A MARSHALLIAN APPROACH TO THE ECLECTIC PARADIGM OF FOREIGN INVESTMENT

THE CLUSTERING OF FILM TNCS IN CENTRAL LONDON

ESRC Centre for Business Research, University of Cambridge
Working Paper No. 119

Lilach Nachum
ESRC Centre for Business Research
Department of Geography
University of Cambridge
Downing Place
Cambridge
CB2 3EN

David Keeble
ESRC Centre for Business Research
Department of Geography
University of Cambridge
Downing Place
Cambridge
CB2 3EN

Phone: 01223 339097
Fax: 01223 355674
Email: ln207@cus.cam.ac.uk

Phone: 01223 333386
Fax: 01223 333392
Email: dek1@cus.cam.ac.uk

March 1999

This Working Paper relates to the CBR Research Programme on Small and Medium-Sized Enterprises
Abstract

This study is designed to examine the effect of the economies arising from the concentration of economic activity in close geographic proximity on the investment activities of TNCs. Using the eclectic paradigm as the theoretical framework, the study explores the extent and the ways in which economies of agglomeration affect the ownership advantages of TNCs, influence their choice of modality to serve foreign markets and form part of the location advantages of a given locality.

In addressing these issues, the study focuses on a set of media industries which has clustered within a distinct part of London, a pattern which suggests that TNCs in these industries derive certain benefits from being located in proximity to other firms in their own and in closely related industries.

The study shows that the impact of agglomeration economies varies considerably by the type of investment, and the economies arising from agglomeration affect the ownership advantages of TNCs to varying degrees, and limit the mobility of those most affected by them. Finally, while agglomeration economies modify the value of certain location advantages, they have limited impact, if any, on others.

Acknowledgements

Helpful advice and information from Ms C. Alberty and Ms D. Kirchner of the London Film Commission is gratefully acknowledged, as is the financial support of the ESRC under the core research programme of the CBR.

Further information about the ESRC Centre for Business Research can be found on the World Wide Web at the following address: http://www.cbr.cam.ac.uk
A MARSHALLIAN APPROACH TO THE ECLECTIC PARADIGM OF FOREIGN INVESTMENT

THE CLUSTERING OF FILM TNCS IN CENTRAL LONDON

1. Introduction

This paper investigates the striking clustering of foreign-owned film production and distribution Transnational Corporations (TNCs) in the Soho area of central London. It argues that such clusters indicate a need for extending and elaborating the eclectic paradigm of Foreign Direct Investment (FDI) to incorporate the powerful impact of locally-specific agglomeration economies. The paper reveals that big foreign film producers operating in this small area often – but by no means invariably – gain major benefits from locating close to other film, TV, video and post-production firms in the cluster. For those TNCs which do benefit, this results in a high degree of local embeddedness and immobility, which affects the nature of their ownership and internalisation advantages and the location advantages of the UK. Some film TNCs, notably those engaged in distribution, do not however benefit from clustering. The impact of agglomeration economies, and their relevance to the eclectic paradigm, thus varies considerably by type of TNC investment.

The eclectic paradigm, as developed by Dunning (1958), Hymer (1960/1976), and Caves (1971), and elaborated by Dunning (1971, 1977, 1980) and Buckley and Casson (1976), predicts that the propensity of firms to engage in cross border activities will be determined by three forces. The first is the firm-specific advantages of the investing firm vis-à-vis firms of other nationalities (Ownership Advantages). The possession of such advantages allows the firm to compete successfully in foreign countries and to overcome the disadvantages of foreignness. The second factor is the advantages of the location in which the investing firm can maximise the return to its advantages (Location Advantages). For foreign activity to take place,
foreign countries should be more locationally advantageous than the home country of the investing firm. Otherwise the production will be concentrated in the home country and foreign markets will be served by exports. Third, it must be beneficial for the firm possessing ownership advantages to use them itself rather than to sell or lease them or their rights to foreign firms (Internalisation Advantages). The firm chooses to internalise the markets for its ownership advantages through an extension of its own activities rather than externalise the sale of them or their rights to independent foreign firms.

The location patterns of Transnational Corporations (TNCs) and the nature of their activities have become somewhat alien to the prediction of the eclectic paradigm, as traditionally formulated. In some industries, TNCs tend to cluster in small localities within countries, typically in proximity to other firms, both foreign and indigenous (see Dunning 1997 fig. 1, for a description of the location of TNCs in selected industries in the USA, and Nachum 1998, table 1, for a description of the location patterns of the leading TNCs in financial and professional service industries within several countries)\(^1\). Furthermore, casual observation suggests that TNCs often take an active part in the various links and networking taking place in these clusters, and that these are important for their competitive success. These location patterns suggest that TNCs derive some advantages from their proximity to other firms and that the cluster of firms may form part of the attraction of particular locations. The relevant geographic area that affects their location may thus be far smaller than a whole country, being instead confined to a region or an urban centre, and often to a small district within it. These aspects of TNCs’ activities cannot be addressed by the traditional formulation of the eclectic paradigm.

The advantages gained by firms located in proximity to each other have been well recognised in the economic literature at least since the time of Marshall (Marshall 1890, 1920). Marshall realised how ‘... great are the advantages which people following the same skilled
trade get from near neighbouring to one another...’ (1920, p. 271), a concentration which Marshall described as an ‘industrial district’. Such advantages result from an increase in the degree and specialisation of skills and their diffusion throughout the community to create an abundant supply of qualified labour, the development of specialised services, an increase in the use of highly specialised machinery, made possible by the combined demand of many firms, and the benefits of large scale industrial production and of technical and organisational innovation which are beyond the scope of any individual firm.

Marshall’s recognition of the collective advantages accruing to firms located in proximity has provided a foundation for a theory of geographical clustering of firms which has inspired considerable research by scholars originating from various disciplines. Taken from different perspectives and often using different analytical tools, these studies have illustrated the gains derived from the clustering of related activities in space, the dynamics of collective learning taking place in these localities and their implications for the patterns of economic activity in particular industries. These studies have shown that links among firms, institutions and infrastructures within a geographic area give rise to various forms of localised externalities that are external to individual firms but internal to the cluster. They facilitate the development of general labour markets and pools of skills, and enhanced interaction between local suppliers and customers².

The application of these ideas to the explanation of the patterns of international business activity is quite new. Until recently, intracountry location patterns, the forces which drive them and their consequences for the competitiveness of TNCs, have gone largely unassessed by foreign direct investment theory. Scholars of international business have only recently begun to acknowledge the need to introduce ideas based on linkages among firms and embeddedness of certain assets in particular localities into their models and paradigms. The most advanced and elaborated attempt has

The present study seeks to make a contribution in this direction, by examining the ways in which the economies arising from agglomeration of activity in distinct locations affect the operation of TNCs based in these localities and the nature of their investment. Using the eclectic paradigm as the theoretical framework, the study assesses the extent to which the economies arising from the proximity of TNCs to a cluster of firms in their own and in related industries affect their ownership advantages, their choice of modality to serve a particular market, and the location advantages of the location in which they operate. It seeks to examine whether and to what extent these concepts, as traditionally conceptualised, need to be modified to acknowledge the geographic embeddedness of some aspects of the activities of TNCs. In addressing these issues we adopt a descriptive, exploratory approach, focusing on TNC investment in the film industry in London, by far the dominant centre of film production and film TNC activity in the UK. The film industry represents a very appropriate sector for investigation of these issues, in that it is characterised by high levels of TNC activity, yet exhibits considerable vertical disintegration and geographical clustering. This examination provides the basis for various propositions about the ways in which agglomeration economies may affect the processes that determine the foreign investments of TNCs.

2. Agglomeration Economies and the Eclectic Paradigm: Some Theoretical Considerations

The participation of TNCs in various forms of networking with other firms located in geographical proximity and the embeddedness of some of the factors which shape the nature of their activities may affect the configuration of the variables of the eclectic paradigm facing them. In what follows, we present the theoretical reasoning for a possible need to modify some of the assumptions underlying the
three tenets of the eclectic paradigm, as traditionally conceptualised, in order to take account of these forces, and to reach a fuller understanding of TNC behaviour.

Several of the assumptions which have underlined the concept of ownership advantages, as traditionally conceptualised, may need to be modified when the economies arising from the agglomeration of economic activity in a distinct geographic area are acknowledged. First, the concept of firm-specific advantages is based on the conceptualisation of firms as having clear boundaries, defined by their ownership (hence the name of these advantages, ‘ownership advantages’). These advantages are assumed to be created and organised independently from other firms, and to be based on the unique capabilities and attributes of individual firms (see Dunning 1993). To the extent that there have been references to the activities of other firms, they have been regarded as competitors rather than as potential collaborators or as a source of learning. Recently there have been attempts to examine the linkages among firms as critical determinants of their ownership advantages. The most elaborated of these is the network approach, associated mainly with the University of Uppsala, and the work on the innovative capabilities of TNCs and the location of such activities (see Nachum 1998 for a review of this work). However, these attempts do not fully acknowledge the spatial nature of these linkages. Notably in the network approach, such links are not confined geographically and may not necessarily occur in geographic proximity. When the activities of TNCs are significantly influenced by their links with other firms in close proximity, the composition and behaviour of this group of firms become important determinants of the ownership advantages of the individual firms comprising the network (Dunning 1995, 1997). Under such circumstances, TNCs often develop and maintain their ownership advantages through their dynamic interaction with other members of the cluster, to such an extent that TNCs caught up in these systems often face a common competitive fate irrespective of their individual competencies and capabilities.
Second, a critical tenet in the traditional conceptualisation of ownership advantages is the assumption of the mobility of such ownership advantages within the firm across countries. This mobility allows the firm to utilise its advantages in different locations, which is part of the rationale for international production (Lall 1980). Firms can benefit from their advantages everywhere, in line with their overall strategic plans, and they choose a location in which they can best utilise their ownership advantages. There have been very few attempts to examine the limitations of this assumption (see Lall 1980, Hu 1995). Hu (1995) addressed this issue in the context of competition in home vs host countries and discussed the conditions under which firms’ advantages are mobile, but he did not refer explicitly to economies which are embedded in a locality as one of the reasons for immobility. Economies of externalities, which derive from the interaction among firms based in proximity to each other, limit the mobility of the ownership advantages of the firms taking part in them, as those become, to a certain extent, embedded in the locality and tied to the links with other firms based in this locality.

Third, in its traditional conceptualisation, the concept of ownership advantages implies that advantages are developed by the parent firm in the home country and then transferred to the affiliates. In recent decades there has been a growing realisation that this assumption is inadequate and underestimates the role played by the affiliates and their ability to develop ownership advantages on their own. A considerable amount of research has sought to identify the type of activities implemented by the affiliates and the role they play within the TNCs as a whole in the generation of ownership advantages (see Taggart 1998 for a comprehensive review of this literature). The engine of subsidiary growth has increasingly been acknowledged as being its distinctive capabilities, rather than the transfer of resources from its parent company (see for example Birkinshaw 1996). Moreover, there has also been a recognition that some of the advantages which affiliates develop or acquire can be transferred to the parent, to the benefit of the TNC as a whole (UNCTAD-DTCI
However, with the exception of the network approach associated with the University of Uppsala, the links that the affiliates develop with other firms in the foreign locality have not been explicitly regarded as a possible source of their competitive advantage and independent identity. The acknowledgement of such links implies that the advantages developed by the affiliates independently of the parent are tied to the locality of the affiliates concerned and to a certain extent at least are unique attributes of the affiliates which distinguish them from the rest of the TNC.

Fourth, ownership advantages were traditionally perceived to take two forms, namely the exclusive or privileged possession of specific intangible assets such as technology, managerial and organisational skills, and the ability to co-ordinate the use of these and other assets in multiple product and geographic markets (Dunning 1993). The establishment and maintenance of formal and informal links with other firms have not been recognised as a potential source of ownership advantage. This ability, however, is what allows TNCs to take part in, and to benefit from, processes of collective learning and innovation occurring among firms based in geographical proximity, and it is thus an important source of ownership advantage by itself.

The conceptualisation of countries as the relevant economic unit which affects the location decision of firms, which underlies the notion of location advantages in the eclectic paradigm, seems to capture only part of the factors in play. Countries are defined by political boundaries, but the geographical, cultural and institutional proximity that provides the advantages may not necessarily coincide with such boundaries. Casual observation of TNCs’ location decisions suggest that often the advantages which attract them to invest in a particular locality characterise only a region or urban centre, and sometimes even a small district within it, rather than the country as a whole. Rather than being fully mobile within countries, these immobile advantages are strongly embedded in particular geographic areas, often for decades and even centuries.
Furthermore, the typical location advantages to which the eclectic paradigm refers are the amount and quality of immobile resources and conditions in particular countries, such as the abundance of natural resources, the institutional framework, culture and government policies. The mere existence of clusters of economic excellence in a particular activity, and the economies arising from taking part in the dynamics of learning in such clusters, have not been regarded as potential sources of location advantages. Nor have they been taken to modify the value of the traditional advantages considered by the paradigm. Location advantages were regarded as unrelated to the amount of economic activity taking place in a particular location, nor does the mere existence of centres of economic excellence strengthen a country’s advantages. The acknowledgement of agglomeration economies suggests that the location of other firms may affect TNCs’ investment decisions and clusters of excellence in particular geographic areas may be part (and often a very important part) of the attraction of particular locations.

The third strand of the eclectic paradigm - internalisation advantages - is based on the idea that when the transaction costs of exploiting firm-specific assets through a market arrangement are high, the owner of the assets may choose to internalise the market transaction through FDI (Buckley and Casson 1976). Firms engage in FDI when it is more beneficial for them to use their ownership advantages through an extension of their own value-adding activities rather than externalise them through licensing and similar contracts with other firms (see Buckley and Casson 1998 for a recent review). When economies of externalities are acknowledged, the idea that firms internalise intermediate markets primarily to reduce the transaction and coordination costs of markets may need to be extended in two ways. The first is the need to encompass the benefits arising as a result of the clustering of economic activities in particular geographic areas in affecting the choice of modality to serve foreign countries. Such benefits may include external economies of scale, lower transaction costs which often characterise transactions within these clusters (Scott
1996), and diminishing risks and uncertainty arising from trust built within these networks of firms. The second is to incorporate inter-firm transactions that are not concerned with control and ownership, but rather with the way in which tangible and intangible assets are managed and organised among firms.

Figure 1 summarises the main areas in which each tenet of the eclectic paradigm may need to be modified in order to take account of the possible effect of agglomeration economies and the embeddedness of certain types of economic activity.

In what follows, we use the framework summarised in Figure 1 to examine to what extent and under what conditions there is a need for the acknowledgement of agglomeration economies and for subsequent modifications of the tenets of the eclectic paradigm. We argue that if agglomeration economies affect TNC investment, the areas summarised in Figure 1 are those in which their impact will be observed. We address these issues in the context of foreign investment by film TNCs in the UK.

The UK has been a recipient of strong flows of FDI in film-related activities throughout the 20th century. Tables 1 and 2 document the two main aspects of activities by film TNCs in the UK - production (table 1) and distribution (table 2).

Tables 1 and 2 reveal that foreign film TNCs have dominated the UK market, in terms of both production and distribution, throughout the 20th century. With the notable exception of the 1990s, the number of British films produced in the UK has fallen behind, by far, those produced by foreign firms in the UK and UK producers have been heavily dependent upon foreign TNCs, notably of US origin, for the distribution of their films.

Inward FDI to the UK in the film industry has originated mostly from the USA. The British Film Commission estimates that in 1997, US
investment accounted for about 95% of total inward FDI in film production to the UK. There are suggestions that TNCs of US origin have accounted for similar shares ever since the decades following the First World War (Murphy 1986, Jarvie 1992, Low 1997). Consequently, any discussion of foreign activity in the UK in this industry refers mainly to investment undertaken by US TNCs.

3. The Location Patterns of Film Companies in the UK and in London

Activities related to film production and distribution tend to display strong patterns of geographic concentration, typically in certain districts of large cities. The most well known example of such a concentration is Hollywood in Los Angeles (see Scott 1996, Storper 1994), but a number of other major metropolitan centres, such as London, Paris, New York and Tokyo, also possess clusters of such activities (Llewelyn-Davies and UCL Bartlett School of Planning & Comedia, 1996). These industries seem to favour such patterns as their production activities are reinforced by spatial agglomeration characterised by many different specialised functions and dense internal relationships, in which geographical proximity increases the efficiency of transaction and information exchange between firms (Scott 1996, 1997, 1998a). The location patterns of film producers and distributors in London provide a striking illustration of this tendency (Figure 2).

No less than 80 and 95% of British and foreign-owned film-related activities, respectively, taking place in the UK are concentrated in London, and within London, there is a strong concentration in the W1 postal code area, an area which has been associated, to a greater degree than any other London quarter, with the creation of arts, literature, music and fashion. This tiny district of Central London has developed as a cultural centre since the 17th century (Richardson 1995, Tames 1994, Summers 1989, Home and Loew 1987, Borer 1984) and has attracted by far the largest number of film producers in
the UK as well as a wide range of specialised film production and post production services (Nachum and Keeble 1999). Figure 2 also shows that the concentration of film-related activities in Soho is not confined to indigenous firms. Foreign firms investing in the UK are attracted to this cluster as well, and are concentrated in this area to an even greater degree than British-owned firms.

This location pattern makes the film industry a particularly interesting case for examination of the issues addressed here. In this type of industrial setting, theory predicts that networking and intra-firm linkages should play a strong role in affecting the competitive advantage of individual firms and their economic performance. The participation of TNCs in these clusters suggests that, though the activities of these TNCs reach many countries and continents, local processes, linking together firms based in close geographic proximity, may also be vital for their competitiveness.

Indeed, a recent study of the cluster of media activities in Central London (Nachum and Keeble 1999) has shown that this concentration is driven by strong linkages among firms, to form an industrial district which represents considerably more than the simple sum of its parts. This cluster is characterised by mutual learning and cultural synergy, made possible by the presence of firms engaged in many interrelated activities in one place, and fostered by the positive spillover effects that tie these firms together into an evolving community whose dynamics are vital for the competitive performance of individual firms. This study also shows that these processes are not confined to indigenous firms. Foreign firms investing in London, as well as British-owned TNCs, take an active part in them and often foster and facilitate them.

The analysis which follows is based on a variety of sources, including a number of detailed case studies of film TNCs operating in London, supplemented by a large variety of secondary sources, which include interviews with industry experts, various kinds of industry
publications, company reports, industrial histories and published documents. According to estimates by the London Film Commission, there are about 35 film TNCs established in the UK\(^8\). All these TNCs were approached and 16 of them agreed to take part in this research. Case studies of these TNCs, most of whom are based in Soho, were conducted during the summer of 1998. In most cases, the first interview was conducted with the chief executive or managing director. Additional interviews were conducted with directors of specific activities (marketing, PR, finance, production). Between 1 and 3 interviews were conducted with each of the affiliates approached. Some characteristics of the TNCs studied are presented in the Appendix. This reveals considerable variation among these TNCs in terms of specialisation, age, and size, variation that minimises the likelihood that the findings could be attributed to any one of these characteristics.

The case study method was judged to be suitable in the context of this study as it provides rich data for theorising and conducting a detailed analysis of the dynamics of inter-firm ties, even though the cases examined may have but moderate generalizability. Given the early stage of research in this area, this method is appropriate for an exploratory study seeking to achieve qualitative depth of understanding of the issues addressed. A statistical approach would miss out on many of the details that can only be insufficiently captured by a quantitative approach. Furthermore, the transformation of some of the concepts addressed into quantifiable, measurable variables, required to conduct a statistical analysis, is likely to raise difficulties in the interpretation of the findings of such analysis. In view of the complexity of strategies and type of activities, such a case-study approach seems to be most suitable, as it provides a richer picture of the basic conditions and firm behaviour than selective statistics can provide. The insight that emerges from the analysis of this range of data is suited to the generation of hypotheses that need to be confirmed by future research, based on a larger sample of firms.
The study has taken a long-term view, starting in the early decades of the 20th century, when film TNCs first invested in the UK, until the present day. Such a long time span enables the examination of great variety of circumstances in which this investment has taken place and of variations over time in the issues of interest here. Another advantage of such an approach is that the investment activities of some of the major film TNCs operating in the UK today go back to the turn of the century, and an historical perspective is thus necessary to understand the changing nature of their activities over this period.

4. TNCs in the Film Industry in London

The activities of film TNCs in the UK have taken three main forms: distribution, mostly of films produced in the home country of the investing TNCs; financing and co-production with local film producers of films which have often then been distributed by the distribution arms of the TNCs; and complete local production. In certain periods these three forms of investment were undertaken in combination, sometimes by the same TNC, while other periods are dominated by one of them.

Investment directed towards the distribution in the UK of films produced by the parent was common among the large US film producers (known as the ‘US majors’) when they first arrived in the UK around the turn of the 20th century. Examples of this investment include Vitagraph (subsequently Warner Brothers) which established a British affiliate in 1912; Fox (later 20th Century Fox) which arrived in 1916; and Famous Lasky Film Service (subsequently Paramount) which in 1919 took over a British distributor which had been set up in 1915 (Chanan 1983). Many of these TNCs have maintained this form of investment (often combined with other forms) throughout the 20th century. Recent examples include Buena Vista, the distribution arm of Walt Disney, and United International Pictures (UIP), the US-owned distributor that handles the distribution of Paramount, Universal and MGM. Finance and co-production investment started in the late 1920s
and has been the most common form of involvement of US TNCs during most of the 20th century. There are numerous examples of such arrangements, in which the US affiliates provide financial backing and the actual production is carried out by UK local producers. Two of the better known examples are Warner Brothers agreement with Enigma, a deal made in 1979 which continues until the present day (Screen Finance 1996) and the 1990 deal between 20th Century Fox and Goldstone (Screen Finance 1990). Foreign investment which involves actual film production by the TNC itself, often in co-operation with local producers, started in the early 1930s, when the US majors established production affiliates in London (Paramount Films Services in 1931, Fox in 1932, Columbia Picture in 1933 and Metro-Goldwyn-Mayer in 1936 (Low 1997)). Subsequent investment of this type was concentrated in the years following the Second World War and again in the 1960s (Murphy 1992). The growing interest of foreign film producers in UK production in recent years (British Film Commission 1996, The Film Review Group 1998) suggests the possible development of another such wave since the mid-1990s. This investment involves both using the UK as a production base for films to be distributed elsewhere (export-seeking investment), and production of films to be distributed in the US and the UK (a combination of export and market-seeking investment).

The main factors which have affected the choice by film TNCs of these different kinds of involvement have been their overall strategies and motivations for undertaking the investment, changes in the location advantages of the UK relative to those of the TNC’s home country, and certain characteristics of the TNCs. Changes in the overall strategy of the parent companies in Hollywood since the 1950s and 1960s in response to financial difficulties have affected these choices. In sharp contrast with the overall integrated structure which characterised US film producers since their origin around the turn of the century, they have adopted a more disintegrated strategy, involving increased out-sourcing of the actual film production to independent film producers (Christopherson and Storper 1986,
Storper 1989). This change has also affected the nature of the activities of their UK affiliates, which have followed the strategy of their parent in Hollywood in out-sourcing an increasing proportion of their production. This in turn has further increased the need of the UK affiliates for local involvement with the cluster of local firms in Soho, where British film producers have been concentrated.

Changes in the location advantages of the UK relative to those of the home country of the investing firms have often been influenced by the policies of various British governments that have sought to protect the local film industry from the dominance of foreign films. The most influential policy of this kind was the Film Act of 1927 (Dickinson and Street 1985, Jarvie 1992, Low 1997, Sedgwick 1997), which attempted to secure the exhibition of a certain proportion of UK-made films and the use of certain amounts of local input in the production of foreign films in the UK. The Act was changed and modified several times, but it provided the framework within which the UK film industry operated until the early 1980s.

Certain characteristics of the TNCs concerned, notably their size and financial strength, have also often affected the choice of the specific type of involvement. There is a tendency for larger TNCs to display a preference for full production, which provides full control over the choice of the script, the crew, and the nature of the distribution and exhibition, whereas various forms of co-production are typically undertaken by smaller TNCs, generally because of their more limited financial capacity and ability to take the risk involved in sole production.

The configuration of the ownership, location and internalisation advantages which have shaped these investments differ considerably, as do also the local links which the foreign affiliates have developed and maintained in the UK. We begin by identifying the specific ownership, location and internalisation advantages relevant for each kind of investment and then use the framework summarised in Figure
1 to examine under what circumstances and in which ways economies of agglomeration have affected them. This examination is then used to generate some hypotheses regarding the effect of agglomeration economies on the three tenets of the eclectic paradigm.

4.1. Ownership advantages

The critical ownership advantage in the distribution of films is the organisational capability to direct films produced in one central location to different consumers in multiple geographic locations and to reach the widest possible geographic coverage\(^9\). Economies of scale internal to individual firms, which help in acquiring the financial resources needed for such operations and to develop the organisational capabilities they require, give considerable advantage to large firms. Because of the large size of their home country market, US film distributors were already very large on arrival in the UK, and have enjoyed a considerable size advantage over UK competitors where, around the turn of the century, film distribution was handled by a large number of small firms operating in small territories (Low 1997). Later on, and for most of the 20th century, US TNCs came to control virtually the entire distribution of films in the UK. In 1997, five US majors (Buena Vista, Columbia, Fox, UIP and Warners) controlled 78% of the distribution market in the UK, with another 15% of the market controlled by TNCs of other origins (Entertainment and PolyGram) (Film Policy Review Group 1998).

The nature of the activity of the distribution affiliates requires limited, if any, links with other firms. Rather, their activities are geared towards their consumers and they seek proximity to the sources of demand. Indeed, the links of the distribution affiliates with other UK film production firms have been minimal. Furthermore, as the reason for the existence of these affiliates has been to distribute the films produced in Hollywood, their orientation has been predominantly towards their headquarters. They are an extension of the parent company to provide a specific function along the value added chain -
the distribution. Firm archives show how strongly UK distribution affiliates were controlled by their parents in Hollywood in the past (Murphy 1986, Low 1997), and a similar situation is also common among these affiliates today. They are monitored by the parent company to such an extent that they do not have control over what films to distribute even in the UK. All decisions (what films, when and on how many screens) are made by the parent companies in the US. One outcome of this limited role is that most affiliates are very small, employing no more than a dozen or two employees.

Under such circumstances, they have no need to take part in the economies of agglomeration occurring among firms clustered in Soho, and these have limited, if any, impact on their ownership advantages. When asked to what extent they are engaged in networking with other firms, and how important these linkages are for their activity, the managing director of a US-owned distribution affiliate based in London explained: ‘...we don’t have very much to do with them [other firms in film and closely related activities]. We get films for distribution from the headquarters in LA [Los Angeles]. Very seldom do we distribute films of local producers. ...collaboration with other firms is irrelevant - they are competitors. We don’t work together, we compete’.

For TNCs providing finance for local film producers, the critical ownership advantages are those related to the financial strength of the investing firms, and their ability to establish and maintain links with local producers to be better able to select the best films for distribution. Throughout the 20th century, US film TNCs have enjoyed considerable financial strength, due to their ability to generate funds both internally and from external sources. The former is a consequence of their vertically integrated organisation form, which incorporates film production, distribution and exhibition under the same ownership (Storper 1989, Enright 1995). This form of organisation has considerable advantages as it secures internal sources of finance and reduces the high risks associated with dependence on
external sources for distribution and finance. In addition to internal sources of finance, however, US TNCs benefited from their ability to raise money externally, on the US stock exchange market.

By comparison, in the UK for most of the 20th century, production and distribution have been implemented under different ownership. Consequently, UK film producers have been dependent on external sources (most often of US origin) for their survival (Murphy 1986, Low 1997, Film Policy Review Group 1998). Furthermore, in the UK film production has been regarded as a cultural rather than an economic activity, and with few exceptions, UK investors have been reluctant to finance these activities (Chanan 1983, Screen Finance 1998). As a result, there has been a chronic shortage of capital, a situation which has led to low budget production with its typically small returns and limited growth options (notably those which are more capital intensive).

This investment has facilitated close links between the foreign affiliates and local film producers. The main reason for proximity has been to reduce the costs associated with the selection of local producers for financial support, as the public relation manager of a US affiliate strongly involved in this form of activity explained: ‘...we need to get to know them [local film producers] very well, to know how they work and what kind of films they are likely to produce, in order to be able to decide when it is worthy for us to support them financially and/or to distribute their films. It is easier to achieve this from Soho than from elsewhere. Here people get to know each other....we drink in the same pubs, eat in the same restaurants’. These TNCs maintain intricate networks of deals, projects, and tie-ins with local and foreign firms based in Soho that link them together in ever-changing collaborative arrangements, but these dynamics are related to the co-ordination of production and have limited, if any, impact on other types of ownership advantages.
The ownership advantages of the production affiliates differ considerably from those of the distribution and finance affiliates. Like the latter, these affiliates have also benefited from the enormous size, reputation and financial strength of the TNCs of which they are part, relative to their UK counterparts. Several additional ownership advantages, related to the organisation of production, are important for this type of investment. First, taking advantage of developments in Hollywood, the US affiliates have been ahead of local producers in technological innovation in film production. The film reviewer of the UK industry publication 'Sight and Sound' wrote in 1944: '...almost every technical and artistic improvement which has been made in the cinema in the last 30 years came from California. ... they [Hollywood firms] invented virtually the entire bag of movie tricks' (Curtiss, 1944, p. 28). This technological lead has persisted for most of the 20th century. Second, following their parents in Hollywood, the UK affiliates have used advanced marketing techniques and have spent large sums of their total production cost on marketing their films, unlike their poorly-financed UK counterparts. In the late 1990s, the average marketing costs of the US majors were $23.3 million per film - over twice the average total film production budget in the UK (Screen Digest 1998). Third, US TNCs had come to regard the management of their corporations as an independent special activity long before this practice became common in the UK. This tendency was further increased after many of these TNCs were taken over by conglomerates, some of whom possessed limited, if any, interest in media and films as such\(^{11}\).

Along with these ownership advantages, which were an extension of knowledge generated by the parent company, the UK affiliates have also developed ownership advantages of their own, mostly related to local co-operation in and co-ordination of production. In the words of the managing director of one of these affiliates: '... what we get from Hollywood is very important. It gives us finance, reputation. But at the end of the day it is what we are doing here in Soho that is the most important. ...it is to put together all the different parts which make a
film, to hire the right people, have the right connections - with suppliers, post-production. This has little to do with Hollywood...’ The production affiliates have largely relied on local resources, such as talent (notably actors, directors), domestic studios, and services provided locally (post production, design, photography, etc.).

When asked what factors are most critical for their successful activity in the UK, these affiliates stressed the importance, along with marketing and managerial expertise, of their ability to establish and maintain links with local providers (or owners) of the resources abundant in the UK, and to co-ordinate production with local providers of various inputs. As the chief executive of a foreign affiliate based in Soho expressed it: ‘...nobody [no film producer], no matter how big, is self-sufficient. So many people with different skills are involved’ ‘...it is the nature of the production that it is very fragmented, and requires co-operation of various different activities, which is a complicated task by itself. ...personal connections are extremely important in this process ... They also help recruiting the right employees - we [like all film producers] employ large numbers of free-lance employees, according to the needs of specific films. ...commercial and social relations are mixed, and it is not possible to establish them from distance.’

The ownership advantages that emerge from the linkages of the affiliates within the locality are characteristics of the individual affiliate, rather than of the TNC as a whole. These advantages are dependent on the cluster of economic activity in Soho for their development and materialisation, and often they cannot be diffused to the rest of the TNC. The possession of such advantages provides the affiliate with an identity of its own, which is somewhat dissociated from that of the TNC as a whole. The managing director of a US production affiliate operating in Soho explained: ‘...in many ways we owe more to Soho than to Hollywood. ...the proximity to other firms based here is vital for our success, both with providers of services (notably the post production), and other film producers. These aspects
don't have much to do with LA [Los-Angeles]. They are happening here. We keep financial ties with the headquarters and sometimes do work together, but we co-operate more with firms based here [in Soho] than with our headquarters'. Similar views were also expressed by another respondent: ‘...much important business is generated in an informal way, through personal contacts. This is happening in Soho, it has nothing to do with our headquarters’.

The dynamics of learning and economies of externalities taking place among the firms based in Soho are regarded by these foreign affiliates as important determinants of their ownership advantages, as expressed by the managing director of a US affiliate which engages in film production in London: ‘... the whole business is about creating ideas, and other firms are often the source of new ideas ...sometimes you can get an idea just by having a few words with someone - and it has to be someone from the industry, so we speak the same language. [There is] a strong sense of learning from each other. Because we are involved in art - there isn’t really that kind of competition [as in other industries] - there is room for many movies as long as they are good. So we have nothing to hide from other companies - rather we see them as a source of inspiration and creativity. ‘..[Soho] is ‘a happening place’ - opportunities can arise when you go out to buy a sandwich.’' The appreciation of the economies arising from the cluster of economic activity as vital for their own performance was expressed by TNCs which, for the most part, have been more developed and advanced in terms of their technology, marketing and management than most of the local firms based in Soho. The creative nature of film production and the need for constant innovation are regarded by these firms as best realised in such an environment.

4.2. Location advantages

Different location advantages have affected film TNCs in the UK in terms of the type of investment undertaken. Distribution oriented investment has been driven by TNCs’ intention to expand the market
for their films, in order to increase the returns for their investment. The location advantages which attract this kind of investment are related to the size and growth prospects of the local market. The substantial size of the UK market, combined with the common language which makes this market more accessible by facilitating demand for US-made films, have made the UK the most favourable destination for US film distributors. Already in the early 1920s, the UK accounted for 10% of total revenues (Low 1997) and 35% of foreign revenues (Jarvie 1992) from film distribution by US TNCs. In the 1990s, the UK remains the main foreign market of these TNCs, just as it has been during most of the 20th century, with some of them obtaining as much as 50% of their foreign earnings from the UK (The Film Policy Review 1998).

Indeed, the choice of location of distribution affiliates within the UK has been affected by consideration of proximity to the main distribution markets rather than to other firms. In the early decades of the 20th century, when US TNC investment was predominantly distribution oriented, many of the affiliates operating in the UK which were listed in the telephone directory of the time were based away from the local film producer firms which were already then clustered in the Soho area. The current location of some of these affiliates in Soho (W1 postal code area) is mainly a result of historical heritage, and the purchase of their premises at a time when the nature of their operation and their links to the locality were different (see ahead). As the Public Relations manager of a distribution affiliate of one of the US majors expressed it: ‘...proximity to other firms located in Soho is not vital for us. ...I know it is critical in the industry but we are different because we don’t produce, we only distribute films produced elsewhere. ...The location in Soho - is probably for historical reasons. We need not be here today. Things were probably different in the past, and since then we are here, but it is certainly not important today’. The recent move of the affiliate of Warner Brothers, which deals predominantly with the distribution of films produced in Hollywood, to a bigger office outside Soho (in EC1), illustrates this situation
clearly. Another example is the location of the recently established Buena Vista International, the distribution affiliate of Disney, outside the Soho area (in W14).

Different location advantages have affected investment undertaken in order to use the UK as a production base. Of importance here has been the need to produce films with a ‘British identity’, and to take advantage of the specific characteristics of the immobile assets of the UK. For example, in the aftermath of the Second World War, the UK, and London in particular, seemed to provide a more authentic background for films based on themes of the War than Hollywood. The success of the Beatles and Bond films and of British pop music in the 1960s made British society exciting and fashionable, and fostered a belief that London, rather than Paris or Rome or Hollywood, was the most exciting place in the world to make films (Murphy 1992). Recently, British audiences have shown a growing preference for locally produced films (The Economist 1998, Screen Digest 1998a), pushing film producers towards the production of films which reflect British characteristics.

A second location advantage is low costs of factors of production. This location advantage has become particularly important since the 1950s and 1960s, with the financial difficulties faced by Hollywood producers, mostly as a result of the rapid spread of TV and escalating production costs in the US (Christopherson and Storper 1986, Storper 1989). The opportunity to produce films in the UK more cheaply, and sometimes considerably so, has been an important attraction ever since. The cost differences are such that on average 3 films and more could have been made in the UK for every 2 in Hollywood (Walker 1986).

Third, well developed production facilities are abundant in London. By the 1930s there were already about 20 advanced studios in the London area (Jarvie 1992), and several other studios were built during the 1940s and 1950s. In the 1960s well advanced post production
facilities started to develop in London, making use of state-of-the-art technology, and UK firms established a lead in this activity\textsuperscript{13}. In the 1990s, the largest sound stages in the world are at London's Pinewood and Shepperton studios. London boasts unrivalled post production facilities as well as the major film labs outside the US - London companies Rank and Carlton dominate the world film processing market (London Economics 1994).

Fourth, London is the international sales capital of the film industry, raising investment and assembling financing packages for Hollywood (London Economics 1994). In particular, the ability to raise funds locally has been a major attraction when fund raising in the US became more difficult. While the City of London has, for the most part, been reluctant to finance UK films, it has financed, and sometimes very generously, US films.

Last, but in no way least, is the pool of talents, notably in British theatres and TV, which could be used in films (Walker 1986). However, this asset is somewhat mobile (the move of British actress, directors and writers to Hollywood is well recognised), which may raise doubts as to whether it can be regarded as part of the location advantages of the UK. Nonetheless, this factor has been a major attraction for US TNCs. As a result of these advantages, London is regarded as the third largest film production centre (after Los Angeles and New York as the first and second centres respectively) (London Film Commission 1998).

Some of these location advantages are characteristics of London, and within it of Soho in particular, rather than of the UK as a whole. When asked what were the reasons for the choice of the UK as the location for their foreign activity, respondents referred to a combination of factors related both to the UK as a whole (language and low production costs) and to those which are tied to London and within it mostly to Soho (such as the cluster of film producers and post production services in Soho and other production facilities in
London). One interviewee expressed the view that ‘...it will be crazy to go anywhere [outside London]. .... If you want the back up and the support of the production facilities, you must be in London. There is no reason to go elsewhere.’

Production-oriented TNCs thus perceive geographic proximity to the cluster of indigenous film producers and service providers in Soho as necessary to provide access to the latter’s location advantages. The location patterns of the overwhelming majority of foreign affiliates which have engaged in film production in the UK over the last century provide strong support for this view (for example, 20th Century Fox, Warner Brother in the 1930s, Columbia in 1940, all purchased premises in the heart of Soho and still own them today).

The marketing manager of the London affiliate of a Dutch company (recently acquired by a Canadian conglomerate), based in Soho, explained the affiliate’s need to be in this location: ‘We have intense interaction with production houses, design companies - they are all local [in Soho]. Everything we need is in Soho: post production, design, all the facilities. It is more efficient to have all these facilities in a very short geographic distance. ...much of the work involves contact with other people. They are all almost exclusively in Soho and it is very convenient to be where everybody else is. ...there are also other media conglomerates based near us. It is good to be close to them - it gives good profile, and an opportunity to monitor their activity closely, via informal connections’.

A similar opinion was expressed by the chief executive of an American affiliate: ‘... we could not afford not to be in Soho - that’s where everybody is. It is an industry where you constantly change ideas and proximity helps doing it... this industry is about who you know - there are about 100 companies producing tv commercials - so why deal with strangers? Also when we need to hire people - for example, a director for a specific film - we take those we know from
personal contacts. ...there is also high prestige in a Soho address - we pay a high rent for it but we cannot do it without’.

4.3. Internalisation advantages

The reasons for the choice of modality to service the UK market, and for the preference to internalise particular value-added activities rather than obtaining them through the market vary across the various types of investment, and have changed over time, in line with the perception of the investing firms of the existence of market failures and the costs of transactions and their appreciation of local firms as suitable licensees.

As part of their overall vertically integrated strategy, US TNCs establishing distribution affiliates in the UK in the early decades of the 20th century adopted the strategy of setting-up fully-controlled affiliates rather than operating through local agents (Jarvie 1992). In most cases, this form of investment has been maintained ever since. There are four main reasons for preferring this modality over licensing for film distribution. First, it reduces the speculative element in film production by making films that are guaranteed international distribution. Film production is a highly risky activity, in which there are limited, if any, ways of anticipating the success of a film. Yet the entire costs of the production are incurred in the production of the first copy, without any guarantee of it finding a distribution outlet. This creates strong incentives to internalise the distribution. Second, by setting up wholly owned distribution affiliates, film producers retain 100% of the distribution rental, which is used as a source of revenues to finance future production, a major obstacle in this highly capital-intensive industry. A licensing deal will entail loss of commission and costs to a third party (while joint ventures involve revenue sharing and are therefore seldom used). A third influence is the difficulty of finding a licensee with the necessary capabilities. UK distributors have been small and financially weak relative to their US counterparts, a difference which has largely excluded the possibility
of finding licensees with adequate capabilities. Fourth, internalisation of distribution allowed US TNCs to employ the distribution expertise they had developed in their home market in the UK.

Because of these advantages of direct investment over licensing, full control over distribution has remained the common mode of most distribution-oriented investment in the UK, as the marketing manager of a well established US distribution affiliate explained: ‘...[licensing] is not an option we consider. ... to the best of my knowledge, it has never been considered in relation to the distribution in the UK. ...distribution by an agent usually involves parting with an agency commission as well as a distributor commission and is used only in countries where very few options are available, such as in less developed markets or in ones that need a high degree of local knowledge, but not in the UK’. The stability of this modality over the last century indicates that increased market knowledge and greater interaction with local firms are not perceived by these firms as changing the balance between the benefits of direct investment vs licensing.

As the activities of US TNCs in the UK widened over time to include co-production, they became engaged in various forms of co-operation with local producers, such as the provision of finance for and distribution of locally produced films, or participation in the actual production of the films. However, the dominant form of operation of these affiliates has remained one of direct investment. The reasons for preferring fully owned affiliates over licensing or other forms of contracting of these production affiliates differ considerably from those which affected the choice of the distribution affiliates. First, and most important, as the previous discussion highlights, the predominant source of advantage of US TNCs in the UK has been their privileged possession of intangible assets, such as reputation and specific knowledge of film production. The motivation to internalise the market for these advantages is substantial, as full ownership and control better enable firms to appropriate the economic rents of their
firm-specific capabilities and more effectively protect their proprietary rights and product quality. Second, direct investment has often qualified US TNCs to obtain incentives offered by British governments to local film production (Dickinson and Street 1985, Low 1997, British Film Commission 1996). Third, the costs of setting up a new affiliate are relatively low in this type of business, reducing the attraction of licensing.

This said, one major component of film TNCs’ activity in the UK that does often involve contracting rather than internalisation is the actual production of films. Over the years there has been a growing tendency for TNCs to acquire films through the market rather than producing them internally, because films from independent UK film producers are often cheaper and of higher quality. However, these TNCs have always retained a local presence in the UK in the form of fully-owned affiliates. The embeddedness of these affiliates in the locality has played a major part in this form of organisation of production. Their consequent increased familiarity with the market and with local producers has allowed the establishment of relations with and acquisition of knowledge on local producers necessary for this form of operation. Another factor that has probably affected this form of operation is the trend towards vertical disintegration of the parent companies, which took place in Hollywood from the 1950s onwards. In this process, studios in the US redefined themselves as profit centres, financing films produced by independent film producers (Christopherson and Storper 1986).

5. Discussion

A number of conclusions seem to emerge from this study of film TNCs in London. First, and most important, is the great variation in the significance of agglomeration economies across various types of investment. Economies of externalities modify the tenets of the eclectic paradigm to different degrees in different investments. Particularly important in this context is the distinction between
production-related investment (of the resource and export seeking types) and investment oriented towards selling and distributing films in a particular market (a kind of market seeking investment which does not involve local production). In the latter, investment is driven by demand rather than supply factors and the attraction of the market is determined primarily by its size. The orientation of the foreign affiliates tends to be towards the parent company and they develop limited links with the locality in which they operate, which in turn affects them to a limited extent, if at all. In contrast, when investment is undertaken in order to use a particular location as a production site, the affiliates tend to become closely involved with firms in their own or in related industries and to take an active part in accessing the economies of externalities available locally. These then become a vital part of their ownership advantages and of the location advantages which attract them. Some of this variation is illustrated in Figure 3, which highlights the type and contents of the links of the affiliates with the locality, more distant areas, and the headquarters.

Second, not all ownership advantages are affected by economies of agglomeration and not all of them to the same degree. Some advantages, notably those related to internal working processes and organisational routines, and those emerging from the proprietary rights of brand ownership or financial strength, are characteristics of individual TNCs and the boundaries of these TNCs, as defined by their ownership, are valid for understanding such advantages. In contrast, advantages emerging from an affiliate’s ability to innovate, to establish productive linkages with suppliers and customers, and to benefit from access to a common labour market, cluster of specialised intermediate inputs, and embedded knowledge of other members of the cluster, are influenced, and sometimes considerably so, by the close interaction of the TNCs with the cluster of firms in their own and in closely related industries. The conceptualisation of ownership advantages as defined by the ownership of the firm may be too narrow in these cases, as the links among firms based in geographical proximity form part of these advantages.
The latter advantages are, to a large extent, an outcome of the intertwining of firms and collective action in a dense transaction-intensive cluster. Consequently, they are tied to the locality which gave them rise and their possession distinguishes the affiliate from the other parts of the TNC. Access to these advantages is dependent on the ability of the affiliates to benefit from the externalities occurring in this locality. These advantages give the affiliates some identity of their own, which is independent of the parent and the TNC as a whole.

Third, the benefits from linkages with other firms are not confined to cases in which the investing firms are weaker than the cluster of firms, in terms of their technological and managerial knowledge, their financial strength, or the scope of their activity, nor are they related to the size of the investing TNC. For most of the 20th century, film TNCs investing in the UK (notably those of US origin) have been more advanced than indigenous Soho film firms, whose proximity they have sought. Furthermore, small and large TNCs alike have sought this proximity, with size by itself seeming to lack any impact on this need. Such proximity appears to provide film TNCs with two main types of advantages. The first are those related to reduced costs of transaction and co-ordination. Such costs are particularly high in the film industry, due to the fragmentation of the production process under different ownership. Second, the cluster of firms in Soho is perceived by the investing TNCs as facilitating the processes of creativity and innovation, so essential in the film industry. These reasons for seeking proximity to other firms differ considerably from investment by relatively weak firms, seeking to locate themselves in proximity to a cluster of excellence as a source of learning and as a way of acquiring new knowledge, which is mostly common among TNCs from less advanced countries investing in developed countries.15

Fourth, the location advantages which attract film TNCs to the UK, notably when such investment is production oriented, are a
combination of factors which characterise the UK as a whole (such as language, government policies, etc.) and those which are specific to London or Soho. The latter are embedded within the locality and immobile within the country. Firms perceive the benefits of these advantages to be confined to investment taking place in the particular locality providing them. It appears that the more TNCs cluster in a particular locality, the less adequate is the country as a whole as the unit of analysis for their location activities and the more important are the location advantages which are embedded in this locality. The location advantages which attract TNCs to invest in a particular locality may not be related to the availability of resources of any kind, but rather reflect the existence of a cluster of economic activity, possibly created as a result of historical accident.

Fifth, the economies arising from agglomeration of economic activity affect various location advantages to different degrees. They seem to have no impact on certain location advantages, notably advantages related to the abundance of certain resources, which often characterise the country as a whole. By contrast, access to some other location advantages, notably those confined to small localities within countries, may often depend on being part of a cluster of related activities.

Sixth, of the three tenets of the eclectic paradigm, internalisation advantages seem to be least affected by economies of agglomeration. The processes taking place within the cluster of film related activities in Soho have affected the modality chosen by these TNCs to serve the UK only to a limited degree. Notably, when the advantages of direct investment over licensing are considerable, diminishing costs of transactions, resulting from greater interaction with other firms based in the locality, do not affect the choice of modality. When there is a tendency to obtain certain value-added activity through the market rather than internalise them, the economies of agglomeration seem to be only one of several forces affecting this preference.
To conclude, the discussion thus far suggests that agglomeration economies in Central London are indeed a powerful factor affecting the investment activities and location decisions of film TNCs in the UK. However, this impact varies considerably by the type of investment and the specific advantages concerned. TNCs engaged in production and production related investments are affected by agglomeration economies to a much greater degree than distribution TNCs. Likewise, agglomeration economies considerably affect some ownership advantages and some location advantages while having limited, if any, effect on others. Acknowledgement of the impact of agglomeration economies within the framework of the eclectic paradigm would thus enhance the power of the latter to explain the patterns of TNC activities.

Given the exploratory nature of the study, and the fact that the lessons that emerge from it are based on observations drawn from a single industry, its findings should perhaps be interpreted as hypotheses for future research rather than as conclusions. A far more systematic empirical investigation is necessary in order to establish general conclusions about the impact of agglomeration economies on the investment activity of TNCs. The nature of film production, in which there are high levels of fragmentation and specialisation, is likely to make the economies arising from geographic proximity more important than in other service industries in which the nature of the production differs. Future research may examine the issues raised here in the context of service industries in which the complete, or large parts of the production process are carried on under a single ownership and there is less tendency towards vertical disintegration.
Notes

1. In some cases, such as the Swiss watch industry, the North Italy textile industry and the City of London financial district, TNCs have joined existing clusters which have initially developed without their participation. In other cases, particularly common in some of the more recently established clusters, TNCs are actively involved in the development of the clusters and in the subsequent dynamics taking place within them. Examples of such clusters are the car industry of North-East England, and some clusters of electronic production in the US, in which Japanese TNCs have played a dominant role (Dunning 1997).

2. Recent examples of these studies include Storper 1997, some of the papers in Lee and Wills 1997, and Scott 1998 which address the most important current issues from the perspective of economic geography; You and Wilkinson 1994, and Wilkinson 1998 which discuss them from the point of view of industrial economists; Krugman 1995, 1998 as the outstanding representative of the economic tradition that emphasises that ‘history matters’; and Porter 1994, 1998 and Enright 1995, 1998, who demonstrate a similar approach by business strategy scholars.

3. This development is explicitly acknowledged in the new edition of Dunning’s book (1958/1998). One of the main changes introduced in the second edition is related to the role played by the affiliates in the generation of ownership advantages. In the revised version there is a clear realisation of the active role played by the affiliates and the two way flow of knowledge and innovation.

4. These aspects of the ownership advantages of firms have received much attention in the network approach (see for example the papers in Forsgren and Johanson (eds.) 1992 and
Johanson and Mattsson, 1994), but until recently they have been dealt with mainly in the context of industrial marketing and have remained outside FDI theory (see Chen and Chen 1998 for an outstanding attempt to incorporate this approach into FDI theory).

5. This is not specific to the UK. The global film industry has been dominated by US TNCs since its origin around the turn of the 20th century. There are no statistical data to document this pattern. Anecdotal indications for it can be found in Nachum 1994.

6. Most of the activity within this postal code area is concentrated in and around a small district known as the Soho area, whose borders are commonly defined by Oxford St., Regent St., Charing Cross Road, and Leicester Square and the streets immediately adjacent to it (Tames 1994).

7. TNCs have had a powerful influence on the clustering of firms in Soho and have played a vital role in influencing the way this concentration has developed and operated. It is likely that the Soho cluster would not have developed to its current extent without TNCs. There are of course asymmetric relationships between the large, powerful TNCs and the community of small, mostly local firms, in Soho, an issue which is, however, somewhat outside the focus of this paper (see Harrison 1994 for a critical view of the role of large firms in small firm clusters such as Silicon Valley and part of Third Italy). It is discussed in Nachum and Keeble 1999.

8. This estimate refers only to foreign TNCs with established operations in the UK and excludes TNCs whose activities are limited to shooting or using production facilities for the production of a single film (though the latter kind of investment often has a considerable magnitude). For the purpose of this
study, it was judged that the long term investment is the main interest. The factors which attract short term investment differ, and sometimes considerably so, from those which affect TNCs with long term operations, and the theoretical framework developed here may be inadequate to examine this investment. For example, by its very nature, short term investment is affected by considerations such as exchange rate fluctuations, a factor which does not affect TNCs which seek to establish a more permanent operation in the UK. The exclusion of this type of investment may introduce some bias into the analysis which follows, as it is often the larger TNCs who establish long-term operations, while the smaller ones tend to favour temporary operations.

9. The cost structure of film production, in which virtually the entire cost is incurred in making the first copy and duplicates require little additional investment, makes it critical to reach the widest audience possible as a way to hasten the flow of revenues to producers (Vogel 1990). This characteristic favours international expansion of the distribution, and has been a major motivation for international activity in this industry (Nachum 1994).

10. On the location patterns of these affiliates and the reasons for them, see section 4.2 on location advantages.

11. These differences between UK and US firms are not confined to film production - see Chandler (1990) for an historical review of these developments in the two countries.

12. Location factors have been less relevant for investment particularly involving the financing of local production, as the factors which have driven this investment have either been legislation by British governments to force foreign affiliates to distribute films produced locally, or strategies of disintegration
pursued by the TNCs as a whole. Therefore location advantages are not discussed in the context of this investment.

13. Post-production is the process of converting the principal photography into a film, whereby all the different elements are brought together and manipulated until they reach a satisfying completion. In the course of this work the sound and picture are edited together, special effects and other optical effects are made and added, and the film’s music score composed and recorded. The role of London as a leading global centre of post-production services is discussed in Nachum and Keeble 1999.

14. Due to the specific nature of film production, in the film industry such investments correspond to horizontal and vertical investments respectively, but it may not necessarily and not always be so.

15. See Chen and Chen 1998 for Taiwanese investment and Lall 1996 for investment of TNCs from developing countries.
TABLES AND FIGURES
Table 1. British and foreign films produced in the UK, 1939-96
(Number of films, over 72 minutes)

<table>
<thead>
<tr>
<th>Year</th>
<th>British films (*)</th>
<th>Foreign films</th>
<th>British/foreign</th>
</tr>
</thead>
<tbody>
<tr>
<td>1939</td>
<td>103</td>
<td>535</td>
<td>0.192</td>
</tr>
<tr>
<td>1945</td>
<td>40</td>
<td>191</td>
<td>0.209</td>
</tr>
<tr>
<td>1950</td>
<td>74</td>
<td>308</td>
<td>0.240</td>
</tr>
<tr>
<td>1955</td>
<td>82</td>
<td>268</td>
<td>0.305</td>
</tr>
<tr>
<td>1960</td>
<td>79</td>
<td>254</td>
<td>0.311</td>
</tr>
<tr>
<td>1965</td>
<td>69</td>
<td>233</td>
<td>0.296</td>
</tr>
<tr>
<td>1970</td>
<td>85</td>
<td>275</td>
<td>0.309</td>
</tr>
<tr>
<td>1975</td>
<td>70</td>
<td>212</td>
<td>0.330</td>
</tr>
<tr>
<td>1980</td>
<td>41</td>
<td>178</td>
<td>0.230</td>
</tr>
<tr>
<td>1990</td>
<td>24</td>
<td>29</td>
<td>0.827</td>
</tr>
<tr>
<td>1995</td>
<td>35</td>
<td>42</td>
<td>0.833</td>
</tr>
</tbody>
</table>

(*) As a result of varying definitions of what constitute 'British films', published information from different sources vary considerably. In this table, British films are defined as films where there is UK cultural content and a significant amount of British finance and personnel. Foreign films are those produced in the UK with only minor financial and/or creative involvement of UK resources. However, these definitions leave much room for ambiguity, particularly when applied to data from different sources, which implies that the data should be interpreted with great caution.


Table 2. British and foreign films distributed in the UK, 1926-1996
(Number of films and shares of total)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total number of films distributed in the UK</th>
<th>Share of all films distributed by US firms (%)</th>
<th>Total number of British films distributed in the UK</th>
<th>Share of all British films distributed by US firms (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1926</td>
<td>580</td>
<td>46</td>
<td>18</td>
<td>11</td>
</tr>
<tr>
<td>1929</td>
<td>504</td>
<td>52</td>
<td>52</td>
<td>31</td>
</tr>
<tr>
<td>1950</td>
<td>400</td>
<td>55</td>
<td>72</td>
<td>10</td>
</tr>
<tr>
<td>1958</td>
<td>360</td>
<td>67</td>
<td>84</td>
<td>42</td>
</tr>
<tr>
<td>1971</td>
<td>235</td>
<td>75</td>
<td>74</td>
<td>59</td>
</tr>
<tr>
<td>1980</td>
<td>188</td>
<td>82</td>
<td>36</td>
<td>22</td>
</tr>
<tr>
<td>1990</td>
<td>217</td>
<td>50</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>1996</td>
<td>264</td>
<td>54</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>

Figure 1. Agglomeration economies and the eclectic paradigm

**Location Advantages (L.A.)**
- the country vs the region
- the mobility of L.A. within countries
- agglomeration economies as a L.A. by itself

**Ownership Advantages (O.A.)**
- o.a. and the links with other firms
- mobility of o.a.
- o.a. and affiliate-headquarter links

**DIRECT INVESTMENT**

**Internalisation Advantages (I.A.)**
- agglomeration affecting the costs of transactions
- agglomeration as changing the balance between various modalities
Figure 2. Location of foreign affiliates and British-owned film producers and distributors in London

Figure 3: The links of film affiliates in London with the locality and the headquarters, by type of investment

**Distribution**
(Vertical investment)

**Finance**

**Production**
(horizontal investment)
includes co-production
References


British Film Commission (1996), Guide to Film Production in the UK London: The British Film Commission


Forsgren M. and Johanson J. (eds.) (1992), Managing Networks in International Business Gordon and Breach: Philadelphia and Reading


45


Nachum L. and Keeble D. (1999), “Neo-Marshallian nodes in global networks: The media industries in the Soho and Covent Garden areas” mimeo, Cambridge University, ESRC Centre for Business Research


Richardson J. (1995), Covent Garden Past (London: Historical Publications)


Screen Finance (1990), “Fox set to sign development deal in first London production move” May 2, p. 6,7


Screen Finance (1998), “Film finance UK” March 19, pp. 4-6


APPENDIX
### Appendix A. some characteristics of the TNCs interviewed for this study

<table>
<thead>
<tr>
<th></th>
<th>nationality</th>
<th>Nature of activity in the UK</th>
<th>size (b)</th>
<th>age (c)</th>
<th>London location</th>
<th>interviews (d)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>British/Dutch</td>
<td>Production and distribution of films, mostly for TV</td>
<td>350</td>
<td>1986</td>
<td>W1 (e)</td>
<td>3</td>
</tr>
<tr>
<td>2</td>
<td>Dutch/Canadian</td>
<td>Production and distribution of films; limited finance</td>
<td>120</td>
<td>1991</td>
<td>W1</td>
<td>2</td>
</tr>
<tr>
<td>3</td>
<td>American</td>
<td>Production of films and ads.</td>
<td>7</td>
<td>1994</td>
<td>W1</td>
<td>1</td>
</tr>
<tr>
<td>4</td>
<td>American</td>
<td>Finance and distribution of films</td>
<td>40</td>
<td>1992</td>
<td>W14</td>
<td>2</td>
</tr>
<tr>
<td>5</td>
<td>American</td>
<td>Finance and distribution of films; limited production</td>
<td>n.a.</td>
<td>1930s</td>
<td>EC1 (f)</td>
<td>1</td>
</tr>
<tr>
<td>6</td>
<td>American</td>
<td>Finance and distribution of films</td>
<td>60</td>
<td>1933</td>
<td>W1</td>
<td>2</td>
</tr>
<tr>
<td>7</td>
<td>American</td>
<td>Finance and distribution of film and TV</td>
<td>80</td>
<td>1940</td>
<td>W1</td>
<td>1</td>
</tr>
<tr>
<td>8</td>
<td>American</td>
<td>Distribution and production of film and TV</td>
<td>300</td>
<td>1985</td>
<td>W1</td>
<td>2</td>
</tr>
<tr>
<td>9</td>
<td>French</td>
<td>Production and distribution of films</td>
<td>50</td>
<td>1910</td>
<td>W1</td>
<td>3</td>
</tr>
<tr>
<td>10</td>
<td>American</td>
<td>Production of films</td>
<td>20</td>
<td>1990</td>
<td>W1</td>
<td>2</td>
</tr>
<tr>
<td>11</td>
<td>German</td>
<td>Distribution of films</td>
<td>30</td>
<td>1990</td>
<td>W1</td>
<td>3</td>
</tr>
<tr>
<td>12</td>
<td>Canadian</td>
<td>Distribution of animation films</td>
<td>3</td>
<td>1992</td>
<td>W1</td>
<td>1</td>
</tr>
<tr>
<td>13</td>
<td>American</td>
<td>Finance and distribution of films</td>
<td>35</td>
<td>1981</td>
<td>W1</td>
<td>1</td>
</tr>
<tr>
<td>14</td>
<td>American</td>
<td>Finance and distribution of film</td>
<td>20</td>
<td>1993</td>
<td>W1</td>
<td>2</td>
</tr>
<tr>
<td>15</td>
<td>French</td>
<td>Production of films</td>
<td>15</td>
<td>1990</td>
<td>NW1</td>
<td>1</td>
</tr>
<tr>
<td>16</td>
<td>American</td>
<td>Finance and distribution of film and TV</td>
<td>25</td>
<td>1985</td>
<td>NW1</td>
<td>2</td>
</tr>
</tbody>
</table>

(a) Nationality - defined by the location of the headquarters (see Nachum 1999, chapter 2, for detailed discussion of the rationale for this choice).

(b) Measured by number of permanent employees. In the case of film production affiliates, this measure provides only partial picture of the size of firms, as these firms employ large number of free-lance employees. However, since the number of the latter changes in line with the needs of specific films, it cannot be used as a measure for the size of firms.

(c) Year of establishment of the UK affiliates.

(d) Number of people interviewed in each TNC.

(e) In most cases, TNCs based in the W1 area code are concentrated in the Soho area.

(f) Based in W1 until 1998.