

## **What is the Place that Reserve Location Strategies of Multinational Corporations in Morocco?<sup>1</sup>**

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### **Abstract**

*The objective of this work is to discuss an issue in terms of articulation between the different characteristics of foreign direct investments FDI as they are done on a horizontal or vertical base. In this context, the investigations driven by MCI in 1998 and the World Bank in 2000 FACS, on the determinants of FDI in Morocco, show that multinational firms MNCs prefer for the most part vertical strategy. This is consistent with the exogenous multinationalization which teaches us that vertical direct investment takes place inside an economic area where the factor endowments differ from one country to another.*

### **1. Introduction**

The strengthening of attraction<sup>2</sup> has become an explicit objective of economic policy as well as in developed countries than in developing countries (Delapierre and Milelli, 1995). In this context, it seems essential to ask about the determinants of localization of the foreign firms in Morocco. As such, the focalization on the action of the multinational enterprises, its vertical strategies (or cost minimization) and horizontal (or market), induce two findings: The first recognizes the vertical direct investment<sup>3</sup> (VDI) logic which is based on differences between factor endowments (Helpma<sup>4</sup>, 1984).

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<sup>1</sup> The authors wish to express their sincere appreciation and gratitude to Ms. Khadija TOUFIK for her precious efforts in reviewing and proofreading this research.

<sup>2</sup> By political attraction, is any action seeking to draw on the national territory these foreign investments. For Michalet (1991), the concept of attraction is the product of two approaches: States seeking to promote their localization advantages; firms seeking to maximize their competitiveness through optimal localization of their various activities.

<sup>3</sup> According to Bellon and Gouia (1998), FDI are vertical when a company approaches to its suppliers or its customers by taking part in their capital. Upstream, it is mainly in the direction of internationalization of countries producing commodities and countries likely to produce subcontract; downstream, these are the countries that have strong potential consumers and, consequently, those who may harbor processing industries.

<sup>4</sup> In this context, Helpman has integrated international investment in monopolistic competition models; it comes in the form of a transfer of specific assets. The investment is an intermediate good and the motherhouse, exported to an intensive production unit in relocated work in a host country. Vertical relocation due to differences of abundances factor, with unique investment and re-import of the production to the country of origin.

However, this theory based on exogenous multinationalization can hardly explain the observations whereby intensive FDI flows are observed between developed countries of the Triad<sup>5</sup>, and negligible flows are observed between them and most part of developing countries. The second statement is that horizontal direct investment<sup>6</sup> (HDI) focuses on the similarity between countries in terms of per capita income and factors endowments (Markusen and Venables<sup>7</sup>, 1995). It is however important to notice that over 90% of FDI flows oriented to developing countries are concentrated on the fast-growing countries of Southeast Asia which offers at the same time potentials of attractive local outlets and high-performance communication infrastructure endowments allowing to reconcile the relocation on the grounds of cost minimization and imperatives of flexibility and reactivity to fluctuations of demand. However, this theory based on endogenous multinationalization showed that foreign investment shall be observed just between developed countries. Thus, it explains badly the strong growth of FDI flows destined to Asian countries beyond the fact that they are high growth markets.

By discussing an issue in terms of articulation between the different characteristics of FDI as they are made on a horizontal or vertical base, it seems opportune to locate the place that multinationalization theories reserve in Morocco. In this sense, we will refer to the investigation that were led by the Ministry of Trade and Industry of Morocco "MCI" in 1998 and the World Bank in 2000.

## ***2. The investigation of MCI and international industrial relocation***

This survey was conducted between May and June 1998, in the form of interviews with managers of 39 foreign-controlled enterprises<sup>8</sup> in the Moroccan industry sector<sup>9</sup>, mostly multinationals subsidiaries enterprises. By undertaking a study on such a subject, MCI is assigned a double objective:

- To highlight the determinants, attraction factors, trends of international relocation strategies to assess the advantages and disadvantages of Morocco in terms of FDI host site;
- Contribute to further the reflection and the consultation around consolidation the Morocco attraction measures.

The survey has revealed the root causes of international relocation decision that the aspect concerning the production cost cut mentioned by 82% of the firm samples, represent the priority factor, especially for textile, clothing and electronics industry. Regarding the type of costs covered, firms are merged; the focus is on labor costs, followed by transport costs and energy costs, and finally financial costs. Unfavorable conditions in the profitability of investments in the country of origin of the motherhouse (slowdown in domestic demand, increased international competition) are a factor used by nearly 50% of the companies surveyed.

In terms of attraction factors of the host country, the survey has identified political stability, infrastructure availability and freedom of use of profits as prerequisites for any decision of relocation. Other factors proved decisive: liberalization and stability of the economy, productivity of labor, labor legislation, proximity of export markets, dynamic local market, factors mentioned by 50 to 60% of the companies surveyed.

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<sup>5</sup> Term for a group of three, used especially in the EEC reports (Kenigswald and Keizer, 1996). North America, East Asia and Western Europe.

<sup>6</sup> FDI is horizontal when the company replicated abroad activity it develops in the country of origin (Bellon and Gouia 1998, op. Cit.). The possibility of a horizontal multinationalization between countries has already been studied by Krugman (1983). For the latter, the decision to set up a factory abroad, rather than continuing to export result of arbitration between the benefits or costs related to the proximity of the host market and economies of scale from the concentration of production in a single plant in the country. Thus, it is now established that the bulk of FDI flows have exploded over the past fifteen years, involves primarily in industrialized countries (such as senders and receivers). The strategy of MNEs can be described as horizontal as it concerns the Crusaders investment flows North-North that develops between the US, Europe and Japan.

<sup>7</sup> An interesting result of the Markusen and Venables model is that growth initially leads to an increase in intra-industry trade (as in models with imperfect competition treated by Grossman and Helpman (1991), but that it gradually replaced by FDI, which would explain why the growth of FDI was significantly more pronounced than that of trade over the last twenty years. between 1986 and 1990, global FDI flows increased 29% per year on average, against 15% for trade in goods.

<sup>8</sup> Selected foreign firms for the survey are originating from the follow countries: Germany, Belgium, Spain, France, Italy, Switzerland, United-States and Corean Republic. Similarly, these firms are been selected by a significant regional repartition of foreign implantation in Morocco (axis Casablanca-Settat, Middle, North).

<sup>9</sup> The branches of industry where operate over 39 foreign-controlled companies are: Agro-Alimentary, Textiles, Clothing and Leather, Parachemistry Chemistry, Mechanics, Metallurgy, Electrical-Electronics.

In infrastructure, the responses of firms indicated that foreign investment will pay particular attention to the following five areas<sup>10</sup>: industrial lands and parks, telecommunications, electricity, roads and means of land transport and air transport.

**Table n°1: Determinants of industrial foreign investments "IFI"**

Determinants of IFI designated by the sample of foreign companies	Proportion of foreign companies have designated the determinant
Reduction of production costs	82 %
Unfavorable condition in the profitability of investments in the country of origin	49 %
Increasing market	33 %
Geographical diversification	23 %
Circumvention of trade barriers	20 %

**Source:** MCI (1999), "International industrial relocations: determinants, factors of attraction, trends. Point of view of foreign companies implanted in Morocco." *Conjoncture*, No. 27, May

By discussing the case of Morocco, the survey aimed to identify its attraction factors. So from Table II, it is clear that political stability, geographic location, the qualities of labor (low cost, performance, qualification underlined in particular by the industrial textile-clothing and electronics), and potential of the internal market constitute strong assets of Morocco. The availability of certain infrastructures, although their cost is found most often uncompetitive, is part of a series of quite satisfactory factors, but the improvement will increase the attraction of Morocco. The presence of local suppliers, aids and subsidies for the implantation, the flexibility of the legalization of labor represent a final group of factors that do not stand out as Morocco's strengths, according to the companies surveyed.

The answers of the companies allowed showing up the sources of their satisfaction and the roots of obstacles encountered. Thus, 17% of companies are fully satisfied with their implantation in Morocco are mainly for reasons related to their business profit and the performance of the workforce. They are 49% companies, while indicating reasons for satisfaction (benefits of the geographical position of Morocco, competitive labor costs, workforce availability, etc.), are from a range of restrictions which the most recurrent are related to the administration, the legal framework, the high cost of infrastructure services, and unfair competition. On the other hand, companies declaring somewhat dissatisfied (34%) involve most frequently the obstacles caused by the Customs, while regretting, as in previous companies, administrative delays, unfair competition and the high cost of services infrastructure.

**Table n°2: Factors of attraction of Morocco**

Ranking	Factors	Perception Factor
1	Political stability	Indisputable
2	Location (export platform, proximity to Europe, gateway role to Africa)	
3	Qualities of labor (low cost, productivity, qualification)	
5	Potential of the internal market	Perfectible
6	Availability of certain infrastructure (electricity, telecommunications, water, port services, industrial land)	
7	Macroeconomic stability	
8	Freedom profits use	
9	Liberalization of the economy	
10	Tax Benefits	
11	Industrial partnership opportunities or strategic alliance	Insignificant
12	Presence of local suppliers	
13	Grants and subsidies for implantation	
	Flexibility of the labor legislation	

Source: MCI (1999, *op. cit.*).

<sup>10</sup> The list of infrastructure sectors included in the maintenance medium consisted of: land and industrial parks, roads, land transport, rail transport, air transport, ports, telecommunications, electricity, water, education system, vocational training, technology base national, research laboratories, institutional framework, financial system.

In terms of expectations, foreign companies advocate strong reforms at the level of Customs, the fight against corruption, improving economic and institutional environment through an effective application of the texts and quick arbitration of disputes and litigation, modernizing labor laws, improved tax incentives for exporters, and reducing energy costs.

Thus, through the analysis of the survey of MCI, Morocco seems best placed to foreign companies in the case of the vertical strategy. The answers confirm the leader position of Morocco in the textiles and clothing industries and electronics where low cost and qualification of the workforce are confirmed by 82% of the sample firms. This is coherent with an exogenous multinationalization which primarily considers VDI which the theory teaches us that it is based on the differences in factor endowments and subsequently the location advantage of the host country (unlike the prices inputs, quality of inputs, etc.)

### ***3. The survey FACS and determinants of settlements of foreign companies in Morocco***

In the framework of the investigation program of Firm Analysis and Competitiveness Survey (FACS), the World Bank, in collaboration with MCI, launched in June 2000, a survey<sup>11</sup> for the analysis of the industrial competitiveness of enterprises in Morocco. The main purpose of the study is to assess, at the microeconomic level, the environment in which Moroccan companies develop with their strengths and weaknesses, to understand its impact on business performance, and identify the necessary measures to improve their competitiveness. The simultaneous achievement of the investigation of FACS in Asia and Latin America will allow companies, business associations, trade unions and public authorities, to measure their performance against other countries, in order to better identify action areas.

The survey questionnaire begins with questions about the beginnings and the social status of the company, including questions about the owner or manager's profile<sup>12</sup>. Next, the survey continues with issues related to:

- Finance: the objective is to examine the financial constraints to production and expansion;
- Technology: the aim is to assess the ease of access to new technologies;
- Relations with other companies: with the aim of evaluating the significance of associations and networks;
- Business environment with the objective of assessing the effects of government regulation on business decisions of companies;
- Execution of contracts: the aim of assessing the implementation problems of the contracts that hinder the development of enterprises;
- Labor relations: aiming to understand the strengths and weaknesses of the labor market;
- International trade: the aim is to examine the facilities of international market access.

An examination of the results of this survey concerning the foreign companies section in Morocco has shown the attractions factors of FDI in direction to Morocco. Indeed, the leaders of nearly 170 of these foreign companies have namely asked been the following question: "What factors motivated foreign investment in Morocco rather than in another country?" The answer consisted in selecting at most three determinants by order of their importance among the ten proposed. The results of this survey are synthesized in the following table:

From this table, it follows that the low cost of labor, proximity to the European market and the availability of skilled labor constitute the three principals criteria involved in the business choice of location foreign companies in Morocco. Other criteria have proved to be marginal: the availability of raw materials, low cost of lands and buildings, the legal and regulatory advantageous environment and low cost credit.

The survey has also shown differences in the evaluation of the attraction across sectors. In this light, clothing, textiles, and chemicals are getting very high scores. In clothing and textiles, foreign investors respectively prefer the proximity to the European market and the low cost of labor. Those who are interested in the proximity of the Moroccan market and the availability of skilled labor put chemistry and clothing first. Thus, in the context of this investigation FACS, Morocco seems best placed to foreign companies in the case of the vertical strategy, as cost minimization appears as a major determinant of localization in the clothing and textile sectors.

<sup>11</sup> The extracts of this survey (FACS-Morocco) were provided to me by the MCI in August 2002.

<sup>12</sup> This information, according to the responsables on this survey, is useful to discern how the business environment affects different types of firms (local enterprises old and new, and foreign companies old and new).

**Table n°3: Determinants of implantation of foreign companies in Morocco**  
**Criteria mentioned among the top three**  
**(Number of citations for the 161 companies indicated)**

Criteria Sector	Low cost of labor	Low cost of lands and buildings	Low cost of credit	Good infrastructure	Availability of skilled labor	Availability of the raw material	Proximity the to Moroccan market	Proximity the to European markets	Favorable tax treatment	advantageous legal and regulatory environment
chemistry	14	2	1	6	6	4	13	6	7	2
electricity	5	-	-	-	3	1	4	4	2	2
supply	9	1	1	2	2	5	4	7	2	1
clothing	38	3	2	8	24	4	9	40	23	1
leather	5	2	-	1	4	1	1	3	3	1
plastic	6	-	-	3	2	1	3	3	2	1
Textile	21	8	1	6	10	2	8	24	11	-
Set	98	16	5	26	51	18	42	87	50	8

**Source:** Author's calculation based on the results of FACS in Morocco.

### 5. Conclusion

In conclusion, both MCI and FACS investigations have allowed us to draw two lessons:

- Exogenous multinationalization which considers the vertical strategy based on the factor differences, highlights the relevance of cost minimization as a major determinant of MNCs location in Morocco.
- Textiles, clothing and electronics are considered as the major industries preferred by the FMN.

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