INDONESIA'S MISSING MULTINATIONALS: BUSINESS GROUPS AND OUTWARD DIRECT INVESTMENT

Michael Carney
John Molson School of Business, Concordia University
mcarney@jmsb.concordia.ca

Marleen Dieleman
National University of Singapore
marleen@nus.edu.sg

ABSTRACT

Why do some emerging markets produce more multinational enterprises (MNEs) than others? Countries such as India and China have recently originated a number of dynamic MNEs whose success in international markets generates important economic benefits for the home economy. Yet in many emerging markets a comparable population of MNEs has failed to appear, an absence that may retard economic growth. Indonesia is a case in point. Official statistics show that Indonesia has underperformed its outward foreign direct investment (ODI) potential. In this paper we describe the internationalization record of Indonesia's major business groups. Using an archival analysis method we find that, with a few exceptions, Indonesia's largest business groupings are focused almost exclusively upon the domestic market. We advance two explanations for this evident underperformance. The first suggests that the apparent absence of MNEs is an accounting error because firms' outward investment exists but is under-reported in official statistics. The second suggests that the statistics are correct and that ODI by Indonesian firms is impeded by a combination of institution and firm-level factors that arrests the internationalization of all but the very largest firms. We discuss policy implications and reflect on the theory of emerging Asian multinational enterprises.

KEYWORDS: Emerging market multinationals, Outward Direct Investment, Indonesia.

CITE AS:
Carney, M., & Dieleman, M. 2011. Indonesia's missing multinationals: Business groups and outward direct investment. *Bulletin of Indonesian Economic Studies* 47 (1), 105-126.

INTRODUCTION

Multinational firms from Asian countries such as India and China are becoming major players in the globalized world economy and their recent dynamism has attracted much attention from scholars (eg: Elango and Pattnaik, 2007; Buckley et al, 2007). Economists and management scholars agree that that outward direct investment (ODI) by emerging market MNEs strengthens their competitive advantages and provides their countries of origin with several economic benefits, such as improved export performance and access to foreign technology(UNCTAD, 2006). Consequently, the developmental implications of ODI underperformance is concerning for policy makers when domestic enterprises lag in their international competitiveness. Existing research focuses almost exclusively on emerging markets producing successful multinationals but the question of why some emerging markets engender relatively few MNEs has received scant attention.

The case of Indonesia is paradoxical in this regard: existing research suggests that some Indonesian firms have successfully internationalized (Lecraw, 1993;), especially those owned and controlled by ethnic Chinese Indonesians (Liu, 2001; Sato, 1993; Yeung 2004) yet official statistics show that ODI from Indonesia's is relatively low limited compared with neighboring states (UNCTAD, 2006). Opinion is divided on how to interpret Indonesian ODI statistics. Indonesian officials often point to the idiosyncrasies of their economy and stress factors such as capital flight, tax evasion, and other disadvantages of ODI. Officials also assume that ODI metrics underestimate actual outward investment because Indonesian firms may misreport or hide their foreign investments. Consequently, the international performance of Indonesian firms is unclear and government ODI policy remains unresolved. In this regard, improved understanding of Indonesian firms' ODI performance can provide insight to the policy debate on whether the Indonesian, and other emerging market governments, should implement policies to accelerate or otherwise influence their ODI.

We contribute to this debate by documenting the internationalization patterns of Indonesia's largest business groupings and developing plausible explanations for them. To do so we use an archival analysis methodology that identifies the ODI events by Indonesia's largest business groups over a 13 year period. Whereas official statistics paint an aggregated overview of ODI, the advantage of our methodology is to provide fine-grained insight into the international investment record of specific firms. We focus upon the ODI of firms affiliated with large Indonesian business groups because they are probably the best endowed with the resources necessary for international expansion. We begin with a brief review of evidence and theory on emerging economy ODI. Subsequently, we outline some shortcomings in the accounting of ODI in Asia's emerging markets. We report our internationalization findings on Indonesian business groups and suggest two explanations. We conclude with policy implications and suggestions for future research.

FDI and ODI IN ASIA

In recent decades Asia's industrializing states have embraced inward foreign direct investment (FDI) as part of their industrial policy programs. States such as China, Korea, Malaysia, Thailand, and Singapore have offered generous investment incentives to foreign MNEs to boost economic development. Since the early 1970s Indonesia too has made its foreign investment rules more accommodating, albeit with occasional backtracking (Hofman, Zhao and Ishihara, 2007). On the other hand, industrializing states have been more circumspect about the promotion of *outward* direct investment by domestic firms due to concerns about capital flight, tax evasion, and the fear that ODI 'hollows out' domestic industry by exporting employment to other countries. Recently, there has been something of a sea change in the way states view the importance of having their own multinationals and recent statistics report a surge in foreign direct investment from emerging economies, with the lion's share originating in Asia (UNCTAD, 2006).

This is because states increasingly recognize the value ODI and countries such as China and Malaysia are actively supporting a 'Go out' international thrust. State accelerated development of local multinationals can enhance national competitiveness by improving access to foreign 'best practice' and technological know-how. The acquisition of knowledge assets can spill-over and diffuse more widely as local suppliers and rivals emulate the practises of the MNE. Foreign technology and practice is often more valuable in the hands local firms because they are more likely to be adapted to local conditions by firms with superior knowledge of domestic circumstances (Szulanski, 1996). Moreover, ODI is critical to consolidate exports sales and market expansion. The World Bank (1994) noted that Indonesian business groups' export performance is limited compared with their Korean counterparts, who have consolidated export markets and gained access to advanced technologies by means of foreign investments. ODI also helps firms to develop international networks and relationships where they can initiate activities rather than serving as dependent subcontractors at the periphery of international value chains (Gereffi, 1994). Research suggests that Indonesian firms engaging in ODI improved both their management expertise and export performance compared with firms that did not make such investments (Lecraw, 1993). Concerns that ODI results in the loss of domestic employment may be overstated as available evidence suggests ODI results in a marginally positive impact upon aggregate employment levels (UNCTAD, 2006: 189) and is more often associated with the creation of higher value-added managerial and scientific jobs.

While Indonesia's inward FDI performance has been quite strong, especially before the Asian Crisis of 1997-1998, its ODI record is relatively poor compared with neighboring countries such as Malaysia. Figure 1 shows that in 2006, at some US$2.7 billion, Indonesia's ODI was less than half that of Malaysia. Indonesia's ODI in 2008 was just 4% a percentage of gross fixed capital formation compared to a figure of 27% for Malaysia.

----FIGURE 1 ABOUT HERE----

In addition, Indonesia has produced few substantial multinational enterprises. In 2006, Indonesia did not have a single representative firm in the list of UNCTAD's top 100 of non-financial transnational corporations from developing countries. Malaysia, in comparison, had six representatives and Singapore thirteen. Countries such as Thailand and Philippines were also represented. In the past five years Indonesia scores below countries such as Thailand and Malaysia in terms of the number of new overseas greenfield investments. In summary, each of these metrics point to relatively poor international investment record.

THEORORETICAL APPROACHES ON ODI FROM EMERGING MARKETS

Research on the emergence of emerging market multinational enterprises, variously described as ‘third world’, ‘late-mover’, ‘peripheral’, and ‘dragon’ multinationals has been underway for several decades (Lall, 1983; Lecraw, 1983; Mathews, 2006; Wells, 1983). More recently, the emergence of Chinese and Indian MNEs has given new momentum to this research stream. One point of consensus in this research is that the success of Western multinational enterprises is attributable to the creation and leverage of proprietary technological and organizational capabilities (e.g: Bartlett and Ghoshal, 1988; Dunning, 1977). In contrast scholars believe that firms from emerging markets typically lack firm specific advantages required to complete successfully in international markets (Wan and Hoskisson, 2003). This is because economic and competitive conditions in the host country provide few country specific advantages conducive to the development of world-class organization and technological competence. Because emerging market firms are located far from sources of innovation, sophisticated customers, and the challenging competitive dynamics that hone the competences of firms more favorable environments, they are encumbered by a liability of origin. In some emerging markets “national champions” have appeared that compete domestically on the basis of local advantages, such as close ties with government. However, these firms find that their local advantages are likely to dissipate in foreign markets (Hu, 1995).

The consensus of research on emerging market multinationals is that many firms internationalize to acquire foreign resources and competences that are unavailable locally (e.g. Luo and Tung, 2007; Yiu, Lau and Bruton, 2007). Child and Rodrigues (2005), for example, suggest Chinese firms’ international strategies address competitive *dis*advantages. To bring their organizational and technological skills up to par firms must invest considerable resources in learning (Wright, Filatotchev, Hoskisson and Peng, 2005), such as through strategic partnering (Ernst, 1998; Tsang, 2002) and gradual accumulation of skills, information and technologies (Hobday, 1995; Kock and Guillén, 2001). To the extent that emerging market firms can leverage their competencies in foreign markets, scholars think that these skills are derived from the capacity to manage in harsh or corrupt environments (Cuervo-Cazzura and Genc, 2008), but these skills are of less value in more advanced markets.

Another stream of research suggests that home country institutions matter for ODI (e.g. Peng, Wang, and Jiang, 2008). However, scholars disagree about whether home country institutions are an asset or a liability. There are several clear examples of both an asset and a liability view. On the liabilities side weak home country institutions, such as unenforced product safety standards, can create negative perceptions in foreign buyers of a country’s enterprises that inhibits their foreign expansion (Cuervo-Cazurra, Maloney, and Manrakhan, 2007). On the other hand, home country institutions can be an asset if they help facilitate the mobilization of capital to support ODI by national champions, as instanced in Korea and China (Aggarwal and Agmon, 1990; Nolan, 2001). Another view suggests that ODI by firms from emerging markets is a response to poor quality home institutions. The push of negative home country institutions and the pull of foreign country institutions drive ODI as firms seek to escape harsh home-country institutional constraints (Witt and Lewin, 2007) or political risks associated with operating in one volatile market. Government discrimination may favor the internationalization efforts of some firms while hindering others. Ironically, negative government discrimination may drive internationalization efforts. For example, denied access to domestic sources of capital small high-technology firms may internationalize to access favorable capital markets abroad

(Yamakawa et al., 2008). Boisot and Meyer (2008) suggest that Chinese firms may internationalize because the administrative and transactions costs of domestic expansion exceed the costs of foreign expansion. In Indonesia and Malaysia, negative government discrimination towards businessmen of Chinese descent may spur internationalization. In summary, extant research suggests that emerging market firms internationalize both because of and despite home country conditions.

In view of the rise in ODI from emerging markets in the last decade, the literature tends focus primarily on why firms internationalize (drivers) rather than on what obstacles might prevent firms from competing in global markets (inhibitors). Our contribution is to complement extant literature by looking at the interplay between institutional factors that enable and inhibits internationalization and how these impact on different firms. In doing this we help explain why some firms fail to internationalize. In combination, theories of institutional drivers and obstacles promise to offer a more balanced account of globalization of firms from emerging markets.

ACCOUNTING FOR ODI IN EMERGING MARKETS

Scholars typically use aggregate statistics such as the volume of annual inward and outward FDI flows to indicate a country's international investment performance. Business scholars also use firm-level indicators such as the percentage of sales derived from overseas and/or the percentage of assets located outside the home country. However, official statistics on ODI collected by organizations such as the OECD and United Nations, and used to construct country-level and firm-level indexes of internationalization, do not necessarily provide an accurate picture of ODI from emerging markets. Due to institutional factors and firm practices in emerging markets, these statistics may significantly over- or underestimate the true level of ODI activity.

One indication of overestimation is that a small number of emerging economies is responsible for a very high share of ODI outflows. For example, in 2005 just four countries (Hong Kong, British Virgin Islands, Russia and Singapore) accounted for 60% of the stock of ODI from developing and transition economies (UNCTAD, 2006). Much of this presumed investment may be statistically inflated by the phenomena of round tripping, which refers to capital outflows channeled offshore into special-purpose entities that are subsequently return the funds to the economy of origin, usually to take advantage of inward foreign investment incentives.

Contrarily, official statistics may understate the extent of emerging economy ODI. Official statistics on ODI are founded on the assumption of direct or indirect ownership of subsidiaries, associate companies, and branches by a common parent (OECD, 1999). This assumption may be invalid if firms display fragmented ownership or if they achieve control over foreign firms by non-ownership means. Firms in emerging markets are often organized as business groups in which inter-organizational linkages are not always characterized by legal ownership but are integrated through a variety of other social and informal mechanisms (Khanna and Rivkin, 2006). Business groups affiliates located in different national jurisdictions may "tunnel" resources from one affiliate to another through devices such as related party transactions (Cheung, Rau and Stouraitis, 2006). In addition, investment and trade are often conducted through ethnic and family networks in a manner that blurs the origin and destination of capital flows (Light, 2005; Rauch, 2001). To the extent that ODI statistics reflect ownership assumptions that are not prevalent in Asia then they might incline us to underestimate the true extent of a firm's international activities.

In much of Asia a substantial proportion of private sector firms are affiliated with a business group (La Porta, Lopez-de-Silanes and Shleifer, 1999). In Indonesia this figure is almost 70% (Claessens, Djankov and Lang, 2000). This fact poses a considerable empirical challenge because capital flows among affiliates are often nontransparent. In emerging markets formal institutions typically provide little support for business and firms come to rely on informal institutions such as family ties, government connections and business group structures to support transactions with their business partners. Indonesia ranks poorly on country corruption measures such as Transparency International's corruption perception index and many firms have adopted pyramidal and opaque corporate governance structures that are believed to facilitate and obscure inter-firm resource exchanges (Almeida and Wolfenzon, 2006; Morck and Yeung, 2003). Pyramidal structures and weak disclosure standards suggest that financial data about individual companies may paint a poor picture of the disposition of a firm's assets. As such, firm-based measures of internationalization, such as the UNCTAD list of largest transnational firms from emerging markets (which is calculated based on a listed firm's overseas assets and sales derived from annual reports) may paint an inaccurate picture of firms affiliated with Indonesian business groups. Moreover, many Indonesian outward foreign investments might not be initiated by publicly listed companies, because families have an incentive to maximize control over foreign currency management within the group, which would be subject to restrictions if a listed company is involved.

It is generally believed that official statistics of Indonesia's FDI and ODI suffer several shortcomings (Hattari and Rajan, 2008). Experts believe official ODI figures are understated. Indeed, our interviews suggest that Indonesia's large business groups face incentives to "hide" their foreign investments. Because the owners of most of the large business groups are of Chinese descent, ODI carries the stigma of lack of loyalty to Indonesia, and is often viewed negatively in the Indonesian press. To avoid problems, large business group owners often set up internationalization platforms in Hong Kong or Singapore, from which internationalization is pursued. Such activities prevent the foreign investments from being reported in Indonesian statistics.

ARCHIVAL ANALYSIS METHODOLOGY

We use a qualitative archival analysis method to complement official macro-level and firm-level statistics, namely systematic collection and coding of published news sources. We decided to focus on business groups because most Indonesian firms operate as part of a group. In addition, the UNCTAD list of the world largest transnational companies from developing countries shows that many of emerging market multinationals are business groups. We first identified the largest business groups in Indonesia, after which we documented cases of their internationalization using the Lexis Nexis database of worldwide news articles. To contextualize our results and facilitate explanations, we conducted background interview with several bankers and executives from the Jakarta business community.

First, we identified a list of Indonesia's top 25 domestic privately owned business groups. Because most Indonesian business groups are owned by families we were able to estimate the approximate size of the business groups from reports of family wealth. We constructed a list of the largest groups in the country based on the following four sources: 1.) a report on Indonesia's largest business groups developed by UBS; 2.) Forbes' report on Indonesia's 40 richest families; 3.) the September 2007 issue of Globe Asia magazine (a local business magazine), which has produced a list of the top business groups as well as 4.) the August 2007 issue of Globe Asia with a list of the richest Indonesian individuals. We limited ourselves to the top 40 of each source (in the case of UBS there was no ranking). The sources converged on what were the main 15-20 groups, and a more varied list of the smaller groups. Based on size and inclusion in multiple sources we selected 25 business groups. An overview of the four lists and our combined list can be found in Table 1.

----TABLE 1 ABOUT HERE----

Secondly, we conducted a structured search each group's foreign business activities in the Lexis Nexis news media database. Substantial foreign investments are typically reported in the business news media, either in Indonesia or in the country receiving the investment. Using each group's names as keywords resulted in a considerable numbers of articles for each of the top 25 groups (Table 2). In addition, for each group we performed complementary searches using the names of the group owners, or the names of prominent group-affiliated companies to deepen the pool of articles on each group's activities.

Third, we conducted a content analysis and coding procedure recommended by Boyatzis (1998) and used in an Indonesian context by Dieleman and Sachs (2008). We first condensed the raw data into "business events", which are discrete strategic decisions taken by a focal company. Examples of events include starting a new line of business, forming a strategic alliance, exiting a business, initiating a merger, expanding production capacity. Events that were a continuation of an already existing line of business were not taken into account such as for example the introduction of a new brand or the upgrading of an existing manufacturing plant. Between 1994 and 2006, a period of some 13 years, we identified a total of 958 business events (n=958) for our sample. We selected 1994 as a starting point because prior to that year the Lexis Nexis database contained too few events for most of the top 25 companies in the list.

Fourth, to determine a business group's international activities we employ a simple count of reported ODI occurrences, using presence/non-presence coding of reported events (Boyatzis, 1998). In this way we identified 197 *(n*=197*)* unique ODI cases and their destination. In this way, we created a 13 year inventory of foreign investments by large Indonesian business groups. Note that the use of presence/non-presence coding does not enable us to assess the importance of any specific ODI event. This can be achieved by going back to the original rich data about each event and interpreting separate events as an emergent pattern. Using the richer underlying data is used for building various explanations for our results, which now follows.

In concluding this section we note some shortcomings with our archival analysis methodology. Not all foreign investments are reported in news media articles there is typically a bias toward the reporting of large investments. As with all sources, news articles can also only partially resolve the nondisclosure problem of foreign investments. For example, conversations with members of the Jakarta business community suggest the existence of substantial foreign investments which have gone unreported in news media articles. Consequently, we expect that our data could be biased because some groups have adopted non-disclosure policies in their corporate communications. Nevertheless, despite these evident shortcomings we propose that our data, in combination with existing macro-level and firm-level statistics, provide a fuller and more accurate depiction of Indonesian business groups' ODI activities.

RESULTS

Table 2 contains, respectively, the sample of 25 business groups, the keywords used in the Lexis –Nexis seach, the number of news articles retrieved for each business group, the number of business events abstracted, the number of ODI events. One group (Wings) was discarded because there was too much "noise", there were too many companies and products named Wings worldwide, and it was not easy to distinguish whether the Indonesian company was concerned. Out of the 24 remaining companies, we found foreign investments in our database for 17 groups.

-----TABLE 2 ABOUT HERE----

Limited internationalization

The data in table 2 suggests that Indonesian business groups have little appetite for international activities. Of the largest 24 groups, most have hardly ventured abroad in the past 13 years. Our results show that eight groups (33%) do not display any internationalization – at least not in a manner that is captured by our methodology. An even larger proportion display very limited international activities. In general, groups without any foreign investments tend to be smaller.

We labeled groups with more than 10 ODI events over the 13 as 'emerging market giants'. We labeled groups with between 6 to 10 ODI event as intermediately internationalized and we labeled groups with five or less ODI events as domestic groups. Based on this classification, only 3 groups (Salim, Lippo, and Sinar Mas) can be properly considered as emerging market multinationals. Moreover, only 30% of our groups had more than 5 ODI events projects abroad over a period of 13 years. This low level of internationalization is in marked contrast with extant literature on ethnic Chinese firms from Southeast Asia, which are typically portrayed as transnational empires that invest extensively in the region and in China (Weidenbaum and Hughes, 1996; Yeung, 2004). Given that all except 3 business groups in our sample are controlled by families of Chinese descent, except for two or three notable exceptions our research does not support the notion of these families being "transnational" enterprises. Rather table 2 suggests a substantial category of Indonesian business groups are focused almost exclusively on the domestic market.

Our results are in line with official ODI statistics that depict Indonesia's ODI as limited compared to surrounding countries. To gain perspective on this official figure, consider a few examples from our database. In 2006 alone, we recorded 18 foreign investments for the LIPPO group. Returning to the original news articles to assess the significance of these investments we found that Lippo's media reported investments sum to almost US$ 2 billion, whereas Indonesia posted an official ODI of US$ 2.7 billion in 2006. While LIPPO is a large group it seems unlikely that they alone account for almost all of Indonesia's ODI in 2006. This example suggests that errors in either or both figures are likely because official statistics underestimate ODI and because reported investments may not match actual investments. However, despite these evident inaccuracies our data appear to point in the same direction as the official statistics in the sense that we found relatively limited ODI among the population of Indonesian's largest business groups.

Distribution of ODI occurrences

Figure 2 provides the distribution of the 197 foreign investments per company. Salim and LIPPO represent 38% of the total business events inventory but account for almost 70% of the reported ODI events, suggesting that these two groups are the most internationally active firms in among Indonesian business groups. The news reports show that these groups have established footholds in Hong Kong and Singapore, from where each has diversified internationally. A third group, Sinar Mas, displays a similar pattern albeit on a smaller scale. All three groups control listed companies in Singapore and have appointed second generation family members as executives responsible for directing the internationalization of their group's activities. By off-shoring the locus of their international thrust these groups can avoid charges of "capital flight" within Indonesian and their investments are unlikely to turn up in official ODI figures of Indonesia. In this respect, our database is more complete than official data.

ODI destination

Figure 3 provides the destination for Indonesian business groups ODI. The primary destination of Indonesian ODI is ASEAN or China. Investments levels in China and India are not surprising given the size of these economies and their rapid growth levels. The literature on ethnic Chinese family groups suggests that Chinese Indonesians may be inclined to invest in their ancestral country, which may also play a role. To the extent that Indonesian business groups invest in developed countries, it is mostly in nearby Australia. This pattern of investments shows that most Indonesian business groups are at primarily regional players (rather than global players), a phenomena that has been documented for other Asian firms (Collinson and Rugman, 2007).

While much of Indonesian ODI is destined for other emerging markets, including those in East and Southeast Asia some firms have invested in more distant emerging markets in Latin America (Raja Garuda Mas), Africa (Kalbe Farma), the Middle East (Bakrie, Salim), and Central Asia (Bakrie, Salim). These trends are consistent with explanations that suggest emerging market firms are more likely to invest in other emerging markets because these markets share institutional characteristics that are similar to the country of origin home (cf. Cuervo-Cazurra and Genc, 2008). For example Buckley et al find (2007) that Chinese firms invest heavily in countries characterized by high political risk suggesting that Chinese MNEs may enjoy a proprietary advantage in managing in difficult institutional contexts.

Longitudinal Trend

Our data shows significant fluctuations in ODI that are likely due to variation in the business cycle (Figure 4). During and immediately after the Asian Crisis of 1997-1998, ODI fell to very low levels. More recently, however, ODI shows a positive trend. However, in combination with the results discussed above, this positive trend may be driven primarily by a small number of increasingly global firms, and obscures the prevailing tendency of limited ODI in the majority of the population of Indonesia's large business groups.

----FIGURE 2 ABOUT HERE----

----FIGURE 3 ABOUT HERE----

----FIGURE 4 ABOUT HERE----

DISCUSSION: EXPLAINING INDONESIA'S MISSING MULTINATIONALS

Relative to its neighbors in the region Indonesia originates limited volumes of ODI. Our analysis finds that these limited volumes are driven by a small number of internationally active business groups. We find that the largest proportion of Indonesian business groups is focused on domestic activities. To the extent that internationalization typically strengthens a firm's competitiveness as well as imparts advantages in the wider economy then Indonesia's economic development may be impeded by the absence of a larger number of home-grown multinationals. Given the accounting ambiguity about international capital outflows from emerging markets we now consider whether both official statistics and our methodology have underestimated the true extent of Indonesian firms' international activities. Secondly, we consider whether our methodology accurately depicts the limited internationalization of Indonesia's business groups, and discuss the extent to which home country institutions explain the patterns we documented.

Hidden Dragons?

The first explanation is a 'hidden dragons' explanation, which suggests that home country institutions cause firms to internationalize in a manner that is not readily identified by conventional methodologies. This explanation suggests that the Indonesia's missing MNEs represents is a 'type two error' or false negative: ODI is significant but we do not see it! A type two error may be explained by the fact that home country institutions drive significant flows of ODI into a large informal transnational economy (Portes and Haller, 2005). If ODI occurs with greater frequency than we are able to detect then Indonesian ODI could resemble an iceberg whose size is in fact much greater than the visible tip suggests. It is also possible that our sample of Indonesia's largest 24 business groups is biased. If the large business groups in our sample are more locally oriented than population of freestanding firms or the affiliates of smaller groups then the missing MNEs might be found among the latter. Our method is unlikely to capture ODI in smaller firms because their international activities do not draw the attention of the international media.

A second possibility is that Indonesian institutions may encourage business groups to conceal their ODI activities in an informal international economy. The informal economy consists of a range of activities that are *unreported*, *unrecorded*, or *informally organized* (Portes and Haller 2005). We cannot say with certainty that the groups in our sample are engaged in any or all three forms of informal activity but we enumerate them as a guide to further research.
First, it is well-established that high tax rates can stimulate increase visible ODI as firms seek to offshore activities to lower tax jurisdictions (Caves, 1996). Equally, high tax rates can stimulate tax evasion through invisible intra-firm transfers such as the use of special purpose entities registered in tax havens (OECD, 1999). Scholars are beginning to investigate how governance structures in emerging market business groups can be used to facilitate tax evasion (Chang, 2003; Desai, Dyck, and Luigi, 2007). More generally opaque business groups' governance structures allow cash to flow upwards into privately held family firms that may seek to preserve family wealth to evade home country taxes by channeling resources into *unreported* foreign investments. While our data are unable to tease out such activity, our interviews with analysts

and bankers suggest that it may be widespread among Indonesian groups. One source with experience of Indonesian business groups explained in a personal interview that, in his view, tax reduction was the main rationale for the complex legal structure of Indonesian business groups, which tended to span multiple jurisdictions.

Second, it is well-established that ethnic diaspora constitute important networks that facilitate international trade (Tung and Chung, 2010; Rauch, 2001). Ethnic based business groups may invest in ventures through minority investments but if investments in such projects constitute less than 10% of the share capital then they are recorded as portfolio investments. Moreover, Morck, Wolfenzon and Yeung (2005) document how family business groups exercise de facto control over great swathes of the corporate sector through pyramidal control structures with equity ownership stakes of less than 10%. Similarly, other capital allocations such as loan guarantees, and credits and loans mediated through the groups an in-house private bank may also go unrecorded as direct investment even though a core firm may exercise de facto control of the invested firm. To the extent that these investments cross borders then they constitute an important source of ODI but they go *unrecorded*. If Indonesian business groups make extensive use of such financial instruments then participation in ODI may be understated.

Third, foreign direct investment may go undetected because it occurs within the family setting where productive foreign investment may be *informally organized* in an intra-family wealth transfer (Tung and Chung, 2010). For example, Saxenian (2002) describes the importance of this phenomenon for foreign-born Silicon Valley entrepreneurs who raise funds through family networks. In addition, trading companies affiliated with business groups facilitate the operation of global commodity chains (Gereffi, 1994) where firms engaged in recurrent relational contracting may control a network of foreign assets without actually owning them. Large segments of these chains are organized into informal subcontract networks so to avoid burdensome regulations. Each of these cross-border capital flows represent significant activities but are unreported as ODI, which understates the scope of international activity. The above discussion suggests that processes of globalization have engendered ethnic and relational communities that straddle geographic boundaries and are “neither here nor there”. Entrepreneurs embedded in these communities escape the sometimes onerous institutions of their adopted nation states and migrated toward a *transnational* network organization form in which foreign direct investment has little meaning because firms cannot easily be identified with a specific national home base (Yeung, 2004).

Missing Dragons?

The second explanation is a ‘missing dragons’ explanation suggesting that a complex interplay of firm ownership and management and weak institutions may leave firms with structural characteristics that impede ODI. First, family owned and controlled firms typically prefer domestic rather than international diversification (Gomez-Mejia et al. 2010). Risk aversion and a desire among family management to retain close control constrain family firms’ international activities opportunities due to the high costs associated with coordinating geographically dispersed operations. Sometimes family firms limit participation in the senior management team to a small cadre of trusted insiders and are less inclined to recruit professional managers that have detailed knowledge of international markets. Moreover, the firm’s most important social and political networks are based on local connections but networks are unlikely to help when the firm ventures across international borders.

This body of research suggests that prevalence of family ownership and control linked with prominent local officials is typical of Indonesian firms, which may constitute a population of firms that is ill-suited to internationalization. Many large Southeast Asian business groups attained prominence prior to the widespread implementation of liberal market policies and growing globalization. These groups became especially attuned to the conditions of a pre-liberalization phase of economic growth and aligned their structures and business practices with them. However, with the progression of liberalization and globalization these firms become increasingly out of tune with emergent business conditions (Carney and Gedajlovic, 2002; Dieleman and Sachs, 2008). Their ability to develop international capabilities and pursue offshore opportunities is hindered by a growing organizational inertia.

The above scenario is especially evident in Indonesian where many business groups emerged in the late 1960s and early 1970s, when Indonesia implemented import substitution policies. Consequently, most groups developed business models focusing on the local market. The Suharto era (1966-1998) was one of growth, but also one of corruption and cronyism, where ample opportunities were available for the well-connected inside the country. Entrepreneurs often formed alliances with politicians to secure sector monopolies, permissions and licenses (Robison, 1986), and organized their groups in response to the challenges of their home institutions, thereby becoming local champions (Limlingan, 1986). In doing so, these groups learned to mobilize resources for repeated entry into multiple domestic industrial and commercial projects (Kock and Guillén, 2001) but they developed little international experience.

In subsequent decades the ASEAN economies grew rapidly and business groups were seemingly well positioned to expand beyond their domestic strongholds (McVey, 1992). However, global capital flows created incentives to remain domestically focused. Established business groups mediated and benefited from the entry of foreign firms into the region (Yoshihara, 1988) and served as a major conduit for a flood of portfolio investment during the emerging economy fever in the early 1990s. These continuities illustrate how dominant organisational forms and the institutional arrangements that engender them evolve along path-dependent trajectories. After working so well for so long the strategies have become ‘locked in’ creating an administrative heritage (Carney and Gedajlovic, 2003) that may have left all but the largest groups ill-equipped to engage in internationalization. Management structures that were once efficiently aligned with the domestic challenges of early stage industrialization are now misaligned with the tasks of developing firm-specific capabilities that could fuel their internationalization. In this path dependent explanation, very few domestically focused business groups are able to abandon their deep rooted business practices and learn the capabilities needed to succeed in global competition.

Policy Implications

In this section we briefly address the question of whether the Indonesian governments should pursue policies to accelerate or otherwise seek to influence their ODI. Policies designed to accelerate ODI typically include some mix of financial incentives along with information and insurance services. One important question is to determine what level and scope of ODI policy might be most appropriate for Indonesia? We suggest that the answer depends upon the selection of an appropriate benchmark. Recent commentary suggests that due to the size of its economy and the rapid levels of growth Indonesia is poised to become a BRIC economy with a more important role in the international economy (Ghosh, 2009). To the extent that Indonesia aspires to BRIC status then the relevant policy benchmark is China. Initiated in 1999, China's 'go global' strategy is part of a comprehensive industrial development strategy aimed at producing internationally competitive firms (Nolan, 2001). China provides promising firms with assistance in finding foreign locations and access to credit and special loans for overseas investments. For firms that show signs of competitive strength the Chinese government offers a range of support mechanisms to assist in the promotion of exports and the acquisition of advanced foreign technology and management skills.

Alternatively, the more focused ODI policies of Singapore and Malaysia may be considered the more relevant benchmark. Coordinated by a dedicated government agency, International Enterprise Singapore (IES), Singapore offers grants, loans, tax incentives and equity financing. IES's Regionalization Finance scheme is designed to help local SMEs to establish overseas operations that are complementary to their Singapore based activities. Recipients must demonstrate that overseas investments produce economic spinoffs for Singapore. Singapore's sovereign wealth funds are intended to secure access to strategic technologies. Malaysia too has recently become more active in promoting ODI offering tax exemptions on income derived from foreign earnings. Malaysia has recently attempted to streamline a range of agencies involved in the promotion of national industrial competitiveness and gives particular emphasis to south-south investment.

However, a significant constraint for the development of Indonesian multinational enterprises is a lack of professional management and scientific and technical personnel. The development of such human capital is often the product of experience and firsthand learning through exposure to international projects. For example, research on Japanese and Korean business groups suggests their successful international performance was aided by the systematic development of management talent that could be utilized across a range of industries (Lincoln and Gerlach, 2004; Ungson, Steers and Park, 1997). Researchers observe that family-controlled business groups are sometimes reluctant to make comparable investments in human resources and often rely upon entrenched family members for senior executive talent (Carney, 1998). The existence of the corporate elite dominated by family firms combined with an absence of opportunities for managers to learn the job may create a self reinforcing dynamic in which a supply of high-quality professional management fails to materialize. Consequently, in addition to proactive and direct ODI policies states may also consider indirect policies aimed at developing skilled professional managers.

Furthermore, governments may look into policies supporting smaller firms. Available empirical evidence suggests that business groups tend to have less foreign sales (Colpan, 2006), which may stem from a preference for group members to trade with one another, which engenders "complacency and a reduced incentive to export" (Hundley and Jacobson, 1998: 935). Business groups can become overly dominant and their political and monopoly power may block the flow of new entrepreneurial firms into the economy (Almeida and Wolfenzon, 2006; Morck and Yeung, 2004). Contrarily to large local family groups, the core competences of newly formed or smaller entrepreneurial firms may be based upon managerial and technological skills which may form the basis of international competitiveness (Peng, 2003). If only a very limited number of very large business groups develop the skills to operate internationally, the spill-over effect of ODI may be limited. The Indonesian government may therefore consider targeting the second tier business groups or smaller stand-alone firms to stimulate new international activities. At the same time, those few groups that are already multinationals may be discouraged from creating overseas internationalization platforms, instead being encouraged to channel back some of the international expertise and profits to Indonesia.

Theoretical Implications

We believe that our results also have more general theoretical implications for the study of the internationalization of firms from emerging markets. As our literature review above showed, extant research emphasizes *drivers* of globalization, rather than on inhibitors. This is not surprising given that UNCTAD statistics show a surge in ODI from emerging economies and newspapers report frequently on a number of high profile cases. However, these indicators alone do not necessarily suggest a general trend in a wider population. Instead, based on our limited study of Indonesian groups, we suggest that they could also indicate a Pareto-type distribution (rather than a normal distribution) with a few "extreme" cases, and a long tail of firms focusing on the domestic market. Pareto-science is being applied to an increasing set of social phenomena, and is thought to be more appropriate in a context of interdependent actors, complex tensions, and self-organizing effects. Such a setting is common in international management research (Andriani and McKelvey, 2007).

The internationalization of Indonesian groups may similarly be characterized by processes of interdependence and self-organization. We have various events in our database in which medium sized groups (e.g. the Ciputra Group) teamed up with a larger group (e.g. the Salim Group) when investing abroad because the latter was better endowed with resources and foreign contacts. The LIPPO group frequently teamed up with business groups from other emerging economies (Malaysia, China) which presumably were drawn into the partnership because of LIPPO's existing international capabilities. In this manner, the most international groups perceive more business opportunities, become experienced and even more successful, and consequently are driven by a 'positive feedback mechanism' (Arthur, 1990) that produces an accelerated internationalization pattern. In other words, a few first mover firms can overcome obstacles to internationalization and become "extremes" (Baum and McKelvey, 2006) that tend to skew aggregate statistics on ODI. If the pattern of internationalization found among Indonesia's largest firms is representative of other emerging economies, they suggest that a promising new research lies in re-directing research away from assumptions of normal distributions towards research that incorporates a focus on the differential dynamics that generates extreme cases of emerging economy giants as well as the dynamics that produce the long tail of firms focused on domestic markets.

CONCLUSION

We find that very few large Indonesian business groups can be characterized as multinationals, and that most groups are either only active in the domestic market, or display limited internationalization. We suggest two explanations for our findings which we call 'hidden dragons' and 'missing dragons'. The first explanation suggests that more Indonesian multinational firms exist, but go unnoticed in existing statistics, the second that only a few

Indonesian multinationals have emerged because of an unfavorable local context for all except the largest firms. Which of our explanations is the more likely? At present we do not know how much ODI goes undetected, and we assume we have overlooked several ODI events. Yet, our understanding of business groups accumulated over the years tells us that while our data and official statistics may not be very accurate, they do display a general trend of limited internationalization of Indonesian firms. We contend that both the familial structure of Indonesia's corporate sector along with domestic institutional factors each plays a role in inhibiting Indonesian ODI with unwanted consequences for Indonesia's economic development. Future research on this point is warranted.

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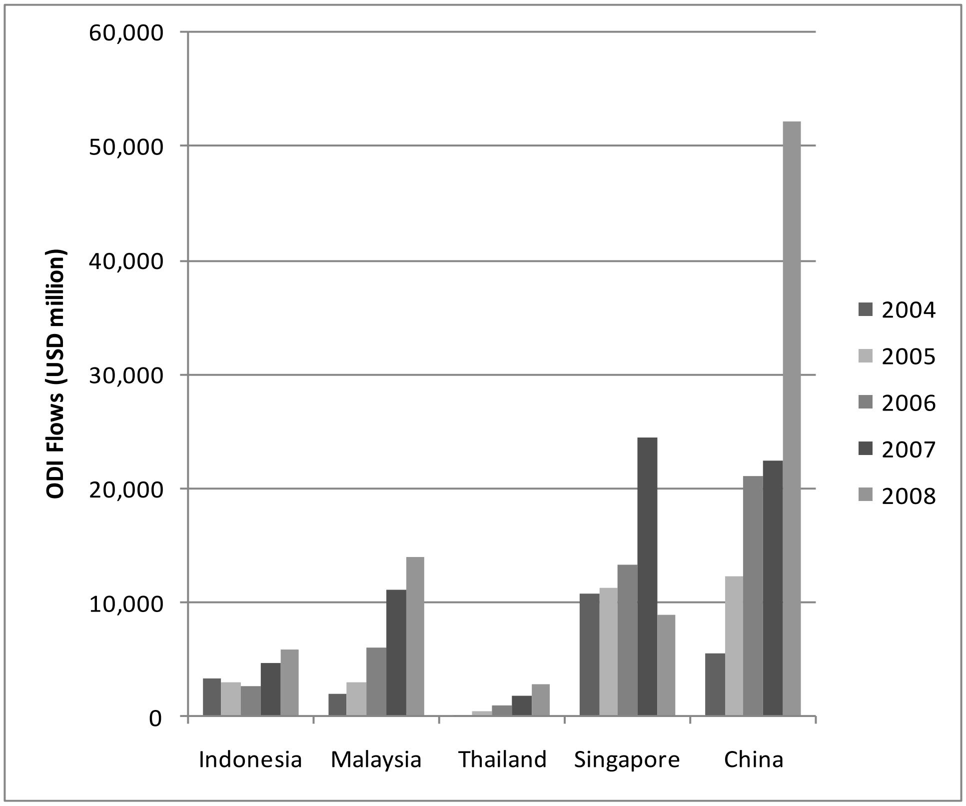
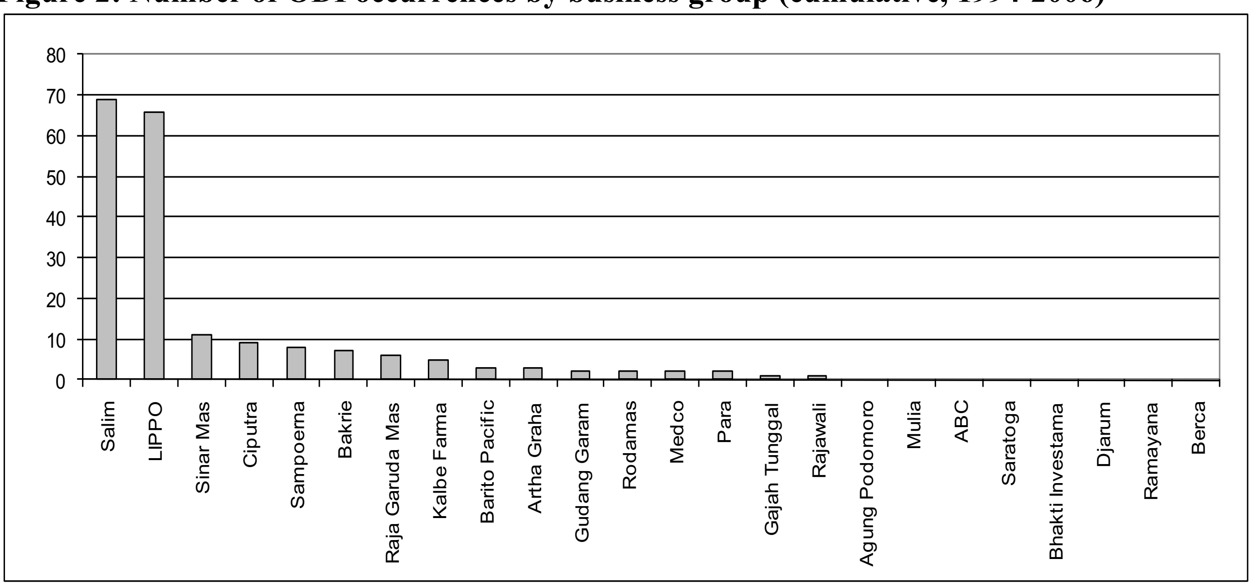
Figure 1: Outward Direct Investment, selected countries



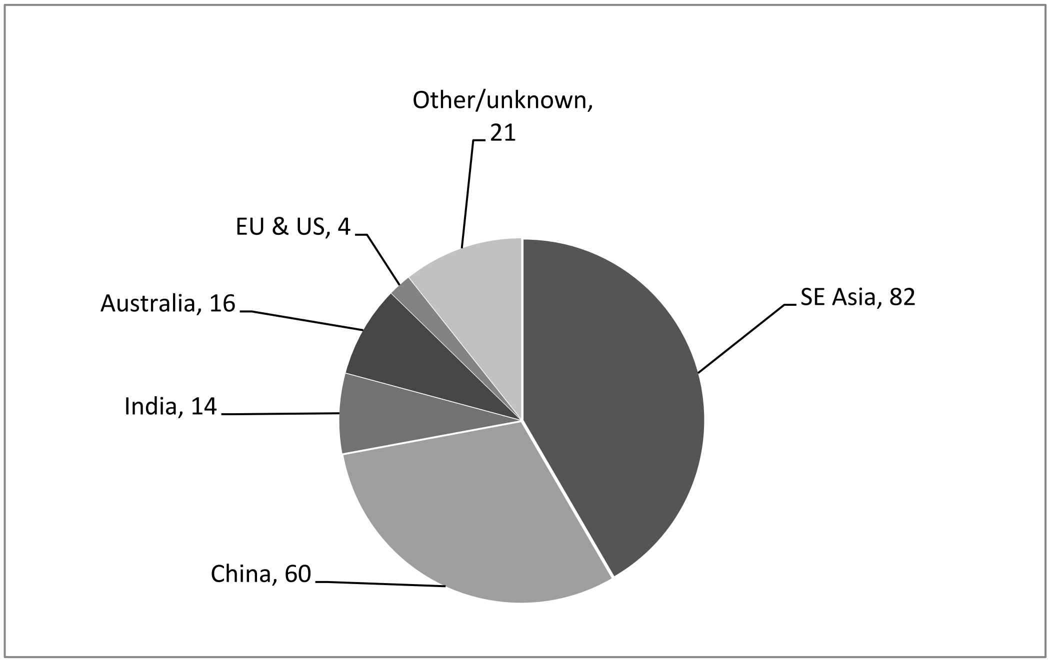
Source: UNCTAD World Investment Report, 2009

Figure 2: Number of ODI occurrences by business group (cumulative, 1994-2006)



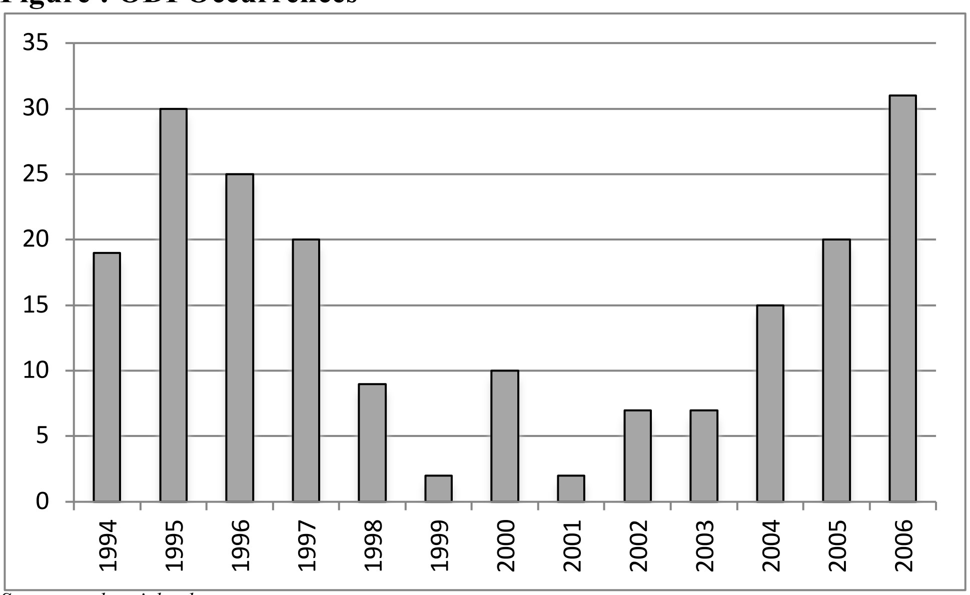
Source: authors' database

Figure 3: ODI Destination and occurrences



Source: authors' database

Figure : ODI Occurrences



Source: authors' database

Table 1: Indonesia's Largest Business Groups

Group*	Family/CEO Name	Ethnic Chinese	UBS list	Globe people rank	Globe Family worth USD bln	Forbes people Rank	Forbes Family worth USD bln	Globe Group Rank	Turnover Globe USD bln
ABC Group	Djojonegoro family	x	x	16	0.560	17	0.360	12	1.900
Agung Podomoro Group	Haliman family	x	x	20	0.505	8	0.900	27	0.600
Artha Graha Group	Tomy Winata (F)/Sugianto Kusuma (G)	x	x	38	0.275	35	0.110	70	0.177
Bakrie Group	Bakrie family		x	8	1.050	6	1.200	8	2.800
Barito Pacific Group	Prajogo Pangestu and family	x	x	17	0.525	13	0.510	20	1.100
Berca Group	Murdaya Po and family	x		27	0.350	16	0.430	na	na
Bhakti Investama Group	Harry Tanoesoedibyo	x	x	10	0.820	na	na	29	0.566
Ciputra Group	Ciputra family	x	x	30	0.335	30	0.145	57	0.244
Djarum Group	Hartono family	x	x	1	4.200	5	1.400	5	3.500
Gajah Tunggal Group	Sjamsul Nursalim and family	x	x	21	0.445	21	0.295	21	1.100
Gudang Garam Group	Wonowidjojo family	x	x	2	3.500	4	1.800	7	2.900
Kalbe Farma	Benjamin Setiawan/F.B. Aryanto	x	x	11	0.650	34	0.115	24	0.733
Lippo Group	Riady family	x	x	14	0.585	11	0.570	9	2.500
Medco Group	Arifin Panigoro		x	9	0.900	9	0.815	22	0.811
Mulia Group	Gunawan Tjandra (Tjan Kok Kwan)	x	x	37	0.278	40	0.080	48	0.311
Para Group	Chairul Tanjung and family		x	15	0.565	18	0.310	31	0.533
Raja Garuda Mas Group	Sukanto Tanoto and family	x	x	6	1.300	1	2.800	11	2.000
Rajawali Group	Peter Sondakh	x	x	19	0.510	12	0.530	25	0.722
Ramayana Group	Tumewu family	x		24	0.395	14	0.440	34	0.500
Rodamas Group	Tan family	x	x	25	0.375	27	0.200	39	0.422
Salim Group	Salim family	x	x	4	2.800	10	0.800	2	6.950
Sampoerna Group	Putera Sampoerna and sons	x	x	5	2.200	2	2.100	6	3.300
Saratoga Capital	Edwin Soeryadjaja	x		18	0.520	23	0.230	13	1.600
Sinar Mas Group	Widjaja family	x	x	3	3.100	3	2.000	3	4.500
Wings Group	Kattuari and Sutanto families	x	x	7	1.100	7 ; 25	1.000; 0.220	14	1.400

* not included: state-owned groups, foreign multinationals, domestic groups majority owned by foreign firms

F: Forbes People Ranking; G: Globe People Ranking

Sources:

UBS list: UBS (2006). Indonesian Connections, UBS, Jakarta. (note: no ranking)

Globe groups ranking: Globe (2007) 100 Top Groups, September. (without state/foreign-owned companies)

Globe people ranking: Globe (2007) 150 richest individuals, August.

Forbes ranking: www.forbes.com; accessed December 15, 2007.

Table 2: Sources and Results

Group Name	Search terms	Lexis Articles	Events in database	FDI occurrences	Type
ABC Group		1,728	3	0	Domestic
Agung Podomoro Group	Agung Podomoro	32	5	0	Domestic
Artha Graha Group	Artha Graha	1,583	35	3	Domestic
Bakrie Group	Bakrie Group	1,282	88	7	Intermediate
Barito Pacific Group	Barito Pacific	2,049	49	3	Domestic
Berca Group	Berca	163	20	0	Domestic
Bhakti Investama Group	Bhakti Investama	1,449	30	0	Domestic
Ciputra Group	Ciputra	2,012	37	9	Intermediate
Djarum Group	Djarum	491	4	0	Domestic
Gajah Tunggal Group	Gajah Tunggal	1,942	15	1	Domestic
Gudang Garam Group	Gudang Garam	7,884	14	2	Domestic
Kalbe Farma	Kalbe Farma	2,111	17	5	Domestic
Lippo Group	Lippo	14,735	153	66	Emerging Market Giant
Medco Group	Medco Group	209	23	2	Domestic
Mulia Group	Mulia	119	0	0	Domestic
Para Group	Chairul Tanjung	146	13	2	Domestic
Raja Garuda Mas Group	Raja Garuda Mas	196	28	6	Intermediate
Rajawali Group	Rajawali	2,960	23	1	Domestic
Ramayana Group	Ramayana	1	0	0	Domestic
Rodamas Group	Rodamas	74	11	2	Domestic
Salim Group	Salim	129,964	210	69	Emerging Market Giant
Sampoerna Group	Sampoerna	8,932	47	8	Intermediate
Saratoga Capital	Saratoga	291	0	0	Domestic
Sinar Mas Group	Sinar Mas	3,730	133	11	Emerging Market Giant
Wings Group	Wings	24,039	discarded	discarded	
Total		**208,122**	**958**	**197**	