ithaca: Cornell University Press, 1996), Part I.

[2]For an enthusiastic tract endorsing the economists' position, see Robert Z. Lawrence, Albert Bressand and Takatoshi Ito, *A Vision for the World Economy*, (Washington DC: Brookings, 996). This is not to say that there is any consensus on the extent to which the phenomenon exists. Elie Cohen points out that those who minimize the importance of globalization underline that third world exports to OECD countries were valued at only 1.16% of the latter's GDP in 1990, while alarmists noted that if the increase of said exports increased

closely at state interest - or more nefariously, at domestic politics - as a reason for divergence from economic "best practice," we begin to get a more accurate understanding of both government and firm behavior. This paper examines the globalization strategies of Korean firms and the political obstacles to such strategies. This is illustrated by the experience of Korean firms in Europe. The constraints are illustrated especially by a case that we will examine in some detail: Daewoo's offer to purchase the French-owned consumer electronics conglomerate, Thomson Multimedia.

I. GLOBALIZATION

The current academic enthusiasts of globalization derive their ideas from neoclassical (and, indeed, classical) trade theory. Ever since David Ricardo provided an argument for trade based on the reasoning of comparative advantage, it has been the mantra of most trade economists that everyone is better off when they specialize in those products for which they have a comparative advantage and import those products for which their resources make this less favored. More recently, the concept of comparative advantage has been replaced by the concept of competitive advantage, put forth by Harvard Business School professor Michael E. Porter, which considers not merely factor endowments, but social and industrial organization as important factors.[3] By extension, firms which can locate branches anywhere in the world are advised to organize their stages of production in those countries where factor endowments and social characteristics are most propitious. Thus, the advantages of trade are internalized by the firm. Indeed, much of the structure of trade is characterized by intra-firm transfers.[4] In the United States, for example, intra-firm transfers accounted for over 40% of imports, while 70% of global royalty fees represented transactions between multinational firms[5] and their foreign affiliates.[6] The importance of intra-firm trade is

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as much in the next 20 years as they had in the last two decades, the figure would reach 55% of GDP. Elie Cohen, *La Tentation Hexagonale* (Paris: Fayard, 1996), pp. 21-22. Nor is the opening of world markets a new phenomenon: Cohen, p. 23; Ronald Rogowski, *Commerce and Coalitions* (Princeton: Princeton University Press, 1989). For an example of the political scientists' position emphasizing the importance of state interests, see Robert Gilpin, *US Power and the multinational Corporation* (New York: Basic Books, 1975), chap. 1.

[3]Michael E. Porter, *The Competitive Advantage of Nations* (New York: The Free Press, 1990).

[4]For a review of the arguments for and against multinationals, see C. Fred Bergsten, Thomas Horst, and Theodor H. Moran, *American Multinationals and American Interests* (Washington D.C.: Brookings, 1978).

[5]The term "multinational firm" should only be understood as a firm with international operations beyond exports, and does not refer, necessarily, to owners coming from more than one country. See Richard J. Barnet and Ronald E. Müller, *Global Reach* (New York: Simon and Shuster, 1974), p. 17.

[6]Martin Wolf, "The Heart of the New World Economy," *Financial Times*, 1 October 1997, p. 12; William J. Zeile, "US Intrafirm Trade in Goods," *Survey of Current Business*, February 1997.

indicated by the figures presented in Table A.

The numbers indicating the growth of multinational firms are impressive: In 1996 the global stock of foreign direct investment (FDI) was valued at $3,200 billion, with a 10-year rate of growth surpassing twice that of gross capital formation and an annual growth rate of FDI of over 12% for the years between 1991 and 1996. As a contrast, global sales, still no slouch, grew at 7%.[7] By the 1990s multinational firms accounted for 7.5% of world output and 18% of world manufacturing (up from 12% in 1977).[8] Certainly, there must be something to the economists' imaginary world, for actors in the real world to try so hard to resemble it.

Initially, of course, the leaders of this movement were located in the United States and Europe. While Europeans created internationally oriented trading companies only slightly after the Renaissance, such companies as the Russia Company (founded in 1553) or the British East India Company (after 1600),[9] for example, the modern era of foreign direct investment probably begins with Singer Sewing Machine's investment in the United Kingdom at the turn of the last century.[10] Reasons for foreign investment vary. Often, they are motivated by the need to secure raw materials and other backward linkages. Such investments spurred the fears of imperialism announced by Lenin and Luxembourg.[11] More recently, firms have been seen to internationalize as a way of selling under tariffs and other barriers to trade, or to defuse fears of unfair trading practices by creating jobs locally. Perhaps the most influential modern theory, however, links foreign direct investment to the product life-cycle hypothesis of Raymond Vernon.[12] Vernon argued that the monopoly rents of a newly innovated product could be extended by exporting to countries with similar consumer tastes, yet with less competition, than the home country of the innovating firm. As competition developed, costs could be lowered by locating production in that country which had previously been the export target. In fact, this argument is strangely reminiscent of Lenin's. Lenin, influenced by Marx's hypothesis on the falling rate of profit, argued that firms invested overseas when profit rates dropped at home due to competition.[13]

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[7] *Ibid.*

[8] *Ibid.*

[9] Oliver Letwin, *Privatizing the World* (London: Cassell Education, 1988), p. 2.

[10] Myra Wilkins, *The Maturing of the Multinational Enterprise* (Cambridge: Harvard University Press, 1974).

[11] V.I. Lenin, *Imperialism: The Highest Stage of Capitalism* (New York: International Publishers, 1939); Rosa Luxembourg, *The Accumulation of Capital-- an Auto-Critique* (New York: Monthly Review Press, 1972), ed. Kenneth J. Tarbuck, trans. Rudolf Wichmann.

[12] Raymond Vernon, *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises* (New York: Basic Books, 1971).

[13] Of course, one should not push this parallel too far. The notion of profit employed by Lenin and Marx derived from the labor theory of value. Marx had noted that firms were driven by competition to employ machinery to reduce costs, yet the extent to which machinery was used, value was not added, because value could only come from labor. The higher the proportion of costs deriving from machinery, the lower the rate of profit.

Table A. Intrafirm Trade for US-based Multinationals

<Imports by Country of Origin>

	Millions of Dollars				
	Total	Intafirm Imports			Other Imports
		Total	By US parent Companies From their Majority-owned Foreign affiliate	By US affiliates from their foreign parent group	
All Countries	532,665	221,059	83,260	137,799	311,606
Canada	98,630	46,061	36,613	9,448	52,569
Europe	112,707	52,226	12,967	39,259	60,481
Latin America & Other Western Hemisphere	68,755	19,992	13,960	6,032	48,763
Africa	14,346	2,922	1,957	966	11,424
Middle East	15,726	4,329	579	3,750	11,397
Asia & Pacific	222,502	94,802	17,185	77,617	127,700

	Percent				
	Total	Intrafirm Impots			Other Imports
		Total	By US parent companies from their majority-owned foreign affiliates	By US affiliates from their foreign parent group	
All Countries	100	41.5	15.6	25.9	58.5
Canada	100	46.7	37.1	9.6	53.3
Europe	100	46.3	11.5	34.8	53.7
Latin America & Other Western Hemisphere	100	29.1	20.3	8.8	70.9
Africa	100	20.4	13.6	6.7	79.6
Middle East	100	27.5	3.7	23.8	72.5
Asia & Pacific	100	42.6	7.7	34.9	57.4

Source: Survey of Current Business, Feb. 1997, p. 33

Yet firms differ dramatically in their patterns of multinational investment. Some organize all stages of production in the receiving country including research and

development, while others are content merely to create assembly operations while maximizing value-added in the home, rather than host, country. The former case is typical of American firms while the latter is typical of Japanese. Reich and Pauly have argued that these variations in patterns of foreign direct investment reflect management incentives in the home country.[14] Characteristics of the home political economy shape corporate structure and behavior, including behavior in host countries. American firms, on a short tether from financial markets, use foreign investment strategies to compensate by seeking greater value-added abroad, while Japanese firms seek to preserve their planning advantage permitted by stable finance, in the structure of their foreign affiliates.[15]

Korean firms also exhibit structures that reflect the conditions of their development at home. The large conglomerate nature of the chaebol was the product of a specific development strategy of the Korean state, with the private and public sector elites being intimately associated.[16] The stupendous and rapid growth of these companies, moreover, was assured by below-market finance allocated politically by the Korean state.[17] As Meredith Woo-Cumings has put it,

> Notwithstanding considerable protest from international development agencies, the Korean state has heavily intervened in the financial allocation process to direct resources into heavy industry sectors. It provided incentives in the form of "policy loans" and interest rate and other subsidies, and it showed a willingness to share the risk of default with firms that were willing to conform to state policies.[18]

By the 1980s, however, a growth strategy based on the Korean market was increasingly difficult to maintain. Continuing domestic market protection, the normal strategy of the developmental state,[19] was harder to justify as the country weakened its claim to be considered a part of the Third World. American pressure was especially unrelenting. If internationalizing the economy meant lowering trade barriers to the Americans, it also had to mean an increasingly outward strategy on the part of Korean firms.

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[14]Louis W. Pauly and Simon Reich, "National Structures and Multinational Corporate Behavior: Enduring Differences in the Age of Globalization," *International Organization,* 51, 1, Winter 1997, pp. 1-30.

[15]*Ibid.*

[16]Joon Hyung Kim, "Economic Policy-Making in Korea," unpublished Ph.D. dissertation, George Washington University, 1997.

[17]Jung-En Woo, *Race to the Swift: State and Finance in Korean Industrialization* (New York:Columbia University Press, 1991).

[18]Meredith Woo-Cumings, "Slouching toward the Market: The Politics of Financial Liberalization in South Korea," in Michael Loriaux, Meredith Woo-Cumings, Kent E. Calder, Sylvia Maxfield, and Sofia Perez, *Capital Ungoverned* (Ithaca: Cornell University Press, 1997), p. 57.

[19]The term *developmental state* is taken from Chalmers Johnson, *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975* (Stanford: Stanford University Press, 1982). Of course, the protection of "infant industries" was justified by America's first secretary of the treasury, Alexander Hamilton, at the end of the eighteenth century.

2. THE DAEWOO-THOMSON AFFAIR

A recent area of expansion for Korean chaebols has been Europe. While Europe only represents a fifth of Korean foreign direct investment, it has been a key part of chaebol strategy.[20] Europe offers high profits to pay down debt and allows Korean firms to diversify away from dependence on U.S. markets.[21] Foreign direct investment also helps off-set protectionist strategies on the part of Europeans often called "Fortress Europe."[22] Another bonus for Korean firms was found in the European labor force. High unemployment and European government premiums for job-creation have often made European labor cheaper than Korean.[23] Indeed, some European countries have a lower union density than Korea, which may account at least partially for the differences in labor costs.[24] Thus by locating in troubled areas of Europe, foreign firms could both improve profit margins and move closer to a market of over 300 million consumers of advanced industrial goods. As one Korean executive put it, "Korean companies have to come to Europe because the Korean market is crowded and Korean labor costs are rising."[25]

It should be noted, however, that firms rarely move because of labor costs alone. The literature on corporate location strategies in the United States, for example, reveals that labor cost is usually of only secondary interest to most firms.[26] This is, strangely, not understood by many economists who explain the stagnation in Western Europe by

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[20]John Burton, "This "Tiger" is Wounded but Still on the Prowl," *Financial Times*, Survey: South Korean Investment In Europe, 6 October 1997, p. I.

[21]Many Korean companies are highly leveraged. This is a heritage of the years of cheap credit from the state-influenced financial intermediaries. However, credit became dearer with the liberalization of the financial system. Korean habits of "moral hazard" (i.e., being insensitive to risk) which were a residue of underpriced finance led these firms to become over-indebted, especially as the Korean economy began to experience domestic recession. On financial liberalization in Korea, see Meredith Woo-Cumings, "Slouching toward the Market: The Politics of Financial Liberalization in South Korea," in Michael Loriaux, Meredith Woo-Cumings, Kent E. Calder, Sylvia Maxfield, and Sofia A. Perez, *Capital Ungoverned: Liberalizing Finance in Interventionist States*, (Ithaca: Cornell University Press, 1997), pp. 57-91. On the problem of "moral hazard," see Michael Loriaux, *France After Hegemony: International Change and Financial Reform* (Ithaca: Cornell University Press, 1991), pp. 10, 284-288.

[22]Burton, *op. cit.*, p. I.

[23]*Ibid.*

[24]According to the International Labor Organization annual report for 1997, union density in Korea was 12.7% of the workforce in 1995, while the figure for France was 9.1%. See Robert Taylor, "ILO Foresees Revival of Trade Union Strength," *Financial Times*, 4 November 1997, p. 7.

[25]J.B. Chun, chief executive officer of the European arm of Daewoo Electronics, quoted in Stefan Wagstyl, "In Search of Firm Ground," *Financial Times*, Survey, 6 October 1997, p. III.

[26]See, for example Roger W. Schmenner, *Making Business Location Decisions* (Englewood Cliffs: Prentice-Hall, 1982); Roger W. Schmenner, Joel C. Huber, and Randall L. Cook, "Geographic Differences and the Location of New Manufacturing Facilities," *Journal of Urban Economics*, 21 (January 1987), pp. 88-104.

focusing on high labor costs and taxes associated with the welfare state--arguments which generally focus on the "inflexibility" of European labor markets.[27] In some countries high labor costs are mitigated by corporatist bargaining structures which facilitate incomes policy and the introduction of labor saving technologies, as well.[28]

Our interviews with Korean executives revealed that not only are labor costs of secondary importance, but that countries with notoriously contentious unions, such as France, end up as attractive locations for foreign direct investment. As a Daewoo executive put it,

> The French labor environment is less favorable than the UK, but it is more favorable than Germany. Poland [has favorable labor conditions because it is highly skilled and cheap], but France is closer to the market [of consumers]. We have three factories in France and good performance in two of them. The third is the newest. We've only been there one year and it takes time for management to learn how to deal with labor there.[29]

Thus, labor productivity varies from factory to factory and is dynamic. Making assumptions about production costs based only on nation-wide averages, or on prejudices about the cost of social protection schemes and other aspects of the welfare state in a given country is likely to be deceptive. Thus, even though manufacturing labor costs average $19.34 per hour in France, and thus, compare unfavorably with $14.19 in the UK, and $17.74 in the US, investment in European facilities can make sense for some industries, precisely because these averages are deceiving about real productivity.[30]

Table 1 shows Korean investment in Europe. Table 2 shows Korean manufacturing investment in France. Figure 1, 2, and 3 illustrate the trends graphically.

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[27]Alberto Alesina and Lawrence Summers, "Central Bank Independence and Economic Performance: Some Comparative Evidence," *Journal of Money and Banking*, 256 (1993).

[28]The German structure of industrial unions allows workers to be transferred out of crafts made obsolete by new technologies. See Kathleen Thelen, "The Politics of Flexibility in the German Metalworking Industries," in Miriam Golden and Jonas Pontusson, eds., *Bargaining for Change: Union Politics in North America and Europe* (Ithaca: Cornell University Press, 1992). On the success of corporatist incomes policies, see Fritz Scarpf, *Crisis and Choice in European Social Democracy* (Ithaca: Cornell University Press, 1991), trans. Ruth Crowley and Fred Thompson.

[29]Interview with Mr. Young-sup Joo, Director, Strategy Planning Team, Corporate Planning Division, Daewoo Electronics, Seoul, Korea, 15 July 1997.

[30]John Tagliabue, "Buona Notte, Guten Tag: Europe's New Workdays," *New York Times*, 12 November 1997, p. D-1. The article derives its data from the Bureau of Labor Statistics and DRI/McGraw-Hill.

Table 1.
Korean Investment in Europe

	Number of projects	Amount in thousands
1990	22	$95,200
1991	36	$89,984
1992	37	$144,187
1993	33	$189,632
1994	56	$427,855
1995	78	$611,245

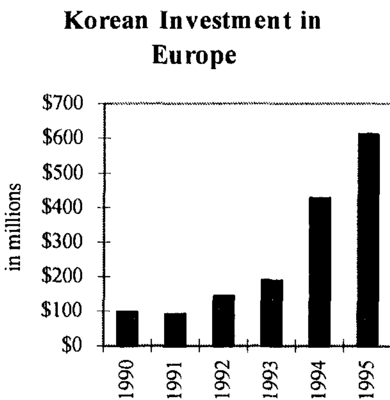
Source: The Bank of Korea

Table 2.
Korean Mfg. Investment in France

	Number of Projects	Amount in thousands
1992	4	$29,860
1993	2	$34,908
1994	3	$45,610
1995	4	$53,167

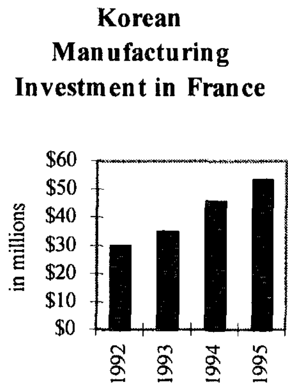
Source: The Bank of Korea

Figure 1.



Source: The Bank of Korea

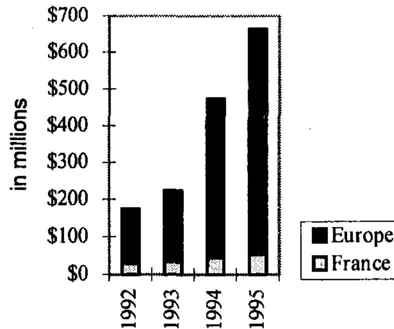
Figure 2.



Source: The Bank of Korea

Figure 3.

Korean Overseas Investment



Source: The Bank of Korea

One of the most aggressive firms locating in Europe is Daewoo. Daewoo has invested heavily in automotive plants in Poland, the Czech Republic, and the Ukraine.[31] It has set up electronics plants in Northern Ireland, Spain, and France. In the eastern European cases Daewoo was applying a strategy with which it was already familiar. It bought formerly state-owned plants, just as it had already done in Korea. However, when it came to applying the strategy to France, it ran up against an obstacle that would prove exceedingly difficult to overcome: politics.

Like Korea, France has a "developmental state" that is an artifact of its relatively late industrialization in the nineteenth century.[32] State intervention in the domestic market has been the norm since at least the regime of Louis XIV's minister, Jean-Baptiste Colbert, and this has meant that markets have been governed by politics for centuries. More recently, the election of François Mitterrand to the presidency in 1982 led to a large number of nationalizations as a response to the continuing stagnation of the French economy since the oil crises of the 1970s.[33] While many of the firms

[31]Christopher Bobinski, "Autos Put Daewoo on Fast Track," *Financial Times*, Survey, 6 October 1997, p. III.

[32]Alexander Gerschenkron, *Economic Backwardness in Historical Perspective* (Cambridge: Harvard University Press, 1962). Some even argue that France did not industrialize until after the Second World War. See Charles Kindleberger, "The Postwar Resurgence of the French Economy," in Stanley Hoffmann, Charles P. Kindleberger, Lawrence Wylie, Jean-Baptiste Duroselle and François Goguel, eds., *In Search of France* (New York: Harper and Row, 1962).

[33]For an extensive examination of French nationalizations, see Harvey B. Feigenbaum, *The*

nationalized by the Socialists were returned to profitability in the public sector, Conservative parties made privatization a focus of their successive electoral campaigns in 1986, 1993 and 1995.[34] In fact, the problems of the French economy were more closely related to the fact that France had tried to inflate its economy while all its trading partners were deflating. This led to a balance of payments crisis, as French demand for imports grew more rapidly than its neighbors. The solution was a series of austerity measures which induced a recession.[35] Although Conservatives, as well as Socialists, had never been convinced of the free-market ideas which dominate the United States, advocacy of privatization proved a convenient campaign tool - it distinguished the Conservatives from the Socialists - and a useful way to fill budget gaps without raising taxes.

Among the groups nationalized by the Socialists and slated for privatization by the Conservatives was Thomson, a conglomerate with activities in both defense and consumer electronics. The defense arm is known as Thomson CSF and the consumer electronics company is known as Thomson Multimedia, both being controlled by a state holding company. Thomson Multimedia itself is a conglomerate representing the acquisition of European consumer product firms such as Grundig and Telefunken, as well as American household names like RCA and General Electric (the latter product line was obtained in a swap of Thomson medical equipment for GE's consumer electronics). While many firms, like Saint Gobain and Elf Aquitaine; were profitably run in the public sector,[36] Thomson Multimedia became deeply indebted. By the end of 1996 the company's indebtedness was estimated to be between 16 and 17 billion francs, or about $3 billion.[37] Had Thomson been a normal, private sector firm, it would have been considered bankrupt.

After winning the 1995 presidential election, Jacques Chirac continued the privatization program he had started as prime minister in 1986. Thomson was a priority on the privatization hit-list, and additionally Chirac had made it clear that he wanted the Thomson group to be privatized "as a whole."[38] Despite the company's heavy losses, two suitors competed to take Thomson off the state's hands, Alcatel Alsthom and Lagardère. The first of these, Alcatel, is a large conglomerate emphasizing heavy

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Politics of Public Enterprise: Oil and the French State (Princeton: Princeton University Press, 1985).

[34]Harvey B. Feigenbaum, Jeffrey R. Henig, and Chris Hamnett, *Shrinking the State: The Political Underpinnings of Privatization* (Cambridge, England: Cambridge University Press, forthcoming), chap. 4.

[35]For an overview of the problems of Socialist economic policy, see Peter A. Hall, "Socialism in One Country: Mitterrand and the Struggle to Define a New Economic Policy for France," in Philip G. Cerny and Martin A. Schain, eds., *Socialism, the State, and Public Policy in France* (New York: Methuen, 1985), pp. 81-107.

[36]Feigenbaum, Henig and Hamnet, *op. cit.*, chapter 4.

[37]Philippe Le Coeur, "Daewoo consacrera 10 milliards de francs è la recapitalisation," *Le Monde,* 1 November 1996, reprinted in *Sélection hebdomadaire du journal "Le Monde,"* 31 October- 6 November 1996, p. 10.

[38]David Buchan, "Tripped on the Way to the Market," *Financial Times*, 5 December 1996, p. 11

engineering and infrastructural projects. The second group, Lagardère, owned the huge French defense contractor, Matra. Thus the choice boiled down to grouping Thomson with an industrial conglomerate or grouping it with another defense contractor. To the surprise of many, Prime Minister Juppé announced the government's decision to pursue a "defense" strategy and awarded the purchase to Lagardère. That is, the privatization would serve to rationalize the country's defense industry, in much the same way as the American merger of Lockheed and Martin Marietta.[39] There was, however, a hitch. Lagardère made it clear that it was only interested in Thomson CSF. Its intention was to spin off Thomson Multimedia to Daewoo, the Korean chaebol.

For Daewoo, the purchase of Thomson made a lot of sense.[40] While Daewoo produced quality products, it felt a need for greater brand recognition outside of Asia. Thomson was a brand name well known in Europe, and equally well known in the US through its RCA and General Electric brands. The complementarity of the Daewoo and Thomson product lines also made the French company a logical acquisition as Thomson produced at the high end of the market, while Daewoo produced at the middle and lower ends of the consumer price spectrum. Moreover, Daewoo had experience working in France as it had already established three factories there. Finally, Daewoo had experience with privatizations, both in Korea and in Poland.[41]

While the French government announced its intention to privatize Thomson in February of 1996, Daewoo did not learn of the opportunity till March, through Mr. Lagardère, a business acquaintance of Mr. Bae Soon-hoon, CEO and Chairman of the Board of Daewoo Electronics.[42] A letter of intent was sent in May, an indicative offer in June, and at the end of July the French government selected the two best offers. When the French prime minister announced the Lagardère-Daewoo offer was chosen, Mr. Joo Young-sup, Daewoo Electronics' manager of the investment, informed us that Daewoo was "shocked", having expected Alcatel to be preferred, as it was by the conventional wisdom. Indeed, several members of the cabinet did prefer Alcatel's offer.

The Daewoo offer was hardly negligible, however. Le Monde reported that Daewoo would invest 10 billion francs to recapitalize the firm, although the actual conditions of disbursement were somewhat vague.[43] Moreover, such disbursements would occur only after the French state had recapitalized Thomson S.A. to the tune of 11 billion francs. Subsequent actions of the French state made these concerns moot.

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[39]Caroline Monnot, "Le gouvernment veut désamorcer la polémique sur la cession de Thomson," *Le Monde*, 31 October 1996, reprinted in *Sélection hedomadaire du journal Le Monde*, 31 October- 6 November, 1996, p. 10.

[40]Our knowledge of Daewoo's strategy comes from interviews with Mr. Soon-hoon Bae, Chairman and CEO of Daewoo Electronics on 16 July 1997 in Seoul, Korea, and with Mr. Young-sup Joo, Strategy Planning Team Director of the Corporate Planning Division of Daewoo Electronics, on 15 July 1997.

[41]Burton, *op. cit.*, p. I; Christopher Bobinski, "Autos put Daewoo on Fast Track," *Financial Times*, Survey, 6 October 1997, p. III.

[42]Interviews with Joo and Bae, July 15-16, 1997.

[43] Philippe Le Coeur, *op. cit.*, p. 10.

French privatization law required the deal be approved by an independent Privatization Commission.[44] While the Conservative government had considered this approval to be pro forma, the Privatization Commission did not consider itself to be a rubber stamp for Juppé and Chirac. The issue, at least ostensibly, was technology transfer.

While the Privatization Commission recognized that Daewoo would expand production of television sets from 700,000 to 3 million units, creating 3,000 new jobs in France, it argued that the technology transfer acquired by the symbolic one-franc purchase was disproportionate. Thomson had made significant advances in digital television, flat screens, and decoders, achieved by way of a research program financed by the French state.[45] Moreover, the commission noted that the offers made by Lagardère and Daewoo did not provide mechanisms by which the two companies would be legally bound to recapitalize Thomson in the amounts they promised. For these reasons the Commission refused to authorize the sale.[46]

When we interviewed Mr. Bae, he was skeptical of the technology transfer argument. Not only did he feel that Daewoo did not need Thomson's technology, he pointed out the French state had invested in ways that could not be recouped. The principal technological achievement of Thomson had been a digital decoder for satellite broadcasts, developed in RCA labs. Moreover, the French state invested additionally in Dmac2 technology, which is analog and now considered passé.[47] Negotiations were also made difficult by confusion as to who was the appropriate interlocutor. Said Mr. Bae, "I didn't know who was in charge of the privatization. Technically, it was the minister of finance, then the president of Thomson....The French government didn't have a clear objective for their privatizations."[48]

The Korean government also did not make things easy for Daewoo. Despite official government policy with a stated purpose of encouraging globalization, Mr. Bae noted that "Actually, they [the Korean government] made it harder. There is a new regulation that 20% of [outward] foreign investment must be supplied from our own capital. The idea is to discourage foreign investment to create jobs at home. I don't think it works and anyway, we use much more than 20% of our own capital."[49]

Daewoo was, in many ways, caught between Korean domestic politics and French domestic politics. In both cases nationalism played a key role. Korean regulations, as mentioned before, give priority to domestic jobs creation. This is, of course, understandable. The stupendous growth of the Korean economy has, in many ways, been built on economic nationalism. This is the essence of mercantilist policy.[50]

Likewise, French economic policy has also been broadly categorized as

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[44]Article 3 of Law no. 86-912 of 6 August 1986.

[45]*Journal Officiel de la République Française*, 5 December 1996, p. 17749.

[46]*Ibid.*, pp.17749-17750.

[47]Interview with Mr. Bae, 16 July 1997, Seoul, Korea.

[48]*Ibid.*

[49]*Ibid.*

[50]For a discussion of mercantilism, see Robert Gilpin, *U.S. Power and the Multinational Corporation* (New York: Basic Books, 1975), chap. 1.

mercantilist.[51] Policy toward inward foreign direct investment has been historically restrictive and the attitudes of French officials have been suspicious and inward looking. This attitude was dramatically illustrated in the 1960s by the wide-spread acceptance of the somewhat shrill arguments made in Jean-Jacques Servan-Schreiber's critique of US-based multinationals, "The American Challenge".[52]

Thus an assumption of French xenophobia in the rejection of Daewoo's offer is not entirely without precedent. The fact that Daewoo is an Asian company also leads to speculation that the motives of the Privatization Commission were not merely xenophobic, but also racist. The rising popularity of the anti-immigrant National Front Party has dogged French Conservatives and Socialists alike. Rejection of a Korean bid to take over the pride of French high technology could not fail to be a political plus in some quarters. As one newspaper report put it, "A huge backlash of public opinion - including the use of some racist images and references to Koreans forcing French employees to work like ants - set a strongly negative mood...."[53] This recalled the remarks of former prime minister Edith Cresson, never known for her diplomatic skills, who, while still in office, had referred to the Japanese as "ants." Such was a common French image of the workforce in Asia. As one French official stated: "Thomson was really a cultural issue."[54]

Understandably, the rejection of Daewoo's offer did much to poison Franco-Korean diplomatic relations. Immediately after the announcement by the Privatization Commission, the Korean government began talking of retaliation prejudicial to French sales of weapons, nuclear power equipment and commercial jets in Korea.[55] The Korean Deputy Prime Minister, Han Seung-soo called in the French ambassador to Seoul to express his "concern", while the Federation of Korean Industries sent a letter of protest to the French embassy.[56]

Ultimately, Franco-Korean relations recovered. But the Daewoo-Thomson affair did leave scars. In June of 1997 the Conservatives lost their majority in the French parliament and the Socialists returned to power under the leadership of Lionel Jospin, an opponent of privatization. Jospin decided to leave Thomson Multimedia under state ownership.

3. CONCLUSION

The argument of this paper is that theories of globalization, however cogent in the

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[51]See the series of essays in Stephen S. Cohen and Peter Gourevitch, eds., *France in the Troubled World Economy* (London: Butterworth Scientific, 1982).

[52]Jean-Jacques Servan-Schreiber, *The American Challenge* (New York: Atheneum, 1968).

[53]Andrew Jack, "France: Benefits are beginning to outweigh the difficulties," *Financial Times*, Survey, 6 October 1997, p. II.

[54]*Ibid.*

[55]Yoo Cheong-mo, "Resentment Mounts over Daewoo-Thomson Issue," *Korea Herald*, 18 December 1996.

[56]*Ibid.*

abstract, often run up against serious obstacles in the real world. Certainly, much of firm behavior is predicted by economic theory. The aggressive expansion of Korean firms into Europe is explained by a number of factors, including saturation of the Korean market and rising labor costs at home, attractive wage differentials in Europe thanks to lower levels of unionization and state-subsidized employment schemes, proximity to consumer markets and diversification of risk. Thus these factors, combined with the specific characteristics of the Thomson Multimedia product line, made Daewoo's offer to purchase the company a logical strategy for corporate expansion.

However, it takes two to tango. While the French government initially approved the sale of Thomson to Daewoo, the independent Privatization Commission prohibited the deal. The Commission's reasoning made some business sense in that the French state was insufficiently compensated for the transfer of technology which it had subsidized. However, speculation that the ulterior motive of the commission was cultural and chauvinistic, rather than simply economic, seems to be reasonable, absent stronger economic reasoning than was presented at the time. In any event, the case illustrates the thin predictive power of economic models taken straight from the textbook. Of course, no economist would pretend otherwise and our intent is not simply to set up a strawman. Rather, the intent of the paper is to illustrate the necessity of integrating political and economic variables to understand international behavior. The tendency to leave either as a residual category is both intellectually unsatisfying and ultimately inadequate.

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