Internationalisation and Globalisation in Banking and Manufacturing in Europe, USA and Japan: why differences are as important as similarities.

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Abstract

This paper investigates the following two main issues. The first is the degree to which the globalisation of production is taking place in manufacturing and banking sectors. The second is the extent to which banking follows the globalisation of manufacturing, which in a sense is an examination of the “follow the customer” hypothesis. This study captures such patterns by examining the international allocation of the revenues and assets from a sample of 108 manufacturing and 46 banking companies of the biggest companies in the world according to fortune 500 and by comparing their trends through the years from 1997 until 2004. The methodology employed resembles a similar investigation of the globalisation trends of MNEs by Hirst and Thompson (1996b) and the analysis relies on the presentation of company-based data using charts and diagrams. The geographical focus will be on the three most influential regions in the world, namely the Europe, USA and Japan triad. Our results indicate that even though there is a home bias in the companies’ sales for both the manufacturing and banking sectors and for most of the regions studied, the globalisation trends uncovered in each region are different in every case. In that sense an argument in favour of the existence of an internationalisation rather than a globalisation process arises, while the differences in the international expansion trends in each region makes us aware of the fact that international production trends may depend on the region under study.
1. Introduction

“Globalization has altered the economic frameworks of both advanced and developing nations in ways that are difficult to fully comprehend … Because of a lowering of trade barriers, deregulation, and increased innovation, cross-border trade in recent decades has been expanding at a far faster pace than GDP … Augmenting the dramatic effect of increased globalization on economic growth, and perhaps at some times, fostering it, have been the remarkable technological advances of recent decades. In particular, information and communication technologies have propelled the processing and transmission of data and ideas to a level far beyond our capabilities of a few decades ago.” (Greenspan, 2005)

The integration of the economies and societies all around the world has been one of the most studied and debated upon topics in economics. Globalisation, which as a term emerged in the 1960s, has become one of the most prominent and at the same time most controversial notions, affecting almost every aspect of contemporary life for at least half a century, with finance playing a leading role in this process especially in the more recent years. The drastic reduction in global barriers in the financial services industry, achieved through advances in telecommunication and information technologies accompanied by deregulation of financial markets, has enhanced integration. This led to a dramatic increase in the levels of international financial trading, especially in the last ten years, while its volumes have been massively higher than those of manufacturing trade. In the case of banking, which is the cornerstone of the financial services system, this accelerating global integration has enhanced even further the sector’s growth and international expansion. The banking sector has always been one of the top performing sectors in the past few years; however it reached its peak in 2007 by being the largest and fastest growing global industry according to Fortune Magazine,
surpassing even the petrol refining industry. According to the Bank for International Settlements, banks have tripled their banking international operations since the beginning of 2000 when their international position volumes were 12 trillion US dollars and reaching 37.2 trillion in 2007.

This study, through the analysis presented in the later sections, intends to examine the integration process in the international banking sector by focusing on the investigation of two main issues. The first is the examination of the degree to which the process of globalisation is taking place in manufacturing and financial sectors and the second is the extent to which finance follows the globalisation of manufacturing. The rest of the paper is organised as follows. Section 2 presents a very brief background review of the literature on banking international expansion, especially in the form of the “follow the customer” hypothesis. Following that, a review of the methods used in the analysis is presented in section 3, while a discussion of the results is taking place in section 4. Finally this paper ends in section 5 where the concluding remarks are laid out.

2. Background

The nature and the extent to which globalisation is taking place has been one of the most debated topics in economics. The opinions vary from those scholars who suggest that globalisation is not something new but an ongoing process that started centuries ago (for example Obstfeld, 1998; Waltz, 2000; Banz and Clough, 2002; Lothian, 2002), to those that question the extent to which such a phenomenon is actually happening (for example Gordon, 1988; Ruigrok and van Tulder, 1993). However since so much has been said over this matter, it would be pointless and out of the scope of this paper to enter such a broad discussion. Nevertheless it has to be stated that the viewpoint adopted by this study is viewing
globalisation as a process rather than an end-state and that the world is far from being fully
globalised. Additionally we agree with those who even though they do not reject the fact that
international production has been taking place in an accelerating pace but favour an
internationalisation argument, i.e. that international production has a home/regional bias and
is mainly taking place through MNE activity mainly amongst major financial and trading
blocks, namely North America, Europe and Asia-Pacific (Tyson, 1991; Kapstein, 1991; Hirst
and Thompson, 1992; 1996a; 1996b; Rugman, 2000; 2005; Rugman and Verbeek, 2004;
Dunning et al., 2007). Such an argument is supported by the findings of this study presented
and discussed later on, while indications of the existence of such a trend are present in table 1
below, where it is clear that more than 80% of the revenues of the world’s 500 biggest
multinationals are produced by companies that are based in Europe, the USA or Japan.

Table 1: “League Table” of the Production of the World’s 500 Biggest (Predominantly
Manufacturing) Multinationals

<table>
<thead>
<tr>
<th>Region where the companies are headquartered</th>
<th>Percentage of total revenues of the world’s 500 biggest multinationals</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2004</td>
</tr>
<tr>
<td>EU-25 (Excluding Britain)</td>
<td>28.27</td>
</tr>
<tr>
<td>Britain</td>
<td>8.00</td>
</tr>
<tr>
<td>USA</td>
<td>37.04</td>
</tr>
<tr>
<td>Japan</td>
<td>14.24</td>
</tr>
<tr>
<td>Rest of Asia/Australia</td>
<td>6.18</td>
</tr>
<tr>
<td>Rest of the World</td>
<td>6.29</td>
</tr>
</tbody>
</table>

Source: Fortune Global 500, various issues

Concerning the banking industry, which is the focus of this paper, a similar picture is drawn
in table 2 below, where again the regional focus of banking operations is obvious with almost
90% of the world’s biggest banks’ revenues coming from companies that have their
headquarters in the triad region mentioned earlier.
Table 2: “League Table” of the Revenues Generated by the World’s Biggest Banks as Reported in the Fortune Magazine Global 500 List

<table>
<thead>
<tr>
<th>Region where the companies are headquartered</th>
<th>Percentage of total revenues of the world’s biggest banks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2004</td>
</tr>
<tr>
<td>EU-25 (Excluding Britain)</td>
<td>42.85</td>
</tr>
<tr>
<td>Britain</td>
<td>14.34</td>
</tr>
<tr>
<td>USA</td>
<td>18.55</td>
</tr>
<tr>
<td>Japan</td>
<td>6.21</td>
</tr>
<tr>
<td>Rest of Asia/Australia</td>
<td>7.95</td>
</tr>
<tr>
<td>Rest of the World</td>
<td>10.09</td>
</tr>
</tbody>
</table>

Source: Fortune Global 500, various issues

These similarities between the international orientation of the banking and the manufacturing sector, apart from being driven from the obvious location advantages of the Europe, USA and Japan triad, could potentially be due to the banking incentive for international expansion in order to service their manufacturing customers. Despite the widened banking operational scope into many different activities, the banks’ role as intermediaries which finance the industrial and commercial projects of the companies operating in the “real” side of the economy still remains at the core of the banking operations. From this view it would not be an exaggeration to claim that the banks’ incentive to follow the international expansion of their manufacturing clients, to provide them with services in any location in which the latter are located, can be considered to be the main banking international expansion cause. This claim is examined by this piece of research.

The “follow the customer” incentive has been incorporated in the analysis of several studies as a determinant of banking international expansion. This has been done mainly through regression analysis and the use of FDI and/or trade linkages between the home and the host countries as a proxy of such an incentive. Starting from the former, the outward volumes of
total FDI\(^1\) or non-financial FDI\(^2\) either in flows or stocks, has been used as a proxy measure and the “follow the customer” incentive has been broadly confirmed. The second large group of studies have used bilateral trade measures\(^3\) as their proxy and again it was broadly agreed that banks have indeed the incentive to follow their clients abroad. Apart from those studies that have examined this determinant through a regression analysis, there have been some studies such as those of Seth and Quijano (1993) and Seth et al (1998) that used an alternative approach. They used a comparative presentation analysis of charts and tables to look at the lending patterns of Japanese and foreign banks operating in the US accordingly. Contrary to the rest of the literature, these studies, even though they do not reject the “follow the customer” hypothesis, suggest that it may have more limited applicability than previously supposed for the countries and the time period under investigation.

In this piece of research, an approach similar to that found in Seth and Quijano (1993) and Seth et al (1998) is adopted, to investigate recent trends in internationalisation of banking and manufacturing companies. This approach is preferred here because we believe that a diagram and chart analysis can provide a different insight to the “follow the customer” hypothesis as tested through regression analysis, and can detect and emphasise differences in the globalisation patterns between banking and manufacturing across regions that the past literature has failed to identify. The methodology used here, is developed in the next section.


\(^2\) Hultman and McGee, 1989; Sagari, 1992; Moshirian and Van der Laan, 1998; Moshirian and Pham, 1999; Esperanca and Gulamhussen, 2001; Moshirian, 2001; Wezel, 2004

\(^3\) Either in the form of total exports from the home country to the host (Goldberg and Saunders, 1980; Goldberg and Johanson, 1990; Budzeika, 1991; Heinkel and Levi, 1992; Wengel, 1995; Brealey and Kaplanis, 1996; Focarelli and Pozzolo, 2000; 2001; Berreta et al., 2005), or in the form of the sum of total imports and exports (Grosse and Goldberg, 1991; Fisher and Molyneux, 1996; Yamori, 1998; Buch, 2000; Moshirian, 2001; Piscitello, 2003; Galindo et al., 2003; Buch and Lipponer, 2004; Magri et al., 2005; Cerutti et al. 2005; Focarelli and Pozzolo, 2005; Claessens and Van Horen, 2007)
3. Empirical Methodology

As mentioned earlier, the purpose of this paper is to examine to what extent the globalisation of banking and manufacturing sectors is happening and the extent to which banking follows the trends set by manufacturing or vice-versa. The investigation of whether banking follows manufacturing internationalisation can be claimed to be a way of testing the “follow the customer” hypothesis discussed earlier. It could be argued that the willingness of the banks to expand their operations abroad to follow the international expansion of their manufacturing clients can be captured by the fact that their international business allocation follows the trends set by the manufacturing sector. As mentioned earlier, methodologically this study has similarities with those of Seth and Quijano (1993) and Seth et al. (1998), however it follows closely the investigation of the globalisation trends of MNEs found in Hirst and Thompson (1996b). It attempts to capture the globalisation patterns by examining the international allocation of the revenues and assets from a sample of the biggest manufacturing and banking companies in the world and by comparing their trends through time. At the same time, the focus will be on the three most influential regions in the world, namely Europe, the USA and Japan in order to see whether the globalisation patterns are different in each case. As globalisation patterns may be location bound depending on where a company is orientated further investigation of the globalisation patterns in different locations can be useful in shedding light on potential similarities or differences in the internationalisation trends of firms coming from a different background (Buckley and Ghauri, 2004).
3.1 Sampling

The main data set used in the analysis consists of data on annual total revenues and their breakdown in revenues produced in the home country of the companies, and in revenues generated abroad. As Dunning et al argue:

… we agree with Rugman and Verbeke … that the data on sales provide one of the most useful measures of the geographical distribution of economic activity (Dunning et al., 2007, p. 188)

Our sample consists of 108 manufacturing and 46 banking firms. Starting from the manufacturing companies, 52 are European, out of which 14 are UK based, 38 are USA based and 18 are Japan based companies. These companies were selected according to their position in the fortune magazine global 500 ranking of the largest corporations for 2005 starting from the largest company in terms of total annual revenues and going down in ranking.4 We have 8 years of observations from 1997 until 2004 and the figures are reported in millions of Euros.

For the banking sector, from the 46 banks that provided information about their revenues, 30 are European, out of which 10 were UK based, 10 are American and 6 are Japanese. The data collected concern again the total revenues and their breakdown in revenues from home and abroad.5 The time period was again from 1997 until 2004, and the figures are in millions of Euros.

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4 Data concerning the total annual revenues for each company and their breakdown in revenues produced at the company’s home region and in revenues produced abroad for the above mentioned companies were obtained through two databases. The British Library based electronic database OSIRIS, and FAME which was accessed through the University of Sheffield.

5 This banking data was obtained through the British Library by using OSIRIS and ONESOURCE. The problem with the latter source is that it did not give the segmented revenue information required for all the companies while its time scope was limited to three years. This data was completed by annual reports of the companies that were available through the companies’ web pages. This was done in order to complete the dataset of the missing information that were not provided by neither OSIRIS nor ONESOURCE, especially for the years previous to 2001.
By accepting Dunning et al’s argument cited earlier, and by following previous similar research using sales data as a measurement of globalisation trends (Hirst and Thompson, 1996b; Rugman and Verbeek, 2004), it will be argued that revenue figures can be used as an adequate proxy for company globalisation. On the other hand it may not be the best, especially in the case of MNEs who can operate and produce overseas; thus an asset distribution could potentially have served as a better proxy for the analysis of this study. However due to the lack of data availability, data collection on total assets and their international breakdown for a company sample big enough to support our analysis has not been possible. Nevertheless some asset data (when available) and their geographical breakdown were collected in order to provide further support to our findings and complement the main analysis, but that was only possible for banking companies and only for a smaller sample than for revenues. In total 36 out of the 46 sampled banks provided information about their asset geographical distribution. From these companies 22 were European, 6 were UK based, 8 were American and 6 were Japanese and the collection of this data was made through annual company reports. For the banking samples, data for 8 years of observations have been collected, namely from 1997 until 2004, and the figures are reported in millions of Euros.

Unfortunately the scope of our research was narrowed, as in every case we had to pool our internationally generated revenues and assets to the very general “revenues from abroad” category. This was due to the limited data availability and the inconsistent reporting format that resulted in an inability to consistently allocate the companies’ geographical breakdown of revenues from abroad to their exact location in a common format for all the companies. Finally, it is obvious that both our samples do not consist of many companies, especially in the banking case where the sample is less than half in size in comparison to the
manufacturing one. There are two reasons involved here. The first and most important reason involves the limitations imposed by data availability. The second reason was the fact that through the process of company short-listing according to revenue size, after a certain point, an individual company’s size became too small to affect significantly the whole sample. Therefore after passing that point we decided not to include any other companies in our sample.

3.2 Data Analysis

The analysis relies on the presentation of our company-based data discussed earlier using charts and diagrams, while the geographical focus is on Europe, the UK, the USA and Japan. More precisely, four charts a, b, c, and d are used in each case for the presentation of the results. In chart a there is information on the proportion of revenues generated abroad to the total revenues from 1997 until 2004 for both manufacturing and banking companies. This in a way is the main chart of the analysis as it provides the main insight as to whether and to what extend the globalisation in each sector and area is taking place.

Chart b will present information on the trend followed by the proportion of the assets generated abroad to the total assets of the banking companies. Chart b is presented as a robustness check of the results obtained by the analysis of the revenue figures. Finally charts c and d present the trend followed by the total revenues of the banking and manufacturing companies (chart c) plus the trend of the revenues abroad of the banking and manufacturing companies (chart d). We need to stress here that for charts c and d the first year of our sample period (i.e. 1997) was taken as the base year and then each of the graph figures were calculated by dividing the actual revenue figure of that specific year by the actual revenue
figure of the year 1997. This was done to facilitate the comparability amongst the graphs, the
sectors and the regions.

4. Results and Discussion

This section discusses, in turn, the results for European, UK, US and Japanese companies.
Following this the results will be brought together and further analysed as a whole.

4.1 Europe Based Banking and Manufacturing Companies

The first region under study is Europe. The European revenues and assets from the home
country include those located in one of the EU-15 member countries\(^6\), while revenues/assets
from abroad refer to non EU-15 member countries\(^7\). Table 3 below presents information
about the revenues and the assets of the European banks and manufacturing companies of the
sample.

\(^6\) Namely Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the
Netherlands, Portugal, Spain, Sweden and the United Kingdom.

\(^7\) In the case of the UK the same methodology is used when the UK is investigated in the European sample. But
when the country is investigated separately in section 4.2 only the revenues and assets from the UK will be
considered as home revenues/assets and all the rest are counted as revenues/assets from abroad.
From chart 3a it is obvious that the manufacturing companies have a more multinational business orientation than banking companies. At the same time, there is a more consistent upward trend in the revenues from abroad for the manufacturing companies, in contrast to the banking sector where after the initial increase up until the year 2000 it remains stable at around 23% to 24% from 2001 until 2004. This creates an opening gap between the sectors with manufacturing leading the multinational expansion trends. Chart 3b shows that the proportions of the assets located abroad for the banking companies follows the same general trend as the proportion of revenues generated abroad, which again supports the use of
revenues as an adequate globalisation measure. Charts 3c and 3d reveal that until the year 2001 the total/abroad revenues for the banking companies have been growing at the same or at an even faster pace than the total/abroad revenues of the manufacturing companies. But from 2001 there is a downward turn where the total revenues of the banking companies decreased up until 2003 where the upward trend started picking up again. On the other hand, in the case of the manufacturing companies, there is a more consistent increasing trend of the total and abroad revenues from 1997 until 2004, apart from a small slowdown in 2001-2002. Overall, until the year 2001 the banking total and international growth of revenues was marginally greater than manufacturing, but that changed from 2001 onwards where the manufacturing companies’ revenue growth came to the leading place.

From this analysis, it is clear that something must have happened around 2001 to 2002 to cause this slowdown in banking total and international operations. This shift could have been caused by either factors internal to the banking market, such as a change in the demand for banking services, or a potential exogenous shock. We believe that the most plausible explanation for such a downturn in our case is the latter, as the time of this occurrence coincides with two global major events. The first was the terrorist attack of September 11th 2001 in the USA, which affected the financial sector not only in the USA but at a global level including the European economy. This shock created conditions of increased insecurity and uncertainty making firms more cautious and reluctant to expand their operations and leading to the contraction of investment activity (Bloom et al., 2007; Ghosal and Loungani, 2000). This must have affected the manufacturing side as well, but to a lesser extent, as the slight slowdown of business from 2001 to 2002 in our data indicates. Another reason that makes us even more confident that the 9/11 attack was responsible for at least part of the slowdown observed in our data, is the bounce-back in the economic activity observed after 2003, which
is consistent with the effects of a temporary shock (Bloom, 2007), rather than with the persistent slowdown that typically occurs in response to a potential productivity and/or demand shock.\(^8\)

The second shock could have been the launch of the Euro from 2002. Even though it is expected that a single currency will reduce transaction costs, improve cost efficiency and create economies of scale and scope in the banking industry in the longer term, in the short term initial investment costs and potential restructuring of their operations may have been necessary which in turn may have led to a downward pressure on revenues (Schmiedel, 2007). In contrast to the 9/11 shock though, we do not believe that this could have significantly affected the manufacturing sector.

### 4.2 UK Based Banking and Manufacturing Companies

Even though it can be argued that the UK can be thought of a part of the European community (we have included the UK in our European sample of analysis earlier as well\(^9\)), we believe that it is of interest to investigate this country separately as well. Britain’s financial and banking industry is one of the leading industries in the country and one of the most influential in the world, while London is one of the most important global financial centres. In addition, since 1979 liberalisation policies have been emphasised. These factors can potentially create a unique environment, making Britain an interesting and important country to investigate separately from the rest of Europe. Contrary to the earlier analysis of the European sample though, here all revenues/assets generated in any other country outside

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\(^8\) See for example, Christiano et al. (2005).
\(^9\) Obviously the UK is part of Europe and should be included in the European sample, regardless of us investigating it separately as well. However, we have examined whether the exclusion of the UK from the European sample alters our results and found no significant differences in our findings.
the UK, including those coming from European Union countries, will be considered to be revenues/assets generated abroad. Table 4 presents information about the UK case.

As shown in chart 4a, the manufacturing companies start off with a greater multinational business base than that of the banking companies. The gap opens up rapidly from 2000 onwards when the manufacturing companies of the sample seem to have shifted their operations abroad even more, with their abroad revenues reaching 52% of the total revenues in 2000 and 57% in 2004. The revenues from abroad of the banking sector on the other hand followed a much flatter course starting from 29% in 1997 and reaching 30% in 2004. These trends lead to the manufacturing sector being definitely more internationalised than banking. Chart 4b reveals an almost identical trend for assets and revenues from abroad of the banking sample supporting the use of revenues as a globalisation measure.

Chart 4c shows that manufacturing business has been booming from 2000 onwards, a trend which may have been a result of an international expansion as chart 4d reveals, where a big increase of the revenues generated abroad takes place from 2000 onwards. This has not been the case for the banking sector, where even though the total and abroad revenues have been increasing this is at a much slower pace. It is interesting to observe here that in both charts 4a and 4b (and to a lesser extend in 4c) there is a slowdown of the total and (mainly) abroad operations from 2001 to 2002. This was more obvious for the banking companies where the revenues decreased, while in the manufacturing sample there was just a slowdown of the revenues growth rather than a decrease. This presents similarities to the Europe case presented earlier and we suspect that it is a result of the crisis that followed the 9/11 attacks in the USA that affected mainly global financial markets.
Overall, it can be concluded that the UK sample behaves very similarly to the European one. Here the manufacturing sector clearly is more internationalised than the banking one. In terms of the expanding trends of their revenues from abroad, even though the two sectors seem to start at a similar growing pace, eventually the manufacturing companies definitely lead the international expansion in the UK.
4.3. USA Based Banking and Manufacturing Companies

Turning now to the case of the United States, table 5 below presents the relevant data. In chart 5a the proportion of revenues generated abroad for the banking companies started at a much lower point in 1997 (15%) in comparison to the one of the manufacturing companies (38%). Yet since then it has been catching up reaching 29% in 2004, while the revenues from abroad of the manufacturing companies followed a flatter course reaching 40% in 2004. Even though at the end of our investigating period there is still an 11% gap between the proportions of manufacturing and banking revenues generated abroad, it looks very likely that at some point the banks may be able catch up with the USA manufacturing level, if the current trend continues. This indicates the extent to which the USA has been the main beneficiary of financial deregulation.

By examining chart 5b we can check whether the banking assets and revenues from abroad follow a similar pattern. It is obvious that from 1997 until 2001 they both have an increasing trend, which is more obvious in the revenues case. Nevertheless, while the abroad assets dropped from 2001 to 2002 and increased again the year after, the revenues from abroad seem to have a similar pattern to that but with a year’s delay. This could be due to the fact that what has affected the abroad assets of the USA banks may have had a lagged impact on the revenues. Again an obvious reason causing this drop could have been the 9/11 terrorist attacks.
Table 5: The USA sample

A possible explanation of the quicker adjustment of the assets, could be the fact that American banks decided to freeze or even call back some of their abroad investment as an immediate response to such a shock. This could have been a defensive reaction due to increased volatility and uncertainty. It is very likely though that the investments affected at this first stage were mainly those being involved in strategic asset seeking (see Dunning, 1993), rather than the revenue generating assets, as these assets are more sensitive to changes in company strategies. Consequently, the revenues may have not been affected immediately.
Yet the impact could be clearer later on, as the international strategic positioning of the companies will be compromised by the contraction of those strategic assets, resulting in reduced international performance. Nevertheless, we can still be confident that revenues can be used as an adequate enough proxy for globalisation instead of assets, as eventually they both seem to be affected by similar factors and follow similar trends (even if there is a small time lag).

Chart 5c reveals that the growth of the total revenues of the banks and manufacturing companies has been almost identical. This is not the case though for the revenues from abroad as we can see in chart 5d where it is obvious that the banks have been growing much quicker than the manufacturing, with the exception of 2003 where a slowdown in the banking revenues from abroad growth is observed.

The above analysis has indicated that the USA constitutes a different case than Europe and the UK. The large economic and financial shock of 9/11 or the market turmoil caused by financial scandals\(^\text{10}\) resulting in a much stricter regulatory environment imposed by the Public Company Accounting Reform and Investor Protection Act of 2002 i.e. Sarbanes-Oxley Act of 2002 (Coffee, 2005), did not seem to hinder the USA banking internationalisation. On the contrary, the evidence we have suggests that US banks have been expanding their operations abroad to a greater extent than their manufacturing peers and overall it can be claimed that in the USA it is the banking sector that seems to be expanding its international operations at a quicker pace.

\(^{10}\) A number of major corporate and accounting scandals took place at around the end of 2001 and beginning of 2002 including those affecting Enron, Tyco International, Adelphia, Peregrine Systems and WorldCom.
4.4 Japan Based Banking and Manufacturing Companies

Finally, the last country under investigation is Japan. Table 6 below presents information about the international positioning of both the Japanese banking and manufacturing companies of our sample. Chart 6a draws a different picture from all of the Europe, UK and USA. In the beginning of the investigation period, the proportion of the banking sector’s revenues from abroad was 30% which was substantially higher than that of manufacturing companies (20%), revealing a more internationalised banking sector. However, these two followed the opposite path as the former followed a continuous downward course (with the exception of the year 2001) reaching 13% of the total revenues in 2004, while the latter reached the 26% in 2004 after following a fairly flat yet increasing trend. Therefore, it can be observed that eventually the manufacturing sector at the end of our period of analysis was more internationalised and increasingly so.

Chart 6b reveals that the trend of the revenues from abroad for the Japanese banks has been very similar to that of their assets abroad. This is an indication that both revenues and assets may have been affected by similar factors, supporting again our assumption that revenues can be used equally well to the assets as a proxy for the degree of internationalisation. Charts 6c and 6d tell a similar story about both the total and the abroad generated revenue growth where in the case of the manufacturing companies there is a constant increase in both 6c and 6d while in the banking sector there was a constant decrease again in both charts, resulting in that opening gap in chart 6a.
Overall, it is clear that in the Japanese case there is a rapid decrease not only in the Japanese banking international expansion but also in the total banking operations from the beginning until the end of our period of investigation. This is something that comes as no surprise, as Japan’s banking and financial system had a major systemic crisis in 1997 resulting in the failure of several major financial institutions (see Hoshi and Hugh, 2000 and Hoshi and Kashyap, 2000 for a more detailed analysis of the causes and the effects of the Japanese banking crisis). Since then banks have not managed to fully recover from the crisis as our
data indicates. This finding is supported by Kanaya and Woo (2000) who stress the importance of weak corporate governance and the lack of an appropriate regulatory framework as some of the main factors to this poor financial recovery. This resulted in the banking sector from being originally more internationalised ending up at a lower level in comparison to the manufacturing sector.

4.5 Further Discussion of the Findings

From the above analysis a first observation that can be made is that even though there may be differences in the internationalisation trends in most of the cases presented it is obvious that there is a home bias in the companies’ sales for both the manufacturing and banking and for most of the regions studied. This finding is in line with earlier studies claiming that business cannot be described as fully globalised (see Tyson, 1991; Kapstein, 1991; Hirst and Thompson, 1996b) and companies still remain at the multinational level (MNEs) rather than becoming transnational (TNEs). A further, and arguably more interesting, point is illustrated by Table 7 below, where a comparative summary of the globalisation trends between banking and manufacturing is illustrating a different picture for every region under study. This table depicts the globalisation trajectories implicit in the results presented above. The top of the table summarises the growth of revenues generated abroad as either manufacturing faster than banking (M>B) or the reverse (M<B). The side of the table summarises the position with respect to the proportion of revenues generated abroad, either M>B or M<B. Within this schema Europe, UK, USA and Japan are located.

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11 An exception to that is the UK manufacturing companies were we see that the proportion of the abroad revenues are more than half of the total, especially during the last years of our investigation, revealing a more global scope of this market.
12 For a definition and the characteristics of an MNE and a TNE see Bartlett and Ghoshal, 1987; Dunning 1993 or Bourdeau et al., 1998.
Table 7: Globalisation trajectories

<table>
<thead>
<tr>
<th>Proportion of Revenues Generated Abroad, 1997 - 2004</th>
<th>Europe &amp; the UK</th>
<th>The USA</th>
</tr>
</thead>
<tbody>
<tr>
<td>M&gt;B</td>
<td>M&gt;B</td>
<td>M&gt;B</td>
</tr>
<tr>
<td>M&lt;B</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: M denotes manufacturing, B denotes banking.

For Europe, at the start of the investigation period manufacturing was more globalised than banking (in terms of a bigger proportion of sales from abroad), while the trends in the growth of revenues generated abroad in both manufacturing and banking have been approximately the same. At the end of our investigation period still the manufacturing sample is more globalised while a small opening gap between the internationalisation levels of the two sectors is observed, caused by a marginally faster growth in the revenues generated from abroad in the manufacturing sample. In general though, the banking industry has been following approximately the same trends as the manufacturing companies throughout our investigation period. The same picture is drawn for the UK as well. This is an interesting result as the UK trends seem to follow those of Europe, showing in that respect that those two regions may be closer than it may have been originally thought. Furthermore, for both Europe and the UK it can be claimed that the “follow the customer” hypothesis has been confirmed. This result is in line with other studies that have empirically investigated this hypothesis in a different context (see for example Sagari, 1992; Goldberg and Grosse, 1994; Moshirian, 2001 or Piscitello, 2003) indicating that the incentive to serve their manufacturing customers’ international operations could be the driving force for the banking expansion abroad.
The cases of the USA and Japan are somewhat different. In the former case, again manufacturing is more globalised than banking at the start of our period, but the revenues from abroad growth are greater for the banking sample. This growth trend continued throughout the whole period of investigation. Even though banking internationalisation levels have not overtaken those of the manufacturing sector yet, if international expansion of the banking sector continues at the same tempo it would be expected that the banks of our sample could potentially reach higher globalisation levels than their manufacturing peers (but see the comments below on the possible impacts of the current financial crisis). This faster growing pace of the banking international spread does not give any indication that the banking expansion abroad is following any trends set by the manufacturing, therefore reasons other than the “follow the customer” incentive may drive the US bank expansion abroad.

A potential explanation for this trend could be that banks may be exploiting potential increased efficiency gains through possible increased capital productivity in the foreign locations. Further analysis of our data along these lines is provided in the Appendix to this paper. It is clear that for the years under investigation not only the abroad capital productivity of the banking companies was increasing but also the home capital productivity has been declining giving the American banks a strong incentive to expand abroad in order to exploit the increased profitability opportunities presented in such a case. This internal globalising advantage for US companies has been reinforced by the external opportunities offered by financial deregulation.

Finally, in Japan contrary to all the previously mentioned cases, the banking sector starts off as being more globalised than the manufacturing companies. Nevertheless the growth of the
internationally oriented sales was bigger in manufacturing, with banking facing negative growth as a result of the 1997 crash and the crisis that followed it. This characterisation continued throughout our investigation period resulting in manufacturing being greater in terms of globalisation levels and maintaining higher growth rates for the revenues generated from abroad. To repeat, in this case we believe that following the banking and financial system crisis in Japan there has been a relative contraction in the international banking business. On the other hand though the manufacturing companies did not seem to have been affected as harshly and this is why there is this opening gap in favour of the manufacturing companies at the end of the period of investigation.

The trends exhibited in table 7 are obviously identified before the onset of the current financial crisis. While relevant current company data is obviously not available a few pertinent comments would seem to appropriate. To some extent the experience of Japan illustrates the possible impact of the current financial crisis. For this country the depression since 1979 has had an asymmetric impact on banking compared to manufacturing. But this effect occurred in the context of an otherwise buoyant international economy. Hence we can suggest an obvious truism that the banking sector will be affected by the current crisis but the extent to which this is greater or less than the impact on manufacturing depends on international demand in markets for manufactured goods. The latter in turn depends on the success of any anti-depression macroeconomic policies.

But the results identified in this paper, and summarised in table 7, allow us to draw a more subtle conclusion. It is clear that different regions occupy different positions in the matrix in the table and exhibit different globalisation trajectories. To this extent there will be different impacts of the crisis in different regions. Ignoring the issue of macroeconomic stability just
referred to it appears that the USA has most to lose from the banking crisis because of its position on the right hand side of the diagram and its pre-crisis trajectory towards the south east in the matrix. Europe (including the UK) and Japan have apparent trajectories that will be reinforced by the banking crisis. It follows from this that there need be no single set of policy responses appropriate in all regions. Furthermore we should not be surprised that the apparent banking regulatory discussions in Europe are different from equivalent discussions in the USA.

These different policy contexts obviously complicate a unified international response to the crisis. If a unified response to the banking crisis is considered necessary, and arguably this is the case given the severity of the crisis, table 7 suggests that there is no obvious policy core for a unified response. These brief comments can be linked to the central theme of this paper. The different relative positions of banking and manufacturing in the core regions of the world economy not only complicate our understanding of internationalisation and globalisation but also appear to suggest an equally complicated policy context for the current banking crisis.

5. Conclusions

This paper has focused on the investigation of the extent to which processes of internationalisation of production are taking place in the manufacturing and the banking sectors and the degree to which banking follows the manufacturing expansion, i.e. if there is evidence supporting a “follow the customer” incentive for a banking international expansion. As far as the extent to which banking globalisation is taking place, our findings suggest that, broadly speaking, banking internationalisation is happening. Nevertheless, there are differences in the trends observed in each region under study, while in almost all the cases a domestic bias in the companies’ operations has been observed. However, this weaker host
market position could be interpreted as well, as the outcome of a rational preference to the
domestic or regional based operations. Apart from the home bias of operations that any
company would be expected to have, this home bias could be due to the fact that MNEs from
those regions under study have the extra motivation to operate domestically, since the region
their headquarters is based in attracts international production. In that sense, companies can
enjoy potential agglomeration advantages in their home base, while in the case of the Europe
the broader common organisational, regulatory, institutional and financial environment would
also help the deepening of integration at the regional level. Finally the fact that Europe, USA
and Japan can provide the right conditions for more extensive and dynamic changes in the
companies’ operational environment, results in the creation of more opportunities for growth
for the MNEs headquartering there, and therefore a further incentive for domestic production
allocation.

Concerning the investigation of the “follow the customer” incentive again the findings we
obtain differ depending on the location under study. Starting with Europe and the UK, in both
those regions banking industry internationalisation appeared to have followed similar trends
to that of manufacturing, while the latter has been leading in terms of the levels of production
allocated abroad. This is a result which can be claimed that confirms the “follow the
customer” hypothesis for the Europe and UK regions. However, this has not been the case for
the USA or Japan. In the first case, even though the manufacturing companies appear to have
a more internationally dispersed operations base, banking companies exhibit greater growth
rates on their internationalisation levels, indicating that the American banking MNCs of our
sample could reach higher globalisation levels than their manufacturing peers in the future
(subject to qualifications about the current financial crisis). Overall, the “follow the
customer” incentive does not seem to affect the American sample of this study, and one
probable explanation could be that banks may be trying to exploit increased efficiency gains through a possible increase in capital productivity in the abroad locations, therefore expanding their international operations at a greater pace. However as we do not have access to a large database to verify this assumption and the fact that the banking crisis has taken place a few years after the last year of the data sample’s observations, it somehow makes us sceptical about how much such a trend would continue. Finally in the case of Japan, again the “follow the customer” incentive does not appear to greatly influence the banking decision to expand abroad for the time period under investigation. Even though banking starts off as being more globalised than manufacturing, nevertheless the growth of international operations was bigger in manufacturing, with banking facing negative international growth. This was probably caused by the financial crash of 1997, which has severely affected the Japanese banking and financial system, and it appears that banks have not yet fully recovered from that shock.

Overall it was shown that globalisation may vary depending on which region is under study, while one of the main contributions of this paper has been the identification of such differences in globalisation patterns between banking and manufacturing across regions not spotted by the earlier literature. Unfortunately the lack of a more detailed data set that would provide information on a more precise revenue and asset geographical breakdown (which would allow for a more in depth investigation of the “follow the customer” incentive to take place) and would include information about the recent financial crisis, does not allow for more concrete conclusions to be drawn about the current ongoing trends and further research is needed on that matter.
Appendix

Capital Productivity

The level of international expansion of the banking sector can be expressed in terms of its home and abroad productivity of capital, as the equations below illustrate:

\[
k_i/k = k_i/r_i * r/r * r/k, \text{ or } k_i/k = [1/(r_i/k)] * r_i/r * r/k \tag{1}
\]

\[
r/k = r/r_d * r_d/k_d * k_d/k, \text{ or } r/k = [1/(r_d/r)] * r_d/k_d * k_d/k \tag{2}
\]

From (1) and (2):

\[
k_i/k = [1/(r_i/k_i)] * r_i/r * [1/(r_d/r)] * r_d/k_d * k_d/k \tag{3}
\]

Where \( k \) denotes the assets of banking companies, \( r \) stands for their revenues, while subscripts \( i \) and \( d \) denote international and domestic. Equation (3) states that the proportion of assets located abroad can be expressed in terms of the inverse productivity of capital located abroad \([1/(r_i/k_i)]\), the proportion of revenues generated abroad \((r_i/r)\), the inverse proportion of revenues generated at home region \([1/(r_d/r)]\), the productivity of capital located at home region \((r_d/k_d)\) and the proportion of assets located at home region \((k_d/k)\). Based on this, the importance of capital productivity in the context of banking international expansion is set out in this appendix as a complementary explanation of the trends observed for each region under investigation.

The USA Case

From the data analysis so far we know that the proportion of assets located abroad for the USA banking companies \((k_i/k)\) has followed a rather stable flat course from 1997 until 2004. Consequently, the proportion of assets located at home region must have followed a stable flat course as well. We also know that the proportion of revenues generated abroad for the USA banks \((r_i/r)\) followed an upward trend while the proportion of the revenues generated at
home \((r_d/r)\) followed a downward course. Consequently, if \(r_d/r\) has been decreasing, \([1/(r_d/r)]\) has been increasing.

The following figure shows the course of capital productivity for the home region \((r_d/k_d)\) and the productivity of capital abroad \((r_i/k_i)\) for the USA banks.

Figure: Capital Productivity in the USA

![Graph showing capital productivity in the USA](image)

Source: OSIRIS, ONESOURCE, annual reports

From the above chart it is obvious that capital productivity in the home region has followed a flat course from 1997 to 2000 and then a downward course from 2000 until 2004, while the productivity of capital abroad for the USA banks has risen from 1997 to 2004. Additionally because \(r_i/k_i\) has risen, \(1/(r_i/k_i)\) must have gone down. So from equation (3) above we have:

\[
k_i/k = [1/(r_i/k_i)] * r_i/r * [1/(r_d/r)] * r_d/k_d * k_d/k
\]

\((\leftrightarrow)\) \((\downarrow)\) \((\uparrow)\) \((\uparrow)\) \((\downarrow)\) \((\leftrightarrow)\)

From the above equation we can see that the two main indicators as to whether the globalization process is taking place, \(k_i/k\) and \(r_i/r\), give different signals. \(k_i/k\) shows that the proportion of assets located abroad for the USA banks have followed a stable flat course overall, while \(r_i/r\) indicates that the proportion of revenues generated abroad have increased for the time period in question. In this case we can not tell with certainty whether the
The examination of the data available firstly indicates a rise in the capital productivity abroad, but this effect cannot give any clear indication as to whether the companies have an incentive to produce abroad. This happens because the revenues generated abroad $r_i$ consists of two components: $r_i = r_i^p + r_i^e$. Where $r_i^p$ is revenues that came from the selling of goods and services abroad that were produced abroad; and $r_i^e$ is revenues that came from the selling of goods and services abroad that were produced domestically and exported abroad. If $r_i^p$ increases that would be a clear indication that the process of globalization is taking place because production of companies abroad is taking place. On the other hand, if $r_i^e$ was increasing that would give an indication of an exporting process rather than a globalization trend. This complexity does not exist with the assets located abroad as $k_i$ is clearly defined as the assets that are only located abroad. Unfortunately, the data does not allow us to separate $r_i$ into $r_i^p$ and $r_i^e$. Therefore, it is not clear whether this rise of productivity of the capital abroad for the USA banks was due to a globalization process or due to an exporting process.

Even though this problem is hindering a straight forward answer as to whether a globalization process is taking place or not, the fact that the productivity of capital abroad has risen throughout the years of research for the USA banks does not reject a globalization process taking place. The reason for that is that even though it does not provide a clear picture as to whether the banking companies have an incentive to produce abroad, it is consistent with the
possible scenario that partly this increased productivity of capital abroad is due to an increased production abroad. In turns, this is going to give an incentive to the USA banks to shift their production abroad and globalize their business. This is because a highly competitive profit maximizing firm, like the international banking corporations under investigation, which operate in an economic and financial environment where the international capital transfers have been extremely facilitated, such as the international banking environment, if it realizes an opportunity for increased profits abroad through an increased capital productivity abroad, it has a great incentive to shift its assets and production abroad and earn more profits.

Finally, the element that definitely gives banks a clearer incentive to transfer their production abroad, and thus triggers the globalization process, is the decreasing capital productivity at the home region. That is happening because when the capital invested at the home region is not as productive as the capital invested abroad, a profit maximizing company will want to stop investing its capital domestically and shift its production abroad. Therefore, since the productivity of capital at home region \((r_d/k_d)\) for the USA banks has been decreasing in the last few years of research, indicates that the USA banks have a strong incentive to shift their production abroad and globalize their business.
References


