Re-orienting the Paradigm:
Path Dependence in FDI Theory and the Emerging Multinationals

Jan Knoerich*

* Lau China Institute and Department of International Development, School of Global Affairs, King’s College London, 30 Aldwych, King’s College London, London WC2B 4BG, United Kingdom; Phone: +44 20 7848 7843, Fax: none, E-mail: jan.knoerich@kcl.ac.uk
Abstract

**Purpose** – This study analyses how path dependence in the evolution of major theories of foreign direct investment (FDI) locked in a theoretical perspective of the multinational enterprise that focused on asset-exploitation. This perspective is challenged by recent contradicting observations of multinationals from China and other emerging economies. A decisive re-orientation of FDI theory is proposed as a way forward to resolve this tension.

**Approach** – Placing FDI theories into the context of FDI patterns prevailing at the time they were developed, Thomas Kuhn’s framework on the evolution of scientific knowledge is employed to track how mainstream FDI theory emerged, went through a period of normal science and then approached a crisis of science in this field.

**Findings** – The evolution of FDI theory is strongly path-dependent, which made it difficult for theory to effectively incorporate new conceptual discoveries and empirical findings about the nature of FDI activity.

**Originality/Value** – FDI theory would benefit from a full re-orientation to a demand-oriented perspective which places the pursuit of advantages, assets, resources etc. at the core of the theory. Such a change is implicit in many recent theoretical advances and would assure theory is generalizable to all types of FDI.

**Keywords:** Chinese multinational firms, emerging market multinationals, foreign direct investment (FDI), OLI, path dependency, theory of the multinational enterprise

**Paper type:** Research paper
Introduction

The arrival of companies from emerging economies such as China, India and Brazil on the world stage since the beginning of the 21st century ushered in a new era in the study of foreign direct investment (FDI) and the multinational enterprise (MNE). These emerging multinational enterprises (EMNEs) exhibited features that were markedly at odds with observations of traditional multinationals known to have expanded globally during the second half of the 20th century, which prompted many scholars to question and revisit established FDI theories (Alon et al., 2011; Child and Rodrigues, 2005; Buckley et al., 2007; Gammeltoft et al., 2010; Yiu et al., 2007; Ramamurti, 2009; Mathews, 2006; Athreye and Kapur, 2009; Moon and Roehl, 2001; Hennart, 2012). Criticisms of extant theory focused on its baseline idea that companies required strong firm-specific advantages (FSAs), such as know-how or branding capabilities, to successfully internationalize (Buckley et al., 2017: 1047; Dunning, 2001a; Hymer, 1976; Vernon, 1966). This requirement contradicted many observations of EMNEs, which were found to be internationally less experienced, less competitive and smaller than their advanced economy peers (Cuervo-Cazurra and Genc, 2008; Luo and Tung, 2007; Gammeltoft et al., 2010; Contractor, 2013). Other distinct features of EMNEs that raised theoretical questions were their strong network orientation, greater risk-taking behavior, institutional constraints and intense state-government relations in emerging home economies (Mathews, 2006; Buckley et al., 2007; Peng, 2012, 2014; Hoskisson et al., 2013; Yiu et al., 2007; Morck et al., 2008; Luo and Tung, 2007; Quer et al., 2015; Yang and Stoltenberg, 2014).

The paradox of EMNEs internationalizing despite weak FSAs was further aggravated by their rapid expansion into economies more advanced than their home country (Ramamurti, 2012; Madhok and Keyhani, 2012; Holtbrügge and Kreppel, 2012; Guillén and García-Canal, 2009),
as shown in Figure 1. Chinese firms expanded into North American and European markets (Anderson and Sutherland, 2015; Knoerich, 2012; Blomkvist and Drogendijk, 2016), and Indian multinationals increasingly focused their FDI on the United States, United Kingdom, Germany and other advanced economies (Pradhan and Sauvant, 2010; Parthasarathy *et al.*, 2017). Companies from other emerging economies such as Brazil, Mexico and Taiwan, and even from less prominent emerging markets such as Jordan, Chile and Costa Rica (Bianchi, 2014; Padilla-Perez and Gomes Nogueira, 2016), have internationalized in the face of highly competitive global incumbents that dominate international markets. Some Chinese firms acquired world leading companies in advanced economies despite their technological and managerial weaknesses, internationally unknown brands and limited international experience (Knoerich, 2010). Such discoveries amplified the tension between extant theory and actual observations of Chinese and other EMNEs. It is increasingly questionable whether traditional FDI theory – and especially the necessity of FSAs that forms the core of it – still accounts for the whole spectrum of global FDI.

Figure 1 goes about here

*FDI between G7 countries and developing and transition economies*

Source: UNCTADStat

This study exposes path dependence in the evolution of FDI theory as the origin of this theoretical dilemma. When FDI was first analyzed after World War II, all to be seen were multinationals from leading Western economies investing abroad by exploiting their international leadership and competitive advantages, often in less advanced economies.
Continuous theorization on FDI over time locked in these observations – most notably in the form of Dunning’s “OLI paradigm”, which emphasized a company’s firm-specific or “ownership advantages” as a foundation of FDI (Dunning, 2001a). But over time, mainstream theory was increasingly challenged by the need to incorporate newly emerging conceptual discoveries and empirical observations that did not fit well with its emphasis on ownership advantages. This study is believed to be the first to examine the consequences of path dependence for the evolution of FDI theory and the resulting lack of fit with more recent trends. The conclusion drawn from this analysis is that as FDI theory evolved, it should have placed lesser emphasis on FSAs as a foundation of FDI to avoid questions about the universal applicability and generalizability of the theory.

This study contributes to the further advancement of FDI theory by laying out why a decisive re-orientation of FDI theory is necessary and how it should be undertaken. It explains why FDI theory should do away with its current focus on the exploitation of FSAs as a raison d’être for FDI activity, and instead adopt a “demand-oriented” perspective. From this perspective, the multinational is not viewed primarily as a supplier of FSAs to other countries, but rather as an entity that uses FDI as a means to satisfy its own demand for specific advantages, assets, resources etc. by pursuing them abroad. Although recent theoretical advances, which take account of the emerging multinationals, are already implicitly falling in line with such a re-orientation, they avoid broader questions about the general paradigm and analytical thrust underpinning FDI theory. The “demand-oriented” perspective developed in this study addresses this shortcoming by providing an appropriate new fundament and basis for the future advancement of theorizing on FDI.

Path Dependence in FDI Theory
Path dependence, a familiar concept in the field of economics, refers to a process whose outcome is conditioned by that process’s own history (Martin and Sunley, 2006). According to Peacock (2009), and Sterman and Wittenberg (1999), the concept of path dependence can be applied to examinations of how scientific knowledge is produced. It is implicit in Thomas Kuhn’s famous work on the evolution of scientific knowledge (Peacock, 2009). Avoiding the term “theory” in favor of “paradigm” (Kuhn, 1970), Kuhn’s thinking centered on the idea of a scientific paradigm going through a life cycle from initial emergence of the paradigm, to normal science, followed by crisis and ending in revolution, when science shifts to a new dominant paradigm (Sterman and Wittenberg, 1999). As this research will show, FDI theory has so far gone through the first three stages of this cycle.

For this study, a history of path-dependency in FDI theory was constructed through an in-depth survey of the theoretical literature on FDI from the 1950s to today. It included seventy original articles or books that developed the theories and forty in-depth discussions of these theories and their evolution by third authors. Several articles included published accounts in which FDI theorists who were active during the relevant periods recalled their experience of the way in which FDI theory evolved. This material was cross-checked with ten comprehensive reviews of FDI theories to ascertain that all the major, enduring and most widely referenced theories of FDI had been incorporated in the analysis. The resulting illustration of the path dependence in FDI theory is depicted in Figure 2.

Figure 2 goes about here

Path dependence in FDI theory
This study does not differentiate “FDI theory” and “theory of the multinational enterprise”, as both represent a confined body of theory, aimed at explaining why FDI occurs and multinationals come into existence. This is in line with language used in previous studies (Dunning, 2003; Hennart, 2009).

The emergence of FDI theories

The emergence stage in the evolution of scientific knowledge is characterized by a lack of common beliefs and agreed scientific standards, resulting in competition among different potential paradigms. Then, at some point, one specific paradigm begins to attract most scientists in the relevant field of study (Sterman and Wittenberg, 1999). Dating roughly back to the late 1950s and up until the mid-1970s, several theories – or paradigms – competed to explain FDI and the activities of MNEs. Precisely at that time, when theories of the MNE underwent a rapid process of conceptual development, FDI was largely an activity reserved to internationally leading companies from high-income countries (Buckley, 2016: 75).

According to Figure 3, in the 1970s advanced economies accounted for close to 100% of all FDI outflows. Unsurprisingly, FDI theory was formulated and conceptualized in accordance with these observations.

__________________

Figure 3 goes about here

Annual outward FDI flows (US$ billion) and percentage of world total

Source: UNCTADStat

__________________
Early theories transferred elements of economic and international trade theory to the cross-border movement of capital (Mundell, 1957), employing relatively simplistic two-country, two-commodities and two-factor approaches and assuming perfect market conditions. It was Stephen Hymer (Hymer, 1960, 1976), together with Kindleberger (Kindleberger, 1969), who contested this purely economic treatment of FDI and the assumption of perfect markets, suggesting that instead, companies invested abroad to overcome imperfections in international markets. This strand of thinking advanced the concept of market power – companies investing abroad by employing oligopolistic or monopolistic advantages which enabled them to overcome disadvantages naturally incurred by the estrangement experienced in a foreign environment. This idea of market power persists in FDI theory up to the present day, awarding Hymer a reputation of father figure in the development of this field of scientific inquiry. Unfortunately, he was not able to further advance his theoretical thinking due to an unexpected early death in 1974.

Vernon’s thesis about the product cycle argued that firms, having developed innovative products in a leading industrialized economy (the United States), expand production abroad once product standardization necessitates a search for more labor-intensive and cost-effective production locations (Vernon, 1966). In resonance with the concept of market power, the companies undertaking investments are leading and dominant international actors from high-income countries investing in less advanced economies to take advantage of lower-end economic activities. Similarly, Kojima’s “macroeconomic” approach, informed by observations of Japanese multinationals, identified comparative advantages enjoyed by investors in host economies as a key explanatory factor for the existence of FDI (Kojima, 1973, 1978).
The well-known internalization approach, developed during the 1970s, focused on the existence of imperfect markets in the international transactions of firms. Forming part of organization theory, this approach extended transaction cost economics to the context of the multinational enterprise. It argues that information asymmetries and the uncertainties of bargaining in the open market incentivize firms to internalize the markets for important economic activities within the confines of the enterprise. If this happens at an international level, MNEs come into being (Buckley and Casson, 1976).

The 1970s was also the time when a group of Scandinavian scholars developed the Uppsala model, also called internationalization approach, which saw the expansion of firms beyond the borders of their home country as a dynamic, sequential process. According to this view, companies internationalize by gradually improving their knowledge about foreign markets and reducing psychic distance with those markets, over time committing increasing amounts of resources to their overseas operations in these locations (Johanson and Wiedersheim-Paul, 1975; Johanson and Vahlne, 1977, 1990). Unfortunately, the rather deterministic nature of the framework and its focus on early stages of internationalization, together with other criticisms (Johanson and Vahlne, 1990), limited its overall potential as a universal theory explaining FDI.

By the mid-1970s, none of these theories had convincingly managed to claim dominance, yet scholars were quite familiar with each other’s efforts as they worked at the same institutions or met at conferences. John Dunning’s main contribution was thus to effectively bring together some of the previously developed ideas under one theoretical framework (Buckley and Casson, 1991: x). In his view, the international activities of companies were determined by their ownership (O) advantages, reminiscent of the concepts of market power and competitive advantage, by internalization (I) advantages obtained from bringing economic
activities within the hierarchy of the firm, and by location-specific (L) advantages, referring to country-specific attributes that attract investments (Dunning, 2000). This tripod of advantages came to be known as the “OLI paradigm”, or “eclectic paradigm” as it effectively drew on and combined several theories into one analytical framework (Dunning, 2001b: 43). This tripod of advantages came to be known as the “OLI paradigm”, or “eclectic paradigm” as it effectively drew on and combined several theories into one analytical framework (Dunning, 2001b: 43).

A product of previous theories by its very nature, the OLI paradigm is a clear illustration of path-dependence in FDI theorizing.

Dunning’s conceptualization of the OLI paradigm as an “envelope for economic and business theories” (Dunning, 2000), as unconventional as it might be, was an ingenious move. It gave him an upper hand in the competition for dominance in FDI theory, eventually elevating him to the leading figure in this field. The OLI paradigm has enjoyed popularity especially among British, Commonwealth and European scholars. That Dunning’s dominant role in FDI scholarship remains uncontested is confirmed by his record on Google Scholar – as of 2017, his citation count was above 62k. This is more than double the citation counts of the next highly ranked FDI scholars on this measure. Taking the list of leading international business scholars provided by Lahiri and Kumar’s (2012: 324/331) ranking exercise (and after cleaning their Google Scholar profiles for inaccuracies), S. Tamer Cavusgil came next (32k), followed by Peter Buckley (31k), Mike Peng (29k) and Paul Beamish (29k). This further confirms the OLI paradigm as the dominant FDI theory in the world.

Normal science in FDI theory

The emergence of the OLI paradigm in the 1970s launched a period of normal science in FDI theory, with the eclectic paradigm forming the standard theoretical reference point to which a great number of scholars and academics committed themselves. The eclectic paradigm was therefore not easily shaken by changes in global FDI patterns or by new theoretical
advancements. This kind of complacence is typical for a period of normal science, in which differences between the theory and actual observations or new discoveries tend to be resolved through a preference for the theory (Sterman and Wittenberg, 1999: 324). Normal science does not aim at discovering novelties, but instead is a cumulative activity aimed at “the steady extension of the scope and precision of scientific knowledge” (Kuhn, 1970: 52).

Dunning actively supported this process. Since the inception of the eclectic paradigm in the 1970s and up until his death in 2009, he spent more than 30 years continuously defending and enhancing the OLI paradigm in an enormous number of publications. There were criticisms of component parts of the theory, for example questioning the necessity of ownership advantages or internalization (Kogut and Zander, 1993; Fosfuri and Motta, 1999), and pointing to a lack of distinction between national and cross-border dimensions of internalization (Barney and Hesterly, 1996). The OLI paradigm also had to survive other scholars’ efforts to promote their own or favored theories (Buckley, 1988; Rugman, 1985).

As will be shown further below, Dunning went to great lengths at explaining new discoveries and observations in global FDI patterns from within the confines of his eclectic paradigm, making continuous efforts to further “articulate the paradigm theory” (Kuhn, 1970: 27). This solidified the process of normal science, enabling scholars to commit to the paradigm and making it difficult to advance any criticisms based on contradictory findings (Peacock, 2009: 108).

The first notable change in global FDI patterns occurred with the first observations of multinationals from developing countries during the 1980s, although their FDI was still of insignificant magnitude when compared with the international total (see Figure 3) and mostly involved investments in other developing countries (Wells, 1983). Examinations of these “third world multinationals” aimed primarily at understanding what kinds of
ownership advantages enabled them to undertake overseas investments despite their inherent technological weaknesses, lack of innovation and poor managerial and branding capabilities. One strand of theory built on Vernon’s work and considered developing country firms to be recipients of standardized technologies in the mature stage of the product cycle (Beausang, 2003). Ownership advantages were derived from small-scale, low-cost, flexible and labor-intensive activities which had been abandoned by advanced economy firms but not yet mastered by other firms in the developing economies (Wells, 1983). The theory of localized technological change provided a more optimistic view, in which developing country firms derived their advantages from the localization of technologies to better fit the conditions in developing countries (Lall, 1983). Proponents of the theory of technological accumulation had even greater confidence in the third world multinationals, suggesting that they are able to innovate along idiosyncratic technological paths as their learning trajectory depends both on localized innovation and the adoption of foreign technologies (Pavitt, 1987; Cantwell and Tolentino, 1990; Tolentino, 1993). All these approaches found developing country multinationals to have at least some sort of ownership advantages, even if these were based on economic activities considered inferior to those of the advanced economy multinationals. Thus, none of these approaches challenged the OLI paradigm. As long as developing country firms continued to invest in countries with a level of development equal to or lower than in their home economy, which was largely the case in the 1980s, the concept of ownership advantages could still function well.

From the 1980s, FDI was also “re-injected” into international trade theory with the increased recognition that scale economies of firms and product differentiation were important in determining trade patterns (Krugman, 1980). The incorporation of FDI into this “New Trade Theory” was informed by both internalization theory and the OLI paradigm (Markusen,
1995), resulting in a wide range of empirical work on trade and FDI (Faeth, 2009; Helpman, 1984; Ethier, 1986). But this approach neither yielded a widely recognized FDI-specific theory, nor did it launch a meaningful challenge to existing theories.

A more significant challenge to the dominant OLI paradigm emerged during the 1990s with the empirical discovery of asset-seeking as an important activity associated with FDI (Almeida, 1996; Dunning, 1996). The asset-seeking perspective focused on the use of FDI as a vehicle for gaining access to valuable assets in host countries, assets which could even be used to overcome firm-specific disadvantages (Wesson, 1993, 1999). From here emerged a duality of asset-exploitation versus asset-seeking in FDI research, where in addition to exploiting ownership advantages, firms could invest in foreign countries to develop FSAs through asset-seeking (Makino et al., 2002). Some scholars emphasized the opportunity to source knowledge overseas through OFDI activity (Park and Choi, 2014; Inkpen, 1998). This corroborated with the development of a categorization in FDI research distinguishing between market-, efficiency-, resources-, and strategic asset-seeking FDI (Dunning, 2000).

Conceptually, asset-seeking appeared to be the opposite of asset-exploitation, and had the safety mechanisms of normal science not been there to defend the latter, the discovery of asset-seeking might have mounted a meaningful challenge to the primary notion of multinationals as exploiters of ownership advantages.

However, scholars did not question the validity of the OLI paradigm. Wesson, who made a meaningful contribution to the development of the asset-seeking concept, argued that it was in conformity with internalization theory (Wesson, 1999: 3). Dunning himself acknowledged asset-seeking as “a new dimension to our thinking about the rationale for FDI” (Dunning, 2001a: 183), and a perspective considered by many researchers to be “a raison d’etre [sic] for MNE activity” (Dunning, 2001b: 45). He approached this challenge by
advocating a reconfiguration of the OLI components to account for asset-seeking activities, whilst articulating the paradigm theory by producing explanations for why the basic tenets of the eclectic paradigm still held firm (Dunning, 2001a: 183). Dunning found a viable solution to this dilemma in the concept of “asset-augmentation”, advancing the idea that firms still need some ownership advantages which confer them with the necessary capabilities to seek assets abroad (Dunning, 2001a: 183). Despite the resolution of this theoretical challenge within the confines of normal science, the discovery of asset-seeking effectively introduced a new perspective from which to examine the activities of MNEs, one that would bring FDI theory closer to crisis mode once the emerging multinationals had begun to invest significant amounts in advanced economies.

*FDI theory in crisis*

A paradigm enters a crisis at the point when the number of anomalies and inconsistencies accumulate to such a degree that scholars eventually begin to question the dominant theory. They respond by engaging in activities aimed at addressing these anomalies and attempt to propose appropriate solutions (Sterman and Wittenberg, 1999). By the early 2000s, at least parts of the dominant paradigm in FDI theory had come under attack, as observations appearing to be inconsistent with the OLI paradigm multiplied. Not only did the share of EMNEs in global FDI flows rise continuously, but these firms increasingly undertook greenfield investments and acquisitions in the advanced economies (see Figures 1 and 3). The concept of ownership advantage did not fit well with this trend, given the many technological, managerial, branding and other weaknesses these companies still exhibited. It was not any more possible to rule out the existence of multinationals
internationalizing without advantages (Fosfuri and Motta, 1999; Hashai and Buckley, 2014). On the other hand, asset-seeking appeared to be an increasingly suitable concept. The debate about the implications of FDI from emerging economies for theory focused initially on Chinese outward FDI, which grew rapidly during the first decade of this century and by 2010 had exceeded the magnitude of outward FDI from the other BRICS economies, Taiwan, South Korea and other emerging economies (according to UNCTADStat). Moreover, China’s domestic political economy, with its high number of state-owned enterprises, presented itself as a striking anomaly. It was the established scholars in FDI research who were first to discuss the anomalies of Chinese outward FDI and their implications for theory. Without doubt having an interest in protecting a lifetime of FDI theorization, they exhibited a strong preference for an extension, rather than replacement, of extant FDI theory (Child and Rodrigues, 2005; Buckley et al., 2007: 501). This conforms to Kuhn’s notion of normal science as a cumulative activity of making scientific knowledge more precise (Kuhn, 1970: 52).

In recent years, there has been a remarkable intensification of FDI theorization aimed at explaining the behavior of emerging multinationals. It is possible to divide this literature into two strands – exploitation-focused versus demand-oriented theories – as presented graphically in Figure 4 along an indicative timeline. Exploitation-focused theories refer to the multinational exploiting technologies, brands and other ownership advantages to engage in FDI. Demand-oriented theories focus on the multinational having a demand for advantages, assets, resources etc. which it seeks to satisfy overseas through FDI. Figure 4 shows how some new theoretical advancements can be fit cleanly into one strand, whereas the locale of the others on this spectrum is somewhere in between.
Two strands of FDI theorization in the crisis era

The first strand perpetuates the focus on the exploitation of advantages as the core of FDI activity, in line with the spirit of theoretical extension. Scholars adhering to this view went on a search for new or different ownership advantages enabling emerging multinationals to engage in successful FDI (Jormanainen and Koveshnikov, 2012). Emerging multinationals were seen to benefit from “special ownership advantages” (Buckley et al., 2007), such as privileged access to funds, resilience, frugality etc. (Ramamurti, 2012; Contractor, 2013). There have been some excesses in this regard, such as the proposal that access to cheap capital might be an ownership advantage of Chinese companies (Buckley et al., 2007; Ramamurti, 2012), which is not much more than reiterating that the possession of funds – from whichever source – is a prerequisite for investment. Rugman (2010), based on his earlier work (2006, originally published in 1981), emphasized country-specific advantages (CSAs), rather than traditional FSAs, as a frequent source of competitive strength for emerging multinationals (Rugman, 2010; Rugman, 2006; Narula, 2012; Chen et al., 2015).

Yet, if some multinationals do invest abroad without exploiting any advantages (Fosfuri and Motta, 1999; Hashai and Buckley, 2014), or even when asset-seeking is found to be the only motive for FDI (Meyer, 2015), a theory focused on the exploitation of advantages may not be universally applicable.

Theories in the demand-oriented strand place multinationals’ seeking-behavior at the core of the theory. According to the linkage-leverage-learning (LLL) approach, companies utilize FDI to develop competitive advantages via linkage, leverage and learning (Mathews, 2006).
Similarly, the springboard perspective views international expansion as an activity EMNEs undertake to acquire overseas assets that enable them to rapidly overcome their inherent competitive weaknesses (Luo and Tung, 2007, 2018).

Some theories have become embedded in a middle ground, whilst giving the demand-oriented strand greater prominence than it received previously. Moon and Roehl (2001) question the market imperfections approach to FDI and the focus on ownership advantages, and recommend replacing the concept of “advantages” with that of “imbalance”. They conceptualize FDI as an activity to rectify an imbalance between ownership advantages possessed and advantages sought through overseas investments. Similarly, the dynamic capabilities perspective describes the ability of EMNEs to engage in both asset-exploitation and asset-seeking FDI as an “ambidextrous internationalization” (Deng et al., 2018).

Furthermore, the resource-based view, which in its original form focuses on firm resources as the source of competitive advantage, has been increasingly used to explain how emerging multinationals use FDI to acquire the resources that they lack from abroad (Deng, 2007, 2013). Building on this, the increasingly popular institution-based view demonstrates how, depending on the circumstances, institutions in the home economy can be a source of competitive weakness as well as competitive strength for emerging multinationals, where weaknesses could be overcome by acquiring resources overseas (Hobdari et al., 2017; Peng et al., 2008).

None of these approaches fully contest the OLI paradigm outright. Yet, the literature from strand two and those theories found in the middle ground confirm that asset-seeking has meanwhile become accepted as an important mainstream concept (Meyer, 2015; Cui et al., 2014). Given the way academia is organized, involving significant pressures to publish in leading journals edited and peer-reviewed by established scholars, it would be imprudent
for a scholar to advance a new theory whilst rejecting established theories. Engaging in a balancing act of advancing new theory whilst endorsing previous theories is thus the norm, confirmed by the large number of theories found in a middle ground between the two strands. Possibly because of these circumstances, all the recent advances have received some degree of recognition, but have yet to gain widespread acceptance. None of these approaches show serious potential to replace the OLI paradigm as the dominant theory.

A Re-orientation of FDI Theory

Sterman and Wittenberg’s examination of path dependence in scientific inquiry finds that competition among paradigms and their order of succession is dependent on the scientific environment within which theory is advanced, on the history of prior paradigms and on self-reinforcing processes supporting some paradigms but not others. Once a specific paradigm begins to dominate, switching to another theory becomes extremely costly, allowing the dominant paradigm to maintain its prominence for long periods of time (Sterman and Wittenberg, 1999).

The previous section’s analysis confirmed such patterns of path dependence having greatly influenced the evolution of FDI theory over the past 60 years. New advancements in FDI theory, aimed at addressing the changes observed in global FDI patterns, were built on top of prior theoretical thinking. Strong tendencies of inclusiveness, with earlier theories being incorporated into later theories, have exacerbated the path-dependent nature of FDI theorization. The eclectic paradigm has been so successful because it managed to incorporate other theories into the paradigm rather than having to refute competing theories to gain legitimacy. It is omnipresent and has locked itself in as the dominant paradigm in this field of academic inquiry (Hennart, 2012: 182).
The sub-optimal development of FDI theory

Although path dependence might be important in supporting the advancement of scientific knowledge, it can lead to pareto-suboptimal outcomes in the development of appropriate theories. With path-dependent processes selecting and giving preference to some theories over others, there is no guarantee that the dominant theory emerging from this process is the most superior among all viable alternatives. To the contrary, historical accidents, the nature of the scientific environment or other factors can, if supported by path-dependent processes, make an inferior paradigm dominate while potentially better alternatives are rejected (Peacock, 2009). It is important to consider this possibility in the case of FDI theory, for four reasons.

First, traditional theories of FDI emerged under a lack of knowledge of future developments in global FDI patterns. At the time of their conceptualization it was certainly impossible to anticipate the new discoveries that followed. The empirical observations available in the initial years of theory development were of advanced economy multinationals, primarily from Western economies, and of investments from stronger into weaker economies, so theory developed accordingly (Ramamurti, 2009, 2012: 43). Similarly, issues such as networks, institutions and state-government relations typical for emerging economies were not considered in great depth. When the emergence of EMNEs combined with the discovery of asset-seeking FDI to pose a significant challenge to established theories, the latter’s survival was assured by processes of path dependence. But because most FDI theory as we know it today was developed at a time when nobody would have been able to anticipate the particularities of current FDI patterns, it is unclear whether extant FDI theory is the most superior theory among all potential alternatives.
Second, one may question whether current FDI theory is in fact falsifiable. According to Karl Popper, the renowned philosopher of science, falsification is the criterion demarcating science from non- or pseudo-science (Popper, 2005). In his view, a theory which is irrefutable, because it can be modified to accommodate all possible observations, is by nature unscientific (Thornton, 2016). Scientific extension, accounting for the recent developments in global FDI trends, could effectively constitute such an attempt at modification. Moreover, the OLI paradigm itself could be questioned for the modifications it has undergone over the years to accommodate new discoveries, such as the incorporation of asset-seeking behaviour into the paradigm by re-branding it as “asset-augmentation” (Dunning, 2001a). Continuous scientific extension and modification may well make existing theories non-falsifiable and thus, in Popper’s view, unscientific. It is for this reason that potential alternative theories should be given greater consideration.

Third, FDI theory is potentially facing a lack of generalizability, in view of the Chinese and other emerging multinationals operating in ways not predicted by such theory. As has been shown, not all EMNEs possess the ownership, oligopolistic and competitive advantages based on which they could make investments in line with the predictions of traditional theory. Moreover, while some may view the identification of new types of ownership advantages as a viable solution to this dilemma, others will view such attempts as no more than a desperate fix. The question is to what extent criteria of generalizability and universal applicability must be fulfilled for a theory to count as legitimate, and how many exceptions may still be tolerable.

Generalizability and universal application is of course not a requirement for a good theory, and emerging multinationals may need a theory of their own. Theories such as the springboard perspective, the LLL approach, the dynamic capabilities perspective or the
addition of CSAs are indeed quite EMNE-specific. But advancing a theory specific to the emerging multinational raises conceptual challenges, such as questions about the appropriate cut-off point distinguishing emerging from advanced MNEs, the precise definition of aspects that make emerging multinationals unique, and the necessity to switch theoretical belonging when emerging multinationals mature and transition to become advanced multinationals. Even more problematic would be to stigmatize emerging multinationals as asset-seekers, while more traditional investors from advanced economies have for several decades had the privilege of being described as asset-exploiters. With asset-seeking featuring strongly in the literature on Chinese outward FDI (Deng, 2007; Young et al., 1996; Child and Rodrigues, 2005; Amighini et al., 2013; Gugler and Vanoli, 2015), this tendency is already prevalent. Thus, any theoretical distinction between emerging and advanced economy multinationals would need to be carefully crafted, and it is not surprising that the backing among scholars for such a separation appears to be limited (Narula, 2012; Ramamurti, 2012).

FDI theory evolved primarily in the field of international business, spearheaded by scholars at the University of Reading, some of whom in later years dispersed to other locations in the United Kingdom and beyond. The thinking and theoretical arguments published by business scholars are however bound by the need to present companies and businesspeople in a favorable light. Academics working in international business are dependent on good relations with companies, on whom they rely to obtain data and funding. The asset-exploitation narrative focusing on the technological, managerial and branding strength of multinationals promotes such a favorable view, as it creates a positive notion of a strong company bringing capabilities and other assets which may spill over into host countries. An asset-seeking perspective may, on the contrary, shine less of a bright light on the activities of
multinational enterprises. This is because, even though target firms or host economies can potentially benefit from asset-seeking FDI together with the investing firm (Knoerich, 2010), it may also raise concerns over issues such as technology theft, reverse knowledge transfer and economic dependency, attitudes increasingly visible towards Chinese multinationals (Giuliani et al., 2014: 681). That activities akin to asset-seeking had been observed as early as the 1950s (Cantwell et al., 2004: 18), yet no corresponding concepts entered theory, is an indicator of such considerations possibly having been present, either consciously or sub-consciously. For similar reasons, traditional theories may still be preferred among business scholars today.

A change in dominant perspective

It is useful, for a moment, to imagine a hypothetical world in which theorization on FDI started only today, with no previous theories available and scholars having full knowledge of the current characteristics of multinational enterprises from both advanced and lower-income countries. This scenario may well have seen FDI theory develop in a markedly different way to what happened over the past 60 years, because the phenomenon that firms go abroad to seek assets, resources, advantages etc. would have been familiar from the outset, rather than treated as a new observation that needed to be woven into already existing theoretical frameworks.

It is likely that asset-seeking – or an associated similar demand-oriented perspective – would have been given prominence in the development of FDI theory. This is not only because asset-seeking is a characteristic of all time periods and done by multinationals from advanced and developing economies – the former having engaged in asset-seeking activities since the 1950s (Cantwell et al., 2004: 18; Sutherland et al. 2017; Almeida, 1996; Dunning,
It is also because recent theoretical advances, especially those referring to emerging multinationals, have shown some preference for a demand-oriented narrative, while placing less emphasis on asset-exploitation. Most new theoretical advances – apart from those simply advocating the addition of ownership advantages – tend to lean towards the right-hand side of Figure 4. Asset-seeking, or an associated concept, therefore deserves to be at the core of FDI theory, rather than an add-on to existing theoretical frameworks.

Moreover, it cannot be proven – neither conceptually nor empirically – that the exploitation of ownership advantages must occur in each case of a foreign investment. As discussed above, examples exist where the clear identification of ownership advantages is a challenge. If a company has the necessary funds, it can make an investment or acquire a firm, for which it may not need any form of advantage. Of course, the same can be argued about asset-seeking narrowly defined, as not all companies invest abroad to seek technologies, know-how and brands. But theorists in the hypothetical scenario are unlikely to have started off with such a narrow definition of asset-seeking. They would have begun developing theory by viewing FDI from a broader demand-oriented perspective, in which the multinational uses FDI to seek, link to or obtain from a foreign location whatever is in its interest. In other words, not only would they have included the acquisition of assets in the theory, but also the pursuit of other advantages, resources and further objects of interest in a foreign country.

Such a pursuit of advantages, assets, resources etc. can be conceived as the essence of any investment, a necessary and sufficient condition for FDI to occur. It is sufficient because FSAs are not a requirement for such a pursuit to occur. It is necessary because without it, the foreign investment would be without purpose and thus would not occur. No matter what ownership advantages a company possesses, it would not invest abroad if it were not for the
existence of some market, technology, factory, linkage, network, workforce or other advantage, asset or resource it considered worthwhile to obtain in the overseas location through a merger, acquisition, greenfield or brownfield investment. A pursuit in a foreign country is thus a universal requirement for an investment to go forward, a reason for internationalization and the birth of the multinational, indeed the *raison d’être* of the MNE. On the contrary, the possession of ownership advantages is neither a necessary (Hashai and Buckley, 2014), nor a sufficient condition for FDI to occur. A multinational without ownership advantages may nevertheless make an investment to obtain assets, advantages, resources etc. abroad; and a company may possess ownership advantages, but it may not invest abroad as it finds nothing worth pursuing in another country. Ownership advantages are rather a tool or means, to be employed in addition to investment capital, which companies may or may not use to invest abroad successfully.

Put differently, rather than focusing on ownership advantages as *a* means for FDI (that is not essentially required), it is better to focus on a pursuit advantages, assets, resources etc. as *the* ends for FDI (required for it to occur). The strength of such a perspective is its universal applicability and generalizability to all advanced and emerging economy MNEs – both invest abroad in pursuit of some sort of advantages, assets, resources or other objects of interest, even if there may be differences in what they pursue specifically. A demand-oriented perspective therefore promotes a holistic view that incorporates all kinds of FDI by all kinds of firms. It further allows for Popper’s requirement of falsifiability – the discovery of any FDI not driven by such a demand and not constituting a pursuit, as unlikely as it may be, would result in falsification. Finally, it encourages parsimony, as the number of different concepts needed to explain FDI are likely minimized.
Conclusions

Employing Thomas Kuhn’s framework on the evolution of scientific knowledge, this study uncovered the constraints on the advancement of FDI theory imposed by deep processes of path dependence in the evolution of the theory over the past 60 years. The eclectic paradigm with its focus on FSAs and asset-exploitation was found to have locked itself in as the dominant theory explaining FDI. Even when challenged by contradicting observations of multinationals from China and the emerging economies, this perspective on FDI continues to dominate, making a “scientific revolution” in FDI theory unlikely. A “paradigm shift” – to use Kuhn’s terminology – would require a widely-accepted re-conceptualization in FDI theory going beyond simple theoretical extension (Sterman and Wittenberg, 1999).

The main theoretical advancement of this study is its proposition of a full re-orientation of FDI theory to overcome the shortcomings of the asset-exploitation perspective uncovered by it. Instead of focusing on FSAs, a preferred perspective should be “demand-oriented”, viewing the multinational primarily as an entity seeking to satisfy its demand for advantages, assets, resources etc. abroad through foreign investment. This demand-oriented perspective ventures beyond the focus on asset-seeking that dominates the existing literature, as it conceptually incorporates all kinds of assets, resources, advantages etc. sought through overseas investment. It therefore provides a much broader analytical fundament, still to be filled with detail by future theoretical reasoning. Recent advances in theory – including the LLL approach, the springboard perspective, parts of the imbalance theory and dynamic capabilities perspective, and aspects of the resource- and institution-based views – have already initiated this shift towards a demand-oriented conceptualization of FDI theory but have fallen short of advocating a full re-orientation.
This is where this study goes decisively beyond previous theoretical advancements, as it advocates for a fundamental re-orientation of the broad perspective applied to FDI and the multinational. Rather than focusing on the strengths and advantages of the multinational to explain its investments, the demand-oriented perspective re-orientates the focus towards the demands, needs and objectives of the multinational. Given that all FDI is motivated by a pursuit of some advantages, assets, resources etc. abroad, fully adopting this perspective has the added benefit of promoting universally applicable, generalizable, parsimonious and falsifiable FDI theories, and of overcoming the need for a particularistic theory specific to the EMNE. The full and decisive re-orientation to the demand-oriented perspective is preferable to previous practices endorsing a duality of asset-exploitation and asset-seeking, which represents a compromise that comes at the cost of parsimony and theoretical focus. The demand-oriented perspective provides an important new conceptual foundation the purpose of which is to entice greater confidence in the advancement of theories decisively opposed to the asset-exploitation narrative.

Theories adopting the demand-oriented perspective potentially offer new and improved ways of understanding and analyzing FDI, given this perspective’s greater power in the examination of specific aspects of foreign investment. Such theories would likely provide more profound insights on aspects that are influenced by the way in which multinationals pursue advantages, assets, resources etc. through FDI, such as the home country impact of FDI and effectiveness of reverse spillovers (Knoerich, 2017; Zámborský and Jacobs, 2016). They might better examine factors that lead to success or failure of investments, which depends on the effective pursuit of the aspired advantages, assets, resources etc. Theories adopting a demand-oriented narrative will likely provide suitable theoretical backing to examinations of various forms of environmental and social impact of FDI, an issue of concern
especially when MNEs pursue lower environmental and labor standards in host countries. They would be effective for examining the attitude of governments towards FDI, for example by explaining rationales for investment protectionism and the increased use of investment screening mechanisms to vet Chinese acquisitions motivated by the pursuit of assets and resources. Theories adopting a demand-oriented perspective may therefore offer important insights for policy and practice and provide theoretical views that may be valued beyond the realm of international business.

Switching to a demand-oriented conceptualization in FDI theory does not necessarily constitute a full “scientific revolution” out of which an entirely new theory develops. As theories adopting a demand-oriented perspective are further developed, many familiar concepts might continue to be endorsed, resulting in a significant shift that nevertheless perpetuates the path-dependent trajectory in the development of FDI theory. A general theory fitting with a demand-oriented narrative could be superior to potential alternatives, yet still incorporate some of the remarkable contributions made to the conceptualization of FDI over the past decades. Alternatively, a decisive theoretical advancement that adopts a demand-oriented perspective could yield an entirely new theory. It all depends on the trajectory taken by theorists in the future.
References


