TAMÁS SZENTES

CONCEPT, MEASUREMENT, AND IDEOLOGY OF "NATIONAL COMPETITIVENESS"

The author of this paper reviewing the perceptions of competitiveness reveals the origin and ambiguity of the concept of "national competitiveness" which is mostly confused with that of development of countries and competitiveness of their enterprises. He investigates the role of transnational companies and governments in shaping the world economic position of countries, presents a critique on the measurement of "national competitiveness" of countries, and heavily opposes the ideological use of the latter for justifying antisocial measures.

KEYWORDS: COMPETITIVENESS, TNC, DEVELOPMENT

JEL F00, F23, O10, O47

1. AMBIGUITY AND VARIOUS INTERPRETATIONS OF "NATIONAL COMPETITIVENESS"

Competitiveness has become a very fashionable term recently, used not only in regard to the marketing of products or services, and the rivalry of enterprises but also concerning nations or rather countries. While competition and competitiveness are well-known notions having been used for a long time, related not only to the market but great many other fields of social life, too, the concept of "national competitiveness" is relatively new. The first comparisons of economic competitiveness of countries appeared at the end of 1970s, and in early 1980s, namely (though not exclusively) in the publications of the *World Economic Forum*. Since the 1980s the comparative competitiveness of countries has received increasing attention in both economic literature and politics.[1] The worldwide spread of the use of the concept of *"national competitiveness"* gained a significant impetus by the famous book of Michael Porter (1990).

The concept of *"competitiveness"* seems to contradict the origin of the word "competition" rooted in the Latin word *"con-petere",* which (unlike the Latin "certare") means: "to seek (or drive) together for something". Consequently, competition does not necessarily imply an action against the other, an endeavour to reach something at the expense of the competitor, but rather implies parallel and interactive efforts for the same aim, and may include even a co-operation or, at least, a certain moral behaviour and requirement.

1 *Erzsébet Czakó* (2003) notes that the genesis of competitiveness (concerning nations) can be traced back to the mid-1980s, before which in economics practically no mention was made on the problem of competitiveness on national level. (p. 339.)

While the competitiveness of *products and services* has got a quite unambiguous meaning, and that of *enterprises, firms* (despite its complexity) is also well-defined enough, the term “national competitiveness” is very ambiguous.

1.1. COMPETITIVENESS OF PRODUCTS AND SERVICES

As regards products and services set up for sale, their competitiveness – as well-known – is basically determined by (a) their *quality* and (b) their *price*.

Just like in the case of all phenomena and processes of a market economy, two aspects, two interrelated sides are to be distinguished, namely (a) a *“physical”*, natural, technical, i.e. “real” aspect or side, and (b) a *“monetary”* one, related to cost, price, exchange value, etc. These two sides can by no means separated from each other; as they represent “two sides of the same coin”. In other words, a particular product or service is competitive, i.e. really marketable under “normal” market conditions, if, on the one hand, it can be sold at a price containing profit for its seller, i.e. realisable as an “exchange value”, and, on the other, it represents utility, a consumable or useable good, needed in its physical quality for a buyer having the required purchasing power to buy it.

The definition of competitiveness of a product or service must involve *these two aspects* (already distinguished by the Classical economics), namely its “realisable value” (manifested in a price containing profit for the seller, and acceptable for the buyer[2]) and its “realisable utility” (manifested in a physical quality meeting the need of the buyer).

It is surprising how often it is only the price of products that is emphasised in regard to competitiveness, particularly when currency devaluation is considered as a successful means of promoting exports even in case of partly or mainly quality problems.

One should not neglect, however, two additional criteria of competitiveness of products and services. Namely: (c) *information* on the latter and (d) *availability* of them, i.e. the access to their supply. For a product can be of a high quality, and its price can also be acceptable for the consumer, but if the latter does not know about it or cannot have (e.g. because of distance and lack of postal transfer facilities) an easy access to it, its “competitiveness” turns to be meaningless, as no comparison is possible with another product, nor a real choice for the consumer. This makes (e) *commercial advertisement* and extended *marketing activity* so important, and may justify the expenditures on them. Since, however, such costs may considerably increase the price of the product, an excessive spending on advertisement and business propaganda may be counterproductive. Moreover, the latter, particularly the commercial breaks in TV, may influence consumers' preferences so much as undermining their assumed sovereignty, and diverting demand not only towards luxurious products, which meet conspicuous consumption and require bank credits, but also some of unfavourable effects on health or environment.

2 It is to be noted, however, that in certain product (and service) categories, e.g. in the case of those luxurious ones meeting the "propensity of conspicuous consumption", a price reduction does not improve competitiveness.

1.2. COMPETITIVENESS OF FIRMS

In general, the *competitiveness of firms* can be defined as their ability to produce (both in terms of price and quality) competitive products and/or services in such a way as thereby ensuring for themselves a lasting level of an aggregate rate[3] of net profit, which is not less than the average level of profits in the given industry, and also a lasting, preserved or growing share in sales in the given market.

For defining and evaluating the competitiveness of firms it is hardly appropriate and sufficient to take only their momentary rate of profit into account[4] or even their ability to make fully use of all their available resources. The momentary rate of net profit cannot be a reliable indicator because in the case of some new enterprises and emerging "infant" industries, as well as, on the other side, of those driving for monopolistic position by applying dumping prices, it is a much higher profit rate in the future that would compensate its present lower rate. A full utilisation of all the available resources is, even apart from the problem of its perception and proper measurement, does not necessarily indicate a success, since it may be accompanied by losses, by a non-profitable performance, while an average or even a higher than average profit rate can often be achieved by companies with underutilised capacities.

In evaluating the competitive position of a firm one should take account also of the *dynamics* of its net profit rate and "total factor productivity", as well as the development of its market share and *position both on the "supply side"* (manifested in keeping or increasing the share in total sales in a given market and also in acquisition of new markets) *and on the "demand side" of the market* (manifested in the access to required resources, to cheaper inputs in a required quality).

Although the related international literature mostly reduces the *"supply-side competitiveness"* of firms to the issues of cost proportions (approaching the latter in accordance with the Classical or the Neo-classical, Heckscher–Ohlin interpretation of "comparative advantages"[5], moreover, ignoring even the original presumptions of the latter, which set limits to applicability), its criteria obviously involves in reality also the success in marketing, thus, in a dynamic sense: the increase in the share of sales.[6]

3 Since nowadays the most typical form of enterprises is the joint stock company which may have, and in the case of multinational firms certainly do have, several affiliates, subsidiary firms with their various rate of profit, what matters for the company as a whole is, indeed, their summarised, i.e. the aggregate rate of profit.

4 *Attila Chikán* and *Erzsébet Czakó* (2002) obviously looked for a definition of firms' competitiveness over and beyond the criterion of a momentary rate of profit. They stated: "We may consider enterprises competitive if they are able to transform available resources into a profit flow while complying with the social values of environment in which they operate and if they are able to perceive and manage external and internal changes that influence their long run operations in order to maintain their profitability ensuring long-term survival." (p. 26)

5 For their critical review see *Szentes, T,* (2003) Ch. III/2 and III/4.

6 As noted by *Ádám Török* (1999), the related indicators are based upon the assumption that a relatively lower level of unit factor costs, as compared to the competitors', necessarily ensures a higher market share and/or higher rate of profit. (p. 28)

A frequently used indicator of the "supply-side competitiveness" is the labour cost per value-added unit, the so-called *Unit Labour Cost* (ULC), which is the ratio of the total wage (and additional) costs to the value added. Its applicability, however, is limited to the comparison of firms engaged in the same industry, because the divergence of factor intensity between different industries makes such a calculation insufficient for measuring the relative efficiencies. Moreover, since the factor intensity even of the same industry usually varies from country to country, and not even its rank is necessarily the same everywhere, this indicator can only carefully be used. (The assumption that a lower ULC reflects a higher relative capital intensity, while a higher one the opposite, is not only based on the neo-classical over-simplification about homogeneous units of both factors of production, able to substitute for each other, but also questions the use of this indicator to measure competitiveness.)

The indicator of *"Unit Total Cost"* (UTC), i.e. the ratio of total factor costs to value-added, or (its reverse:) that of *"Total Factor Productivity"* (TFP), i.e. the ratio of value-added to the total costs of inputs[7], may be more applicable in comparing firms' competitiveness, since such indicators are, in principle, indifferent to factor intensity differences. In view, however, of differences in life-time of machineries, in technological level, and in the (growing) share of research and development expenditures as well as in the (declining) share of blue-collar workers' employment costs[8], etc. which all have a significant effect on the future changes in UTC or TFP, on the differences in the tempo of such changes between firms engaged in different industries, it is only the growth rates of the above indicators that can be meaningfully applied at all. Although a steadily high rate of growth in TFP does not only provide a basis for, but also reflects an improving competitiveness, as it likely indicates both cost-efficiency and quality improvement, there is, in fact, no guarantee that it is accompanied by successful marketing as well.

The *"demand-side competitiveness"* of a firm is often identified with, and measured by, a relatively higher growth of the unit value of exports, exceeding that of the partners. The latter may reflect, indeed, a success in marketing, such as following from the appropriate quality of products, i.e. meeting the consumers' preferences, instead of cost reduction or productivity increase only, which concern competitiveness in prices rather than in quality. Such an indicator, however, belongs, in my opinion, also to the evaluation of the supply-side competitiveness, at least from the point of view that it indicates the change in the relative exchange value of the *supplied* export product. Insofar as the conception of "demand-side competitive-

7 While an aggregate indicator of productivity, in general, would simply imply the ratio of total output to total inputs, TFP reduces the numerator to the value-added only, thereby avoiding double accounting. In the denominator TFP includes not only the costs of the factors of production (i.e. labour, capital and Nature or land) in the strict sense of the word, but also all the other input costs (such as raw material, energy, marketing, after-sale service, etc. costs). Insofar as the invested capital involves (must finance) all the costs of production and marketing, TFP may be considered as one of the indicators of capital efficiency, which, however, unlike the rate of profit, does not show how much remains as net profit out of the total of value-added, and also differs from the "capital/output ratio" not only as its inverse, but also in measuring value-added only from total output. TFP could also be interpreted (in consonance with the Classical and Marxian conceptions) as measuring the total productivity of labour in value terms (but without double-accounting), if the tracing back of all the costs to those of ("live" and "dead" labour (i.e. labour performed at the present and in the past) were practically possible.

8 In the "high-tech" industries the increase in TFP mostly follows from the growth of value added, in which R&D investments and the resulting technological progress play substantial role, in the "low-tech" industries it is often due to the reduction of employment.

ness" is reduced accordingly, the bargaining power of the firm on the demand side of the market, i.e. its ability in getting access to relatively cheap but high quality input-elements is, unfortunately, overlooked, despite its importance for competitiveness.

For the measurement of the "demand-side competitiveness" in the above sense, the "Unit Value Index" (UVI) is widely applied (although in the comparison of that of countries, rather than firms'). It is the ratio of a change in the unit value of export (i.e. total value of export divided by its total volume) to the change in the weighted unit value of exports of the major competitors, where the weights reflect the shares of the latter in the given market.[9]

The importance of the *"bargaining power of buyers"* appears also in Michael Porter's analysis (1990), particularly as it facilitates the shifts in input costs, and points to possible monopolistic position in the input markets, as well, i.e. on the side of demand, a kind of "monopsony". (p. 34, 45)

It is to be emphasised, in general, both regarding the *competitiveness of (1) products and services, and (2) the firms* supplying them, that in reality *"market imperfections"* predominate, which imply the lack or limitedness of free competition, the existence of concentrated economic powers (monopolies, oligopolies, etc.), the lack or inappropriate information of consumers, while transnational companies increasingly "internalise" trade, and organise cross-border transactions within their own networks, practically outside a competitive market.

1.3. "NATIONAL COMPETITIVENESS" AS A VAGUE, AMBIGUOUS CONCEPT CONFUSED WITH DEVELOPMENT OF A COUNTRY

Contrary to the above described concept of competitiveness of products and services set up for sale and that of firms supplying them, the term *"national competitiveness"* is very ambiguous for various reasons. Namely: (a) despite the attribute "national" it actually refers to countries rather than nations, which are not always the same, (b) it usually relates to the economy only, or involves non-economic factors merely from economic points of view; (c) its literature, while considering performances of countries in the process of development, focuses on those of the enterprises in markets and the conditions for the latter.

It is worth mentioning that *Michael Porter* himself denied (1990) that nations themselves can be "competitive": "We must abandon the whole notion of a 'competitive' nation as a term having much meaning for economic prosperity... Productivity is the prime determinant in the long run of a nation's standard of living...The only meaningful concept of competitiveness at the national level is national productivity...". "Seeking to explain 'competitiveness' at the national level, then, is to answer the wrong question. What we must understand instead is the determinants of productivity and the rate of productivity growth. To find answers, we must focus not on the economy as a whole but on specific industries and industry segments". (pp. 8–9)

9 See *Török, Á.* (1999), p. 31.

As a matter of fact, nations or countries may compete, indeed, *in quite many fields,* not only in the economy. Such as in education, science, arts, culture, and sports[10], also in space research, in regard to environment protection, social welfare, life security, political regime, level of democracy, international prestige and influence, etc., unfortunately also in armament, in acquisition of scarce resources and power (moreover, earlier, particularly during the time of colonialism in territorial conquest, too). They actually compete *in the process of development* and its sustainability.

Even *in the sphere of economy*, however, the very meaning and content of "competitiveness" can vary and be quite different according to and depending on the chosen *level of analysis* and action. Namely, whether it is (1) the level of firms, enterprises, (2) the level of industries, economic sectors, (3) the level of territorial units, regions within a country, (4) the level of national economy as a whole, (5) the level of transnational regions, i.e. of regional integration, or (6) the global level of the world economy is taken as a level or unit of analysis.

The economic interpretation of "national competitiveness" is heavily mixed up with the concept of economic development, on the one hand, and that of the competitiveness of enterprises of countries. This probably follows from the *market*-oriented, i.e. very economic perception of competitiveness, and also from the fact that *Michael Porter* actually identified the competitive advantages of nations with those of their *firms*. Thus he considered competitiveness as a basically micro-economic issue.

Michael Porter disagreed (1990) not only with those views defining the competitiveness of nations by rich natural resources or abundance of cheap labour, etc., i.e. by given endowments, but also those explaining it by other "macroeconomic" phenomena, such as depreciating currency, low rate of interest, or government policy in general, and even those referring to management practices.

He noted (1990): "Some see national competitiveness as a macroeconomic phenomenon, driven by such variables as exchange rates, interest rates, and government deficits. But nations have enjoyed rapidly rising living standards despite budget deficits (Japan, Italy, and Korea), appreciating currencies (Germany and Switzerland), and high interest rates (Italy and Korea)." "Others argue that competitiveness is a function of cheap and abundant labor. Yet nations such as Germany, Switzerland, and Sweden have prospered despite high wages and long periods of labor shortage." "...Another view is that competitiveness depends on possessing beautiful natural resources. Recently, however, the most successful trading nations, among them Germany, Japan, Switzerland, Italy and Korea, have been countries with limited natural resources that must import most raw materials." "More recently, many have argued that competitiveness is most strongly influenced by government policy. ...Yet such a decisive role for government policy in competitiveness is not confirmed by a broader survey of experience..." "...A final popular explanation ...is differences in management practices, including labor-management relations... The problem with this explanation, however, is that different industries require different approaches to management." (pp. 3–5.)

10 In the field of sports "competitiveness" refers only to the physical and spiritual ability to participate in a championship with merely the chance of winning, but not to the result itself, to winning a prize by top performance.

In Porter's view, the (ill-defined) question why a nation is more "competitive" internationally, i.e. more successful in the world economy, is in fact a question of "why *firms* based in a nation are able to compete successfully against foreign rivals in particular segments and industries." (p. 10). The "competitive advantage" of firms belonging to a certain nation manifests itself in its *lower cost level* and/or its *differentiated products* commanding "premium prices". But competitive advantage can be sustained by a firm over time only if it provides higher-quality products and services or produce "more efficiently", which all refer to "productivity growth."

According to him (1990) "Lower cost is the ability of a firm to design, produce, and market a comparable product more efficiently than its competitors. ... Differentiation is the ability to provide unique and superior value to the buyer in terms of product quality, special features, or after-sale service... Differentiation allows a firm to command a premium price, which leads to superior profitability provided costs are comparable to those of competitors." (p. 38.)

These points of him hardly contain anything new, which was not emphasized earlier in economic literature. However, at the price of contradiction, but fortunately enough and correctly, *M. Porter* went further (1990) by bringing the issue closer to that of the *multinational enterprises* (MNEs), called also (according to the official term of UN) as *transnational companies* (TNCs) acting on global level, and to certain macro-economic aspects as well as government policies related to such foreign companies, too.

M. Porter noted (1990): "Multinationals that are the leading competitors in particular segments or industries are often based in only one or two nations. The important questions are why and how do multinationals from a particular nation develop unique skills and know-how in particular industries? Why do some multinationals from some nations sustain and build on these advantages and others do not?" (p. 18.)

He also stressed that *multinational companies* follow a global strategy "in which trade and foreign investment are integrated" and intend to choose as a *"home base"* those countries ("nations") where their "competitive advantages" can easily be created and sustained. Their home base is "the location of many of the most productive jobs, the core technologies, and the most advanced skills". When choosing the home base the companies take into account those differences "in national economic structures, values, cultures, institutions, and histories" which "contribute profoundly to competitive success" (p. 19).

The confusion of "national competitiveness" with the issue of development of countries, and the market-oriented approach of its perception as well as the focus on the favourable conditions for those firms belonging to a given country, hardly follow only and simply from the influence of Porter's best-seller book. There is another, more convincing explanation. Namely the fact that those engaged in the economics of enterprises have recognised and increasingly taken into account that in the contemporary world economy, under the conditions of accelerating globalisation process and worldwide networking of transnational companies, the very competitiveness of firms is not any more a local or micro-economic issue. Instead, the latter, even in the case of small and medium domestic firms, must be interpreted and evaluated *in an international context*, compared with those in other countries, and thus it is heavily depending on the macro-economic environment and government policy, consequently institutional factors as well. Such a recognition in enterprise economics has actually completed that in development economics regarding how much the development of countries has been shaped also by foreign firms, particularly transnational companies (not only in economic but also in social and political aspects).

The *business approach* may, of course, induce, on the one hand, to identify national development with economic growth and, on the other, to consider the concept of economic growth as that of "national competitiveness" and to put the emphasis on those micro- and macro-economic conditions heavily influencing the operation, efficiency and profitability of enterprises, and also the use of related indicators.[11] Nevertheless, this can hardly justify such an extremely oversimplifying and biased perception of the development of countries and the confusion of their competitiveness with that of enterprises!

As a matter of fact, in the related international literature the competitiveness of products and services in the market is *often confused* with that of the firms, companies or industries supplying them, moreover with the "competitiveness" of nations or countries in regard to their ability to develop rapidly.

The *confusion* of development and competitiveness clearly appears in annual reports of the *World Economic Forum* (WEF).[12] The former reports of *WEF* defined "national competitiveness as the ability of a country to achieve sustained high rates of growth in gross domestic product (GDP) per capita"[13] Its 2010–2011 report defines it as the set of institutions, policies, and factors that determine the level of productivity of a country, which in turn determines the sustainable level of prosperity that can be earned by an economy. In this report *Klaus Schwab*, the editor notes (p. xi): "The Report contributes to the understanding of the key factors determining economic growth, helps to explain why some countries are more successful than others in raising income levels and opportunities for their respective populations", i.e. in the very process of development.

The confusion of economic development and the competitiveness of countries and their enterprises, while causing ambiguities in perceptions as well as biases in measurement, may be easily understandable, even if hardly acceptable, in the light

11 In the earlier (2000 and 2001) reports of the *World Economic Forum* (WEF) applied the so-called Current Competitiveness Index which included two sub-indexes, namely the company operations and strategy index, and the quality of the national business environment index. Its latest report (2011) states that since 2005 its applied comprehensive indicator, namely the Global Competitiveness Index "captures the microeconomic and macroeconomic foundations of national competitiveness." (p. 4.)

12 *Jeffrey D. Sachs* as one of the main contributors stated in an earlier report of WEF that "competitive countries are those that have the underlying *economic* conditions to achieve rapid *economic* growth for a number of years, taking into account their starting level of incomes." – Quoted by *Schuelke, R. W.*, (2000), p. 1)

13 Quoted by *James R. Martin* (2007), who also notes that the *International Institute For Management Development* (IMD) defined national competitiveness as "the ability of a country to create added value and thus increase national wealth by managing assets and processes, attractiveness and aggressiveness, globality and proximity, and by integrating these relationships into an *economic* and social model." (p. 1.)

of the *interconnections*, moreover interactions between them. The latter are also pointed out in WEF's reports, which state that more competitive economies tend to be able to produce higher levels of income for their citizens, and that a competitiveness-supporting economic environment can help national economies to support high incomes.

In the 2010–2011 report of WEF it is noted: "Competitive economies are those that have in place factors driving the productivity enhancements on which their present and future prosperity is built." "The productivity level also determines the rates of return obtained by investments (physical, human, and technological) in an economy. Because the rates of return are the fundamental drivers of the growth rates of the economy, a more competitive economy is one that is likely to grow faster in the medium to long run." (p. 4.)

There are also some *common determinants* of both the development and the competitiveness of countries and firms. Such as primarily the available quantity and quality of *human resources*, the extent of their employment, consequently, indeed, the level of *productivity* of the actually employed labour power, which depends not only on its physical and intellectual capabilities, behaviour and motivations, but also the applied *technologies*, the type of division of labour and specialisation, the *organizational patterns and management*, etc., as well as *natural resources and environment*. The formation and for "national" and/or enterprises' competitiveness favourable or unfavourable changes of all these are to a great extent influenced by the *role of the State*, the government policy as well as the *culture, moral* and *socio-psychological attitude of the people*, moreover, *"external" factors*, too, such as the international environment, demonstration effects of other countries, changes in the world economy and international politics.

It is to be noted that in the contemporary cases of "organic" participation of a country, i.e. when the so-called external, international relations extend beyond the more or less occasional trade transactions only, and embrace also capital flows or even some labour migration, too, and within the national economy transnational companies are operating, those factors and effects called "external" have to be qualified as mostly "internal". This is a fact which is almost completely ignored when references are made to the international environment, globalisation, or the effects of global crises, in the literature of "national competitiveness", including the reports of WEF.

It appears also as a *common feature* that neither the world economic position and competitiveness of countries, nor those of their enterprises are independent of their *sizes*. This is not only an important issue of economies of scale but also an issue of bargaining power and influence on partners, competitors and market processes, too.

In addition, neither in the case of "national" nor in that of enterprises' competitiveness the *geographical position*, the location closer or more remote to the "geographical centre of the world economy", and the *effects of climatic changes, natural catastrophes* and the ability to manage them, should be left out of consideration.

Despite such obvious interconnections and common features, the confusions of the concepts in question have to be somehow removed.

1.4. PORTER'S "NATIONAL DIAMOND" OF COMPETITIVENESS

The "competitiveness of nations" in the sense of creating attractive, favourable conditions for the inflow and/or local rise of successfully competing transnational companies depends, of course, on a multidimensional complexity of interacting factors and circumstances. Some of the most substantial and interacting components of the latter are presented in *Michael Porter's* (1990) famous model, called *"national diamond",* which embraces the major "determinants of national advantage"[14]. Although it hardly contains any new discovery, as an analytical tool it is well applicable.

The "diamond" consists of four poles, each representing the "determinants of national advantage":

(1) "*Factor conditions*. The nation's position in factors of production, such as skilled labor or infrastructure, necessary to compete in a given industry."
(2) "*Demand conditions*. The nature of home demand for the industry's product or service."
(3) "*Related and supporting industries*. The presence or absence in the nation of supplier industries and related industries that are internationally competitive."
(4) "*Firm strategy, structure, and rivalry*. The conditions in the nation governing how companies are created, organized, and managed, and the nature of domestic rivalry." (p. 71)

Among the *"factor conditions",* Porter distinguishes between *"basic"* and *"advanced factors",* and also groups the various "factors" into the following "broad categories: (a) human resources, (b) physical resources, (c) knowledge resources, (d) capital resources, and (e) infrastructure. The distinction among factor endowments of the last two can, in fact, be criticised, because "knowledge resources" obviously belong also to "human resources" (among which Porter himself mentions "skills", too), while infrastructure is a necessary condition, rather than a factor, of production. "Basic factors" – according to Porter – include natural resources, climate, location, unskilled and semi-skilled labour, and loan capital, while the "advanced factors" embrace "modern digital data communications infrastructure, highly educated personnel such as graduate engineers and computer scientists, and university research institutes in sophisticated disciplines." (p. 71)

Porter correctly emphasises the growing, decisive importance of such advanced factors as *"knowledge resources"* ("the nation's stock of scientific, technical, and market knowledge bearing on goods and services"), which "reside in universities, government research institutes, private research facilities, government statistical agencies, business and scientific literature, market research reports and databases, trade associations, and other sources". (p. 74)

He notes: "The importance of basic factors has been undermined by either their diminished necessity, their widening availability, or ready access to them by global firms through for-

14 According to *M. Porter* (1990): "Nations are most likely to succeed in industries or industry segments where the national 'diamond', a term I will use to refer to the determinants as a system, is the most favorable." (p. 72.)

eign activities or sourcing on international markets. These same considerations make the returns available to basic factors low, irrespective of their location. ... Basic factors may explain some of the trade *within* firms, reflecting the location of selected activities in various nations to tap into low factor costs. But they do not explain the location of the home base in most industries. Basic factors remain important in extractive or agriculturally based industries ...and in those where technological and skill requirements are modest and technology is widely available... Advanced factors are now the most significant ones for competitive advantage. They are necessary to achieve higher-order competitive advantages such as differentiated products and proprietary production technology. They are scarcer because their development demands large and often sustained investments in both human and physical capital." (p. 77)

Among the *"demand conditions"* Porter points not only to the size of the domestic market and the resulting opportunity of benefiting from economies of scale, but also to the pattern of demand, the segmented structure of demand ("distribution of demand for particular varieties"), the differentiation and sophistication of consumers' preferences.

"The most important influence of home demand on competitive advantage is through the mix and character of home buyer needs. ...Nations gain competitive advantage in industry ...where the home demand gives local firms a clearer and earlier picture of buyer needs than foreign rivals can have. Nations also gain advantage if home buyers *pressure* local firms to innovate faster and achieve more sophisticated competitive advantage... ...A nation's firms gain competitive advantage if domestic buyers are, or are among, the world's most sophisticated and demanding buyers for the product or service..." (p. 86, 89)

Porter also notes that even a narrow domestic market can imply advantage insofar as it may force the companies to export, and that the firms of small national economies can also be competitive in those segments of the market that represent a major share of the domestic demand, but a small one in other countries.[15]

As regards *"Firm Strategy, Structure, and Rivalry",* Porter refers to the ownership structure of firms, to their owners' and managers' goals, motivations[16], to the relationship between the latter and the employees[17], to "attitudes toward skill development, toward risk taking", to committed behaviours, etc. and particularly to the role of rivalry between firms which induce them to improve performance

15 "...the size and pattern of growth of home demand can reinforce national advantage in an industry... Some authors argue that a large home market is a strength, because of the existence of economies of scale. Other commentators see it as a weakness, reasoning that limited local demand forces firms to export." "...small nations can be competitive in segments which represent an important share of local demand but a small share of demand elsewhere..." "Sometimes, smaller countries represent very large markets for particular products." (p. 88, 92, 94.)

16 "Company Goals ...are most strongly determined by ownership structure, the motivations of owners and holders of debt, the nature of the corporate governance, and the incentive processes that shape the motivation of senior managers." (p. 110.)

17 "One important determinant of individual behavior and effort is the reward systems... The attitude toward wealth also varies across nations... Another important dimension is the relationship between the manager or employee and the company." (p. 113.)

and innovate.[18] Moreover, it is the local rivalry between firms, that he considers the most important in “factor-creation”.[19]

The fourth pole in Porter's “diamond”, namely *“Related and Supporting Industries”* refers to the importance of input-linkages, but separated, unfortunately, from that of output-linkages[20]. The competitive advantage resulting from the “supporting industries” manifests itself – according to Porter – in the access to the most cost-effective inputs supplied by the existing reliable and internationally competitive local firms and in the innovation process resulting from a continuously co-ordinated co-operation with them.

Porter notes: “The presence of internationally competitive supplier industries in a nation creates advantages in downstream industries in several ways. The first is via efficient, early, rapid, and sometimes preferential access to the most cost-effective inputs.” “More significant than access to machinery or other inputs is the advantage that home-based suppliers provide in ongoing coordination....Perhaps the most important benefit...however, is in the *process of innovation and upgrading*... Suppliers help firms perceive new methods and opportunities to apply new technology.” (p. 101, 103)

The so-called “related industries”, which are “those in which firms can coordinate or share activities in the value chain when competing, or those which involve products that are complementary”, provide competitive advantages by opening “opportunities for information flow and technical interchange”. (p. 105)

Porter intends to draw up also the *dynamics* of competitive advantages, in which he very realistically attributes primary role to the *“clustering”* of vertically or horizontally interlinked industries.

He notes: “The existence of a cluster of several industries that draws on common inputs, skills, and infrastructure also further stimulates government bodies, educational institutions, firms, and individuals to invest in relevant factor creation or factor-creating mechanisms.” (p. 135) “The systemic nature of the 'diamond' promotes the clustering of a nation's competitive industries. A nation's successful industries are usually linked through vertical (buyer/supplier) or horizontal (common customers, technology, channels, etc.) relationships.” (p. 149) “A concentration of rivals, customers, and suppliers will promote efficiencies and specialization. More important, however, is the influence of geographic concentration on improvement and innovation.” (p. 157)

He also stresses correctly that “competition is profoundly dynamic in character”, and that “firms gain and sustain competitive advantage in international competition through improvement, innovation, and upgrading”.[21]

---

18 “Domestic rivalry...creates pressure on firms to improve and innovate.” (p. 118.)

19 “Factor creation is perhaps most strongly influenced by *domestic rivalry*.” (p. 134.)

20 The input and output linkages together appear in Porter’s “value chain” and “value system” rather than in his “national diamond”. He defines a “firm’s value chain” as “an interdependent system or network of activities connected by linkages. Linkages occur when the way in which one activity is performed affects the cost or effectiveness of other activities.” (p. 41.)

21 In regard to innovation, Porter emphasises not only the role of rivalry in inducing it, but also the “saturation” of home demand, which forces local firms to continue innovating and upgrading. (p. 96.)

What seems, however, somehow missing in his otherwise enlightening model is a clear and logically structured presentation of the *historical changes* determining in different periods the development of the competitive advantages of "nations" and their position in the world economy. In particular, the very process in history remains rather obscure, in which owing to newer and newer "stations" or "revolutions" of technological progress those "drawing" industries (or specific economic activities) functioning as the *dynamic "engines" of development have shifted* from one sector of the economy to another one, thereby giving birth to new types of business organisations or opening new spheres of operation to existing ones. The same applies to the shifts in the centre of gravity in the world economy, despite its significant effect on the competitive advantages of countries in proximity to it. (Such a deficiency can hardly be remedied by the reference to the role of a "chance")[22].

The *major message* of Porter's eclectic theory – in consonance with that of *J. H. Dunning* (1993) – is, nevertheless, undoubtedly realistic by pointing to the fact that nations (countries) as well as firms can *create* competitive advantages. In the contemporary world economy the created advantages become more important and decisive for national development, than some given "comparative advantages".

M. Porter (1990) stresses: "While classical factors of production are more and more accessible because of globalization, competitive advantage in advanced industries is increasingly determined by differential knowledge, skills, and rates of innovation which are embodied in skilled people and organizational routines. The process of creating skills and the important influences on the rate of improvement and innovation are intensely local." (p. 158)

While in the past the economic policy recommended by the theories of international economics was to make use of the given "comparative advantages" in trade, today a *new paradigm*, following from such modern, eclectic theories as elaborated e.g. by Dunning and Porter, and reflecting the new conditions of the world economy, suggests a policy of *creating* "competitive advantages". Namely: by providing favourable conditions and attractive terms for the rise locally, and/or the inflow from abroad, of transnational firms which choose the country concerned as "home base" and can successfully operate in dynamic industries and services on international level.

What obviously follows is that in order to attract or give birth to such internationally competitive TNCs choosing the country as a "home base", the country itself and particularly its government can do a lot, by developing human capital, promoting the development of education, training, research and development capacities, technological progress, infrastructure, and the input-output linkages as well.

22 Under the category of "chance", Porter refers to "major technological discontinuities", "significant shifts in world financial markets or exchange rates", "political decisions by foreign government", wars, etc., which allow shifts in competitive position. (p. 124.)

National governments have both opportunity and responsibility to create competitive advantages[23], and thus the role of the State may change rather than fade away under the conditions of accelerating globalisation and worldwide TNC-activities. (See later!)

Michael Porter (1990) stresses the role of the "home nation" in creating and sustaining competitive advantages: "Competitive advantage is created and sustained through a highly localized process. Differences in national economic structures, values, cultures, institutions, and histories contribute profoundly to competitive success. The role of the home nation seems to be as strong as or stronger than ever. While globalization of competition might appear to make the nation less important, instead it seems to make it more so." (p. 19)

In spite of all the merits and realistic points of Porter's concept of "national diamond", it actually reinforced rather than eliminated the confusions of development and competitiveness of countries as well as that of enterprises.

1.5. NECESSARY DISTINCTIONS IN CONCEPTS

Although economic performance is a major determinant of countries' development, and the efficiency of enterprises plays an important role in it, one should not identify or confuse them. Nor should the competitiveness (even if reduced to the economy only) of countries and that of their firms be confused.

Whatever our opinion about the concept of "national competitiveness" can be, and however sceptical, moreover critical views we may have on the perception of countries' competition as a "zero-sum game", it seems reasonable for a better understanding of these concepts and a clearer viewpoint of analysis to distinguish at least (apart from special or partial ones) the following *variants of competitiveness of countries:*

(a) competitiveness in the process of *development* in general, which refers to development of society as a whole, not only to economy,[24]

(b) competitiveness in their efforts to reach or keep better *position in international relations*, bigger influence and stronger bargaining power (even if not economically[25]), or to be less subject to others' dominance,

23 "Government's real role in national competitive advantage is influencing the four determinants" (pp. 126–127.)

24 This point has been stressed in development studies for a long time, justifying the very distinction between the latter and "development economics", and inducing the application of non-economic indicators as well, in measuring the level of development. I may refer (as one of the invited participants) to the expert committee mandated by the General Assembly of UN to classify the "least developed countries" in 1971, which in its report introduced non-economic indicators, too, as for example the ratio of illiteracy, besides per capita GDP and percentage share of manufacturing industry in GDP, among the criteria.

25 A country, as the case of the former Soviet Union proved, may gain a much better status, even a superpower position (in terms of military strength) in the international relations, than in the world economy (in terms of its economic power and level of development).

(c) competitiveness in endeavouring to remain in the developed centre of the world economy or to catch up with the more developed countries, i.e. to maintain or improve *their world economic position*, and

(d) competitiveness in striving against each other, mainly by means of the *activity of their enterprises*, to gain *bigger share in world markets* of non-renewable resources, products, services and factors of production.

The latter two, namely (c) and (d) are obviously related to *competitiveness in the economy* only, even if they are shaped to a great extent also by the first two. For both analytical and methodological reasons the distinction of these two *as economic variants of competitiveness of countries* seems useful, moreover necessary.

For the sake of simplicity they can be called:

(1) *"world economic competitiveness"* and

(2) *"world market competitiveness".*

While studies on the former include, besides many issues of international economics, also those from, and are closely interrelated with, development studies[26], those on the latter involve issues of the economics of enterprises.

The *"world market competitiveness" of countries* or nations, as follows from above, refers (primarily, albeit not exclusively) to enterprises producing and marketing their products and services in "international trade".

In consonance with Porter's view and the above note, *Chikán, A.* and *Czakó, E.* (2002) state that: "National economic competitiveness is most of all determined by the performance and continuous adjustment of enterprises." Apart from the fact that the competitive advantage of a "nation" does not necessarily require, as *M. Porter* also stresses[27], that all enterprises are "competitive", the question arises: what determines the "performance" of the enterprises and what their "adjustment" actually means. Nevertheless, the above definition seems, indeed, relevant.

However, the same authors also add: "… results of enterprises are aggregated at macroeconomic level, and return on employed factors of production leads to a sustainable economic growth and increasing living standard at national level." (p. 26) The assumption that the results of enterprises can simply be aggregated and the final outcome is a sustainable economic growth coupled with increasing living standard, is a bit na?ve over-simplification (very similar, in fact, to the Classical vision about the maximum social welfare resulting from the sum of the self-interest-motivated individual activities). Sustainability of economic growth depends on several other conditions, too, including ecological and social ones, while even a sustained growth of the economy does not necessarily bring about social welfare for the majority of society. (It is exactly in view of the latter that the indicators of national development have been completed by such as measuring intra-society income gaps, public health conditions, cultural and educational development, too.)

While competition in the world market means competition of enterprises, based in different countries, with their tradable products and services, i.e. in international

26 Since the literature of "national competitiveness" mostly belongs to that of economics, while development studies are interdisciplinary, in the following we mainly (though not exclusively) concentrate on economic issues.

27 "Is a 'competitive' nation one in which every firm or industry is competitive? – No…" – *Porter, M. E.* (1990), p. 5.

trade, and also competition of countries with their internationally mobile factors of production, mostly capital, partly labour, in international factor markets, the *world economic competition* of countries is a much broader term, the meaning of which includes

- competition to gain by means of seizing those new opportunities opened by technological revolutions and through flexible adjustment to changes in the international environment, *more favourable position in the world economy*, to acquire a leading position or to catch up with the more developed countries, and for this aim
- competition in developing *dynamic sectors, activities in the national economy* and supporting directly or indirectly their successful enterprises,
- competition for *external development resources*, such as manifested in foreign direct investments (FDIs), foreign loans, research results, immigrant labour in need (particularly highly qualified manpower through brain drain), and (since in the contemporary world economy all these mostly and increasingly depend on being integrated and how in the international network of transnational companies) also
- an intensive competition in the policy *to attract* the inflow of transnational firms, their stay and settle their "home base", and/or to develop transnational firms within the national economy.

In the contemporary world economy the competition between countries extends, beyond international trade, to capital flows as well, and, despite all the justifiable criticism and ideological lip-service against transnational companies (TNCs), practically all governments intend to invite and keep their foreign direct investments (FDIs). Thus, "national competitiveness" involves also the *ability of a country to attract FDIs and become the "home base" of TNCs.*

While *Paul Krugman* (1994) flatly denies that countries or states (like firms) are competing with each other and gaining benefits at the expense of others in international trade, *Peter Dicken* (1998) points to that "one of the goals of nation-states is to maximize the material welfare of their societies", and, thus, in an increasingly integrated and interdependent global economy... nations are forced to *compete* with one another in a struggle to attain such goals. States compete to enhance their international trading position and to capture as large a share as possible of the gains from trade. They compete to attract productive investment to build up their national production base which, in turn, enhances their international competitive position. (p. 86)

In our country, Hungary, and concretely at our university, *those scholars engaged in international economics and development studies* are, quite understandably, dealing with global and regional issues and focussing mainly on the changes in the world economic position of countries, their economic growth, general development, and the major reasons behind them. Thus, they are more concerned with the "world economic competitiveness" of countries, and the related indicators, than *those engaged in the economics of enterprises*, who for obvious reasons concentrate on the operation and efficiency of firms, the national and international environment, legal and institutional conditions of business, including favourable or unfavourable government policies.

This difference or rather a disciplinary division of labour is also manifested in that the former researchers tend to investigate the long-run and global tendencies rather than short-run and local ones, while the latter mainly (though not exclusively) investigate those shorter and local processes as well as those external, international conditions that play important role in determining the efficiency of operation of enterprises within a country or internationally.

Along with such a division of labour it seems a common recognition that both in the development of countries and in the efficiency of enterprises a determining role is played by the *human factor*, a fact which is manifested not only in national, more precisely all-social level of productivity and its rise, but also in total factor productivity of enterprises, in the quality of economic and business management as well as civil services, in the behaviour and culture of the people, the political and economic elite, and in the government policy, too.

As regards the issue of *transnational companies*, i.e. such firms as operating in several countries, following global strategies and developing extended networks in the world economy, which as a subject belongs to micro-, macro- and international economics alike, the related research fields of those interested in world economics and those in enterprise economics are obviously overlap.

It is to be noted that today, in the era of TNCs, it is hardly correct and justifiable even to consider the sphere of firms in general as "micro-spheres". Moreover, the emergence and spread of international production systems organised and operated by the TNCs, and the rise of networks and clusters of their business activities make the competition and competitiveness of firms change into those of the TNCs' international production systems, networks and clusters.

2. THE ROLE OF TNCS IN "NATIONAL COMPETITIVENESS"

One of the most controversial issues in international economics and development studies is that of the transnational companies (TNCs) which have not only transnational activities extended to several countries in an international network but also involve equity capitals owned by persons or firms belonging to different countries as well as multinational management.[28] They have emerged not only in the fields of production and commerce but also in banking and in communication and information services.

The effects of TNCs on the countries' development and competitiveness are contradictory in double sense. Namely: first in the sense, one the one hand, that nowadays all over the world governments are induced (or even forced by some international institutions such as particularly IMF, World Bank and WTO),to follow an economic policy attracting them, providing favourable conditions, various allowances and even privileges, while, on the other hand, their activities heavily influence the external as well as internal relations of the countries concerned.

28 This is why they may be called transnational or multinational companies alike.

Second, in the sense that their effects are both, but not equally, favourable and unfavourable.[29]

Apart from ideologies, an objective evaluation is possible only in concrete cases and concrete terms. Those ideological biased views either praising or condemning the TNCs and also the process of globalisation promoted by them, mostly neglect the very context of their operation, the general features of the world system, and also the very interactions between TNCs and local forces. This seems true even in the case of those financial institutions, multinational giant banks the responsibility of which for the recent financial, particularly debt crises can hardly be doubted.

Countries which manage to get built-in position in the international network of TNCs and are able to meet their frequently changing demands, may have a higher rate of economic growth and improved competitiveness, while those countries remaining outside their networks and are neglected by them, are doomed to lag behind. The former may seize and enjoy new opportunities opened by TNCs in the use of new technologies, know-how, management system, marketing, financing and employment facilities, etc., while the latter mostly miss, or pay higher price for, such opportunities. However, when the former cease to be attractive for the TNCs, the latter move out of their economy, causing thereby backwash effects (manifested in the loss of former markets, secure demand conditions, and number of jobs, in numerous un- or underutilised machineries and technologies, etc.) and often a growing deficit in central budget and balance of payments), too..

Whichever cases are taken into account, it is obvious enough that development as well as competitiveness of countries (actually both of those variants of the latter mentioned above) are heavily influenced by the activity of and the relationship with the TNCs.

The modern "eclectic" theory of foreign investments and business policy of multinational enterprises (MNEs), in other words: transnational companies (TNCs), is mostly attributed to *J. H. Dunning*. While breaking with the over-simplifying concept of Neo-Classical economics, which practically reduces the reason of investing capital abroad to a higher return resulting from relative capital shortage in the foreign economy concerned, Dunning presents the most realistic picture of the *complexity* of FDI motivations and business strategy of the MNEs.

Having outlined the alternative choices of the MNEs, namely between the export of products, the sale of know how, and FDIs, *Dunning* logically groups the various motivations of the latter, and categorises them as according to different criteria.

J. H. Dunning, in his excellent book (1993), categorises the major types of motivations of foreign direct investments (p. 56), as follows: (a) resource seeking, (b) market seeking, (c) efficiency seeking, and (d) strategic asset or capability seeking.

(a) *"Resource seeking"* may practically refer to *all* the possible resources (natural, labour, capital resources, including physical and human capital, technologies, know how-s, management, administration, organization and marketing skill, credit and loan facilities, etc.) which are needed for the operation of the company.

29 For more details see *Szentes, T,* (1982) and (2003).

Regarding *resource-seeking investments, Dunning* notes that "resource based investment had declined to about one-third of worldwide MNE activity. ...On the other hand, FDI to gain access to technology, information and specialized management skills is more important than it used to be." (pp. 57–58). However correct this statement is, the *shift* from the "colonial type" of investments aimed at both acquiring natural resources and making use of cheap unskilled workers in the export-oriented primary production, to investments in the industrial and service sectors for benefiting from "relative international wage differences" (i.e. from wage differences bigger than productivity differences) is somehow blurred. Instead of concluding about a decline of "resource-based investment", it is more relevant to speak about the increasing orientation of FDIs towards the acquisition of more and more qualified (but only relatively cheaper) human resources, intellectual, research and development capabilities.

(b) *Market-seeking investments* aim at sustaining or protecting existing markets or exploiting or promoting new markets that provide economies of scale and/or economies of scope.

This motivation may stem – according to Dunning – from (1) the need to follow the main suppliers or customers to new markets, (2) the need to adapt the products to local tastes or to indigenous resources and capabilities, (3) the intention to economise on transport costs by serving the local market from an adjacent facility, and (4) the necessity "to have a physical presence in the leading markets served by ...competitors". (pp. 58–59) These may be, indeed, important motives behind the orientation towards certain markets, but hardly exclusive ones.[30]

A quite typical and frequent motive, namely to have built-in position within a regional economic integration area, a customs union or common market, thereby enjoying the benefits from an enlarged market and avoiding the tariff and non-tariff barriers, is left out of the list, although e.g. the European integration process has obviously induced many US-based and Japanese, recently Korean and Chinese companies to invest in the region for this very reason.

It is also to be noted that the export of capital (also in the form of loans or even financial aid) can be the means of promoting the export of products from the capital exporting country, in general. (In the case of "export credit" such a link between lending and exporting is clearly manifested.) Foreign direct investments, unlike loans that must be repeated (moreover, in increasing amount, if debt servicing has already started) in order to keep the same market for exports, may create and also extend the market abroad more lastingly. This is because they are not only accompanied, as usual, by the export of investment goods, machineries, equipments, etc. when they are made as "green-field investments", but also due to the fact that the resulting affiliates need further supply of spare parts, technologies, machines for replacement, etc. during their operation. In addition, the demonstration effects both on production and consumption of the recipient country may

30 The World Investment Report of *UNCTAD* (2002) classified the market-seeking FDIs as conditioned by (1) the market size and per capita income, (2) market growth, (3) access to regional and global markets, (4) country-specific consumer preferences, and (5) structure of markets. (p. 24) Here, the reference to (3) regional markets makes the point that was missing in *Dunning's* list.

also generate demand for imports from the country where the invested foreign capital originated from.

Since the new technologies have made product differentiation much easier, TNCs are increasingly interested in such markets providing, besides economies of scale, by their size, also economies of scope, by their appropriate structure of differentiated demand.

(c) *"Efficiency seeking"* obviously refers to the already mentioned aggregate profit rate of the company, i.e. to how its aggregate productivity can be increased (by better technologies, improved quality of labour, economies of scale and scope, etc.), and how its total costs can be reduced (by economising on their various components, including both "internal" and "external" costs).

Efficiency-seeking is, of course, the most general and natural intention of all business enterprises, as it is a precondition both of earning profits and of surviving in competition. In the case of joint-stock companies, such as TNCs, exporting parts of their capital and investing in several countries, "efficiency" primarily refers to, and is measurable by, the *aggregate rate of profit*, which depends – as *Dunning* stresses (1993) – not only on the profitability of the affiliates themselves, but also on "the effect that foreign production has on the profitability of the rest of the investing organization" (p. 56). Efficiency-seeking implies the intention "to take advantage of different factor endowments, cultures, institutional arrangements, economic systems and policies, and market structures... by concentrating production in a limited number of locations to supply multiple markets". It is manifested in two main kinds: (1) utilising the advantages arising from "differences in the availability and cost of traditional factor endowments in different countries", and (2) taking "advantage of the economies of scale and scope, and of differences in consumer tastes and supply capabilities" "in countries with broadly similar economic structures and income levels" providing "created competences and capabilities". (pp. 59–60)

The latter, which may involve also those "created advantages" manifested in the availability and high-level efficiency of qualified labour, of R&D capacities and well-developed economic and social infrastructure, can explain the observed *shift* also in efficiency-seeking towards the already developed and the newly industrialised economies where such local advantages contributing to increasing efficiency have been created.

The most important method of economising on costs and increasing the aggregate profit rate, namely the one taking advantage of the *"relative international wage differences"* (i.e. relative to productivity differences) or "relative international productivity differences" (i.e. relative to wage differences), is, unfortunately, not marked out..

(d) The *"strategic-asset seeking"* refers not only to the aim of smashing and pushing out the rivals in competition, but also – if reasonable – to possible "strategic alliance" with them.

This motivation implies, of course, the natural aim of companies, namely and according to *Dunning*, "to strengthen their own competitive position or weaken that of their competitors" by "capitalising on the benefits of common ownership of diversified activities and capabilities, or of similar activities and capabilities in diverse economic and potential environments", by "opening up new markets, creating R&D synergies or production economies, buying market power, lowering transaction costs, spreading administrative overheads, advancing strategic flexibility and enabling risks to be better spread".(p. 60.) Such methods are, practically, the same as involved in efficiency-seeking and market-seeking, too. What appears as really new in "strategic-asset seeking" is the willingness of the contemporary TNCs to enter strategic alliances with their competitors, particularly in the field of expensive research and technological development, or just to share certain markets.

In order to outline a general framework for the analysis[31] of the transnational corporations' business strategy and FDI policy, *J. H. Dunning* elaborated (1993) his famous *"OLI paradigm*, in which "O" stands for ownership-specific advantages, "L" for location-specific advantages, and "I" for internalisation advantages. (pp. 81–84)

(a) As regards *ownership advantages*, they imply the most direct control over the operation of foreign subsidiaries and those resources badly needed for a TNC, or the quality of inputs for their final product, for the protection of their copyright, brand names etc.

Keeping or taking over the ownership may be necessary for maintaining the reputation of the firm among consumers, for protecting its brand name, which depends on the reliable quality of the supplied products. If contract-manufacturers cannot provide the required quality or for the production process those inputs bought from independent firms fail to meet (regularly) the requirement, the establishment of a direct control by means of acquisition, i.e. full or partial ownership, promises the best solution.

Although ownership has not lost its importance in the contemporary business relations and competitive power, a certain *shift* can be observed (as reflecting that in the pattern of business interests, too), namely away from the advantages gained by the "possession of natural resources" in general. Instead, ownership control over R & D capacities, new results of product and technology development, and industrial research activities become more and more decisive advantage (either to increase competitiveness by applying first the research results, or to prevent others from getting an access to the latter).

(b) The *location advantages* may include, of course, all those specific conditions of a given country or region, as distinctive from others', providing "comparative advantages" and "basis" for international trade (such as considered in the classical and neo-classical trade theories), but also many other, objective or created circumstances (for example, the geographic position as related to the contemporary centre of gravity of the world economy, the "economic" and "cultural distance" from, in fact the closeness rather to the home base of the company, the hospitable, TNC-friendly atmosphere, "free trade zones", tax and other allowances, etc.).

31 As Dunning notes (1993): "A paradigm ...seeks to present a general framework for analysing the relationship between phenomena from which it is possible to formulate a variety of competing or non-competing theories. Perceived in this way, a theory is a derivative of a paradigm, but one paradigm may be able to accommodate several theories." "...a theory is a set of propositions about the nature and form of the behavioural relationship between a set of phenomena, the validity of which can be empirically tested." (p. 64.)

In Dunning's list such "location-specific variables" include – among others – favourable resource endowments, lower input prices, higher quality and productivity, lower transport and communication costs, investment incentives and other government policies, such as tax allowances, duty-free imports, "industrial park" facilities, etc. favouring foreign investors. Location advantages may include also those general conditions shaped by the economic, social, educational, cultural and political development of the country, i.e. created by the society as a whole, that are manifested in its *"economic" and "cultural" proximity* to the locations the TNCs are accustomed to.

As a matter of fact, all the variants of the "basis" for international trade, to which the standard textbooks of international economics pay so much attention, can actually be applied here, in the context of which of the given or created location advantages can attract foreign direct investments.

Such variants are – as well-known – the following:

- the available natural resources and favourable natural conditions;
- the higher relative labour productivity (as considered by the Classical scholars);
- the relative abundance of labour or capital (as in the focus of the Heckscher–Ohlin model);
- the given technological level and the availability of qualified labour and researchers (as appearing in the concept of "technological gap" and of "product life-cycle");
- the economies of scale, i.e. the given opportunity to economise on the internal costs of production by increasing the output (as involved in the concept of "trade based on internal economies");
- the existence of favourable externalities, i.e. the opportunity to economise on costs by making use of already given facilities of a developed material or social infrastructure (as involved in the concept of "trade based on external economies");
- the actual pattern of consumer preferences that differs from other countries' (as taken into account in the concept of "trade based on differences in tastes"); and
- the intra-society differences in consumer demand, which induces or facilitates product differentiation (as reflected in the related concept of trade theory).

(c) *Internalisation advantages*, which refer to the manner (the "how") of operation, imply those advantages that a TNC can gain by vertically integrating the segments or various functions of the production process (the "value-chain") or horizontally diversifying, and organising economic activities in a conglomerate. Internalization implies the organization, within the same company, of cross-border transfers of products and services among its subsidiaries located in different countries. Its great advantage follows not only from saving such transactions from market fluctuations and uncertainties, but also from making possible to use special, manipulated or even artificial prices, the so-called "transfer prices" in accountancy, and thus, by means of over-invoicing or under-invoicing the imports or exports, to reduce the local tax burden.

The aim of internalisation is to achieve security of supply, to reduce transaction and information costs, to protect the acquired intellectual property rights, to avoid "buyer uncertainty", "underperformance or misrepresentation of foreign agents", to protect the quality of inputs, etc. While some of the latter also belong to ownership-specific advantages in general, the major advantage of internalisation is the very organisation of international transfers of products and services *within the "gates",* i.e. outside the uncertain market, and also the avoidance of heavy taxation by applying "transfer prices".

It seems, however, necessary to complement *Dunning's* OLI-paradigm by a fourth type of advantages which are increasingly important for and aimed by TNCs While internalisation ensures the advantage of the facility for the TNCs to supervise a wide range of production and service activities and various business functions and also the advantage of centralisation of the decision-making on strategic issues, another, seemingly opposite tendency, namely *externalisation* also brings about significant advantages. Such as, particularly, the advantage of a high *flexibility* in business operations, which is of utmost importance under the contemporary conditions of sharpening competition and rapid changes in technologies as well as in demand structures.

(d) *"Externalisation-specific advantages"* are those resulting from outsourcing, from contracting and subcontracting independent firms within the network of a TNC, from the application of the putting-out system (including its new variant, "tele-employment" of relatively cheaper labourers working at home, on computers, in remote areas). By means of externalisation a TNC can economise on costs on a global level, can get a reliable, organised access, based on contracted co-operation relations, to the relatively cheapest inputs from outside the circle of its own affiliates. It may also carry out, for the sake of rationalisation and reorganisation, *shifts* in its structure and location of production more easily, rapidly and at much lower costs, than in case of keeping the production of the inputs concerned, i.e. the supply of those products and services to be used by it, within "in-house", within the sphere of its own affiliates' activities.

It is to stressed, however, that such an externalisation of certain functions and stages of the production process, insofar as taking place within the network of the same TNC, involving the complexity of directly and indirectly managed co-operation relations, does not contradict at all, but rather *complements* the strategy of internalisation. The application of both methods enables the company to combine centralisation and decentralisation, to benefit from specialisation on the core activities kept "in-house", as well as from flexibility that is ensured by the external conglomerate's complementary activities.

As the 2002 World Investment Report of *UNCTAD* (2002) also stressed, there is a "growing tendency for firms, even large TNCs, to specialize more narrowly and to contract out more and more functions to independent firms..." "Some are even opting out of production altogether, leaving contract manufacturers to handle it while they focus on innovation and marketing." "...TNCs also increasingly use national suppliers and contractors in host economies. Specialization does not stop there: leading TNCs are also entering into joint innovation arrangements with other firms – competitors, suppliers, or buyers – and with institutions like research laboratories and universities. Thus, the emerging global production system is increasingly open in terms of ownership, but with tighter coordination by lead players in each international production system."

"In fact, this dichotomy, between externalised, market-governed transactions and internalised, hierarchically governed transactions, grossly simplifies the richness of the regulatory mechanisms in the contemporary economy. The boundary between internalisation and externalisation is continually shifting as firms make decisions about which functions to perform 'in-house' and which to "out-source" to other firms. What we have in reality, therefore, is a spectrum of different forms of co-ordination which consist of networks of interrelationships within and between firms structured by different degrees of power and influence. Such networks increasingly consist of a mix of intrafirm and interfirm structures. These networks are dynamic and in a continuous state of flux." (Pp. xxii. and 8–9.)

Contrary to the one-sided approaches of both neo-liberalism and nationalist or ultra-leftist rhetoric, *Dunning's* works do also point to the *"double face"* of the foreign capital investments, in general, and of the activities of TNCs, in particular.

In the light of both Dunning's analysis and empirical facts it is clear enough that transnational companies bring about equalisation in income level or development resources *neither within nor between countries* (but may increase the "gaps"). However, their efficiency oriented and integrated business policy organising and managing their cross-border activities in production and services may bring about not only potential dangers and damages for a country, but also potential advantages and *new opportunities*. This is particularly so because such firms when intending to capitalise on all the available local assets throughout their corporate system, are ready to *locate or relocate* any "link" in the value-added chain wherever it improves most their overall performance, their aggregate rate of return to invested capital. It addition, a host country may enjoy and keep the benefits from the export-oriented activities of TNCs and from a built-in position in their international production system but only if it develops further its own resources, particularly the human resources, and location advantages and promotes the technical and technological up-grading of local firms and their input-output linkages with TNC affiliates.

The fact of *new opportunities* opened by TNCs for the less-developed economies has been emphasized even by *UNCTAD* (1999), which has always paid particular attention to the interest of developing countries: "The decision to locate any part of the value-added chain wherever it is best for a firm ...to convert global inputs into outputs for global markets means that FDI and trade flows are determined simultaneously. They are both immediate consequences of the same locational decision...Reduced obstacles to trade and FDI and the possibilities that they open up for TNCs to disperse production activities within integrated international production systems create new opportunities for countries. The challenge is to attract FDI and then to maximize the benefits associated with it in order to realize the opportunities arising from the new environment." (p. xxiv.)

As regards the *new opportunities* opened by TNCs (as already mentioned), they may follow also from the changes in their business interests and shifts of their orientation (as already noted and partly appearing also in Dunning's work). Such as

- the *shift* from the "colonial type" of investments aimed at both acquiring natural resources and making use of cheap unskilled workers in the export-oriented primary production, to investments in the industrial and service sectors for benefiting from "relative international wage differences",
- the orientation, owing to their interest in product differentiation made possible by advanced technologies, towards such markets providing not only

economies of scale by their size, but also economies of scope, by their appropriate structure of differentiated demand, and

- the *shift* also in efficiency-seeking towards the already developed and the newly industrialised economies where such local "created advantages" manifested in the availability and high-level efficiency of qualified labour, of R&D capacities and well-developed economic and social infrastructure, may contribute a lot to increasing efficiency.

In general, the *potential advantages*, benefits from the direct investments of TNCs and the operation of their affiliates include, on the one hand, (a) the access to additional financial resources, investments or reinvestments over and beyond the host country's own financial capacity, (b) the access to foreign, more up-to-date production technologies, know-how, and to management and organisational skills, (c) international business contacts, (d) additional information facilities, (e) new markets within the TNCs' network, (f) participation in their organised cross-border trade (avoiding the uncertainties of market fluctuations), (g) employment and in-service training opportunities for local labour and (h) secured supply facilities for the local "supporting" firms, contracted manufacturers and service industries, etc.

The *potential disadvantages*, dangers or losses include, on the other hand, (a) the reduction of the scope of "national" decision-making on the structure of production, on the commodity and geographical patterns of trade, i.e. a reduction of the "national sovereignty" over the economy (which, by the way, under the circumstances of extending and deepening interdependencies also in other forms, is an increasingly anachronistic, illusory concept), (b) the influence on the policy-makers (by strong lobbies or even corruption), (c) the transfer of "inappropriate" technologies, (d) the drain of resources, the appropriation of business facilities, state supports, various privileges and allowances, and the seduction of the most qualified experts, technicians and labourers (a kind of "domestic brain drain"), (e) the application of restrictive business practice, etc., which all adversely affect the smaller local firms, (f) the avoidance of taxation by applying "transfer prices" and the repatriation of profits over and beyond a "normal" measure, (g) "trade creation" at the expense of local suppliers and "trade diversion" at the expense of traditional partners, (h) the risk of their disinvestments and capital flight causing thereby sudden drop in employment and deterioration of the balance of payments, etc.

The far greater *flexibility* of the modern TNCs in their organisation, strategy and choice of locations, in the distribution of specific functions, combination of various means of control, transfer of units, regional headquarters or even the "home base" from one country to another, their *looser ties* with their original "birth-place" and their higher *responsiveness* to market changes, etc. seem to intensify the challenge they set to their partners, both home and host countries, and also open much greater opportunities for those of the latter following a policy for real national interest.

The spread of the TNCs' *international production systems* and changes within the latter undoubtedly open (a) new opportunities and set (b) new challenges and risks for the less developed economies, too.

(a) Since one of the main motivations of organising international production systems is the aim of economising on costs, the increasing level of the latter (particularly of wages and environmental protection costs) in the more advanced countries tends to induce *relocation*, i.e. transfer of the mostly affected activities to relatively (i.e. as compared also in productivity) cheaper areas. It is not only this relocation, facilitated by improved transport techniques, which implies both a new opportunity and a new danger, but also a possible *upgrading in the value-chain* within a TNC's production system, of some of those primary products, too, which represent the traditional exports of many developing countries. *Contract-manufacturing and contract-servicing* facilities can be utilised fairly well by those firms in less developed countries, which are made capable to meet the requirements in terms of the quality, quantity and time of the supply. They can grow up to the level of *supplying and servicing also outsiders* of the given production system, i.e. acting as partly independent firms in international market or even developing gradually into export-oriented transnational companies themselves. In addition to the already existing producing and servicing activities, *newer and newer "links",* suitable for out-sourcing, are arising in the value-chain of production systems, as a result of the increased tradability of services and of the sharpening competition making cost-reduction an imperative for the TNCs, which open entirely new areas for international division of labour.

(b) The technological development, fuelled by competition, raises the *entry-level criteria* and performance requirements in terms of quality supply, skill, technological sophistication and reliability, for those firms of the less developed economies, seeking for contract-manufacturing or contract-servicing facilities within the international production systems of TNCs, i.e. for incorporated position in the networks of the latter. Even more difficult can the entrance become for independent firms to a market which is dominated by a TNC, its affiliates or its contracted partners with built-in position in its international production system, because of the accumulation of the already acquired or created competitive advantages of the *first entrants*[32] enjoying, even if temporarily, a more or less monopolistic position. The future development of a particular production system and, therefore, the business prospects of those incorporated in it are rather *uncertain*, particularly in the spheres of production where technology changes rapidly and permanent upgrading is a precondition of survival. Even worse or more uncertain is the prospect, in general, for those firms operating in some traditional labour-intensive industries with low level of technology, insofar as markets are later or sooner saturated and/or new producers with higher-level technologies and new types of products push them out of the market. (Some of them may adversely be affected also by further trade liberalisation.)

It is also to be noted that despite the growing *externalisation* in the international production systems of TNCs, the latter remain in strong dominant posi-

32 The 2002 World Investment Report of *UNCTAD* stressed: "Once production has been rationalized to serve regional or world markets, first movers tend to build strong cumulative advantages, reaping economies of scale and scope and drawing upon clusters of suppliers and institutions." (p.119.)

tion within such systems, over those many formally independent producers involved in them, by means of keeping direct ownership control on research and development, trade mark management, strategic alliance making, etc. and certain key functions in hand, such as determining the technological and quality requirements, standards, norms, and enforcing their observance.

A considerable *risk* follows from the fact that the great sensitivity of TNCs vis-a` -vis changes in cost level, market disturbances, economic policy, legal regulations, taxation, etc. make them inclined to relocate their production system or parts of it. Such a relocation is easier and less expensive for them in the case of activities requiring cheap, less skilled labour and involving relatively smaller investment of physical capital, than in that of highly capital-intensive, particularly skilled labour intensive activities. Consequently, relocation is not only more frequently affect the less developed countries but causes also more harm to them. It is also a great risk whether a given production system will expand or contract, and what new-comers will be co-opted.

In view of the above-outlined motivations of TNCs which have become the major actors in the world economy and the potentially favourable or unfavourable effects of their activity, the *"national competitiveness"* of countries in general, and both the "world economic" and "world market" variants can hardly be assessed out of the context of their activity and changing business policy. Countries may actually improve or worsen their competitiveness as also depending on the extent and way of being involved in the TNCs' network, and how they meet the changing needs of such companies. The countries, recently among the formerly under-developed ones, which have succeeded not only in attracting foreign TNCs but also developing their "own" (in the sense of providing "home base" for them) have a higher rate of economic growth, improved world economic as well as world market competitiveness.

It seems strange enough, moreover contradictory, that although *Porter's* concept of "national competitiveness" and his "national diamond" defining the favourable conditions for FDIs are basically TNC-oriented, the WEF's reports, inspired by him, on "national competitiveness" almost completely disregard how the business policy of TNCs affect the changes in the position of countries in the ranking list. The effects of outward FDIs by which positions can be gained inside foreign economies, and not only trade relations but also the economic policy in the host countries can be influenced, are also left out of account.

The international literature on "national competitiveness" ignores the very problems of the structural effects of international capital flows. It hardly pays attention to such effects of the business policy of TNCs as often proved to be detrimental to the competitiveness of numerous countries. At the same time it attributes great importance to favourable business environment, hospitable investment climate among the determinants of "national competitiveness". Most of the authors reject any restriction or discriminative treatment of the activities of TNCs, and qualify the government interventions in the market processes as unfavourable in general. Such a viewpoint is still influential in the selection and evaluation of indicators applied by WEF.

3. THE CONCEPT OF "WORLD ECONOMIC COMPETITIVENESS" OF COUNTRIES

The *"world economic competitiveness"* of countries and changes in it are mainly shaped by longer-run effects and alterations of domestic and international circumstances, while *"world market competitiveness"* depends rather on contemporary or shorter-term ones. However, their *interrelationship* manifests itself not only in a positive sense, i.e. when reinforcing, promoting the improvement of each other, but also in a negative sense, in weakening, worsening each other, moreover, in such trade-offs, too, as appearing when improvement of one causes detriment to the other.

It hardly needs proofs that certain policies aimed at improving the world economic competitiveness of a country particularly by raising the quality level of manpower, increasing research and development capacity, and developing infrastructure as well, etc., are contributing also to the improvement of the market competitiveness of products, services, factors supplied by its enterprises. It is not less obvious that the more the competitiveness of those products and services produced by its enterprises improve, and the more the efficiency of these enterprises increase, the more its national economy can grow and its world economic competitiveness also improves.

However, the same time some counteracting effects, opposite to each other, and *trade-offs* must also be taken into account – not only between, on the one hand, those factors, conditions and changing circumstances shaping "world economic" and, on the other, those determining "world market" competitiveness, but also separately, in both cases. It is well-known (the political and ideological implications of which we shall return), that in order to improve "national competitiveness" and/or to reduce economic or financial disequilibria, particularly external indebtedness, a restrictive, "belt-tightening" policy may be necessary which often implies primarily measures to the detriment of social and welfare expenditures as well as the wage level. This, in turn, tends to worsen the conditions of human resources on which the social productivity level, i.e. the primary determinant of competitiveness, basically depends. Not a less well-known trade-off appears between the demand increasing measures aimed at stimulating economic growth and the restricting ones aimed at economic equilibrium or reduction of budget gaps.

Similarly, the application of economic policy measures aimed at attracting the investments of foreign firms, particularly TNCs, and thereby increasing the domestic production capacities, may have a contrary effect on the position of the domestic small and medium firms and may also worsen the central budget.

Although such and similar contradictions and trade-offs are numerous, indeed, and may be very intensive (forcing the government of quite many countries to face very serious economic policy dilemmas or even insolvable problems), they gain very little attention (if any) in the literature of "national competitiveness" and the international reports concerned.

The concept of *"world economic competitiveness"* – as already indicated – primarily refers to the position of a country in the world economy. In other words, it is a question on whether the country concerned belongs to those countries being in the developed centre of the world economy, or to its under-developed periphery (or, perhaps, stands in-between). This question, however, cannot merely be reduced to that about the level of development and even less the level of income. . Nor is it enough to question how successful the country concerned appears in international trade, because the very answer to the latter to a great extent depends on other than trade relations, particularly on international capital flows, and in view of the fact that the openness of a country vis-à-vis the world economy cannot be reduced to its "trade openness", which means that its role, activity and position in the world economy exceeds those in trade.

The world economic position of countries can only be evaluated in the context of all the main interdependencies which have developed in various spheres of international economic relations, i.e. as different variants, mostly with an asymmetrical pattern, of *interdependencies between unequal partners*. Thus, when investigating the "world economic competitiveness" of a country a primary attention should be paid to such, more or less *non-symmetrical interdependencies*, and the concomitant relative advantages or disadvantages of each of their variants, which depend on which side it is actually located in their structure, whether on the dominant, less vulnerable, more influential, initiating, and favourable side or on the subordinated, vulnerable, guided and unfavourable side.

In the contemporary world economy the *main variants of the non-symmetrical interdependencies* are manifested:

- in the unequal pattern of *international division of labour* and types of specialisation, i.e. in the disequalising distribution of the various roles in production and service activities, which partly appears
- in the biased commodity and geographical pattern of *international trade*, i.e. in the disproportionate export and import compositions and directions,
- in the asymmetrical pattern of international flows of investment capital and unequal distribution of stocks of foreign capital assets, resulting inequality in *international ownership and control relations*, which intensively shape trade patterns and affect other fields of international relations, too,
- in the unequal *international financial relations*, namely between creditors and debtors as well as those providing and those receiving international financial assistance, which stem from international flows of loans, bonds, various securities, speculative "hot money", etc. and from international financial assistance, appear in stock of net debt, and tend to result a growing, cumulative indebtedness of a number of countries, making them subject to the control or influence of the creditors and donors,
- in the hierarchic order of *international monetary relations*, appearing in a pyramidal structure of monetary system with large-scale differences in the international role, relative position, value, reserve base, and stability of national currencies, as well as their supply and demand conditions, and their relationship, exchange rate changes, etc., and involving a few leading and also reserve currencies on the top, many convertible but weaker currencies in the middle and numerous "soft", non-convertible or not fully convertible currencies on the bottom,
- in the asymmetrical pattern of *international flows, transfers of technology, intellectual property rights, soft-wares* and the concomitant technological

relations, namely between those developing, producing, selling or transferring modern technologies, and those receiving or buying and adopting only the technologies developed by others, which results from and also tends to reproduce the very unequal distribution of research and development capacities and technology production among countries, even if no country can do without imported technologies today,

- in the unequal direction and composition of *international migration of manpower* (however limited, often administratively restricted it is), which, besides a less significant two-ways flow, is mostly characterised by the regular outflow of unskilled or semi-skilled cheap labour from the less developed regions, seeking for employment in more developed countries, and by the immigration of the most qualified, highly educated manpower, particularly scholars, scientists and artists into the most developed countries, i.e. brain drain, which represents the greatest loss for the source countries and the greatest benefit for the recipients, and last but not least
- in the radial structure of *information flows*, namely from a few most developed countries producing, providing, selling, disseminating, spreading information towards those receiving or buying them, which cause great many disadvantages for the latter not only in cost and time but also in reliability and cultural effects.[33]

Unfortunately, the international literature on "national competitiveness" pays no, or (if at all) very little attention to the role and changes of the above mentioned asymmetrical interdependencies and their interrelations with the internal economic and social structure of countries. Even in the *World Economic Forum's* global competitiveness reports we can find only recently and still very sporadically some indicators related to one or another manifestation of them, with mostly one-sided interpretation. (Such as concerning FDI only in case of its inward flow as bringing about benefits for the recipient, but missing the case of outward FDI as a means to gain position in foreign economies, thereby improving "national competitiveness".)

The "main stream" of economics *ab ovo* refrains from investigating the ownership relations and neglects the effects of international capital flows, particularly FDIs and creditor-debtor relations on the economic structures and distribution of roles in international division of labour. It simply explains not only capital flows but also labour flows by differences in relative factor endowments and the resulting differences in marginal productivities and factor incomes. As regards international labour flows it does not pay sufficient attention to the selective immigration policies of governments, and more or less misses to investigate the effects of brain drain[34] on the international distribution of intellectual capital and the R & D capacities, i.e. on the most decisive determinant of national development and competi-

33 For a detailed investigation of the asymmetrical interdependencies in the world economy and how to evaluate them see *Szentes, T.* (1995), (2003), (2011).

34 It must be noted that in the latest reports of *WEF* we can find at least indicators on brain drain, too, which implies the acknowledgement of the fact that the competitiveness of certain countries depends also on external, international factors.

tiveness Although in regard to "market imperfections" it also stresses (like the neo-institutional theory) the problem of unequal information received by actors of the market, the effect of the same problem internationally is hardly taken into account by it when "national competitiveness" is dealt with.

As a consequence, in the related literature, including even the reports of WEF, those *demonstration effects* manifested in consumption pattern and life-style which (and also those diffusing them) bear responsibility for the heavy and often cumulative indebtedness of masses of consumers and numerous States, are hardly mentioned, in spite of many writings on them, particularly in the publications of the *Latin-American school of dependency*. Moreover, the higher level of the propensity to consume of the population is mostly taken only as an incentive for economic growth and technological development[35], without pointing to its unfavourable effects, particularly in case of luxurious expenditures, on economic equilibrium and the natural environment.

Although in the economy the term competitiveness is of market origin, the analysis of the above outlined asymmetrical interdependencies is badly needed as an indispensable method for evaluating the "world economic competitiveness" of countries. However, in view of their effects on the positions in the various markets and the advantages or disadvantages there, such an analysis is also useful in the investigation of the "world market competitiveness".

There is *another aspect* of world economic competitiveness as well as national development in general, which is not less important but often also neglected, namely that concerning *internal integration of the economy and social cohesion* of the countries concerned. It is about the degree of integration or disintegration in the economic and social structure within countries, i.e. to what extent the various parts, sectors and actors of the economy are interlinked or isolated as enclaves, and to what extent cohesion or segregation prevails among social classes and strata. This issue is closely interrelated with that of the external factors, particularly the above-mentioned interdependencies in the world economy.

The *internal integration of the economy* is determined by the development, extension and deepening of *input-output linkages* among the actors. It is not only the size of the domestic market and its growth but also the market's structure and quality that depend on these (forward and backward) linkages, and the spread in the national economy of research results, technological innovations, skills and experiences, too. They play an important role in broadening employment facilities and should be taken into account in the selection of dynamic, "pulling" industries as well as in the evaluation of the overall effects of FDIs and TNCs' activities.

The *integration* or disintegration *of society* depends on the size and decrease of inequalities between social strata, in terms of income gap, wealth distribution, life style and unequal opportunities, as well as on the self-organisation of the civil society and its spirit of solidarity and cooperation. The decrease in social inequalities

35 In the latest report of *WEF* (2011) we can read: "For cultural or historical reasons, customers may be more demanding in some countries than in others. This can create an important competitive advantage, as it forces companies to be more innovative and customer oriented and thus imposes the discipline necessary for efficiency to be achieved in the market." (p. 7.)

has become not only an accepted criterion of national development and its sustainability, but it is an obvious precondition to avoid marginalisation, segregation, xenophobia versus immigrants, racism and the separation of a narrow elite from the masses. All these require, of course, *democracy* which in real terms can hardly unfold without the appropriate strength and activity of the *civil society* controlling both the State and the market.

The internal integration both in economic and social (including cultural) sense presupposes the development of adequate channels and infrastructure of communication and information services and their efficient operation.

A disintegrated economy with a "dual" structure, and a society split into two parts alienated from each other, obviously hinder and distort the process of development and also reinforce the unfavourable effects of external factors, the asymmetry of interdependencies, which also contribute to disintegration.

In order to promote development and improve competitiveness of a less developed country and its position in the world economy, a purposeful national policy is required which aims at making less asymmetrical the existing interdependencies with other (more developed) countries along with efforts to reduce or avoid disintegration within economy and society.

In the light of the interrelationship between asymmetrical international interdependencies and internal socio-economic disintegration[36] a special attention should be paid to the *interactions*, in general, *between the external and internal determinants* of both national development and competitiveness in the contemporary world. Unfortunately, such interactions are rather neglected in the literature and reports on national competitiveness.

Not less neglected in the literature on national competitiveness is the issue of how the very *nature of the leading sectors* or branches of economy, and the *"physical" character of their products and services* affect the development potential and competitiveness of countries This is so despite the fact that the more or less favourable position of a country in the international division of labour and even the direction and tempo of its economic development as well as the integrating or disintegrating character of the latter, heavily depend on *which* sectors, or branches, industries, activities function as the leading ones. The various economic branches, industries and economic activities may – even apart from prices of their products and relative price changes, moreover, from whether they provide "comparative advantages" of old type – have and generate quite *different effects on the development and competitiveness of a country* as according to how much, to what extent they stimulate and/or necessitate, require and presuppose

(a) the development of human and especially intellectual capital, the improvement of labour quality, an increasing level of education, progress in science, the growth and appropriate use of R&D capacities and as a result of the latter

(b) technological progress, technical innovations,

(c) the unfolding, proliferating and thickening of input-output linkages which tend to integrate the national economy, broaden its market and facilitate the spread

36 For more detailed explanation see *Szentes, T.* (1971), (2003), (2011).

of research results, innovations, new technologies and improved labour cultures within it,

(d) the development of infrastructure, its extension and improvement, which is so important for the input-output linkages and for social cooperation.

Over and beyond the above, differences appear and are to be taken into account also in respect of how and to what extent they can provide

(e) such newer variant of comparative or created competitive advantages as the economies of scale, product differentiation and economies of scope.

What follows from all the above (mostly neglected) points on the importance of reducing the asymmetry in external interdependencies and prevent or decrease internal socio-economic disintegration and also selecting and promoting the appropriate dynamic sectors of the national economy, is the great *responsibility of the State* for the promotion of development of the country and improvement of its position in the world economy.

4. THE ROLE OF THE STATE IN PROMOTING DEVELOPMENT AND IMPROVING COMPETITIVENESS

The historical experiences clearly show that the State has always played an important role in the course of development of (independent) countries in various ways. In view of the interactions of "internal" and "external" factors determining development in the context of the contemporary world economy, and taking into account particularly the increasing importance of the created competitive advantages and improved competitiveness, the *role of the State* in economic affairs has not been fading away or even reduced, but rather changing only. While globalisation, regional integration and TNCs' activities undoubtedly undermine the "national" framework of regulating economic activities, and make "national" or state sovereignty over the economy an anachronistic or illusory concept[37], the unfolding new conditions in the contemporary world economy, shaped by revolutionary progress in communication and information technologies, by enhanced flexibility and responsiveness of the business strategy of TNCs, and also by changes in international power relations, call, paradoxically, for *a more, not less active role* of the local forces, social actors and institutions, including particularly the governments.

The old controversy of liberalism versus "dirigisme" has lost its relevance, and the real issue concerns the direction, the selected spheres and the ways and means of the government's actions in the economy, rather than its dimension and enforcing capacity.

Since national development is a multidimensional process that involves not only the development of the economy implying, over and beyond a quantitative growth, *structural and institutional changes*, but also *social, cultural and political*

37 *J. H. Dunning* emphasises (1993): "Unless a country is completely isolated from the rest of the world, any sovereignty it enjoys is bound to be constrained, in the sense that whatever decisions it chooses to take are, to some extent, influenced by forces beyond its jurisdiction." (p. 529.)

development of the nation, the need for the activity of the State and its responsibility appear in great many spheres.

It is almost a commonplace that the market – even an assumed "perfect" one with equal partners, who are equally well-informed and independent of each other as atomistic units, among whom none can possess concentrated economic power – is unable to ensure a just or even a socially acceptable distribution of incomes and an equal chances, equal development opportunities to all members of society. What follows from this recognition is that the State must take care of those lagging behind and/or doomed to poverty not because of their own mistake, and also all those incapable of work. (It can, of course, implement this task either directly by making use of its own financial resources, or indirectly, by mobilising private resources for the same purpose through incentives and allowances, or rather combining both methods.)

Anyway, it is not the task of the market to ensure social equality or justice. Its spontaneous mechanism has *ab ovo* differentiating, moreover polarising effects, which tend to lead to formation of concentrated economic powers, i.e. "market imperfections". It is the task of the State to restrict such tendencies (by means of law, regulating competition, by anti-trust acts, etc.).

Over and beyond such more or less traditional functions of the State as related to defence, security, diplomacy, political and legal actions, cultural, public health, social and environment protecting tasks, and establishment of appropriate institutional framework for economic activities and local enterprises, etc. certain *new* tasks and responsibilities have emerged under the contemporary conditions of accelerating globalisation and regional integration, and also under the growing pressure of the civil society. They include

- development of R&D capacities,
- reduction of social inequalities,
- prevention or correction of the disintegrating effects of globalisation and regionalisation in the economy and society,
- management of interest conciliating and coordinating mechanism with employers' and employees' representatives,
- development of environment-conscious culture in society,
- promotion of social cohesion, cooperation and solidarity, and prevention of alienation, segregation and marginalisation, xenophobia and racism, ethnical, religious and other conflicts.

These tasks, however general, are also important for "national competitiveness". There are, of course, many others that are more directly related to it.

Market spontaneity can never ensure more symmetrical international interdependencies and successful catching up of a less developed country with the more advanced countries, nor the required integration of the economy. This fact also calls for *purposeful actions* of the State in both aspects. In addition, as the investments of TNCs or even the national firms are usually oriented by considerations other than those of the future development of the national economy as a whole, a certain *regulatory role* of the State is of an utmost necessity.

Accordingly, at least three different, but also interlinked, aspects or spheres of the role of the State in the process of development can be distinguished:

(1) initiating and promoting such *structural changes in the economy and institutional reforms* as needed for development and improved competitiveness, and taking care of *public health, education, cultural life, social security as well as political freedom;*
(2) *creating* directly and indirectly *"competitive advantages",* thereby improving the export competitiveness of its products and services, attracting FDIs, and providing "home base" for TNCs of foreign and local origin;
(3) *regulating* as much as possible, and by means of market-conform methods and legal acts, the *economic activities* within the country, encouraging savings and investments, influencing by various incentives and legally prescribed rules the investment orientation in accordance with a national development strategy, promoting the generation of input-output linkages within the national economy, and also correcting or compensating, by social policy, those socially undesired effects following from the operation of the market.

As regards (1) the tasks of the government in promoting the rise and operation of a system of institutions appropriate for the economy, and also facilitating such structural changes in the latter as marking an up-grading in development process as well as shifts in favour of a specialisation which promises dynamic comparative advantages, they are not opposed even by those liberal scholars believing in the harmonious operation of the market. The same applies even more to the tasks of the government in the field of public health, education, and social security, not to mention other traditional responsibilities of the governments. (Even such a "father" of liberalism as Adam Smith, who praised the "invisible hand" of the market, explicitly emphasised these responsibilities of the State.)

The role of the State in regard (2) to the *creation of "competitive advantages"* seems, in a sense, rather new. At least insofar as it goes further than undertaking by the government of such investments as yielding return, if at all, only in the long run and thus not considered profitable for private entrepreneurs, as, for example, investments in the material and social infrastructure, in general.

The latter have always been viewed, even by liberals, as parts of the necessary activity and responsibility of the State, which has to ensure some basic and favourable conditions for private business not only by establishing an appropriate legal and institutional order, but also by supplying the required public goods, by developing the system of transport, communication, information, energy and water supply, education and public health. While the supply of many of such public goods and, particularly, investments in communication and information have increasingly been privatised in many countries, a purposeful creation of competitive advantages for *attracting FDIs* and preparing a *"home base" for TNCs*, remains primarily a task of the government.

The so-called "national competitiveness" applies, as already noted, not only "world market competitiveness", i. e. export competitiveness of the products and services supplied by the firms located in the country concerned, and the ability of the latter to successfully compete with firms of other countries, but also and primarily the "world economic competitiveness" including the capability of the country to attract the direct investments of TNCs and become the "home base" of such and/or locally arising companies. Consequently, the State bears responsibility for *creating*, directly and indirectly, *competitive advantages*.

In view of the main determinants of national development and competitiveness, the improvement of which also requires making the national economy attractive for TNCs' investments and activities, the task of the government involves:

(a) the promotion of the development of *"human capital"* in general, and *"intellectual capital"* in particular, i.e. making and financially supporting investments in education and training for improving the quality of labour (also in terms of computer literacy), and in R&D capacities for up-grading national development resources, including the establishment of "science parks" in the country, which collect researchers and facilitate practice-oriented research by especially favourable conditions, by co-operation among researchers, and by an easier access to the users of research results;

(b) the support to be given by concessional loans, tax incentives, financial guarantees, etc. to the *inventions in technologies and innovations* made by local firms or citizens, and also to the introduction of technological research results into practice;

(c) the encouragement, by WTO-conform methods, of the development of *input-output linkages* between the TNC affiliates and other local firms[38], including measures of assistance to the latter for improving their supplier capabilities, output quality and marketing facilities, and also the organisation of "industrial parks" with the required infrastructure and "clusters" of interrelated economic activities;

(d) the development of *infrastructure*, particularly in the spheres of modern communication and information, including the extension of training facilities in computer use and telecommunication methods;

(e) the implementation of an *economic policy* that meets the requirement of reliability, transparency and credibility, and involves purposeful efforts *to reduce the "economic distance"* (in terms of the rules, principles, regulations and mechanisms of the economy) between the country and the home countries of the investing foreign companies;

(f) the development, by appropriate *cultural and educational policies*, of a modern social attitude (free from prejudices), responsiveness (to new ideas), a communicative, responsible, risk-taking and co-operative spirit, which all can *reduce the "cultural distance"* between the country and the most advanced ones (even if the latter have not, in fact, fully developed yet such characteristics in their entire society).

It is to be added, that *reliability* (creditworthiness), *transparency* and an approximate *predictability* of the government policy as well as stability in the institutionalised rules and mechanism of the economy are also extremely important for attracting foreign investors and, of course, for all the actors, too, in the economy.

38 "To benefit fully from export-oriented FDI, facilitate an upgrading of export-oriented activities and make them sustainable, host countries need to encourage linkages between foreign affiliates and local suppliers." But "...linkage promotion strategies also have to adapt to the changing nature of corporate strategies." – *UNCTAD* (2002), p. xxix.

Contrary to usual assumptions, such *incentives*[39] *as tax allowances or other privileges* are not the only and always necessary, moreover, by no means the best methods of attracting foreign firms or helping national entrepreneurs in a longer run. Even worse is a policy that tries to ensure an attractive investment climate by keeping the level of wages down. The latter completely neglects that wages are components not only (and often not at all decisively) of costs but also of effective demand, and that it is by no means the "absolute" cheapness of labour but the international wage difference in relative sense only (i.e. as compared to a smaller difference in labour productivities) which may represent a local advantage in respect of labour for the transnational investors.

The role of the State as (3) a *regulator* in the economy extends to great many tasks, such as particularly

(a) to interventions for protecting the economy and the national currency against external shocks, which more frequently take place recently,

(b) to anti-cyclical policies in general, and to measures aimed at preventing or overcoming crises,

(c) to fiscal and monetary policies aimed at increasing employment, encouraging savings and investments,

(d) to corrections of the socially polarising effects of the market, by appropriate tax and social policies,

(e) to protect natural environment in the country and provide assistance in case of natural catastrophes.

Although the power relations between huge TNCs and a small national economy can be extremely unequal, and their interdependence is markedly asymmetrical, the State in the host country can, nevertheless, do a lot, owing to its legal power and to the competition among TNCs, for ensuring as much benefits at as little costs, as possible from the TNCs' activities in the process of national development.[40] Since a participation in their worldwide network is definitely better than remaining outside of it, while the actual position gained in it does matter a lot for the type, direction and tempo of national development and competitiveness, the elaboration, by making use of experts, of a longer-term *development strategy* also appears among the tasks of the government.

The international competitiveness of enterprises of a country, thus its "world market competitiveness" as well, can be improved even by a non-democratic, moreover a dictatorial State (although it is doubtful whether in a sustainable way). However, its development in a real sense, i.e. extending to the entire society, and in a sustainable way, as well as its "world economic competitiveness" resulting in better position in the world economy require as prerequisites:

- *democracy* but not only in a formal sense,

39 The *World Investment Report 1996* also stresses that "...incentives do not rank high among the determinants of FDI" and that "...incentives can be a waste of resources... and, when they are successful, can be distortional." – *UNCTAD* (2002), p. 181.

40 "Much depends on the strategies pursued by TNCs, on the one hand, and the corresponding host-country capabilities and policies, on the other." – *UNCTAD* (2002), p. xxiii.

- permanent *cooperation between the government, the employers' and employees' organisations*, their interest conciliation, and
- the *control of the civil society* over government actions.

All these are needed in view of the fact that not only “market imperfections” exist but so-called “government imperfections”, too.

As an excessive role both of the market and the State is equally harmful and dangerous for the society, the solution, preventing the dominance of both, requires such a combination of their role as meeting their original functions as well as the new conditions. It also requires that the upper hand and controlling role should belong to the civil society which needs both the market in order to avoid its subordination to a dictatorial State, and also the State in order to be saved by the latter versus the polarising effects of the market.[41]

■ ■ ■

All what has been stated about “national competitiveness” and the two variants distinguished in the above, clearly point to the *very complex, multidimensional nature* of this subject, involving great many factors and conditions behind each of its elements. In addition, since the world economic competitiveness of a country is not independent of that of other countries, it can be interpreted in a *relative* sense only, which means that it may improve or worsen due to causes other than sufficient or insufficient efforts of its own, namely because of changes in opposite direction, of the competitors, or simply due to the shift of the gravitation centre of the world economy.

5. MEASUREMENT OF “NATIONAL COMPETITIVENESS” BY COMPOSITE INDEXES

Whenever and wherever competition exists, its participants wish to know which their actual place is in the ranking list. Moreover, even without competition, whenever and wherever performances are compared, there is a need for measuring them, and so is a demand for determining thereby their grading. Problems, quite serious ones, however, arise when competition simultaneously involves actions of heterogeneous nature, of unequal difficulty in different fields, and/or performances are of multiple character, consisting of manifold activities.

The endeavours and efforts manifested in the international literature to give “national competitiveness” such an interpretation as making possible to measure it, are quite natural and understandable. However, even if they result in a certain enrichment of information and knowledge, it is very questionable to what extent they can really succeed. Serious, well-founded doubts can be raised, indeed, in regard to the very measurability of such a compound, complicated and changing phenomenon by means of any composite index.

41 The idea of a strong civil society, which is not subordinated to but equally controlling both the market and the State was presented in a very illuminating way by *Marc Nerfin* (1987).

In the related international literature[42] and reports we can find a great number and variety of indexes applied to measure and compare "national competitiveness" of countries, some of them originate from development economics, while others refer to the efficiency of enterprises and those circumstances influencing the latter.

In the early period of what had been named (in a misleading way) "development economics" a single index, namely the per capita GDP or GNP was used to measure the level of development of the countries, and their ranking list was constructed accordingly. However, it has become obvious for a long time (and not only recently when this issue came up again) that development, particularly in a sustainable sense, can by no means be oversimplified to economic growth and the measurement of its level reduced to one index only. Consequently, in the evaluation of the development level of countries and its changes, as compared to others, and in their ranking list as well, *several other indexes* are also applied, such as *related to non-economic aspects* (level of education, culture, public health, social inequalities, security, environment protection, etc.) While the per capita GDP and its growth rate are still the main indexes in the reports of international institutions (UNCTAD, World Bank, etc.) surveying the countries' development performances, the Human Development Index as a composite one (including, besides the former, also cultural and health indexes) has gained also an important role in them. Moreover, a new, corrected variant of national income calculus has also appeared which takes the degree of exhaustion of natural resources into account, and result in the so-called "adjusted net national income".

It is to be noted and appreciated that in the annual Global Competitiveness Reports of the *World Economic Forum* (WEF), too, certain non-economic factors and the related indexes have also gained increasing attention and role. (The same is true in the case of the reports of IMD, too.)

WEF produces the ranking list of countries on the basis of one or two aggregate composite indexes only (while IMD makes use of four[43]). In the earlier reports of WEF two were applied for a long time, namely the *"Growth Competitiveness Index"* and the *"Current Competitiveness Index",* which was renamed and called from 2003 as *"Microeconomic Competitiveness Index"* and later as *"Business Competitiveness Index".*

The *Growth Competitiveness Index* (GCI) was supposed to express those factors and circumstances that are shaping the medium and long-term growth of the economy. It was based on three sub-indexes characterising (a) the quality of the macro-economic environment of the countries (including indexes of macro-eco-

42 As regards the related Hungarian literature, a short (and critical) survey on the various concepts and measuring methods on "national competitiveness" can be read in *Szentes, T. et al.* (2005).

43 *IMD* in the measurement of national competitiveness applies four sets of characteristics, namely those on economic performance (including foreign trade, FDI, employment, etc.), government efficiency (institutions, economic policies, legal rules, etc.), business efficiency (productivity, management, financing, labour market, etc.) and infrastructure in broad sense (including public health, education, science, environment protection, etc.). On the basis of these composite characteristics it presents an "Overall Competitiveness Scoreboard".

nomic stability, budget expenditure ratio, credit-worthiness, etc.), (b) conditions of public institutions (including the legal and contract regulations, degree of corruption, etc.), and (c) the technological readiness (innovations, development of information and communication technologies, etc.)

The *Business Competitiveness Index* (BCI) (like its predecessors) was to show and evaluate the micro-economic conditions that determine a sustainable level of productivity. A former report of WEF (2004) pointed to that the macro-economic and institutional factors are necessary but not sufficient determinants of competitiveness, while it is the *enterprises* operating in each economy, that actually create wealth. (p. xiv.) In view of this, BCI evaluated two special fields of business environment: (a) the sophistication of enterprises' operation and strategy, and (b) the quality of micro-economic business environment – in regard to three groups of countries categorised according to their income level.

These two composite indexes still more or less reflected in a way the distinction suggested by us (not only and not so much between development and competitiveness, in general, but particularly) between "world economic competitiveness" and "world market competitiveness" of countries. However, the 2004 report of WEF has introduced a new, single index called *"Global Competitiveness Index"* which merges in a multiple combination both the former GCI and BCI.

This new GCI by *intermixing* the content of world economic and world market competitiveness creates the impression, moreover *misbelieve* that whatever is favourable for the enterprises and improves their and also the country's market competitiveness, is necessarily favourable also for the country concerned as promoting its development and helping it to reach better position in the world economy. It is contrary to such experiences as pointing to cases when arrangements, economic policy measures that favoured the enterprises turned to be unfavourable for social development and world economic position. This new index is also mixing up the long-term determinants of the competitiveness of countries with those rather short- or medium-term factors determining that of the enterprises.

The new "global" competitiveness index is based upon three fundamentals, basic principles: (1) Productivity is complex: 12 pillars of competitiveness, (2) Stages of development, and (3) Transitions. These principles seem to reinforce the *confusion* between development and competitiveness.

The *first principle* specifies the *12 pillars* of competitiveness which are as follows: (1) Institutions, (2) Infrastructure, (3) Macroeconomic environment, (4) Health and primary education, (5) Higher education and training, (6) Goods market efficiency, (7) Labour market efficiency, (8) Financial market development, (9) Technological readiness, (10) Market size, (11) Business sophistication, (12) Innovation. Each pillar is assigned to one of the three sub-indexes, the first four of them into that called *"Basic requirements"*, the next five into the *"Efficiency Enhancers"*, and the remaining three into *"Innovation and Sophistication Factors"*.

The various indexes and sub-indexes belonging to the individual pillars seem to reflect, on the one hand, the still influential neo-liberal views and, on the other, the endeavour to overcome its oversimplifying economistic approach to reality. They also reflect the enterprise-oriented perception of national competitiveness, on the one hand, and its interpretation in the context of socio-economic development of countries, on the other. While economic openness, participation in international trade and capital flows are taken into account as favourable conditions for "national competitiveness", hardly any unfavourable effects of them are counted in spite of general notes on global crises and uncertainties in the world economy.

This "double face" can be illustrated by a few examples. In the 1st pillar e.g. "government regulation", in the 8th pillar the "extent of taxation", "agricultural policy costs", "prevalence of trade barriers", FDI regulations ("business impact of rules on FDI"), and in the 7th pillar "rigidity of employment" are qualified as unfavourable factors, while in the latter the "flexibility of wage determination" as a favourable one. On the other hand, the importance of such sources and determinants of development as education is represented by two pillars, namely the 4th and 5th, the conditions of public health makes half of the 4th, "female participation in labour force" as well as "cooperation in labour-employer relations" are qualified as favourable factors in the 7th pillar, while in the latter "brain drain" as unfavourable, and in the 11th "state of cluster development" and "value chain breadth" as reflecting issues of increasing importance are also taken into account

Although certain sub-indexes (very few and sporadic only) such as on "country credit rating" in the 3rd pillar, "prevalence of foreign ownership", and those related to trade in the 8th, the already mentioned "brain drain" in the 7th, "FDI and technology transfer" in the 9th, "foreign market size" in the 10th, "control of international distribution" in the 11th pillar, point to external factors and conditions, too, the competitiveness of countries is still basically and decisively interpreted as an internally determined phenomenon, and its changes is explained accordingly – contrary to globalisation and the effects of global crises which are emphasised in the same report.

The *second principle* is about the assumed universal and successive stages of development in one or another of which each country is classified on the basis of its per capita GDP level. Accordingly, in the 1st stage, which is called *"factor-driven",* economic development is basically promoted by primary factors, in the 2nd stage, called *"efficiency-driven",* it is promoted by increasing efficiency, and in the 3rd stage, called *"innovation-driven",* by research and innovations. The authors of the report assume that for countries in different stage of development the various pillars and sub-pillars are not equally important, which makes necessary to take the related indexes or sub-indexes into account with different weights. It is also assumed, consequently, that the up-grading of countries, i.e. moving from a lower to a higher stage, implies the need for them to concentrate in their competitiveness-improving strategy on factors and conditions other than before. Thus, when a country intends to reach e.g. the third stage and the related level of per capita GDP, it must turn from a technology importing country into technology developing and exporting one in the process of the innovation-driven growth of its economy.

The *third principle* simply concerns those countries being in a "transition" between two of the stages of development mentioned above. In the case of the countries which are between the first and the second stage, the importance of "basic requirements" and the role of basic factors decrease and that of the efficiency enhancing factors increase, of course. Those countries placed between the second and the third stage need a shift in the structure of factors determining competitiveness in favour of innovations.

The second and third principles clearly manifest a new variant of the conventional theory of the stages of economic growth and the concept of a unilinear process of development. The authors of the report themselves refer to the theory of *W. W. Rostow* (1960). But even apart from the classification of countries on the basis of their per capita GDP, which has been criticised as insufficient and not always reliable index, for a long time in development studies, and also from the wide criticism of Rostow's and others' stage theory, the distinction of the three stages makes sense only in a very relative sense, namely regarding proportions only. The basic factors of production hardly loose their importance in the 2nd and 3rd stages, as the role of human labour (its highly educated and qualified variant) is the most substantial determinant of both efficiency and innovations, while innovations (even if primitive ones) had always played an important role in progress, already in the earliest historical stages of human societies.

However numerous[44], important and relevant are the data collected by and with the assistance of the partner institutions in almost two hundred countries and from international organisations; however appealing is the classification of countries on the basis of numerical values and according to distinguished stages of development; however sophisticated, regularly controlled and completed is the mathematical apparatus[45] which is used in the construction of composite indexes and in computation of countries' scores and rank; and however useful the information provided thereby to governments all over the world[46], the *major shortcomings* of the reports can hardly be disregarded. Such as the following:

- *Most of the data* received are *"soft"* in the sense that they originate from completed questionnaires and personal interviews, in the case of which the answers, moreover some of the questions themselves *reflect subjective opinion*[47] or prejudicial expectation.
- Although the so-called *"hard" data* are collected from official institutions of the countries concerned (such as their statistical bureaus) and international organisations, in some cases and respects their *reliability or appropriateness*[48] *can be questioned*.

44 For the latest report of WEF (2011) approximately 20 thousand data were processed.

45 In the calculus of countries' scores not only full- and half-weight variables, weighted averages, log-transformation and min-max transformation methods are used, but in case of extreme outliers beyond the sample minimum or maximum, adjustments are applied, and when the variables included in the components indicate distortions in their weighted average, corrections are made in a way. It is also to be mentioned that in view of the robustness analysis on GCI, made in 2009, according to the methods of the European Commission Joint Research Centre, certain modifications were introduced.

46 In the editorial Preface of WEF's latest report it is emphasised that the "Report ... offers policymakers and business leaders an important tool in the formulation of improved economic policies and institutional reforms."

47 In the latest WEF's report out of the already mentioned 20 thousand data cca. 12 thousand came from questionnaires or interviews.

48 It is enough to point to the well-known problems, particularly in less developed countries, of calculating the gross domestic product and its PPP variant, moreover in some cases even the number of population. As regards the doubts about appropriate use of data, an example is the way how "domestic competition" is calculated in WEF's report, namely as a sum of consumption, investment, government spending and exports.

- The *12 pillars* of competitiveness and their components are defined in a rather *arbitrary* way, some of which are overlapping or heterogeneous, and the *choice of weights* applied in different sub-indexes and in different stages seems also arbitrary.
- The same is true regarding the *second and third principles*, which reflect, as already noted, the unhistorical concept of unilinear process of development and the widely criticised Rostowian "stage"-theory.
- Despite the great number of data and variables expressed in sub-indexes, there are only *very few* among them which are related to *external, international determinants* of competitiveness, and even such sporadic variables are mostly evaluated one-sidedly contrary to their double-face.
- The reports completely *miss* any information and evaluation on *the global context of "national competitiveness",* i.e. on such important issues as
  - interdependencies between unequal partners and the concomitant unequal
  - differences in the position of countries within global networks of TNCs,
  - role of the demonstration effects of conspicuous consumption radiating from the wealthiest countries, in the indebtedness and budget deficits of many countries,
  - differences in development opportunities resulting from the type of specialisation and the shifts in the pattern of international trade as well as in the gravitation centre of the world economy, etc.
- In the reports such an important domestic aspect is also neglected as the different effects of the type of specialisation and leading industry on the internal socio-economic integration or disintegration of countries. And so on.

What follows from all the above is that the prevailing practice of measuring the competitiveness of countries in the reports discussed above, is criticisable in several respects. Consequently very *well-founded doubts* can be raised regarding the *ranking list* of countries – not only concerning the actual level, tempo and direction of their development, but even their market competitiveness in a narrow sense.

The expression of the level of "national competitiveness" of countries and their ranking accordingly by *one single composite index*, such as GCI, is itself an extreme over-simplification, even if its components are clearly defined and ranking lists are presented also in view of them separately. Since countries may compete in many fields, even in regard to the economy, their competitiveness cannot be measured by one or two indicators only, just like the competitiveness in sport can by nom means be determined in general, without specifying in which type of sport it is to be measured, since different sports have obviously different criteria and requirements for competitiveness.

6. THE IDEOLOGY OF "NATIONAL COMPETITIVENESS"

Although the age of imperialism with the big rush for colonial territories had passed long time ago, and Marxist-Leninist ideology about the "historical competition between the system of capitalism and that of existing socialism" has been discredited by the collapse of the Soviet empire, strangely and paradoxically enough the *competition* of countries and country groups aiming *to win at the expense of each other* has been reborn in new form, and the related concept of their *competitiveness* to be compared became a fashionable, widely accepted idea both in politics and economics. It is a paradox not only in the light of the original meaning of "con-petere" (as noted before), but also and particularly in view of the increasingly urgent need for co-operation in order to overcome the more and more frequent crises in the world economy, to force terrorism back, to prevent the drastic deterioration of natural environment and ecological catastrophe, and to save humanity from the ever growing dangers.

The concept of "national competitiveness", as we already noted, definitely bears the mark of a *market- and enterprise-oriented viewpoint* of competition which implies such a rivalry of enterprises is manifested in the *struggle for bigger share in the market.*[49] While development in order to improve living conditions and well-being is a rather general aim of human societies all over the world, and comparisons of their progress and achieved level are naturally motivated by intentions to learn from each other, the economic competition of countries and their aim to improve their competitiveness appear as an explicit or implicit intention *to triumph over others or to avoid defeat*. This is why reports on the competitiveness of countries, which present the ranking lists, became (at least for the political leaders) almost as important as war bulletins. (What matters for ordinary people, indeed, is the actual conditions and quality of life rather than the rank of their country in terms of competitiveness.)

Nevertheless, nobody can doubt that the reports of WEF and other institutions (such as IMD) on the competitiveness and ranks of countries are very instructive, rich in useful information. By presenting a sort of check-list they may induce or stimulate governments to act accordingly and implement necessary reforms.

In the case of Hungary the latest report of *WEF* (2011) called very realistically attention to such primary shortcomings from the point of view of business competitiveness as the level of tax rates, frequent changes in tax regulations, insufficient financial resources, corruption and uncertainties in economic policy.

In the same report of WEF (2011) we can read: "The clear and intuitive structure of the GCI framework is useful for prioritizing policy reforms because it allows each country to identify strengths and weaknesses of its national competitiveness environment and pinpoint those factors most constraining its economic development. (p. 44)

Nor can it be doubted that the introduction of newer and newer variables, the completion of earlier indexes by new indexes or sub-indexes (particularly those reflecting an increased attention to *sustainability* of development and competitiveness,

49 *James R. Martin* (2007) correctly points: "Part of the controversy related to the competitiveness reports is the term 'competitiveness' .As many economists have pointed out, countries do not compete the way companies compete." (7)

its both ecological and social conditions[50)] improve the content and scope of applicability of such reports.

The competitiveness reports, however, can be subject of well-founded critique not only for the ambiguous interpretation of "national competitiveness" (i. e. its confusion, we have already noted, with development and enterprises' competitiveness) and also for the method of measuring it (as discussed in the previous subchapter), but mainly because a *neo-liberal approach* still predominates in them, and the resulting over-simplifications provide a favourable soil and wide opportunities for *political manipulations*. It is perhaps not an over-exaggeration to say that they implicitly (willy-nilly) embrace and represent an *ideology* which corresponds to the neo-liberal "counter-revolution" in development studies.

As already pointed out, certain basic principles of the construction of Global Competitiveness Index imply a return to the conventional conception of the unilinear process of development with the same successive stages. This conception explained both the higher level of development of some countries and the underdevelopment of many others simply by their internal endowments, capabilities, and policies – "in such a way as to take the intellectual question out of its historical context"[51] and completely neglecting the role of external forces, international effects. Thereby it presented an apology for colonialism in the past and unequal international relations at the present time..

As a matter of fact, the reports of WEF seem to go even further than the conventional "stage"-theory in the sense, that they do not only place all the responsibility on the individual countries themselves (surprisingly enough: in the era of accelerating globalisation, transnational activities and worldwide information services), but encourage, moreover, almost compel intellectually and politically the governments to accept the *neo-liberal principles of economic policy*.

Jeffrey D. Sachs, one of the first contributors to WEF's earlier reports stated: "The single *economic* policy variable that best distinguishes rich from poor countries is *economic* openness. Poor countries have higher tariffs than richer ones... Poor countries report higher hidden import barriers. Poorer countries report more difficulties in getting foreign exchange for importing...." – Quoted by *Ronald W. Schuelke* (2000), p. 1.

Although the latest report of WEF points to the "uncertainty in the global economy", and also states among others that "the recent economic crisis has highlighted the degree if interdependence of economies worldwide". However, the evaluation of, and the explanation of changes in the competitiveness of countries still reflect the above mentioned conventional approach and neo-liberal views of the "mainstream" economics, which has been heavily criticised even by very moderate and objective scholars.[52]

50 See Chapter 1.2 of WEF's report (2011) which outlines a long-term view on "sustainable competitiveness" and presents the framework of the *"Sustainable Competitiveness Index"*

51 Quotation from *Leibenstein, H.* (1957), p. 3.

52 Just to mention three distinguished scholars' view, see the writings of *Stiglitz, J. E.* (1989), (2010), *Krugman, R. P.* (2009), and also of a Hungarian one, *Csaba L.* (2009a), (2009b).

Most of those *data* received from questionnaires or interviews reflect not only subjective but – due to the formulation of questions and expected answers – often *ideological* assumptions and *prejudices*, too. The viewpoints of their evaluation mostly express the neo-liberal conception (which is quite different from the original idea of liberalism[53]) on the role of the State which is to be restricted to serve the interests of capitalist enterprises by ensuring defence, security and order, protecting private properties and undertaking uneconomic investments in infrastructure, public health and education, etc., i.e. to create and maintain favourable conditions for their successful operation both within and outside the national economy. Government interventions in the economy are basically qualified as unfavourable, worsening the competitiveness of the country, too, and accordingly taxation, agricultural policy, customs procedures etc. represent "business burdens".

While among the criteria of "national competitiveness" there are also a few which are about other aspects, such as social cohesion and environment protection, the evaluations in the reports neglect rather than reveal the very contradictions and trade-off between market spontaneity and social cohesion, the profit interests of companies and environment protection, etc. and, in general, the idealised principles (involved in the former "Washington consensus") of privatisation, liberalisation and deregulation, on the one hand, and national development in a real sense of the word, on the other. No attention is paid to the harmful effects, as experienced in quite many cases, of the "structural adjustment" programs (prescribed particularly by IMF) and the concomitant *restrictive measures* involving drastic reduction of budget expenditures, etc. on social cohesion and development. Nor is it paid to the consequences of the *demonstration effects* of conspicuous consumption which is stimulated also by commercial propaganda and advertisements in TV, and the related *irresponsible credit policy* of commercial banks on indebtedness, "bubbles" in financial markets and mortgage crises, thereby deteriorating the competitiveness of many countries.

The *measurement of "national competitiveness" by a single composite index* such as GCI, and the ranking of countries accordingly, represent a method which, however sophisticated mathematical apparatus is involved, cannot be taken seriously. It may be compared to such an obviously ridiculous, fortunately non-existing experiment in medical science as (let's assume) the ranking of the patients in the list of healthiness or living potential on the basis of a single index composed by all laboratory findings, roentgen pictures, MR and CT diagnoses, blood pressure, Spiro-scope result, age, weight and height, etc.

One could raise the question: How and why can such a method be considered as well-founded, indeed, and gain even scientific acknowledgement, instead of taken at best as serving a rough approximation only with more or less reliable and partly relevant information?! A few decades ago a similar question could have been raised (and de facto had been posed by some scholars) in regard to the that time famous concept of "vicious circle" of underdevelopment and poverty which was

53 On this difference see *Szentes, T.* (2009), pp. 106-110.

expressed in short by *Ragnar Nurske* (1958) as follows: "A country is poor because it is poor" (p.256). The non-sense involved in this old concept was not less obvious than in the case of the single GCI index measuring numerous different qualities, criteria and conditions of "national competitiveness". Neither the former, nor the latter can appear in medical science. (We may imagine what a patient would say if the doctor summarised the diagnosis by stating: You are sick because you are sick.".)

In social sciences, however, such non-senses may sometimes gain ground because and insofar they express ideological views and serve political and/or economic interests.

This is one of the reasons why a "New Enlightenment" should come which, besides other effects, would "free all social science theories from ideological (mis)interpretation, from their apologetic misuse and manipulative distortion for legitimising political interests and practices, and put an end to the 'religious' belief in any of them as a single 'vehicle of Truth'".– *Szentes, T.* (2003), p. 385.

As a result of the great and worldwide effects of WEF's reports, the improvement of "national competitiveness" in accordance with the views still prevailing in them has become a *general requirement* so much that even those governments trying to preserve what remained (mostly in ruins only) of the "social market economy" and welfare State, can hardly escape from the related recipe of economic policy. An appropriate *obedience* is expected and experienced even more from the governments of countries in "transition" from the communist system of the "centrally planned economy" (in fact: war economy) to market economy. Moreover, the European Union which according to the original ideas was established to promote the economic integration of countries along with increasing social cohesion and welfare, nowadays also seems to give the improvement of competitiveness priority at the expense of the former.

The appropriate interpretation of national development as a complex, multidimensional and democratic process which has to embrace the entire society and all of its spheres is increasingly replaced by its old conventional perception again – quite anachronistically – which reduces it to economic growth only, and by the confusing and mostly business-oriented concept of "national competitiveness".

The concept of "national competitiveness" and the method of measuring it have become – independently of the intention and goodwill of those scholars having elaborated the WEF's reports and ranking lists – *ideological instruments* which for the time being have proved very efficient against the views arguing for the diminution of social and international inequalities and the development, both on national and global level, of an "oeco-social market economy". By alleging the necessity to improve competitiveness as a reason governments (not only those led by conservative, nationalist or liberal political parties but also those calling themselves socialist or popular) may feel themselves authorised to implement *restrictive anti-social measures* and forget their welfare tasks. As more and more governments act accordingly (whether of their free will or being compelled), social unrest, demonstrations, strikes, revolts are the consequences. While in the process of collecting information for the reports most of the data are based upon the opinion of enterprise leaders concerning business conditions, no information coming from public opinion poll or research is conducted on the *views of the masses* about their life conditions is used. The quality of life hardly matters, anyway, in the evaluation of “national competitiveness”.

Although the authors of WEF's report cannot be accused for it, but the basically enterprise-oriented interpretation of “national competitiveness” suits fairly well the interests of the giant transnational companies and commercial banks as well as those benefiting from speculation in money markets. This observation does not question the importance of the competitiveness of enterprises, nor that of the need for all countries to cooperate with TNCs and attract FDIs.

In order to avoid misunderstanding, the sharp criticism of the reports on “national competitiveness” does not mean at all an underestimation of the usefulness of information from the enormous data involved, and the hard work of experts elaborating them, nor, particularly in the case of the more recent reports of WEF, the observable intention of the editors and main contributors to apply a less biased and somehow more realistic approach. However, the ideological message, the *misleading interpretation of national development* as confused with market competitiveness, the presented *guidance for politics*, and last but not least the implicit acceptance of the prevailing but obviously unsustainable pattern of development of the economically successful countries as models to be followed by others, must be rejected.

It is, indeed, high time to recognise that for the survival of humanity

- all nations and countries having a common destiny and depending on each other must cooperate, i.e. in accordance with the original meaning of “con-petere”,
- they must seek for solutions together on the global problems, consequently
- they should not continue the practice manifested in the intentions to gain at the expense of others which is practically a “negative-sum-game”, and cannot continue it anyway for long without catastrophic consequences,
- thus, the only promising option for the future of humanity is a substantial change in the pattern and direction of development, which breaks with the dominance of market forces and the market-type attitude of nations and their members vis-à-vis each other as well as the Nature, and by promoting mutual respect, understanding, solidarity and cooperation may ensure a real opportunity of sustainable development for all the people in the world, and enable each of them to contribute to and also benefit from a common welfare.

Our criticism concerning the concept of “national competitiveness” and the reports on that of countries was aimed *by no means* at questioning (what is so obvious, namely) that the development and welfare of society necessarily require economic growth coupled with a dynamic equilibrium, and so does the growth of the economy an efficient, profitable operation of its enterprises, for which favourable business environment is needed. What we intended to question and criticise is but the *order of priority* which seems to be turned upside down by the “official” or at least fashionable interpretation of “national competitiveness” and its measurement.

7. SUMMARY

Unlike the competitiveness of products and services in the market, and that of enterprises supplying them there, the concept is very important, indeed, for all the countries, which make efforts to achieve or sustain economic growth and a favourable position in the contemporary world economy, the concept of "national competitiveness" is ambiguous, moreover misleading. Its perception involves confusions not only based on a primarily and mostly economistic, market- and enterprise-oriented approach, and involves confusions not only between development and economic growth of countries but also between competitiveness of the latter and that of their enterprises. While nations or countries may compete in many specific fields and various ways, this concept is about economic competition only, and focuses on those circumstances within the countries' economy that matter for their enterprises' successful operation and competitiveness in the market.

In order to overcome the above mentioned confusions a distinction is suggested between

(a) the world economic competitiveness of countries as a broader concept implying their more or less successful endeavours to improve, by means of general development and socio-economic integration, their position in the asymmetrical pattern of interdependencies of world economy, and

(b) the world market competitiveness of countries, which refers to the share of their more or less competitive products, services and factors of production exported by their enterprises, and to those more or less favourable conditions influencing the operation and efficiency of the latter.

The reports on "national competitiveness", such as those annually published by the World Economic Forum, are based upon a very great and increasing number of data coming from institutions, researchers and firms all over the world, and providing *useful information*, indeed, on the performances and conditions of countries. The elaboration of the reports, i.e. the processing and converting the numerous data into numerical indicators, and evaluating them requires undoubtedly very hard work of distinguished experts, internationally well-known scholars, which is to be appreciated. It can hardly be doubted, either, that the reports may serve as guidance for economic policy makers – but not necessarily in the proper direction in all cases.

In view of the *major shortcomings* of the reports which cannot be disregarded (such as some subjective or unreliable elements in the collected data, more or less arbitrary choice of the weights applied in indexes, the influence of the "stage-theory", the little attention to global, international effects on "national competitiveness", etc.), *serious doubts* can be raised regarding the ranking list of countries. The more so, as the measurement of the level of "national competitiveness" of countries and their ranking by *one single composite index*, such as GCI, is itself an extreme over-simplification.

The competitiveness reports can be subject of well-founded critique not only for the ambiguous interpretation of "national competitiveness" (i. e. its confusion with development and enterprises' competitiveness) and also for the method of measuring it, but mainly because they are still heavily influenced by *neo-liberal* *views* and may be used as *ideological instruments* for justifying *anti-social policies* and inducing or compelling the governments to implement *restrictive measures* and forget their welfare tasks. The reports also reflect an implicit acceptance of the prevailing but obviously unsustainable pattern of development of the economically successful countries as models to be followed by others.

REFERENCES

Agarwala, A. N.–Singh, S. P. eds. [1958] *The Economics of Underdevelopment*. Oxford University Press, London

Chikán, A.–Czakó, E.–Zoltay-Paprika, Z. eds. [2002] *National Competitivenes in Global Economy. The Case of Hungary*. Akadémiai Kiadó, Budapest

Csaba, L. [2009a] *Crisis in Economics?* Akadémiai Kiadó, Budapest

Csaba, L. [2009b] "Orthodoxy, Renewal and Complexity in Contemporary Economics", *Zeitschrift für Staats- und Europawissenschaften*, 7. évf. 1. sz. 51–82. o.

Czakó, E. [2003] "Have competitiveness research projects brought a system paradigm shift?", *Society and Economy*, 25, 3., 337–349.

Dicken, P. [1998] *Global Shift: Transforming the World Economy*. Third edition. Paul Chapman Publishing Ltd, London

Dunning, J. H. [1993] *Multinational Enterprises and the Global Economy*. Addison-Wesley, New York

International Institute for Management Development [IMD] [2004] *World Competitiveness Yearbook*. Lausanne

Krugman, P. [1994] "Competitiveness: a dangerous obsession", *Foreign Affairs*, March-April, pp. 28–44.

Krugman, P. R. [2009] "Making Mathematical Beauty for Economic Truth – Appeal to Students", *New York Times*, September 2.

Leibenstein, H. [1957] *Economic Backwardness and Economic Growth*. New York

Martin. J. R. [2007] "World Competitiveness Reports." Summary. In: *Management and Accounting WEB*.

Nerfin, M. [1987] "Neither Prince nor Merchant: Citizen – An Introduction to the Third System", *Development Dialogue*, No. 1. pp. 170–195.

Nurkse, R. [1958] "Some International Aspects of the Problem of Economic Development". In: Agarwala, A. N.–Singh, S. P. eds. [1958] *The Economics of Underdevelopment*

OECD [1994] *Globalisation and Competitiveness: Relevant Indicators*. OECD, Paris

OECD-DAC [1988] *1988 Review. Development Cooperation*. OECD, Paris

Porter, M.E. [1990] *The Competitive Advantage of Nations*. Macmillan, London

Rostow, W. W. [1960] *The Stages of Economic Growth. A Non-Communist Manifesto.* Cambridge University Press, Cambridge

Schuelke, W. R. [2000] "Global Competitiveness Report. Sinagpore Wins Again!", In: *World Economics News*. July 1, 2000.

Schwab, K. [2011, ed.] *The Global Competitiveness Report 2011–2012.* Geneva, Switzerland

Stiglitz, J. E. [1989] "Markets, Market Failures and Development", *American Economic Review, Papers and Proceedings*, May

Stiglitz, J. E. [2010] *Freefall: America, Free Markets, and the Sinking of the World Economy.* W. W. Norton & Company.

Szentes, T. [1971] *The Political Economy of Underdevelopment*. Akadémiai Kiadó, Budapest [1988: 5th, enlarged edition]

Szentes, T. [1982] "The TNC Issue: Naive Illusions or Exorcism and Lip-Service?", *Review*, Fernand Braudel Center. SAGE publ. New York. Vol. IV. No. 2. Fall. pp. 229–252.

Szentes, T. [1995] *A világgazdaságtan elméleti és módszertani alapjai*. [Theoretical and Methodological Fundaments of World Economics]. Aula, Budapest

Szentes, T. [2002] *World Economics 1. Comparative Theories and Methods of International and Development Economics*. Akadémiai Kiadó, Budapest

Szentes, T. [2003] *World Economics I1. The Political Economy of Development, Globalisation and System Transformation*. Akadémiai Kiadó, Budapest

Szentes, T. et al. [2005] *Fejlődés, Versenyképesség, Globalizáció. I.* [Development, Competitiveness, Globalisation], I. Akadémiai Kiadó, Budapest, III. fej.

Szentes, T. [2009] *Ki, mi és miért van válságban?* [Who, what and why in crisis?]. Napvilág Kiadó, Budapest

Szentes, T. [2011] *Fejlődés-gazdaságtan*. [Development Economics], Akadémiai Kiadó, Budapest

Török, Á. [1999] *Verseny a versenyképességért?* [Competition for competitiveness]. Miniszterelnöki Hivatal ISM, Budapest.

UNCTAD [1999] *Trade and Development Report* UN New York and Geneva

UNCTAD [2002] *World Investment Report 2002.* UN. New York and Geneva.

World Economic Forum [2004] *The Global Competitiveness Report 2004–2005.* Palgrave, Macmillan for WEF.

World Economic Forum [2011] *The Global Competitiveness Report 2010–2011.* SRO-Kundig, Geneva