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Multinational Firms

Effects on World Economy and Influence on the Global Governance

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LIST OF ABBREVIATIONS

ASEAN	Association of South East Asian Nations
CSR	Corporate Social Responsibility
CSV	Creating Shared Value
EC	European Community
EEC	European Economic Community
EMU	European Monetary Union
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HRW	Human Rights Watch
ICT	Information and Communication Technology
IIAs	International Investment Agreements
ILO	International Labour Organization
IMF	International Monetary Fund
IT	Information Technology
JV	Joint Venture
M&A	Merger and Acquisition
MNE	Multinational Enterprise
NAFTA	North America Free Trade Agreement
NGO	Non-Governmental Organization
OECD	Organisation for Economic Co-operation and Development
OLI	Ownership/Location/Internalisation

R&D	Research and Development
RIA	Regional Integration Agreements
TNC	Transnational Corporation
TNI	Transnationality Index
TRIMs	Trade-Related Investment Measures
UNCTAD	United Nations Conference on Trade and Development
WEF	World Economic Forum
WOS	Wholly-Owned Subsidiary
WTO	World Trade Organization

ABSTRACT

Nel 21° secolo le multinazionali hanno raggiunto una crescita considerevole, e si sono diffuse su così larga scala che oggi è necessario considerarle come attori molto importanti nel mondo globalizzato. A partire dai telefoni cellulari alle auto, dalle scarpe ai gioielli, dal caffè bevuto a casa all'hamburger di un fast food, è sempre più probabile che i prodotti che caratterizzano la nostra vita quotidiana siano messi sul mercato dalle aziende multinazionali. Non si può ormai più negare che abbiano un impatto considerevole nelle nostre vite, e le loro attività si sono estese ad un punto tale che i loro effetti devono essere valutati non solo in termini di vite individuali ma anche in termini macroeconomici, per gli impatti che hanno a livello internazionale. Oggi, come in passato, le loro azioni sono state l'oggetto di molti dibattiti, i quali arrivano spesso alla conclusione secondo cui le multinazionali sono cattivi attori, che agiscono solo per il proprio esclusivo interesse, commettendo ingiustizie come lo sfruttamento di lavoro minorile, evasione delle tasse e inquinamento dell'ambiente. Tuttavia molti studi confutano queste posizioni e dimostrano invece che i fatti tendono a screditare questi pregiudizi. Naturalmente queste valutazioni vengono effettuate prima di tutto nel campo in cui le multinazionali agiscono di più, cioè la sfera economica, ma tengono in considerazione anche l'influenza che esercitano in campo sociale e culturale. Per quanto riguarda il loro contesto principale, le multinazionali hanno giocato un ruolo così fondamentale nella sempre crescente integrazione economica globale che spesso sono state definite come la più evidente manifestazione del processo di globalizzazione. In questa tesi i principali punti di cui si tratterà sono 3: nella prima parte si studierà la multinazionale all'interno dell'ambito economico, analizzandone caratteristiche, modalità di diffusione, ed esaminando i vari approcci di studio presenti in letteratura. In una seconda parte ci si focalizzerà sugli effetti economici che l'azienda multinazionale può avere nel paese ospite e nel proprio paese d'origine, nonché sui possibili impatti sull'ambiente. Infine, nella terza parte verranno analizzati il ruolo e peso politico che possono avere oggi le multinazionali nel contesto di una governance globale, valutando i rapporti esistenti con gli stati e le organizzazioni non governative.

Il concetto di globalizzazione sarà il punto di partenza dell'analisi: si vedrà come questo processo si sia sviluppato nel corso degli anni, quali cambiamenti e innovazioni abbia portato, soprattutto a livello economico. Verranno presentati due opposti corpi d'opinione riguardo alla globalizzazione, uno che vede con favore questo fenomeno, notando come abbia portato benefici per gran parte della popolazione, e un altro che invece vi si oppone, vedendo in esso la causa delle disuguaglianze e dei problemi sociali e ambientali. Si noterà comunque che entrambe le linee di pensiero sono concordi nell'affermare che la globalizzazione ha portato a una più profonda connessione e integrazione dei mercati, processo di cui le multinazionali si sono rivelate le protagoniste. Le percezioni a riguardo della condotta di queste ultime sono però spesso ambivalenti: se da una parte vengono apprezzate per l'innovazione, la conoscenza e la tecnologia che possono portare con sé, dall'altra invece vengono temute perché percepite come una minaccia per la ricchezza e l'identità nazionale. Dal momento che rappresentano la principale caratteristica distintiva delle multinazionali, e l'indicatore più significativo della rilevanza del fenomeno multinazionale, si studierà attentamente l'importanza degli investimenti diretti esteri. Il crescente coinvolgimento in investimenti verso l'estero ha contribuito notevolmente al processo di frammentazione della produzione e alla diffusione mondiale di tecnologia e innovazione. Verrà poi fornita una descrizione generale della geografia delle imprese multinazionali, prendendo in considerazione sia la locazione delle sedi centrali, sia quella delle affiliate. Infine, verrà analizzata la diffusione geografica degli investimenti esteri, identificando quali siano i principali paesi investitori e quali invece i principali riceventi.

Nel secondo capitolo verrà fornita un'analisi dettagliata dell'impresa multinazionale. Inizialmente si cercherà di trovare una definizione di questo attore che consideri tutti i diversi contributi presenti in letteratura. La presenza di diverse definizioni è dovuta al fatto che le multinazionali non costituiscono una categoria omogenea, bensì si distinguono a seconda dei livelli di diffusione, gradi di penetrazione dei mercati stranieri, meccanismi operativi e culture d'affari. Verrà poi offerta una visione d'insieme della storia delle multinazionali, con l'intento di dimostrare che esse sono attori piuttosto vecchi, che hanno influenzato gli eventi dell'economia globale da

tempi remoti. La loro influenza oggi non deve essere data per scontata, ma deve essere vista come il risultato di un percorso di sviluppo e miglioramento incessante. I primi contributi che cercano di spiegare l'esistenza delle multinazionali risalgono agli anni '60. In questa parte del capitolo si cercherà di revisionare alcune delle teorie economiche più importanti sull'esistenza e crescita di questo attore, a partire dal modello proposto da Hymer sui vantaggi esclusivi di un'impresa, continuando con la teoria del ciclo di vita del prodotto di Vernon, per terminare con il paradigma OLI o paradigma eclettico di Dunning. Questi modelli cercarono per la prima volta di identificare le motivazioni che spingono le multinazionali a investire all'estero, ma il quadro teorico più completo viene fornito da Dunning nel 1993. Per analizzare in modo approfondito queste motivazioni, è necessario studiare il processo di produzione internazionale con l'aiuto di modelli interpretativi capaci di individuare le differenze tra i diversi tipi di investimento diretto estero. Infatti, un investimento fatto con l'obiettivo di ottenere l'accesso e di sfruttare particolari materie prime (resource seeking investment), è sicuramente diverso dall'investimento fatto per vendere un determinato prodotto o servizio in un mercato straniero (market seeking investment), e da quello il cui obiettivo è di raggiungere migliori livelli di produttività e migliori performance (efficiency seeking investment) e infine è differente dall'investimento che viene fatto per entrare in possesso di competenze e capacità considerate essenziali (strategic-asset seeking investment). Inoltre, per valutare gli effetti della produzione internazionale è importante considerare anche la modalità di ingresso nel mercato estero scelta dalla multinazionale. Infatti, gli effetti derivanti dalla creazione all'estero di impianti completamente nuovi, attraverso un investimento greenfield, saranno diversi dagli effetti che nascono da operazioni di fusione e acquisizione o da joint venture. Nel capitolo poi verrà affrontato un argomento che ancora oggi rappresenta uno dei principali punti di divergenza nel dibattito sulle multinazionali: il radicamento territoriale. Per alcuni studiosi la caratteristica di essere liberi da qualsiasi vincolo o connessione territoriale è fondamentale e distintiva delle imprese multinazionali; per altri invece, che prendono in considerazione l'indice di transnazionalità, il paese d'origine rimane ancora molto importante e rappresenta il contesto principale d'attività. Sono le differenze presenti nella mentalità d'affari, nella disponibilità di infrastrutture e di forza lavoro qualificata che spingono le multinazionali a mantenere

alcune attività nel paese di origine, e a localizzarne all'estero delle altre. Si riporterà infine il concetto ideato da Doz, Santos e Williamson sulle imprese metanazionali, attraverso il quale gli autori suggeriscono come le imprese potrebbero sfruttare con successo la conoscenza che è nascosta in tutte le località disperse in cui operano. Per concludere verranno analizzate le principali determinanti che influenzano questa scelta della localizzazione.

L'obiettivo del terzo capitolo è quello di fornire un'analisi degli impatti che le multinazionali possono avere nei paesi ospiti, nei rispettivi paesi d'origine ed infine sull'ambiente. Esiste una difficoltà intrinseca nella valutazione di questi effetti a causa di quello che viene chiamato problema controfattuale, ossia l'impossibilità di stabilire con sicurezza cosa sarebbe successo se l'investimento non fosse stato fatto. A seconda delle percezioni di positività o negatività dell'investimento, gli studiosi, policy makers e gente comune hanno spesso basato le proprie supposizioni sulla desiderabilità degli investimenti esteri. Praticamente ogni connotazione positiva o negativa è stata attribuita alla condotta delle multinazionali, a seconda che si sia ideologicamente a favore o contro la globalizzazione e i suoi attori. Mentre spesso queste valutazioni sono date sulla base di pregiudizi, in questo capitolo le affermazioni verranno basate sull'evidenza empirica e sull'abbondante letteratura presente sull'argomento. Le conclusioni a cui si giungerà risultano piuttosto sorprendenti, in quanto contraddicono le opinioni più diffuse. Per quanto riguarda gli effetti degli investimenti in entrata, verranno considerati aspetti quali l'iniezione di capitali, la creazione di collegamenti con le imprese domestiche, le ripercussioni sulla misura e qualità dell'occupazione e gli effetti sui salari. Riuscire ad avere un quadro chiaro e trasparente di questi effetti è importante perché su questa conoscenza i paesi ospiti basano le loro politiche di attrazione o restrizione degli investimenti. Per gli effetti sui paesi d'origine, si studieranno le ripercussioni degli investimenti in uscita sull'occupazione e sulla composizione della forza lavoro. Infine, per quanto riguarda l'ambiente, verrà screditata l'opinione comune secondo cui le multinazionali tendono a spostare la produzione dove la regolamentazione ambientale è più indulgente. Si vedrà anzi che spesso esse adottano tecnologie moderne e avanzate che permettono loro di inquinare meno e di essere più produttive.

Nell'ultimo capitolo si tratterà della rilevanza dell'impresa multinazionale come attore politico nel contesto delle relazioni internazionali, in particolare nella loro relazione con gli stati e in maniera minore con le organizzazioni non governative. All'inizio si darà una nuova valutazione della posizione occupata dagli stati nel contesto della globalizzazione e alla luce della crescente importanza delle multinazionali. E' opinione diffusa che gli stati stiano a tal punto perdendo la propria autorità da non venir più considerati giocatori di rilievo nell'arena internazionale. Si sosterrà invece l'idea secondo cui gli stati esercitano ancora un'influenza considerevole sulle questioni globali e quindi anche sugli aspetti economici. Come regolatori dell'attività economica gli stati possono adottare misure e politiche che influenzano i meccanismi e le dinamiche delle imprese multinazionali. Tuttavia, anche se la loro importanza non viene messa in discussione, è necessario notare che comunque il loro ruolo si è modificato. Lo stato è passato dall'essere l'unico detentore dell'autorità ad essere uno tra diversi attori economici, e pertanto ha dovuto incrementare le interazioni con un'altra parte influente, cioè le multinazionali. Nel corso degli anni la loro relazione si è sviluppata, ma non è mai stata semplice e ben definita. Gli stati hanno a loro disposizione una serie di misure con cui possono condizionare la misura e il tipo di investimento, ma nonostante queste limitazioni la rilevanza delle multinazionali come attore politico emerge dall'influenza che riescono ad esercitare non solo nel campo economico, ma anche nella sfera culturale e sociale. A proposito del ruolo esercitato dalle multinazionali in ambito sociale, verrà riportata la teoria del valore condiviso di Porter, il quale sostiene la necessità di operare una rivalutazione delle multinazionali che porti a vedere questo attore non più come la causa di problemi sociali bensì come la loro soluzione. Secondo questo punto di vista le imprese operano il bene sociale perché così facendo inseguono anche il proprio personale interesse, perché ciò che è buono per la società è buono anche per l'impresa. Tutto ciò potrà essere reso ancora più fruttuoso nel momento in cui multinazionali, governi e ONG cominceranno a vedersi come partner, mettendo da parte i rispettivi pregiudizi e collaborando insieme per raggiungere obiettivi di larga portata.

INTRODUCTION

In the 21st century multinational firms have grown so considerably and they have spread so widely that we need to consider them as very important actors in today's globalized world. From mobile phones to cars, from shoes to jewels, from the coffee we drink at home to the hamburger we eat in a fast food shop, it is highly likely that the products of our everyday life are supplied by multinational firms. It is undeniable that they have a considerable impact on our life, but their activities have been increasing and have expanded to an extent that, today, their effects must be evaluated not only in terms of single individual existences but also in macroeconomic terms, for the impacts they have at the international level. For years their actions have been, and still are nowadays, the object of many different debates, which often come to the conclusion that sees multinational firms as wicked actors, behaving only for self-interest, committing iniquities such as child exploitation, tax evasion and environmental pollution. Many studies, however, confute these positions and demonstrate that facts, in reality, tend to discredit these prejudices. Of course, evaluations are made especially in the context in which multinationals operate more, namely the economic sphere, but they also take into consideration their influence in affecting the cultural and social fields as well. As for their main context, multinationals have been playing such an important role in increasing the global economic interdependence that, often, they have been said to be the most evident manifestation of the process of globalization. In this thesis we are going to deal with three principal issues: the first part will study multinational firms as merely economic actors, analyzing their characteristics, modalities of action and examining the different contributions on their study made by scholars in literature; in the second part we will study the effects that multinationals can have on host countries, on countries of origin and on the environment; and finally we will analyze the relevance of multinational firms as political actors in the context of the global governance.

The concept of globalization will be the starting point: we are going to study how globalization has developed throughout the years, which changes and innovations it has brought and with what consequences, especially on the economic level. We will

see that there are two opposite bodies of opinion regarding globalization, one that favours and one that opposes this phenomenon. According to whether one belongs to one category or the other, the effects of this phenomenon will be seen respectively in a favourable light, noting that this process brings benefits for the largest part of the world population, or in a bad light, underlining that it is the cause of most of the existing inequalities and of social and environmental problems. However, something on which both parties agree is the fact that globalization has led to a deeper connection and integration of the markets, a process in which multinational firms have showed to be the protagonists. Still, as in the case of globalization, the perceptions towards their conduct is ambivalent: if on one side they are appreciated for the innovation, knowledge and technology they can bring to a country, on the other side they are also feared because they are seen as a threat to national identity and wealth. Since it represents probably the main distinctive feature of the multinational enterprises, we will then study the importance of foreign direct investments: the always increasing involvement in investments abroad has given a considerable contribution to the process of fragmentation of the production and to the international spread of technology and innovation. The chapter will go on providing a general description of the geography of multinational firms, taking into account both the location of headquarters as well as of affiliates and subsidiaries. Finally, the last section will deal with the geographical diffusion of foreign direct investments, identifying which countries have been historically the principal outward investors and which countries, instead, have represented the main investments recipients.

In the second chapter the reader will be provided with a deep and detailed analysis of the institution of the multinational firm. Initially, we will try to come up with a definition of multinational enterprise that takes into account the various different contributions that have been given in literature by several scholars. Distinct definitions derive from the fact that multinationals do not constitute a homogeneous category; rather, dissimilarities stem from different sizes, different levels of diffusion, different degrees of penetration of foreign markets, different operating mechanisms and business cultures. Then, we will continue by offering a general overview on the history of the internationalization of the production, to show that multinational firms

are quite old actors that have been affecting the events in the global economy since ancient times. Their influence today should not be taken as a given, but it must be seen as a success that has been achieved as the consequence of a path of continuous development and improvement. The first contributions that try to explain the existence of multinational enterprises date back to the 1960s, when several scholars started wondering why firms should engage in transnational production. We will try to review some of the most preeminent economic theories over the existence and growth of multinationals, starting from the "ownership-specific advantages" of Hymer, continuing with Vernon's model of the product life-cycle, arriving at the eclectic or OLI paradigm of Dunning's theory. These models tried to find the first motivations that pushed multinationals to invest abroad, but the most complete framework was provided by Dunning in 1993. In order to analyze carefully these reasons, it is necessary to study the international production with the help of interpretative models capable of understanding the differences among the several kinds of foreign direct investment. For instance, an investment made with the aim of gaining access to and exploiting a particular raw material (resource seeking investment), is certainly different from the investment made to sell a determined product or service in the domestic market of the host country (market seeking investment); it is also distinct from the investment whose objective is to reach an increased productive efficiency and a better performance (efficiency seeking investment), and finally it is different from the so-called strategic-asset seeking investment, whose purpose is to come into possession of competences and capabilities that are considered essential. Besides, to evaluate the effects of the international production it is important to take into consideration also the mode of entry into the foreign market chosen by the multinational firm. In fact, the effects deriving from the creation of a completely new productive establishment abroad (through a greenfield investment) will be considerably different from the effects related to operations of mergers and acquisitions and of joint ventures. The chapter then deals with a topic that represents one of the main points of diversion in the current debate on multinationals: it concerns the territorial embeddedness of multinational firms. While for some scholars the characteristic of being free from any territorial connection is fundamental and distinctive of the transnationality of multinationals, according to others, and thanks to evidence resulting from the

transnationality index, it becomes clear that the country of origin still matters a lot and that it continues to represent the prevalent context of activity. Differences in the business mentality, in the availability of infrastructures and in qualified labour force will push multinationals to keep some activities at home, and to locate abroad some others. Finally, we will also report the concept of Doz, Santos and Williamson on metanational firms, a notion through which they suggest how firms can successfully exploit the knowledge that is hidden in all the scattered locations where they operate. Since, as we will see, multinational activity is likely to be geographically localized in specific areas, we are going to see which are the determinants influencing the choice of location.

In the second part, corresponding to the third chapter, the objective is to give an analysis of the impacts and of the consequences that multinational firms can have in the foreign host countries in which they decide to establish their production, in their countries of origin, and also, moving beyond the purely economic aspect, on the environment. As a starting point, we underline the intrinsic difficulty in evaluating these effects because of what has been called the counterfactual problem: that is to say that we cannot know for sure what would have been the situation if the investments were not made. According to the perceptions of positivity or negativity of the investments, scholars, policy makers and common people have based their assumptions over the desirability of foreign investments. Virtually every positive or negative connotation has been given to the conduct of multinational enterprises, according to whether one is ideologically in favour of globalization and of its actors, or in opposition to them. However, while these judgements have often been taken out of prejudices, we are going to base our statements on the empirical evidence and on the abundant literature on the topic. The conclusions we are going to reach are quite surprising since, in most cases, they contradict the conventional wisdom. As for the effects that inbound investments can have on the local economy, we will take into consideration aspects such as the injection of capital, the creation of linkages with domestic firms, the repercussions on the size and quality of employment, and on wages. To have a true and transparent framework of the impacts of inward investments is very important because host states would base their policies of

attraction or restriction of the investments on these assumptions. As for the effects on home countries, we will study the repercussions of outbound investments on the employment and on the compositions of labour force. Finally, regarding the environment, we will discredit the widespread opinion according to which multinational firms tend to move production where environmental regulations are laxer, namely in the pollution havens. Rather, they often adopt state-of-the-art technologies that enable them to pollute less, and they push governments to make these technologies compulsory, so they actually contribute to the raising of environmental standards.

The last chapter is dedicated to the study of the relevance of the multinational firm as a political actor in the international arena, in particular in its relations with states and NGOs. At the beginning we try to give a new evaluation of the position of states in the context of globalization and in the light of the increasing importance of multinationals. While it is commonly believed that states are losing authority and can no longer be considered significant players in the international context, we support the idea that states still exercise a considerable influence on global issues, and also on economic aspects. As regulators of the economic activity, states can adopt measures and policies that influence the mechanisms and the dynamics of multinational firms. Nevertheless, even if their status in the international context cannot be questioned, it is also undeniable that some of their roles have changed. From being the sole holder of authority, the state has now become one among several economic actors, and it has been forced to intensify its interactions with an increasingly influent party, namely the multinationals. The relationship between these two parties is not easy and straightforward, because, if on the one hand they share some economic objectives, on the other hand there are issues in which their points of view differ considerably. We are going to study how this relationship has developed throughout the years, and to see which are now their respective advantages during the bargaining process. We will see that there are several measures that states can adopt in order to influence the size and the kind of foreign direct investments, starting from conditions of entry into the market, performance requirements and exit conditions. Finally, we will analyze how more and more often multinational firms are exercising their influence not only on

economic aspects, but also on cultural and social issues, increasingly resembling a complete political actor. Related to this topic is the theory of creating shared value by Porter and Kramer, that is reported at the end of this chapter. According to these scholars, it is necessary to re-evaluate the conduct of multinational firms to shift them from being the cause of social problems to the possible solutions of them. According to this point of view, multinationals adopting this concept will actually create social value by pursuing their self-interests, and they will do it even more successfully when they work together with governments and NGOs, putting aside their respective prejudices and divisions and collaborating to reach large scale solutions.

1. WHAT IN THE WORLD IS GOING ON?

1.1 Globalization is the way

Nowadays the word "globalization" is on everyone's lips. It touches virtually all aspects of human life: culture, politics, society, economy and so on. Many things have been said about globalization, and many definitions have been given by politicians, academics and journalists. It seems that this word has become a "catch-all" term: it has been given credit for all the good and it has been blamed for all the bad happening in the world. According to Dicken (2007), the word globalization is not only one of the most used, but one of the most *mis*used and *con*fused as well[1].

The term was first coined in the 1960s but it came into vogue during the 1990s. During these years there was a rising awareness of the interconnection of the world: it became evident that, very often, events happening in one part of the world would have deep and quick effects on the life of people in other parts of the world. This interrelation was clear also when considering the products of everyday life: the geography of production, distribution and consumption was increasingly becoming, if not global, at least much wider. Products started to be complex enough to require different parts, and these many parts began to be produced in distinct countries, implying several stages of production, and then they were assembled somewhere else. A single state did not accommodate the whole production process anymore. In the words of Joseph Stiglitz, winner of the nobel prize in economics in 2001, globalization:

> "Fundamentally is the closer integration of countries and people of the world which has been brought about by the enormous reduction of costs of transportation and communication, and the breaking down of artificial barriers to the flows of goods, services, capital, knowledge, and (to a lesser extent) people across borders[2]".

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[1] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy.* London: SAGE Publications Ltd, p. 3.

[2] J. Stiglitz (2006) *Globalization and its discontents.* London: Penguin Books, p. 9.

This process was caused mainly by the developments occurring in two sectors: transportation on one hand, and information and communication on the other. For the biggest part of history these two kinds of technology travelled at the same speed: information could only move as far and as quickly as the transport infrastructure allowed. However, this connection was broken thanks to the invention of electronic technology[3], which enabled information to travel much faster. Advancements in transportation technologies continuously decreased the costs of transport, which have been very high for a long time in human history. Major innovations in this field were the use of steam power and the development of the railways. Of staggering importance was the introduction of containers in the 1950s. These steel boxes allowed the storage and movement of big quantity of products, and they simplified the passage from one mode of transport to another. The use of containers drastically reduced the time necessary to load and unload ships, and it reduced the costs of transporting freights over long distances. As for information and communication technology (ICT), improvements in electronic communication have changed the speed at which information travels. The telegraph, the telephone, computers, the internet, all these advancements meant lower communication costs and therefore increased communication and exchange among people located in different and faraway countries. Wolf reports the incredibly large and fast developments of the last century: there was a huge decrease in the price of a three-minute phone call from New York to London: from 250 $ in 1930 to few cents today; there are about 30 million internet users today, but they were only 5000 back in 1986[4]. All these developments led someone to speak of "the end of geography" (O'Brien, 1992) or "the death of distance" (Cairncross, 1997). However, according to some scholars, these claims can be misleading. In fact, even though these innovations "have shrunk the world" somehow, places and distance will always play a relevant role.

Particularly important in the process of globalization have been the changes in states' policies: barriers to the flows of goods, services and people, imposed by

[3] P. Dicken (2007)) *Global Shift: mapping the changing contours of the world economy,* p. 79.

[4] M. Wolf (2001) *Will the Nation-State Survive Globalization?*, in *Foreign Affairs,* n° 80, pp. 181-182.

governments, have been falling. States have become more accessible and penetrable to other countries. According to Wolf, these policies, and not technology advancements, have represented the main incentive towards international economic integration. In fact, while in the last century and a half technological innovations have always pushed towards a more integrated world, the same cannot be said for states' policies. Only in the 1970s did a strong push towards liberalization start in the developed countries, then spreading to the developing ones and reaching also the former communist states in the 1990s. From that moment on, we can say that this trend has continued.

As it was said before, globalization covers different aspects of life, ranging from culture to economy. However, in this thesis the focus will be on the economic one. Still, it is important to note that a clear-cut division among these features is not possible, since they are all embedded with each other. Therefore, economy itself cannot be considered an isolated entity, but it is quite deeply linked to the political, social and cultural environment in which it works.

Looking more deeply at this economic side, we can say without any doubt that globalization implies a profound degree of connection and a greater integration of the market, and an increase in the exchange of goods among different countries of the world. There is a key to read this highly interconnected system: it consists of thinking "of economic processes (production, distribution, consumption) in terms of *connections* of activities, linked through *flows* of both material and non-material phenomena into circuits and networks"[5]. This leads to think at economies as networks. According to Anne Krueger, who served as first deputy Managing Director of the International Monetary Fund (IMF) from 2001 to 2006, globalization is "a phenomenon by which economic agents in any given part of the world are much more affected by events elsewhere in the world"[6]. Another definition is given to us by David Henderson, former Head of the Economics and Statistics Department at the Organization for Economic Co-operation and Development (OECD). He describes globalization as "free

[5] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 10.

[6] M. Wolf (2004) *Why globalization works.* London: Yale Nota Bene, p. 14.

movements of goods, services, labour and capital, thereby creating a single market in inputs and outputs"[7].

1.2 Conflicting perspectives on globalization

Given these interpretations inside the realm of economic globalization, we can note that there are two conflicting bodies of opinion over the good and bad of this phenomenon.

On one hand we find people in favour of globalization: they see all the aspects that globalization has brought as positive. According to them this phenomenon takes along many benefits that affect the greatest majority of people. They think that with free and integrated markets everybody will be better off.

On the other hand we can find the anti-globalizers, namely those people who see globalization as a problem. For them this process has brought much more inequalities, it represents the cause of the poverty of some countries and of the deterioration of the environment. The free market is a destructive force, therefore it must be regulated in order to avoid even worse consequences. Many people inside this group see the multinational corporation as the evil to fight against. Multinationals are guilty of exploiting the population in developing countries and of causing harm to the environment. What has been noted by Bhagwati (2005) is that during periods of economic growth, anti-globalization movements decrease; instead, when there are economic crisis these movements become more intransigent. Besides, according to a survey commissioned by the World Economic Forum (WEF) in 2002, we can see that nowadays there is a slight attenuation of no-global movements compared to the 1990s[8]. It is also interesting to notice a quite curious aspect that emerged from this poll: it was highlighted that, in comparison to the developed countries, people in the developing ones were more favourable and optimistic about globalization. This is particularly relevant considering that it represents a change in the trend, compared to

[7] M. Wolf (2004) *Why globalization works,* p. 14.

[8] Survey available at: <http://www.globescan.com/news_archives/press_inside.html>.

the past. In fact, in the decades after the Second World War in the developing countries there was a widespread scepticism towards globalization. On the contrary, in developed countries there was a positive attitude. Nowadays people in developed countries still have this kind of attitude, but they have been outweighed by people in developing ones.

1.3 Who plays the key role in the process of globalization?

In this context of economic globalization and market integration there is hardly any doubt that the main actors are the multinational corporations. They have been playing a major and growing role in recent years and they have been described as the most prominent demonstration of this process. For all these reasons they are increasingly becoming the focus of several studies, and their conducts have been very closely watched over by economists and academics. Even though their role as principal actors cannot be questioned**,** there has never been an uniform perception towards them. Still now, it is easy to see that there are conflicting feelings towards them: if on one hand they are seen as the bearers of innovation and wealth, on the other they are seen as a threat to the national identity and prosperity of a state. If on one side politicians and policy makers are happy when national enterprises become bigger and expand abroad, on the other they are afraid when foreign brands compete with national ones or when national activities close down to open new businesses abroad.

Besides, multinational enterprises are considered valuable for the knowledge they create and spread, but often they are also blamed for misdeeds such as exploitation of child labour, tax evasion or the circumvention of norms for the defence of the environment. Having said so, it is easy to note that according to whether one is a proponent or an opponent of the multinational enterprise, the judgement they give can be diametrically opposed. At this point it is necessary to give a first definition of multinational firm, even if, as we will see in the next chapter, a sole and univocal definition does not exist. Anyway, generally speaking, a multinational corporation is “a firm that has the power to coordinate and control operations in more than one

country"[9]. There are some unambiguous characteristics that can be given to multinational enterprises. They are relatively big (usually bigger than national enterprises), their production is fractioned in different countries and it can be moved from one place to another quite easily; besides, they are global actors that can exercise their great influence to reach their aims. There are some data that can confirm their considerable role in the world scenario. According to the United Nations Conference on Trade and Development (UNCTAD), nowadays there are about 82000 multinational enterprises and about 810 000 foreign affiliates. The latter employ about 77 million workers and they are responsible for about a third of the world exports of goods and services, and account for more than one-fourth of the world's output.

A distinctive and fundamental feature of multinationals is their capability to invest abroad. Multinational activity can be measured considering this very important element: the flow of Foreign Direct Investments (FDI). The OECD defined foreign direct investment as follows:

> "It is a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor"[10].

Put another way, it is an investment made by one firm in another firm, which is situated in a different country. This means that the investment crosses national boundaries, and it reflects the willingness of the direct investor to be involved in a long-term relationship. According to both the OECD and the IMF, this willingness becomes concrete when the direct investor owns at least 10% of the voting power, therefore implying that he has a significant degree of influence over the management and organisation of the foreign company. According to data made available by UNCTAD in different years, there was a significant increase of FDI in the first 50 years of the last century, but its growth was even more considerable after the end of the Second World War. There have been downward trends in the early years of the 1990s

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[9] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 16.

[10] Organisation for Economic Co-operation and Development (2008) *OECD Benchmark Definition of Foreign Direct Investment.* Available at: <http://www.oecd.org/daf/inv/investmentstatisticsandanalysis/40193734.pdf> .

and during 2001-2003, but they were followed by recovery and again upward trends. The fact that, apart from years of economic recession, the flows of FDI have been increasing is another proof of the growing relevance of multinational enterprises as global actors.

Their influence has been considerable also taking into account world trade. Increase in the flows of trade between different countries is one evident characteristic of globalization. According to data of the World Trade Organization (WTO), after the Second World War there was a gradual and rapid growth of trade. It rose by 6,7% each year between 1948 and 1953, then by 7,4% between 1958 and 1963, and it reached a growth of 8,6% between 1963 and 1968. These growth rates were bigger than the rates of growth of production. In recent years there has been a contraction, and in 2003 trade increased by 4,5%. Nowadays multinational enterprises are responsible for approximately three-fourth of all world trade[11]. Therefore, it can be assumed that a significant portion (about one-third) of it can be classified as intra-firm trade: this means that the exchange takes place between parent companies and their affiliates in different countries. So, it is a kind of trade which crosses national boundaries but it occurs within the boundaries of the company.

1.4 The geography of multinationals

Now we want to give an overview on the geographical spread of multinational enterprises. Even if it has expanded so much as to reach a world-wide network, the phenomenon of multinational firms is definitely characteristic of the developed North of the world. Here in fact the base of about 58 700 multinationals (that represent the 71,6% of the total[12]) is situated. However this percentage is decreasing year after year due to the growing number of multinationals located in South-East Asia.

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[11] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 38.

[12] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale.* Torino: UTET Università, p. 129.

The European Union is for sure the main area of diffusion, where the headquarters of about 53% of the total number of multinationals can be found[13]. According to data emerging from UNCTAD statistics, within the European Union, the state with more multinational enterprises is Denmark, followed by Germany[14]. Japan represents another crucial point when considering the home base for multinational enterprises. Here, in fact, there are the headquarters of about 4700 firms. Another area that needs to be considered is the one of North America. Here the number of multinational enterprises is relatively low (about 3900) compared to the former two zones. Nevertheless, North America plays a pivotal role in global economic relations. To explain this fact, we need to remember that America and Europe have two different administrative subdivisions: while a German firm with a branch in the UK is considered a multinational, the same cannot be said of a company with its headquarters in New York and a branch in Florida.

This general description given so far tends to reflect the vision of the world presented by Kenichi Ohmae in 1985. According to him the world economy is governed by a *global triad*, meaning that it is organized upon a macroregional tripolar structure, whose three main centres are North America, the European Union and Japan. These spaces share a number of characteristics, such as a similar technological infrastructure, the presence of firms that are both capital-intensive and knowledge-intensive, and the fact that they are home to the biggest part of innovations in industry. This theory was widely accepted since it gave a good reflection of the reality at that time, when these three powers were accountable for more than 50% of world exports and for two-third of global Gross Domestic Product (GDP)[15]. They were the origin of almost all the outflows of foreign direct investment, and they received two-third of the total inflows of foreign direct investment, showing that most of the FDI flows happens to be

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[13] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale.* Torino: UTET Università, p. 129.

[14] UNCTAD (2009) *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development*

[15] A. Vanolo (2006) *Geografia economica del sistema-mondo: territori e reti nello scenario globale.* Torino: UTET Università, p. 64.

between developed countries. Still in 2000, 430 of the 500 largest multinational enterprises of the world had their headquarters in one of these three regions[16].

However, Ohmae's view did not consider the developing countries, in particular the ones belonging to the region of South-East Asia. This is a considerable and increasingly important territory, where there are 13 900 headquarters, corresponding to 17% of the total world number[17]. According to Rugman and Verbeke (2004), Ohmae's theory today can be applied if we extend the triad to a "broader" triad, consisting of the countries taking part in the North America Free Trade Agreement (NAFTA), the European Union expanded to 28 member states, and Asia, especially South East Asia. As for the latter, important developments are represented by the creation of a free trade agreement between China and the countries of the Association of South-East Asian Nations (ASEAN), between India and countries of ASEAN, and the creation of an agreement on economic partnership between ASEAN states and Japan.

In developing countries in the remaining areas of the world, the presence of multinational enterprises is very limited: in Africa only 746 multinational firms can be counted, and most of them are located in South Africa; a similar situation can be found in Latin America, where there are only 851 multinationals.[18]

Things vary substantially when we consider the geographical spread of multinationals' affiliates and subsidiaries. In this perspective the main areas of diffusion are South East Asia (with 356 000 foreign affiliates) and the European Union (336 000 affiliates)[19]. In the first region, more than half of the subsidiaries (around 286 000) are situated in China, which offers low costs of labour force and a market characterized by an increasing purchasing power. In Europe, the most attractive countries are Romania and the Czech Republic. The first two macro regions are then

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[16] A. M. Rugman, A. Verbeke (2004) *A perspective on regional and global strategies of multinational enterprises*, in *Journal of International Business Studies,* n° 35, p. 4.

[17] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 129.

[18] Ibidem.

[19] Ivi, p. 132.

followed by Latin America, where we can find about 40 000 foreign affiliates, and then by North America with 9400 subsidiaries. Lastly comes Africa, which hosts just 6100 affiliates[20].

1.5 The geography of foreign direct investments

In this section we want to allow the reader to have a general overview on today's geographical spread of foreign direct investments. All the data provided below are taken from different editions of the World Investment Report, published every year by UNCTAD, and from information contained in OECD database.

1.5.1 Main outward investors

Foreign direct investments have been made mainly by the developed countries of the so-called North of the world: in 2008 these countries were responsible for 81% of the total[21]. The United States have always been the main outward direct investor: between 1950 and 1975 the investments coming from the US represented 40%-50% of the world total. However, recent trends show that the US are losing importance as an outward investor, and they are being replaced by some European countries, mainly the UK, Germany and France. Considered as an overall area, the European continent is responsible for the biggest number of outward investments: in 2008 the European volume of FDI was 940 billion dollars, while the North American one was of 390 billion dollars[22]. Clearly, this is due to the different administrative jurisdictions of Europe and America: an European country investing in another European country is making a foreign direct investment; the same cannot be said for American states. If we consider single countries, the United States remain the main outward investor. Also Japan, particularly since 1985, has been playing an increasingly important role as an investor: while its share of global investments in the 1960s was 0,7% of the total, in the 1990s it

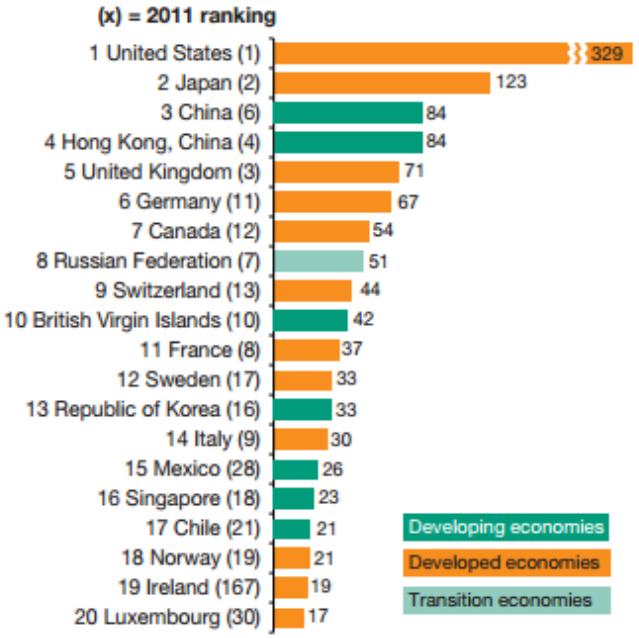
[20] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale*, p. 133.

[21] Ivi, p. 143.

[22] Ivi, p. 144.

became 12,2,%. Still, probably the most surprising fact is represented by the continuous growth of some developing countries as sources of investments. We can see that while in 1960 they owned just 1% of the total share of outward investments, this portion grew to 3% in 1985 and to 8% in 1995. South East Asia is a very important region in the network of foreign investments, where the countries that underwent the most rapid growths in the last decades have been China, Hong Kong, Singapore and Taiwan, and in the last World Investment Report two developing states show up in the first five investor economies, namely China and Hong Kong. Below we report the last available data published by UNCTAD on the top 20 investor economies.

Figure 1.1. Top 20 investor economies, 2012 (billions of dollars).



Source: UNCTAD, *World Investment Report*, 2013.

1.5.2 Main investment recipients

Considering the outward investments, the imbalance between developed and developing countries, even if it is decreasing, remains quite evident. Instead, when we turn our attention to the inward investments the situation varies notably. What we see is a more complex geographical structure, in which areas and countries are more

globally interconnected. In the rank of the countries attracting more investments we find both developed and developing economies. Countries of the North of the world have been playing a consistent role as investors and as beneficiaries of investments as well, but recent trends show that their dominant role is the one of investors. Conversely, the role of developing countries as recipients of investments has been of much greater importance. The United States are the country with the greatest share of inward investments: in 2005 it was responsible for 16% of the stock of global inward investment[23]. This is a proof of the change of interest of investors: while before they were attracted by regions which were rich in resources (such as Canada and Australia), now they pay more attention to those countries which are groundbreaking in the industrial sector (the US and continental Europe)[24]. For the last twenty years Japan has represented the main exception to this trend, accounting for less than 1% of the stock of the world's inward investments. Recently the situation has changed because Japan loosened some of its restrictions to inward investments, reaching 7.7% of the global flows of inward FDI[25].

When we turn to consider developing countries, we see that the area attracting huge amounts of investments is Asia, which, in 2012, accounted for 58% of the total flow of investments to developing countries, with China coming in the second position, after the USA, in the ranking of the countries absorbing more investments. In the same year, for the first time ever, developing economies attracted more FDI than developed countries[26], and as we can see below, there are nine developing countries in the rank of the top twenty host economies:

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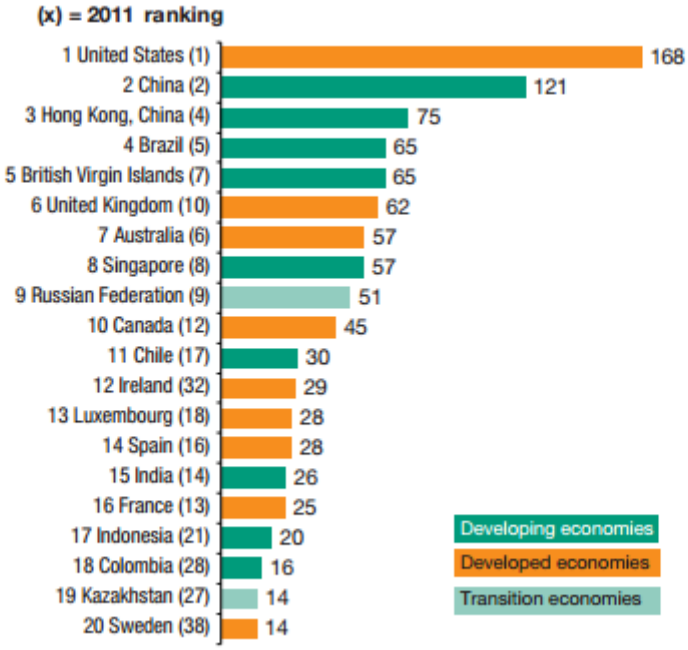
[23] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy.* Cheltenham: Edward Elgar Publishing Limited, p. 30.

[24] Ibidem.

[25] Ibidem.

[26] UNCTAD (2013) *World Investment Report: Global Value Chains: Investment and Trade for Development,* p. 2.

Fig. 1.2. Top 20 host economies, 2012 (billions of dollars)



Source: UNCTAD, *World Investment Report*, 2013.

Given this brief and rapid overview on the characteristics and spread of the multinational phenomenon, in the next chapter we will look at multinational firms more closely and deeply, giving some definitions and looking at their development through history.

2. MULTINATIONAL ENTERPRISES

2.1 Definitions

As it was already said before, there is not only one and shared definition of multinational enterprise, and scholars do not completely agree on what a multinational company is. According to UNCTAD, it is a firm which comprises a parent enterprise and its foreign affiliates. For parent enterprise it is meant an enterprise that controls assets of other entities in countries different from its home country. It does so by owning a certain equity capital stake, in order to be able to exercise a significant influence over these entities. This significant influence materializes when the company owns at least 10% of the voting power or of ordinary shares. In other words, it is a company which has its headquarters in one country (that we can call home base), and it operates in at least one foreign country, called host country. Therefore, the term "multinational" implies that the activity of the firm is spread in more than one country. Multinational firms seek to improve their profits expanding abroad, acquiring new resources, diversifying supplies and markets for sales. In the words of Dunning, "a multinational or transnational enterprise is an enterprise that engages in FDI and owns or controls value-added activities in more than one country"[27]. Similarly, as reported by Goldstein and Piscitello, a multinational is a firm that engages in at least one direct investment abroad. Over time, the differences among the terms "multinational" and "transnational" have been fading away, and in this thesis they are going to be used interchangeably. Similarly, the words "firm", "company" and "corporation" will be used as synonyms, even though each of them has a specific legal connotation.

According to the degree of involvement of the investor we can distinguish among three different types of controlled firms, that we are going to call with the general term "affiliates". We have branches, which are firms totally owned by the investor; subsidiaries, in which the investor owns 50% or more of the capital stake; and associates, in which the investor owns from 10% up to 49% of the capital stake.

[27] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 3.

According to Vanolo, there are three peculiar aspects that can be addressed to the activity of a multinational company[28]:

- Coordination and control of different stages of production in different countries;
- Capability of taking advantage of geographical differences and of different national policies;
- Flexibility, namely the capability of changing supplies and operations between different geographic areas.

As it was already stated before, through the act of a foreign direct investment, that is through investing outside national boundaries, a firm can achieve the territorial expansion of its production. It is important to underline that there is a difference between FDI and portfolio investment. While the former are made to gain an important degree of control over another firm, and they imply the transfer not only of financial capital but also of technology, organisational expertise and cultural values, the latter involve just the transfer of financial capitals, they do not imply a significant influence on the management of the company, and they can be easily disinvested.

Multinationals have been called with many different names: multinational enterprises (MNEs), transnational corporations (TNCs), international business enterprises. Whatever the name we give to this actor, what we imply is a company that, having its headquarters in one country, makes investments abroad and coordinates and controls operations in firms situated in different countries, being directly involved in the management of the firms themselves. These actors will be the main focus of this thesis. From this first overview on multinational enterprises it should be clear that they do not make up an uniform and homogeneous category. Rather, there are differences not only concerning the size and the spread of these firms, but also their operating methods and their business culture. The multinational dimension of these actors should be seen as the result of different aspects playing together, rather than as the consequence of a single aspect: the transnationality of a company is

[28] A. Vanolo (2006) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 74.

a multidimensional concept. Finally, we need also to bear in mind that, although these companies have an almost global character, still they keep being linked to the culture and to the socio-economic background of the territory in which they were born and in which they grew up. In particular this is the thought of Dicken, who is convinced that every firm is strongly linked to a specific location; that is to say that, even if we are in a globalized world, economic activities are geographically localized. To study this territorial embeddedness or placeness, a particular index has been created, namely the Transnationality Index. A deeper analysis of this aspect of multinational firms will be given later on in this chapter.

2.2 A brief history of multinational enterprises.

In this section we are going to focus on the historical evolution of multinational corporations. We do so in order to see the different stages they have gone through and the external situations that affected their progress. It is important to walk this path to understand that the power of today's multinationals does not have to be assumed as a given, but it is something that has been achieved and that has led to today's big success both economically and politically. It should also be remembered that, historically, each country underwent a peculiar path of economic development, due to the fact that every nation was characterized by different resource availability and different demands of domestic markets. Therefore, each developmental course of international production is likely to be different.

2.2.1 From the origins to the First World War.

As it is correctly stated by Dunning and Lundan in their book "Multinational Enterprises and the Global Economy", the search to improve economic prosperity has been operated by individuals, social groups and governments since the beginning of modern civilization. It has long been present, and it was pushed mainly by three factors: the aspiration of fostering trade and financial activities, the desire to take possession of new territories and acquire new forms of wealth, and finally the need to find out new ways to use domestic savings[29]. The first signs of primordial forms of transnational

[29] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 146.

enterprises can be traced back to 2500 B.C., when Sumerian merchants used to sell their own goods by placing agents in foreign ports. Embryonic forms of multinationals are also the ones characteristic of the civilisations of the Middle East, and later of the colonising activities of the Phoenicians and the Romans[30].

Between the 13th and 18th century, overseas ventures were undertaken mostly by the states as a way to bring forward the political aims of their governments. Europe can be considered as the cradle of multinational firms, European nations being both home and host for international business. The Early Middle Ages saw the birth of several trading firms based in different parts of Europe, with the spread of offices and representatives throughout the continent. In this category it is worth mentioning the Hanseatic League[31], as a first example of an early trading multinational enterprise. It was a commercial confederation of merchants, with base in Lübeck, that had the control of trade in Northern Europe. Merchants in different cities of this area wanted to trade among them, therefore they created some societies (Hanse) to promote commerce among them and to protect their interests and privileges.

Turning into the 14th century, we need to shift our attention to Italy. In the peninsula in fact there was the birth of lending institutions, banking and trading houses. These institutions fostered trade through a network of branch offices that were spread throughout Europe. Particularly noteworthy is the activity of the Medici, based in Florence and with branches not only in Italy but also in London, Avignon, Geneva and Lyon[32]. As stated by Dunning and Lundan, 150 Italian banking firms were acting as truly multinational companies at the end of the 14th century.

In the late 15th and early 16th century several expeditions for the occupation of new lands took place, the main ones were guided by Bartolemew Dias, Vasco de Gama, Ferdinand Magellan and Christopher Columbus. After the discovery of America, international trade became more intense and trading companies came to play a crucial role, particularly for silk and spices. Two well-known trading companies of this period

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[30] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 146.

[31] Ibidem.

[32] A. Goldstein, L. Piscitello (2007) *Le multinazionali.* Bologna: Il Mulino, p. 10.

were the British East India Company and the Dutch East India Company. Great Britain and the Netherlands were two nations with a strong commercial and maritime vocation; they directly supported their commercial ventures as a means to reach their economic and political purposes, promoting trading activities and their territorial acquisitions[33].

As pointed out by Jed Greer and Kavaljit Sin, the multinational enterprise as we are used to knowing it today did not appear until the 19th century. The modern multinational was born in the 1870s, in conjunction with the industrial revolution, which marked a turning point in the development of this actor. It was in these years that companies had increasing incentives to be involved in trade and to invest abroad, looking for new resources for their home production. There was a strong acceleration in the exchange of goods and services, as well as an intensification of the flows of people and capitals. This was possible thanks to a period of peace at the international level, as well as within countries, thanks to the advancements in the sectors of communication and transport, and thanks to the development of better storages techniques[34]. Besides, this period saw the appearance of managers and administrators who had been professionally trained, therefore more skilled and experienced in the management of a firm.

In the first industrial revolution (1780-1830), the process of becoming multinational touched just commercial activities, rather than production ones. Things changed with the second industrial revolution (last three decades of 1800), when new tools, from the telegraph to transatlantic ships, allowed a centralized management of a multiplicity of production centres. All these factors represented an important watershed for international business: while previously the kind of capitalism dominant in international commerce was a merchant capitalism, with the industrial revolutions this was being replaced by an industrial capitalism[35].

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[33] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 148.

[34] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 11.

[35] K. A. Reinert (2012)) *An Introduction to International Economics: New Perspectives on the World Economy.* Cambridge: Cambridge University Press, p. 150.

In this period the role of the United States started being central, since they were better equipped to take advantage of the latest technological developments. They became important both as a destination as well as a source of foreign direct investments. Another change occurring in this period was the switch in sector: the focus changed from spices and textile, to metals and rubber and finally also to agriculture. Agricultural multinational enterprises were responsible for nearly all world production. It is worth mentioning the Boston giant United Fruit Company, that by 1899 controlled alone 90% of US imports of banana, and by 1915 became one of the biggest multinationals in the world[36]. Finally, another sector that attracted considerable attention and flows of FDI was the oil sector. The Anglo/Dutch company Royal Dutch Shell owned oil wells in Indonesia already in 1900 and controlled at least 20% of Russian oil production by 1914. Standard Oil was probably the company which followed the most aggressive international strategy: by 1907 it had taken the control over 55 foreign enterprises[37].

At the beginning of the 20th century the industrial production was turning more capital-intensive. The function of the assembly line and of the economies of scale was growing so important that there was a switch from the period of industrial capitalism to what was called Fordism. In these years previous to the First World War, the markets of today's emerging countries were the ones which attracted most flows of investments (about 60%) of the total. According to Dunning, when the war started, the total stock of FDI amounted to nearly 15 billion dollars, equivalent to 9% of world gross domestic product. The main investor was Great Britain, who accounted for nearly half of the investments, followed by the United States, France and Germany. Between the late 19th and early 20th century all these countries exercised little governmental control both on inward and outward investments, and they paid little attention to the behaviour of multinational enterprises[38].

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[36] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 166.

[37] Ibidem.

[38] Ivi, p. 173.

2.2.2 Between the First and the Second World War.

As it can be easily imagined, the years between the two World Wars represented a period in which the conditions for international trade became harsher. The climate worsened not only economically but also politically speaking. In fact, there were increasing controls on imports and increasing tariffs on commerce. Many European nations involved in the war were forced to liquidate most of their investments in order to finance their military expenses; trade among European countries decreased and it was nearly reset with Russia, after the abolition of private property and the resulting expropriations. The only country that was immune from the harsh conditions of the war were the United States. US multinational firms kept growing during the 1920s, loans given by Wall Street to the rest of the world increased, and the US switched from being a net debtor to being a creditor nation. Nevertheless, the US, similarly to other countries, suffered from the collapse of the international capital markets in 1929.

Even though in these years the situation was hard, multinational enterprises did not disappear. They preferred to focus on their national markets, even if new protectionist policies made it less convenient to export. Investments from Europe declined, but US multinationals extended their activity quite considerably. Investments in the sector of natural resources kept growing. According to data made available by Dunning and Lundan, in the inter-war years multinational activity continued to grow, and there was a considerable increase in international capital stake. Another feature of the inter-war period was the birth of cartels, used to control supply and to keep the prices high. The main multinational enterprises in the oil sector (Standard Oil, Royal Dutch/Shell and Anglo-Persian) went from being competitors to being partners[39].

2.2.3 The post-war period

At the end of the Second World War it was hard to predict that in the following years an incredibly quick economic growth would have taken place. Trade and investments underwent a period of substantial extension.

[39] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 20.

Just after the end of the war and until around 1960, American multinationals' supremacy over their competitors was undisputed. US production installations were only superficially hit by the bombings of the war, that instead had destroyed many factories all over Europe and Japan. Besides, US multinationals expanded and were stimulated by the dynamic domestic demand, and were able to improve their production methods and their organization. Reporting a study of Vaupel and Curhan, Dunning states that, considering the 174 main multinationals at that time, two third of them were American. However, especially since the 1960s, the perspectives of economic growth were encouraging also in Europe and Japan. Even if the Second World War, similarly to the First, forced many European countries to give up their investments, in a short period of time these nations were able to start again their flow of foreign direct investments. Multinational companies began to play a fundamental role in global economy and trade, occupying a position they had never reached before. This happened thanks to technological improvements in shipping and in transport by air, thanks to the development of better infrastructures, that allowed a faster and safer transfer of goods and people; thanks to computerization, that facilitated the control and the production in distant places, and also thanks to better political conditions, created by Bretton Woods agreements and by the Marshall Plan, which facilitated the penetration of American multinationals into the European market. As reported by Goldstein and Piscitello, in these years nearly half of the total stock of FDI was owned by American investors. The UK followed at a considerable distance, controlling about 18% of world FDI; then we find the Netherlands (10%), and France (6%)[40]. As for Japan, even if its growth rate was increasing rapidly, it accounted only for a very small part of the flows of investments. After the war there was also an expansion of intra-firm trade, that is trade taking place between foreign affiliates and parent companies, or within affiliates themselves. According to Greer and Sin, by the 1960s intra-firm trade accounted for about one third of all world trade[41].

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[40] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 23.

[41] J. Greer, K. Sin (2000) A Brief History of Transnational Corporations, available at <http://www.globalpolicy.org/component/content/article/221/47068.html>.

Notwithstanding this uninterrupted growth and this dynamism in international trade, in the 1980s the stock of properties that firms owned abroad did not even reach 5% of world GDP[42]. Oil shocks, monetary devaluations and recession acted as a constrain to economic growth. However, in the 1990s a new wave of globalization emerged, characterized especially by an expansion of foreign direct investments. Thanks to the integration between different technologies and their smaller prices, companies were able to take advantage of the reduction of the barriers to international trade and of the increasing regionalization of the world economy. Multinational enterprises started new strategies related to the expansion and differentiation of the activities, and to the penetration of new markets. What became particularly important was the research of new partnerships, mergers and acquisitions and the stipulation of new agreements of cooperation. The production chain was fragmented in different structures, that were separated but integrated. These foreign affiliates do not represent a secondary unit of production compared to the central headquarters; rather they represent working units that are almost independent and able to coordinate a vast range of activities. Besides, both these affiliates and the headquarters have been increasingly investing on research and development sector, having considered the fact that a good global strategy needs to be based on the capability to coordinate a combination of knowledge, abilities and functions that are located in different areas of the world.

2.3 Inside the multinational enterprise

Up to this point we have seen how multinational corporations are irreplaceable actors in today's globalized world. What we are going to do now is to try to understand why a firm decides to become multinational. Since transnational corporations are capitalist enterprises, the most important objective they pursue is profit. However, there are also other incentives pushing MNEs towards transnationalization, such as the wish to become bigger, or to become the industry leader in one particular sector, or the wish to expand their share of a market. Therefore, considering all these different reasons,

[42] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 28.

as Dicken puts it, the question should not be "Why transnationalize?", but it should be "Why *not* transnationalize?[43]".

2.3.1 The first contributions

The 1960s were the years that saw the appearance of the first theoretical contributions trying to explain the existence of multinational enterprises. Until that moment most interpretations took inspiration from the classic theory of international trade. According to it, if a country is relatively rich in labour force, and weak in capital, that country would specialize in labour-intensive production; conversely, a country that is well-equipped with capital would specialize in a capital-intensive production. These two countries exchange their products between them and this trade benefits both of them. Because of the fact that until that moment capitals were moving from rich to poorer countries, this theory had been working. But, when capitals started being exchanged among developed and rich countries, this classical theory was no longer sufficient and appropriate to explain international trade.

Stephen Hymer's contribution emerged from his PhD thesis. It was the first time that the firm, rather than international trade, was taken as the focus of the analysis. According to Hymer, domestic companies have an advantage over foreign firms since the former know their domestic market far better that the latter do: for instance, they have a deeper knowledge of the business environment and legislation, they know customers' tastes better and they can adapt to the changes in taste more easily and quickly. For these reasons Hymer pointed out that for foreign firms to be able to access a foreign market successfully, some kind of "ownership advantages" would be required. We can describe these ownership advantages as firm-specific assets, such as the possession of specific knowledge or technologies, or some innovatory or marketing advantages. Only by possessing these assets a foreign firm would be able to nullify the intrinsic advantages that a domestic firm has in its own domestic market.

Also Vernon's model of the product life-cycle dates back to the 1960s. It was particularly important because it was the first time that the relationship between international trade and foreign production was closely studied, and also because

[43] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 108.

Vernon, for the first time, introduced a locational dimension in the study of the life-cycle of a product[44]. The model was based on the examination of the behaviour of US multinational enterprises, and it tried to explain the increase of commercial exchange and flows of investment between the US and Europe in the period after the end of the Second World War. Vernon identified three phases in the life-cycle of a product, each of them corresponding to different methods of production and to different types of organization of the activities of the firm.

The first phase of introduction of a new product is characterized by uncertainty and by the need of keeping a high degree of flexibility to be able to adapt quickly to consumers' tastes. Since the product is being produced for domestic consumption in the home country, its production would be located as near as possible to the consumers, that is in the United States. In this phase, if there is a foreign demand of the product, this would be supported through exports. Gradually, the product becomes standardized (phase of maturity) and so the attention can be switched from flexibility and from the characteristics of the product to the research of ways to reduce production costs. In this phase there is a growing demand of the product from other developed countries. These markets are first reached through exports, but when the cost of this extra production, together with the costs of transport exceed the cost of producing directly abroad, American firms decide to substitute exports with the creation of new foreign affiliates, which in turn export to other third countries and even back to the parent company. Eventually, in the third stage (phase of saturation) the product becomes completely standardized. When demand approaches its saturation point, it is essential to find ways to minimize costs. Therefore the firm decides to move its production towards those countries with low-cost labour force, which are usually developing countries. In this phase, the demand in the US domestic market is still expanding, but the production here is decreasing; production instead is increasing in developing states.

This model was able to describe quite well the reality of that time, but nowadays it has its limitations. As Dicken (2007) pointed out, considering the increasing complexity

[44] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 114.

of the network of multinational firms, it is simply unrealistic to rely upon a model that just implies a linear transition from a firm committed only to its national market to a firm involved in international trade and production[45].

The importance of geographical location emerges also in Dunning's model, called "OLI paradigm" or "eclectic" paradigm. It was developed in 1976 and it identifies three interrelated conditions which explain when a firm decides to be involved in international production. These conditions are the following:

- A firm can have specific advantages that differentiate it from other competing firms coming from other countries. These Ownership advantages are deeply embedded within the firm and are, for instance, types of knowledge, organizational and human skills.
- The firm makes the most of these advantages if these are exploited directly by the firm itself, that is to say that it does not have to sell or lease them to other companies. These are known as Internalization advantages. Given the fact that firms spend big amounts of money on research and development, they would be incentivized to protect their knowledge against competitors, and to exploit this knowledge themselves.
- Finally, these advantages are geographically specific, meaning that they are linked to the territory in which the firm is situated. They are called Location-specific factors, and they are unlikely to be transferred, therefore they have to be used in those locations. Examples of those factors are political conditions, infrastructure provisions, ideological and cultural attributes, and so on. When speaking of location-specific advantages, we can distinguish between two categories of firm: firms that orient their production towards the market and firms with a production oriented towards costs. As for the first category, the choice of opening a foreign affiliate is linked to the need of proximity between the producer and the final consumer. This necessity is relevant for products that require a rapid distribution and for those products that, in order to be sold more, need to

[45] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 115.

be modified to better adapt to local tastes. Therefore, firms choose this strategy when they want a deeper knowledge of the market they are dealing with, but also when they want to gain more visibility. When deciding the location for the opening of a new affiliate, an important factor to be taken into consideration is the structure of domestic demand. Markets in which the consumption levels are high, for instance US and EU markets, will be more appealing.

On the other hand, cost-oriented productions aim at producing goods that are competitive because they are cheaper. From this point of view, nowadays the most important factor to consider is the cost of labour force, since its prices can vary considerably from zone to zone.

From all these advantages the OLI (Ownership, Location-specific and Internalization advantages) acronym derives. Even if this paradigm was criticized because it was seen as a simple list of factors explaining the multinational phenomenon[46], nevertheless its framework of interpretation was a significant step forward in the direction of understanding the process of transnationalization of multinational firms.

2.3.2 Why investing abroad?

Different multinational enterprises would have, very probably, different motivations for engaging in international production. As we will see, there is not one sole theory that is able to cover all the determinants of the foreign activities of multinational firms, but these motivations can be distinguished thanks to Dunning's well-known classification. In 1993 he identified four categories of determinants of foreign investment, which are all distinct but one of them does not exclude the others.

However, before describing Dunning's work, we want to make another distinction: the one between horizontal FDI and vertical FDI. We can speak of horizontal investment when a company duplicates its home-based activities in an affiliate located in a foreign country. Put another way, the firm reproduces abroad all the production

[46] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 79.

process to produce the same or similar products. This kind of investment represents a way of substituting international trade, since firms replace exports with foreign production. On the other hand, vertical foreign direct investments take place when the production chain is fragmented internationally, locating each phase of the production in the place where it can be accomplished at the least cost. Contrary to horizontal FDI, this kind of investment usually acts as a stimulus for international trade, because it implies the transfer of intermediate products among the places where the production process is scattered.

The first type of investment identified by Dunning is the resource seeking investment. In this case a firm is pushed to invest abroad in order to gain access to resources that are poorly available, or not available at all, in the home base, or that are here more expensive. Needless to say, the objective is for the firm to become more competitive and for its activity to become more profitable. According to Dunning it is possible to distinguish three main kinds of resource seekers[47]:

- First, the type of resources that firms look for are physical and natural resources such as minerals, timber and agricultural products. The main reason for engaging in this kind of investment is the research of cost minimization and of a secure source of supply.
- A second type of resource seekers are the ones motivated by the search for human resources, in particular inexpensive and unskilled labour, or specially trained labour. The countries that usually engage in these investments are those countries with high costs of labour, and the investments have been usually directed towards the industrializing developing countries.
- Third, companies are pushed towards resource-seeking investments by their necessity to obtain organizational and managerial expertise and technological capabilities.

Over time resource-seeking investments have been the ones which enterprises have resorted to more often as a motivation for international production. However, recently

[47] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 68.

this has changed, and nowadays finding the reason of investment only in the research of cheaper resources or of cheaper labour force is incomplete[48].

A second and growing determinant for international production is market seeking. The aim of this investment is to supply goods and services to markets of the host country and/or to markets neighbouring to that country. Market-seeking investments are undertaken as a way of reinforcing and protecting already existing markets, that before used to be supplied by exports. However, this method, due to rising barriers imposed by host governments, or due to too high transportation costs, can happen to be less profitable than actually producing locally. In addition to the size of the market and to the prospects of its growth, Dunning identifies other four main reasons according to which it is worthy for multinational firms to be involved in market seeking investments:

- The first reason why firms engage in this kind of investment is simply because they follow their suppliers that in turn have opened facilities abroad.
- A second determinant of market-seeking investments is the need to adapt and tailor products to local tastes and demands, and this would be facilitated by the physical proximity of the production to the customers. Furthermore, foreign producers need to become familiar not only with local needs, but also with local laws and legal procedures, with the local language and local business culture in order to be competitive with local producers, that otherwise would have an intrinsic advantage.
- The third reason is that producing in the foreign market can cost less than supplying that market from a distance. This is particularly true for those products whose costs of transportation are especially high. Firms can be prompted towards these investments by government regulations, raising barriers and import controls. Finally, companies that are located in countries that are far from important markets will be more motivated to establish production abroad.

[48] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 147.

- A fourth reason, that is becoming increasingly important in determining market-seeking investments, is the fact that a firm might consider it inevitable to start production in those markets that are already served by its main competitors or where its main customers are situated.

According to Dunning, the most important of all these determinants is the action that host governments can take in order to attract investments[49]. Examples are the imposition of severe tariffs on imports or the increase of import controls, but recently governments have also offered incentives such as tax concessions.

The determinants we have seen so far are the two central motivations for international production. However, Dunning identified other two categories.

The third type of investment is efficiency-seeking investment. Its aim is to rationalise the production structure of a firm, as expressed by the author, "in a way that the investing company can gain from the common governance of geographically dispersed activities[50]". Having a range of activities in different geographical areas makes it possible to take advantage of the different political structures, of the different factor availabilities and different economic policies. This explains why, especially big and experienced multinationals engage simultaneously in investments towards developed countries, to improve their technology-intensive activities, and in investments towards developing countries, to take advantage of unskilled and cheap labour force.

Finally, the last category encompasses strategic-asset seeking investments. Their objective is to gain access to competences or resources that the firm perceives as essential in order to enrich its portfolio and to increase its global competitiveness. Dunning and Lundan distinguished several reasons why a company may engage in this kind of investment: one firm can be acquired by another firm with the aim of preventing another company from doing the same; two firms can set up a collaborative alliance to join and reinforce their capabilities against a more powerful

[49] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 71.

[50] Ivi*,* p. 72.

competitor; or else a firm can acquire a company which produces complementary goods with the objective of expanding the range of products available for its clients[51].

2.4 Foreign market entry modes

There are different ways thanks to which a company can fulfil its wish or necessity of internationalization. These modes can be seen as a continuum that starts with exports, implying a low level of international commitment of the firm, and ends up with FDI when, as we have already seen, the international engagement is bigger.

Reinert (2012) gives a deep analysis on how firms can enter a foreign market. According to him there are three broad categories of entry: exports, contractual, and investments. As a starting point Reinert takes a firm whose sales take place only in its home country. However, if or when a firm decides to expand its sales abroad, what is the first step it might follow in order to do so? The firms might engage in exports. Even though this activity may seem to be simple, in reality it implies several extra costs which actually allow only few companies to start exporting successfully. There are basically two exporting modes: one indirect way, which implies that the firm does not take direct care of exporting activities but rather it relies on another specialized company (a sale agent or trading company) in order to conclude the export activity; and a direct way, in which the firm is directly engaged in the export transactions without mediators.

The contractual mode of entry implies a more significant degree of involvement of the enterprise, that decides to start producing abroad. However, differently from FDI, the relation that is being created is market-based, not ownership-based. It consists of a contractual agreement being signed between the firm in the home base and a foreign producer. It allows the foreign producer to manufacture the company's product. Reinert identifies three types of contractual entry[52]:

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[51] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 73.

[52] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy,* pp. 143-145.

- Licensing: a licensing agreement allows a foreign firm to use the production process of the home-base enterprise in return for payment. In other words, a licensor in the home country gives limited rights to a foreign company. These rights can include the use of patents, of trademarks, technology and know-how. In return, the licensee pays royalties to the firm in the home country.
- Franchising: in this case a franchisee pays fees and royalties to the home country firm (the franchiser) in return for the license to use its production process, to be identified with its trademark, and to sell its products. The franchising mode of contractual market entry implies a greater degree of control over the production and marketing of the franchisee. Additionally, the franchiser usually supplies the franchisee with assistance to be sure of the appropriateness of its conduct. Even if the search for a competent franchisee company can be expensive and time consuming, nevertheless this entry mode can lead to a quick development of international markets and it can be a precursor of a future deeper involvement in that market. We are used to finding this mode of entry for international hotel and fast food chains[53], such as McDonalds.
- The third type of contractual market entry is subcontracting, also known with the name contract manufacturing or foreign outsourcing. It consists of a contract signed by the home country firm and a foreign company, and it implies the delegation of specific activities of the production process to the foreign firm. Over time this form of market entry has become more and more important. It allows the home country firm to retain control over research and development, marketing and sales, and it allows the entry into markets that may be protected by high tariffs or barriers.

Finally, the third way of producing abroad is through investments, that is when a firm engages in FDI. There are three different ways in which a foreign investment can take place: greenfield investment, mergers and acquisitions (M&A) and joint ventures

[53] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 144.

(JV). Greenfield investments are the ones that require the biggest commitment of the home country firm since they are not directed towards already existing industrial structures but rather they imply the creation of new subsidiaries from scratch. Even if this process brings additional costs due, for example, to administrative or bureaucratic procedures, or to the search of labour force, nevertheless it has some advantages. By creating a completely new subsidiary that the home country owns totally (for this reason they are called Wholly-Owned Subsidiaries: WOS), the parent company can move to the host country all its firm-specific advantages, without running the risk of losing the control over them. This is important especially when the competitive advantage of the firm is based on specific technological and marketing knowledge. It is clear that in this investment the firm uses its own resources and knowledge, that will combine later with the ones it acquires from the local market. The greenfield investment is particularly welcomed in host countries because it creates new jobs in the local market.

Foreign direct investment can also take the form of mergers and acquisitions. With a merger the home-country firm buys only one part of an already existing company located in a foreign country; instead, with an acquisition it buys all the shares of the foreign company, that therefore becomes a WOS. With this process the investing firm can take advantage of the firm-specific activities (skills, technologies, supply networks and so on) of the firm acquired. Additionally, compared to the greenfield investment, the acquisition represents a quicker mode of entry, since the foreign investor can base its activity on an enterprise that is already working and experienced. However, also this way of accessing a new market has some disadvantages: the investing firm would have to face new costs arising from the need to coordinate and integrate the new production. Nowadays cross-border M&As play a role that is quantitatively very relevant. Compared to the previous year, in 2011 there was a 53% increase in M&As, being valued in 526 billion dollars[54]. According to Dicken (2007), it is one of the most common modes of entry, offering "the attraction of an already functioning business

[54] UNCTAD (2012) *World Investment Report 2012: Towards a New Generation of Investment Policies*.

compared with the more difficult, and possibly more risky, method of starting from scratch in an unfamiliar environment[55]".

Finally, the third type of FDI to be considered is the joint venture. A cross-border joint venture is created when a home-country firm and a foreign-country firm join together to give birth to a new business entity, that is separate and distinct from the parent companies, of which they "own a sufficiently large proportion to give each of them some degree of control or influence over key areas of decision making[56]". In this way the two companies share risks, knowledge and resources between them, and this can act as a method to avoid barriers and to overcome government restrictions. Being involved in a joint venture can be the best cross-border strategy when each company brings to it its own peculiar resources and capabilities, creating a set of competences that is variegated and complementary[57].

So far we have described the path that enterprises can naturally follow in their way towards internationalization. This has been called a sequential or evolutionary approach, delineating the process of a firm moving from indirect exporting to greenfield investment as its knowledge and understanding of the foreign environment increase. However, it should be clear that this process is not inevitable and it is not the same for all firms. Firms can move not in a sequential way, some stages may be bypassed, and a firm can start producing abroad right from the beginning of its activity. In Dicken's opinion this is the case especially for firms located in small countries such as Switzerland. Therefore, the term "born global firms" has been forged to identify those companies that focus their activity on niche markets and that are able to start transnational operations from their very inception[58].

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[55] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 116.

[56] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 269.

[57] Ivi*,* p. 271.

[58] Ivi*,* p. 246.

2.4.1 Determinants of the choice of entry mode

Over the past decades a lot of work has been done by several scholars trying to find out which are the determinants that guide a firm in the choice towards a specific mode of entry. Great attention has been given to the role played by national culture, but, as we will see, it was not possible to identify specific factors that are able to explain and predict precisely what would be the exact choice of a firm that is approaching a new market.

In Reinert's opinion (2012) the main factors that need to be taken into consideration when analyzing the choice of entry mode of a firm are[59]:

- The degree of control that the parent firm wants to exercise;
- The level of resource commitment;
- The degree of dissemination risk.

Knowledge capital plays a very significant role. It can be described as the body of intangible assets (such as information, skills, experiences...) that is deeply embedded in the employees of the firm and in the firm itself. Closely linked to it comes the concept of dissemination risk, that refers to "the possibility of a foreign firm obtaining knowledge capital of the home-country firm and exploiting it for its own commercial advantage[60]". When a home-country firm possesses some technological or intellectual advantages, it is highly likely that it wants to keep the control over them, therefore it will probably decide to engage in a greenfield investment. In this way it can transfer all its set of knowledge in a wholly-owned company. If the aim is primarily to maintain a low level of dissemination risk, also the entry through exports can be considered a viable solution. Conversely, if a firm does not own firm-specific knowledge and if it has a low commitment towards research and development, it is likely that the firm will look for these technological or intellectual capabilities abroad, deciding to choose the way of acquisitions. If the main concern of a firm was to limit its level of resource

[59] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 149

[60] Ibidem.

engagement, the choice of the mode of entry would fall back to either exports or contractual modes.

Also other factors have been taken into account by scholars, for example the size and the rate of growth of the market in which the firm is willing to entry. The bigger the host market and the faster its growth rate, the greater the likelihood that the home-country firm will have a propensity for mergers and acquisitions. This mode of entry will be preferred since it allows an almost instantaneous access to the market, because the home-country firm will base its activity on an already functioning company.

Additionally, some characteristics of the host country are believed to be important in the choice of the mode of entry. If a large cost differential (in labour, in infrastructures and so on) is present between the home and the host countries, there will be a preference for greenfield investments. Also cultural distance has been studied for long as a key factor affecting the mode of entry. Scholars such as Kogut and Singh (1988) came to the conclusion that the larger the cultural and economic distance between the two countries, the bigger the probability of accessing the market through a greenfield investment. Most M&A procedures take place between developed countries with similar cultural and socio-economic characteristics. This can be due to the fact that in a similar environment the costs of integration and assimilation are lower. Greenfield investments are also more frequent when the business environment in the host country is friendly. Concerning the host country labour force, the more it is skilled and well-qualified, the more it will attract greenfield investments, since the building of a new enterprise from scratch will also imply the recruitment of workers from the talent pool.

Other determinants that have been analyzed are, for instance, the degree of multinationality of the home-country firm and its size. Hennart and Reddy (1997) found that if a firm has already many affiliates in several countries, there is a high probability that it will enter in a new foreign market through an acquisition. This is due to the fact that, having already acquired a multinational experience, the firm will be capable to deal better with the risks associated with the acquisition, and to integrate affiliates of different nationalities more easily.

Brouthers and Brouthers (2000) identified a correlation between the size of the firm and the mode of entry it will choose. According to them, the bigger the dimension of the firm, the greater the possibility that it will engage in an acquisition, since this kind of operation requires more managerial expertise and financial resources. For the same reasons, the bigger the target company, the smaller the probability that the investing firm will act through an acquisition.

Joint ventures should be considered separately, since they do not imply full ownership of the foreign affiliate, but just a shared ownership. According to the study conducted by Chen and Hennart (2002) over Japanese investors in the US, the presence of barriers or limitations to the entry of a market will increase the probability of entry through a joint venture[61]. This will be the preferred way of approaching a new market also when the company does not possess enough competitiveness to engage in a full ownership, or when the enterprise, that is involved in high-technology sectors, needs to share the high costs of research and development with another firm. As for cultural distance, it is an important factor also considering joint ventures. When the cultural and business environment in the host country is distant and unfriendly to the home-country firm, this would engage preferably in a joint venture, since the alliance with a local firm would guarantee a deeper knowledge of local rules, and therefore it would allow to bypass potential difficulties[62].

The potential disadvantage of being involved in a joint venture is that the home country firm might lose the control over its intangible firm-specific activities (such as know-how, managerial skills...) in favour of the partner enterprise. Besides, different long-term objectives may arise from the two firms, and this can lead to difficulties and conflicts over the management of the joint venture. If a firm does not have enough international experience and it does not know foreign markets good enough, it can make the wrong decision concerning, for example, the location of a new structure or

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[61] S. F. Chen, J. Hennart (2002) *Japanese Investors' Choice of Joint Ventures Versus Wholly-owned Subsidiaries in the US: The Role of Market Barriers and Firm Capabilities,* in *Journal of International Business Studies,* vol. 33, n° 1, p. 6.

[62] B. Kogut, H. Singh (1988) *The effect of national culture on the choice of entry mode,* in *Journal of International Business Studies,* vol. 19, n° 3, p. 414.

the adaptation of its products to local preferences. Therefore, lacking of experience, a firm might prefer, at the beginning of its internationalization process, to access a new market through a way that implies a low commitment, and gradually, as its practice and knowledge increase, turn towards modes of entry which presuppose greater engagement and control.

The choice of creating a joint venture rather than a fully-owned subsidiary is also linked to the political situation of the country in which the investment is going to be made. In fact, if the country at issue is facing risky political instability, the firm might choose to start a joint venture because it is the mode that needs a smaller investment compared to the others, and that allows to withdraw more easily and with the least losses in case of necessity.

These that we have seen so far are the several factors that have to be taken into account when analysing which is the preferred mode of entry of a company into a foreign market. However, we have to bear in mind that these circumstances can occur simultaneously, therefore the choice that multinational enterprises have to face is not that easy and straightforward.

2.5 Territorial embeddedness or placelessness?

In the previous sections we have analysed why and how a multinational enterprise enters into a foreign market. Since the beginning of this dissertation we have identified several characteristics according to which the level of transnationality of a firm can be given. Helped by Dunning and Lundan (2008), we want to remind the reader some of them:

- The number of countries in which the firm has established its foreign production;
- The degree of internationalization of the firm's high-value activities, for instance, research and development;

- The number of affiliated companies located abroad over which the home-country firm exercises full or partial control[63].

Often the supporters of globalization have affirmed with strength that, since multinational enterprises represent the embodiment of the effects of globalization, they all share the characteristics of being global. Ohmae can be definitely recruited among the group of the hyper-globalists. In 1990, as cited by Dicken, he wrote that: "Country of origin does not matter. Location of headquarters does not matter. The products for which you are responsible and the company you serve have become denationalized"[64]. He believed that the push of the global economic competition will end up by levelling the form of organization, structure and strategies of international enterprises, so that they will become completely independent from any geographical context.

However, this point of view of the hyper-globalists have been increasingly called into question. In particular, Dicken spoke about the "myth of the global corporation", challenging the view that sees multinational firms as placeless and boudaryless[65]. In order to reject the hypothesis of the global corporations, Dicken avails himself of the Transnationality Index (TNI). This is an index developed by UNCTAD as a means to measure how global a company can be or to see how much nationalistic elements can still affect an enterprise that expands abroad. The index is made up by the average of three indicators expressed in percentage terms: the ratio of foreign sales to the total sales, the ratio of foreign employment to total employment, and the ratio of foreign assets to the total assets. The final average is a value included between 0 and 1. If the value is higher than 0,8, that means that the company is strongly oriented towards the international market; if the value is lower than 0,5, this indicates those enterprises that have their prevalent context in their national market.

If transnational corporations were really eradicated from their national environment, as Ohmae and the hyper-globalists supported, among the biggest

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[63] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 3.

[64] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 124.

[65] Ibidem.

multinational enterprises it would be plausible to find many firms characterized by a high index of transnationality. Thanks to data made available by UNCTAD[66], it is possible to see the list of the world's top 100 non-financial multinational corporations, ranked by the amount of foreign assets that they own. We are going to report only the first 25:

Table 2.1. The world's largest 25 non-financial TNCs, ranked by foreign assets, 2008.

Ranking by Foreign Assets	Multinational Corporation	Home economy	Industry	TNI (Per cent)
1	General Electric	United States	Electrical & electronic equipment	52,2
2	Royal Dutch/Shell Group	United Kingdom	Petroleum expl./ref./distr.	73,0
3	Vodafone Group Plc	United Kingdom	Telecommunications	88,6
4	BP PLC	United Kingdom	Petroleum expl./ref./distr.	81,0
5	Toyota Motor Corporation	Japan	Motor vehicles	52,9
6	ExxonMobil Corporation	United States	Petroleum expl./ref./distr.	67,9
7	Total SA	France	Petroleum expl./ref./distr.	74,5
8	E.On	Germany	Utilities (Electricity, gas and water)	55,8
9	Electricite De France	France	Utilities (Electricity, gas and water)	42,2
10	ArcelorMittal	Luxembourg	Metal products	87,2
11	Volkswagen Group	Germany	Motor vehicles	60,5
12	GDF Suez	France	Utilities (Electricity, gas and water)	56,4
13	Anheuser-Busch Inbev SA	Netherlands	Food, beverages and tobacco	87,9
14	Chevron Corporation	United States	Petroleum expl./ref./distr.	58,1
15	Siemens AG	Germany	Electrical & electronic equipment	73,0
16	Ford Motor Company	United States	Motor vehicles	54,3
17	Eni Group	Italy	Petroleum expl./ref./distr.	56,4
18	Telefonica SA	Spain	Telecommunications	70,3
19	Deutsche Telekom AG	Germany	Telecommunications	50,3

[66] UNCTAD (2010) *World Investment Report 2010: Investing in a Low Carbon Economy.*

20	Honda Motor Co Ltd	Japan	Motor vehicles	72,2
21	Daimler AG	Germany	Motor vehicles	54,5
22	France Telecom	France	Telecommunications	51,0
23	Conocophillips	United States	Petroleum expl./ref./distr.	43,4
24	Iberdrola SA	Spain	Utilities (Electricity, gas and water)	56,4
25	Hutchison Whampoa Limited	Hong Kong, China	Diversified	82,0

Source: UNCTAD, *World Investment Report,* 2010.

In the last column of the table we reported also the transnationality index of these firms. As we can see, the firms that are ranked in the first places according to the number of foreign assets, do not occupy the same positions when we consider their index of transnationality. Therefore, taking into account the two distinct values, we can obtain two rankings that differ markedly. Considering these top 25 companies, their TNI ratio is hardly over 50, meaning that their home context still accounts for about half of their operations and activities. According to these data, the largest transnational corporations do not possess high degrees of "globalization". In 2008, of the list of the 100 world's largest multinationals, only 55 had a TNI higher than 60, and only 26 of them has a TNI above 75 (meaning that more than three-quarters of their activity were based outside their national borders). This leads us to think, and this is also the opinion of Dicken, that even though these companies administrate international activities, they still remain deeply linked to their national roots.

Taking into consideration just the transnationality index, the ranking of the first 25 multinational corporations would be very different, and it would look as follows:

Table 2.2. The world's largest 25 non-financial TNCs, ranked by transnationality index, 2008.

Ranking by TNI	Ranking by Foreign Assets	Corporation	Home economy	Industry	TNI (Per cent)
1	37	Xstrata PLC	United Kingdom	Mining & quarrying	93,2
2	87	ABB Ltd.	Switzerland	Engineering Services	90,4
3	40	Nokia	Finland	Electrical & electronic equipment	90,3

4	66	Pernod Ricard SA	France	Food, beverages & tobacco	89,1
5	67	WPP Group Plc	United Kingdom	Business services	88,9
6	3	Vodafone Group Plc	United Kingdom	Telecommunications	88,6
7	72	Linde AG	Germany	Chemicals	88,3
8	13	Anheuser-Busch Inbev SA	Netherlands	Food, beverages & tobacco	87,9
9	46	Anglo American	United Kingdom	Mining & quarring	87,5
10	10	ArcelorMittal	Luxembourg	Metal products	87,2
11	27	Nestlé SA	Switzerland	Food, beverages and tobacco	87,1
12	88	Air Liquide	France	Chemical/Non-metallic mineral products	86,9
13	61	Liberty Global Inc	United States	Telecommunications	86,2
14	58	Astrazeneca Plc	United Kingdom	Pharmaceuticals	85,4
15	100	Teva Pharmaceutical Industries Limited	Israel	Pharmaceuticals	84,4
16	41	Lafarge SA	France	Non-metallic mineral products	84,2
17	57	Volvo AB	Sweden	Motor vehicles	82,3
18	25	Hutchison Whampoa Limited	Hong Kong, China	Diversified	82,0
19	55	Cemex S.A.	Mexico	Non-metallic mineral products	81,6
20	4	British Petroleum PLC	United Kingdom	Petroleum expl./ref./distr.	81,0
21	31	Roche Group	Switzerland	Pharmaceuticals	80,3
22	82	CRH Plc	Ireland	Non-metallic mineral products	79,5
23	63	BAE Systems Plc	United Kingdom	Aircraft	78,9
24	65	Philips Electronics	Netherlands	Electrical & electronic equipment	78,8
25	97	Schlumberger Ltd	United States	Other consumer services	76,9

Source: Adapted from UNCTAD, *World Investment Report, 2010.*

What can be deduced from these data is also the fact that the index of transnationality differs considerably according to the country of origin of the firm. In fact, most of the transnational corporations with a high degree of transnationality are based in relatively small countries (such as the United Kingdom, Switzerland and Luxembourg), making the perspectives towards an international market understandable. On the other hand, enterprises having their headquarters in big countries, for example in the

US, display relatively low values of transnationality. However, this is only a trend, and there are several exceptions to it.

All these data, in Dicken's opinion, constitute the proof that hyper-globalists are wrong in supporting the idea that "transnational firms are abandoning their ties to their country of origin[67]". If this was true, these firms would have high values of foreign assets, of foreign employment and of foreign sales, making up a high value of the index of transnationality. But as it was proved thanks to UNCTAD data, this was true only for a limited number of enterprises. The firms that in 2008 ranked in the first 25 positions according both to foreign assets value and to TNI were only five: Vodafone Group, British Petroleum PLC, ArcelorMittal, Anheuser-Busch Inbev SA and Hutchison Whampoa Limited.

The index of transnationality is considered very useful as a means to measure the geographical spread of a company. However, it has the limit of simply distinguishing the home activity from the foreign activity, without actually specifying where the foreign activity is scattered. A firm can be characterized by a high level of transnationality, let's suppose a TNI of 80, but it can be possible that all the 80% of its foreign activity is based in only one foreign country[68].

Generally speaking, the geographical context still plays an important role: knowledge, infrastructures and capabilities can be very specific of a determined location, and they can limit the possibility of a firm to move its production easily from place to place. When considering the significance of the national embedding we should pay attention not only to its economic aspects but we should also take account of its cultural dimension: cultural, social and political elements can play a very important role. Multinational enterprises are organizations made up by individuals and by the social relationships among them, so they bear these characteristics, and even when they expand their economic horizons, their nation-specific features continue to be dominant. However, this does not imply that all firms coming from the same country would be identical, in fact different conditions and different paths of development

[67] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 124.

[68] Ivi, p. 126.

would lead to distinct behaviours and distinct structures. The different national environments contain practices and customs that make them peculiar cultural and business systems.

This aspect of the importance of national roots becomes even more significant when we consider the country of the Triad. Being the most relevant actors in the world's economy, they are oriented towards the principle of market capitalism. Nevertheless, they have got some peculiar features that stem from their own national context and that are a proof of the different cultural values affecting firms' behaviour. Now we are going to see which are the distinctive aspects characterizing and distinguishing the countries of the Triad: America, Japan and Europe.

2.5.1 A comparison among American, Japanese and European firms

According to a study conducted by Doremus and his collegues over the characteristics of firms based in the US, Japan and Germany, there is

> "little blurring or convergence at the cores of firms based in Germany, Japan or the United States.. Durable national institutions and distinctive ideological traditions still seem to shape and channel crucial corporate decisions.. The domestic structures within which a firm initially develops leave a permanent imprint on its strategic behaviour[69]."

The American system is essentially based on the idea that the market should benefit the consumers by maximizing their wealth; instead, it pays less attention to its equal distribution. The American market is characterized by a high degree of competition, its enterprises are driven by profits and they do not have to follow high standard of behaviour with regard to their employees and their community since their main aim is to enrich their investors. Besides, in the US kind of system the state intervention is very limited.

On the other hand, the Japanese system is quite different. Among its objectives there is the willingness to reach the social impartiality. In order to do so the state plays a considerable role and its interventions in the economy are frequent: to protect some

[69] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 127-128.

industrial sectors or to promote international competitiveness. Contrary to the American model, in the Japanese system the main objective of the economic activity is not profit maximization; rather, economic activity is subordinated to the achievement of social goals, for example keeping a high level of employment[70]. Therefore, private companies are invested of public responsibilities towards the community. Besides, private firms have built up a network of self-regulation that may lead, as a consequence, to discriminatory behaviours. This is totally incomprehensible in an Occidental mentality, according to which the same economic rules should be effective for all economic actors. Also the policies of competition vary markedly between the two countries: while in the US the antitrust model is in force, in Japan it is common to see companies that cluster themselves in networks of competition and cooperation. They form the so-called *keiretsu*: they are structures made up of enterprises that engage in interlocking business relationships. They form a kind of broader family in which personal and informal relationships are as important as economic and commercial transactions. They are the equivalent of the American trusts, and one example of keiretsu is Mitsubishi. Often these relationships do not form only among companies, but they stretch to high political personalities, involving sometimes even the Ministers of the Economy[71].

As for the European system, we can say that it occupies an intermediate position between the American and Japanese models. Despite the presence of differences among the distinct countries of the European Union, the European system, similarly to the Japanese one, is overall characterized by the fact that social well-being somehow conditions firms' economic activity. The concept of corporate social responsibility have been created to mediate between the forces of the market, that do not always care about social needs, and social well-being itself. The presence of the state in business activity is stronger compared to the American model, but weaker compared to the

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[70] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 115.

[71] A. Vanolo (2006) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 89.

Japanese one. The state and the associations of entrepreneurs cooperate in order to procure a better management of the economy[72].

The differences that we have just seen show us that, even if somehow we can speak of a co-evolution of the business systems, that may converge with regard to certain characteristics, nevertheless they diverge with respect to others. The simple fact that these firms under analysis are multinational implies that they will carry on their operations in a number of countries with different economic, social, political and cultural features, and in order to be successful they will need to adapt and seize these characteristics of the host environments[73]. The degree of success and competitiveness of a firm would be related to its capability to behave accordingly to the economic and cultural context of the host environment. However, even in doing so, the national history and culture would continue to influence the structure, the behaviour and the decision-making process of the firm. Therefore, geography still matters, and the idea of placelessness that was associated with multinational enterprises has been rightly questioned.

2.6 Localization of multinationals' production networks

The fact that different geographical contexts are characterized by different production factors and by different ways of doing business prompts MNEs to analyze carefully which would be the preferable context where to locate a specific activity: it would be convenient for a firm to scatter some of them, while some others would be better conducted if kept in the home base. Helped by Dicken, we will analyze the strategy adopted by multinationals with regard to some of their main activities.

The firm's home country will be the preferred location for the control and coordination of the whole set of activities, since it is the place where its headquarters can be found. It is here that all the main decisions regarding the MNE are taken, and it is also the place where the financial activity is based. Another main role conducted in

[72] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 115.

[73] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 133.

the home base is the elaboration and transmission of information. Besides, the headquarters represent the place where the final and definitive decision-making process takes place. Additionally, a very important role is played by the so-called regional headquarters offices. They are situated at an intermediate level between the home base headquarters and a particular region in which the production is spread. Their role, therefore, is to act as a mediator, informing the headquarters and coordinating and integrating their work. For this reason they are usually, but not always, situated near the production centres of the multinational.

Contrary to the activity of control and coordination that, as we have seen, tends to take place within the boundaries of the home country, marketing and sales represent the function that is more geographically scattered than all the others. To explain this it is sufficient to take into consideration the fact that, in order to be successful, these activities have to be located near the markets in which the firm serves its products. This is because the geographical proximity allows the firm to adapt better its products to local tastes and it prevents it from misunderstanding the foreign business cultures. While marketing functions are often aggregated in the regional headquarters, being responsible for the activity of a whole region, sales units are smaller and more scattered[74].

As for the production units, there is not a geographical pattern that we can assume as a general model that would be valid for the majority of multinational enterprises. In fact, the decision of where to locate the production would inevitably change from firm to firm because the factors that a firm is looking for would vary according to the sector to which the firm belongs and on the type of goods it produces.

The geographical spread of the sector of research and development has been for long the focus of research of several scholars, who have supported even opposite opinions. Instead, something on which almost everyone agrees is the importance of the role of multinationals in developing technological capabilities. Since multinational

[74] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 146.

enterprises are responsible for about three-fourths of all the world civilian R&D[75], it becomes relevant to know where MNEs choose to locate their R&D facilities. As a premise we should bear in mind that information and knowledge do not share the same meaning. The former is made up by a set of figures and data, while the latter implies the intellectual acquisition of the information. The passage between information and knowledge happens thanks to a learning process, through which a person can fully understand and interiorise the meaning of the information in order to add it to his own expertise[76]. Besides, knowledge has another peculiar feature: it has a cumulative character. This means that basic and elementary know-how is needed in order to be able to assimilate new and more complex data. This distinction between information and knowledge is noteworthy since it lets us aware of the fact that the spread of knowledge is not a zero cost process: to transform information into a wisdom than one can completely and fruitfully use, it is necessary to undergo a learning process that can be more or less wearing (and so expensive), according to the set of expertise that one already possesses. Knowledge can also be distinguished in two categories: tacit and codified (or explicit) knowledge.

- Tacit knowledge is a kind of knowledge that is deeply-rooted and embodied in the persons. It is intuitive and it is not easy to share. It is hard to codify, and in order to be effectively transferred it is necessary to have a close interaction with the so-called knowing subject: it is possible to learn through observation, imitation and by doing.
- Codified knowledge instead is completely and easily transferable to others even without the knowing subject. It can be shared and fully explained thanks to words, to codes and scientific formulae. It is usually found in books, manuals and documents, and so it can be easily transformed into information.

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[75] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 183.

[76] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 124.

Tacit knowledge can be transformed into explicit knowledge thanks to a process of codification. This process, however, cannot transmit the whole knowledge, and so practice, attempts and errors are necessary to deeply understand the operation[77]. Nevertheless, it represents a way leading to cost reduction since it prevents a person from directly observing the knowing subject. Still, these processes of codification are often imperfect; it follows that a significant gap between different places regarding technological expertise endures. Even with explicit knowledge, the learning process implies the possession of other and already assimilated capabilities. Places that lack these capabilities would not be able to fully exploit this knowledge. For this reason it has been observed that innovation is truly fundamental for the economic development of a country. As UNCTAD noted, it is no longer sufficient to acquire new technology from other countries or firms; what is important is to undergo a learning and innovatory process to be able to make an efficient use of these new technologies.

In the past, there were scholars who saw R&D as an activity that was mainly performed in home countries as a way to allow firms to keep secret their knowledge and to protect new ideas and technologies. This was valid as a general rule, and also UNCTAD stated that "R&D is among the least internationalized segments of the TNC's value chain; production, marketing and other functions have moved abroad much more quickly[78]". This bias of operating R&D functions in the home country stems from constraints imposed by linguistic factors and by the difficulty of exchanging knowledge that is person-embodied. However, in the last years this view has been increasingly questioned, and there is evidence of a rise in the spread of R&D activities. ICT developments have led to an increased easiness of communication. Therefore, information and explicit knowledge have become available virtually to everyone; it follows that the key factor of competitiveness becomes the capability to create new knowledge. This ability is usually associated with few and restricted area, that are normally found in the developed North of the world. According to UNCTAD, "When

[77] A. Vanolo (2010) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 125.

[78] UNCTAD (2005) *World Investment Report: Transnational Corporations and the Internationalization of R&D,* p. 121.

R&D internationalization took place, both home and host countries were found in the developed world[79]". However, nowadays things are changing, and we need to leave the simplistic and stylized idea that sees the world divided between developed areas, where high knowledge activities are possible, and developing areas where only simple and routine processes can take place. New countries, especially in Asia, are being considered as the target of the decentralization of highly specialized services. This phenomenon is caused not only by the need to adapt locally or to integrate in the local established knowledge, but also by the fact that creativity and talent are no longer found only in the Triad countries, but also in different countries such as China and India. These two countries are increasingly occupying a prominent role in the sector of research and development thanks to their well-prepared scientists and engineers. Beyond being well-trained, the payment that can be given to them is far smaller than the one given to their American or European peers. There can be a 30-60% cost advantage in these countries[80], so the trend of moving R&D functions there becomes fully comprehensible. Highly specialized processes are now becoming the object of policies of decentralization, and countries once considered only as areas where simple and routine activities could be delegated, are now becoming the places where high knowledge-intensive activities can take place.

2.7 The model of Metanational firms

In the literature we can find a very interesting approach regarding the identification and access of firms to new technologies: it is the model of the metanational firms developed by Doz, Santos and Williamson in the early 2000s. Their starting point is the observation of the reality: they saw that the dynamics of global competition, the more and more rapid development of technological innovation and the switch of enterprises towards the creation of products more and more individually-designed have prompted multinational enterprises to engage in operational processes increasingly through

[79] UNCTAD (2005) *World Investment Report: Transnational Corporations and the Internationalization of R&D*, p. 99.

[80] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 185.

decentralization pushes. According to them, individuals within the firms need to be empowered, everywhere they are situated. In fact, if individuals feel that their knowledge is being appraised, they would undergo a process of self-realization, from which, in the end, also the firm itself would benefit. The global society has not only blurred the geographical boundaries between states, but it has also annulled the knowledge monopoly that was once owned by industrialized countries. A wider range of actors comes to posses different kinds of knowledge, linked to technology or to peculiar aspects of territoriality, that allow firms to understand better the necessities of local markets. The metanational firm is the kind of enterprise that has the ability to manage and fruitfully coordinate the complex patrimony of knowledge that is scattered throughout the network of local communities in which the firm operates. The alternative represented by a metanational firm consists of the fact that it does not limit its activity to exploit its local and national advantages in the international arena, but it creates new value through the access to competences and knowledge that are situated even in faraway places. A metanational firm relies massively on people, anywhere these are located, because it believes that their knowledge, their experiences and their direct participation can help the firm reach its objectives.

In the words of the authors, the competition on the global level has changed, and so, while:

> "Yesterday, becoming a global company meant building an efficient network of production, sales, and service subsidiaries capable of *penetrating markets around the world,* [...] today the challenge is to innovate by *learning from the world.* Tomorrow's winners will be companies that create value by searching out and mobilizing untapped pockets of technology and market intelligence that are scattered across the globe[81]".

In the next future the more successful companies will be the ones capable of finding new specialized knowledge anywhere in the world, and of mobilizing this knowledge in order to create new products and services. This operation would become strategic in the context of a worldwide knowledge economy, an environment that implies that all

[81] Y. Doz, J. Santos, P. Williamson (2001) *From global to metanational: how companies win in the knowledge economy.* Boston: Harvard Business School Publishing, p. 1.

the knowledge necessary for the success of a firm cannot be found in just one place, but instead it is geographically spread. So, the vital action that enterprises should take is to exploit knowledge that is locally diffused and transfer it on the global scale. The winners in this knowledge economy will not offer standardized goods, produced in their national market, therefore their advantage will not stem from their home countries; rather, their strong point would be the capacity of undergoing a continuous process of innovation, deriving from the ability to assimilate new knowledge coming from different *pockets of technology* that are scattered throughout the world. Consequently, their advantage has been called "metanational advantage": deriving from the Greek, the prefix meta means "beyond" and it indicates that metanational firms do not base their advantage on their national markets but they go beyond, taking advantage of the unfulfilled potential of geographically dispersed areas, and appraising the knowledge found there, they are able to innovate more efficiently than their competitors. Metanationals will flourish giving value to the sources of uniqueness and to cultural and geographical differences.

Doz and his colleagues identify three levels of competition in which metanational firms need to vie[82]:

- The first level is called sensing: it is formed by the identification and the access to new and relevant technologies, competences and knowledge that are located in dispersed geographical areas. To efficiently achieve this objective a firm needs to improve its competences with regard to the identification of new sources of knowledge.
- The second level regards mobilizing: it consists of the efficacy and speed with which firms can connect the different dots that are spread around the globe, and then use them to create new and innovative products and services. In order to do so some peculiar structures, able to transform new knowledge into new products, are needed. These structures have been given the name of

[82] Y. Doz, J. Santos, P. Williamson (2004) *Da globale a metanazionale: le strategie di successo nell'economia della conoscenza.* Bologna: Il Mulino, pp. 7-9.

"magnets", since they are capable of attracting geographically scattered, but potentially relevant, knowledge.

- The third level is about operationalizing: it is represented by the activity of optimization of sales, of distribution and marketing to the global scale, in order to launch on the market these new products and services as rapidly and efficiently as possible. In other words, once a new product or service have been created, its profit potential must be exploited and materialized.

According to Doz, Santos and Williamson geography is becoming more and more irrelevant. Not only being globally spread does no longer represent a competitive advantage for a firm, but an increasingly important fact is that valuable and sophisticated knowledge is not situated in single main markets, rather they are globally scattered and deeply embedded in faraway contexts. Today's multinationals have to create new factors of differentiation between them, and one of these can be the alimentation of different innovation processes based on a local level. While multinational enterprises have been using their national roots as a way to create their competitive advantage, metanational firms will need to rely on the art of learning and taking advantage of relevant knowledge anywhere this is being created. The authors affirm that to be truly successful, multinationals need to break free of their geography since in the world there are many unexplored knowledge pockets that can potentially be far more valuable for the innovation process of a firm.

Continuing with this line of thought, Doz et al. also stated that for firms, being born in the "wrong" place can actually bring some advantages. With "wrong" it is meant a place that is outside the traditional capitals of the highly technological and innovative sectors. Therefore, in order to be globally competitive, these firms need to look for potential and valuable knowledge outside their national environment, and so they become more keen in identifying and exploiting this knowledge trapped in local niches throughout the world, developing the abilities of sensing, mobilizing and operationalizing since they represent the only way to survive in the global market. This is emblematic of the fact that geography does not leave any more any permanent mark in the development of a firm. The study of multinational firms such as Acer and Nokia brought the authors to identify six consecutive steps that firms should follow to

be able to exploit the potential and hidden knowledge scattered around the world[83]. They include:

- Becoming an explorer of global knowledge, sifting the world in the search of new technologies and new needs of the market;
- Finding out new ways to access to niches of new knowledge and then immerse the firm in them;
- Creating a "magnet" in order to gather all the knowledge that stems from many and different parts of the world;
- Melding together the knowledge deriving from different sources to create innovative products and services;
- Moving the understanding of the innovation and its potential to the personnel in charge of the operational activities;
- Giving value to the innovation in the global market in order to maximize sales and profits.

The process to become a metanational firm seems to be clear and straightforward, but there are some hidden traps that need to be given attention. One of the first mistakes that multinationals make is to think that they can simply adapt or "shoehorned"[84] metanational objectives and capabilities into the already existing multinational structures. This method is always going to fail because the routine operational activities of a multinational are completely different from the processes of sensing, mobilizing and operationalizing that are typical of a metanational firm. While the focus of the former is to streamline the operations, maximize the profits, exploit already existing knowledge and adapt their national advantage on a global scale, the latter implies the creation of new and strong relationships with external actors, the discovery and integration of new knowledge and the maximization of the learning process.

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[83] Y. Doz, J. Santos, P. Williamson (2004) *Da globale a metanazionale: le strategie di successo nell'economia della conoscenza,* p. 77.

[84] Ivi, p. 85.

The second trap consists in believing that information and communication technologies can nullify the distance between places and mobilize knowledge that is dispersed all over the world. This is a delicate point, in fact, even if the sector of ICT saw a remarkable development, distance still places many obstacles. The authors speak of the "tyranny of distance"[85]: if the multinational firm does not understand that the knowledge that it is trying to mobilize is tacit and dependent from the context, the result will only be confusion and misinterpretation. Ideas and notions that may appear simple can actually hide a complex set of knowledge, that can be applied successfully only in that environment, since "complex knowledge is very sticky to its origin[86]".

A possible solution to this trap exists, and it is believed to be co-location. In a situation of co-location the creation of knowledge is easier since all the actors involved share the same language, the same culture and the same technical or professional expertise. When people are physically and cognitively close to each other the management of knowledge becomes far more direct. When people are together, a bidirectional communication takes place: we give value not only to the words we hear, but also to gestures, emotions and silences. Besides, co-location facilitates frequent interaction and it determines a higher probability of random encounters with peers and colleagues. In this environment of common language, common learning process and common values, the exchange of tacit knowledge is fostered. A possible alternative to co-location can be to re-create it through a process of mobilization of the necessary knowledge. It is important to bear in mind that knowledge alone cannot move from one place to another. What actually moves is a carrier within which knowledge can be found. This carrier can be a person, a project, a tool and so on. Unfortunately, it does not matter how good and efficient the carrier is, the nature of the knowledge is going to change. Since the moving knowledge is going to be applied in new contexts, it becomes crucial to be able to predict and recognize these changes to prevent misunderstandings from happening. However, co-location remains the best solution, and the job of accessing new complex knowledge is always best done by local

[85] Y. Doz, J. Santos, P. Williamson (2004) *Da globale a metanazionale: le strategie di successo nell'economia della conoscenza*, p. 113.

[86] Ivi, p. 117.

insiders[87]. This process is not easy and direct, in fact it can take a lot of time and substantial investments. It follows that the location of the investment has to be the fruit of a pondered choice. Even if there are no precise factors indicating who the next innovators will be and where the next technological developments will take place, Doz et al. identify some markers thanks to which some hotbeds of innovation can be distinguished[88]:

- Identify non-conventional behaviours among the consumers who are less conditioned from previous products experiences;
- Identify places where technologies are converging because in such context it is more probable that innovatory trends will reciprocally strengthen creating a new foundation for future knowledge.
- Identify public and university research centres equipped with resources and capabilities.
- Monitor interesting people and find out where they move and live.
- Control the growth of the international call traffic and of internet nodes, because they signal a concentration of communities that are curious and educated.
- Identify those countries which offer national regulations favourable to innovation.

Historically, some firms decided to look for new knowledge in the places that their competitors had already discovered (a wait-and-see approach). Needless to say, this is an easy choice that will not allow the firm to be the leader in its sector: since it enters that market later than its competitors, and it uses the available knowledge that others are already exploiting, the firm, in the best case, would reach an equal level of competitiveness with respect to the other enterprises.

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[87] Y. Doz, J. Santos, P. Williamson (2004) *Da globale a metanazionale: le strategie di successo nell'economia della conoscenza,* p. 145.

[88] Ivi, p. 140.

To conclude, according to the authors, metanational and multinational enterprises differ markedly at least in three main aspects[89]: the former organizes its network of operations around places and around their team of people, knowledge and capabilities, while the latter arranges its operations around its national subsidiaries; the managers of the metanationals are trained and they behave following the principle of "think local and act global", maximizing the unique and original contribution that each place can generate; managers of the multinationals instead are used to doing the opposite, "think global and act local", following the procedure of first expanding and then adapting. Additionally, multinationals are characterized by a mindset that favours a global extension in which the main activity is to teach to the world, rather than to learn from the world. They are attracted by locations that have similar characteristics to the home base, which allows the implementation of policies that provide maximum profits with the minimum level of adaptation. This usually creates a unidirectional flow transporting products, systems and knowledge that goes from the home base headquarters to the foreign subsidiaries. Conversely, metanational firms are attracted by the uniqueness and distinctiveness of locations, because they can learn from their original knowledge: differences are the main sources to create innovation. Today's globalization challenge has changed: the race to the penetration of the markets is being replaced by the race to learn from the world[90]: advanced countries of origin are no longer a requirement sufficient to win in the knowledge economy. Successful firms will be the ones that are able to discover and manage new sources of differentiation, acquiring knowledge that is trapped in niches scattered around the world.

Another recent and interesting model shaped around the multinational firm is the one designed by Porter and Kramer. According to these two scholars a big problem in today's world is represented by the fact that business has come to be seen as an enemy of society wellbeing. A vicious circle has been established: the more business is perceived to create its profits at the expense of communities, the more communities and public policies become tough and impose stricter regulations on them. In this

[89]Y. Doz, J. Santos, P. Williamson (2004) *Da globale a metanazionale: le strategie di successo nell'economia della conoscenza,* p. 186.

[90] Ivi, p. 223.

context, the fundamental aspect that has been lost is the fact that business and society do need each other, and that business can increase its profits by simultaneously creating social value for communities. Companies in the first place must abandon the focus on short-term financial gains to concentrate more in the long-run success that can be achieved by meeting important customer needs[91]: societal questions have to be at the core of business's action, not at the periphery. The concept of creating shared value implies this new process in which the creation of economic profits for a firm leads also to the creation of value for the society. There is no necessary trade off between these two aspects: for too long companies, governments and non-governmental organizations have seen each other as enemies and have behaved accordingly, but it is now time to see that these actors actually share some objectives. The conventional wisdom according to which companies can increase their profits by applying low labour and environmental regulations is increasingly being denied, giving space to the opinion that firms can represent a possible solution to societal issues, especially when a cooperation is established between them and governments. We will come back to this concept more in depth in chapter 4.

2.8 Factors influencing the choice of location

As we have seen so far, economic activities remain mainly geographically localized. What we are going to do now is to try to identify which are the factors that can influence multinational firms in the choice of the location of their investments.

2.8.1 Regionalism

Many scholars have noted that areas in which a regional integration is present are attractive for multinationals' investments thanks to the fact that in these zones commercial costs are reduced. This process underwent a period of considerable growth especially in the 1990s and nowadays the always increasing number of regional integration agreements (RIAs) has made of regionalism one of today's main characteristics of the global economy. Often, belonging to a regional space acts as an

[91] Harvard Business Review, available at: <http://hbr.org/2011/01/the-big-idea-creating-shared-value>.

incentive to the growth of national exports first, and then it represents an intermediate stage towards the growth of exports outside the regional zone. It has been noted that regional integration develops first between countries that are geographically close to each other or that share some historical or cultural features. Therefore, taking into consideration the countries of the Triad, we can note that European countries have a particular propensity to make investments in Eastern Europe, the US pay special attention to Latin America, and Japan to South-East Asian countries. Deaglio (2005), starting from this observation, invented the archipelago metaphor, according to which in the world we are witnessing the creation of "islands" (that are, basically, regional conglomerations of countries) that tend to develop their own supranational rules and institutions. However, these islands then form an archipelago, establishing a set of global institutions and rules that gives uniformity to the whole world economy.

We already saw before, thanks to Ohmae's model of the Triad powers, that these "mega-regions" are responsible for a really vast share of the world trade, production and investments. What we want to point out now is the fact that these actors, namely Europe, North America and South East Asia, are also areas where regional integration agreements are in action. These agreements are respectively the European Union (EU), the North American Free Trade Agreement (NAFTA), and the Association of South East Asian Nations (ASEAN) and ASEAN Free Trade Area (AFTA).

In the words of many scholars the European Union is by far the most prominent example of political and economic integration, a reality that has consolidated through a long process of successive deepening and broadening. The project started in 1957 establishing the European Economic Community (EEC), including just six countries, and since then it has continued to grow until reaching today the number of 28 countries and implying far more than just an economic institution. Since its foundation, the community has undergone many significant stages of development. Here we want to highlight just some of them, in particular the progresses that took place in the late 1980s and 1990s. These include the Single European Act, which prepared the ground for abolition of the barriers among its members; the creation of the Single European Market in 1993, which established the free circulation of goods, services, people and

capitals; and the creation of a single European currency, which bases were placed in the treaty of Maastricht in 1992, and which became reality in 1999 when the European Monetary Union (EMU) was given birth. Which consequences has this increased integration brought with regard to multinational firms and their investments? According to many scholars, the dimension of the market in which the investment is going to be made plays a considerable role in the choice of the location: the bigger the market, the greater the share of FDI it attracts. The creation of the Single European Market is a good example of this fact. It reduced the costs of international trade and it allowed a remarkable growth of the internal market. Thanks to UNCTAD data and to Navaretti and Venable's work (2006) we can see that during the 1990s there was a considerable expansion in the volume of FDI in Europe: American and Japanese firms were increasingly attracted by the fact that from that moment on they could access the whole European market without restrictions or barriers. Also smaller European countries, such as Ireland and Belgium, were able to attract a good share of these investments since they represented a suitable way of entry into the regional market and a platform for exports, in particular when they offer more convenient fiscal regimes[92]. The increase in the volume of inward investments in Europe was also caused by the growth of FDI among European countries: the European integration led to a quite new configuration of European industry, with several mergers and acquisitions taking place and a new and different location of economic activities throughout Europe.

2.8.2 Clusters

Another aspect which is believed to act significantly in the choice of investment location is the geographical concentration of economic activities in clusters. The physical proximity to other enterprises can have positive effects on the productivity of the firm thanks to externalities, which are "the positive spillovers created when activities in a particular place are connected with one another[93]". Spatial closeness

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[92] G. B. Navaretti and A. J. Venables (2006) *Le Multinazionali nell'economia mondiale.* Bologna: Il Mulino, p. 103.

[93] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 21.

provides knowledge and technology spillovers and a bigger availability of specialized production factors; besides, there can be stronger links with supplier and clients. A specific reason that is able to explain why clusters develop in the first place does not exist. However, it has been said that some areas are preferred to others since there, probably, the historical origin of a determined activity can be found. Once the cluster is created, it evolves thanks to cumulative stages that can include: the attraction of linked activities, the stimulation of innovation and of the spirit of entrepreneurship, and an intensification and enlargement of the local labour market[94]. When moving to a foreign country, a firm has to face more uncertainties and difficulties, compared to the national enterprises. Therefore, the firm would favour the choice of following previous investors: the fact that they already moved their production in that specific place gives to that location a good degree of attractiveness. Thanks to all these effects, the spatial concentration of economic activities makes possible the fact that investments in these areas have a bigger yield.

2.8.3 Export Processing Zones

Especially in recent years and more and more frequently, firms have decided to make important investments in those areas, usually found in developing countries, characterized by low costs of the labour force, by the availability of soil, water and infrastructures at moderate prices, and by financial facilitations. These are the so-called Export Processing Zones (EPZ), which the International Labour Organization (ILO) defines as follows: they are "industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being (re-)exported again[95]". In exchange for these favourable conditions the foreign firm has to export the biggest part, or all of its output. In other words, they are special economic zones, that can take different forms (such as free trade zones, maquiladoras...) in which materials or semifinished products are easily introduced with the objective of being here transformed and then exported. This process supports the export capabilities of host countries. The rapid increase of the number of EPZs, as

[94] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 23.

[95] International Labour Organization (ILO), <http://www.ilo.org/public/english/support/lib/resource/subject/epz.htm>.

shown in the table, reflects its importance as a source of employment: according to estimates of the World Bank, in 2008 they generated around 68,5 million workplaces, of which 61 million were located in the Asia-Pacific area[96]. Other common locations for EPZs are Mexico, the Caribbean and Latin America. Even if in the beginning the activities developed in these zones belonged mainly in the sectors of clothing, textiles and the assembly of electronics, they are now accessing also the branches of high technology, science and logistics.

Table 2.3. Growth in Export Processing Zones.

	1986	1997	2002	2006
Number of countries with EPZs	47	93	116	130
Number of EPZs	176	845	3000	3000
Employment (millions)	NA	23	30	66

Source: Jean-Pierre Singa Boyenge, *ILO database on export processing zones,* 2007.

We can say that the success of export processing zones derives from the fact that multinational enterprises have always paid notable attention to the different fiscal measures of host countries, since their main objective is the maximization of their global profit. Even if a favourable fiscal environment will attract a bigger share of FDI, in the long run it can have deplorable effects on the economy because it can lead to discriminations among different sectors, creating a very complex and delicate system in which tax evasion can be present.

2.8.4 Availability of infrastructures

Another determinant that influences the choice of the location of multinationals' investments is the availability and quality of public infrastructures in the host country.

[96] World Bank (WB), <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/TRADE/0,,contentMDK:20540534~pagePK:148956~piPK:216618~theSitePK:239071,00.html>.

It has been proved that a better accessibility to infrastructures is positively correlated to a greater productivity of the investments and to reduced costs of production. Needless to say, the importance that enterprises give to infrastructures depends on the kind of enterprise and on the sector in which it operates but, other things being equal, countries better equipped in infrastructure will be preferably chosen as a location for investments.

3. MULTINATIONAL ENTERPRISES: WHICH ROLE IN THE GLOBAL ECONOMY?

3.1 The counterfactual problem

The presence of multinationals in a country can have several effects of different kind: not only economic, but also social, cultural, political and environmental. In this chapter we are going to study and focus on the economic effects of the activity of multinational enterprises both on host countries and on home economies. Indeed, opinions and worries of scholars, policy makers and common people over the conduct of multinationals stem mainly from the perceptions that those people have of their positive or negative effects. Multinational firms are often seen as the main protagonists of globalization and as the only beneficiaries of this phenomenon. In fact, there are several ways through which a foreign direct investment operated by a multinational can increase the economic well-being of a country. FDIs can cover the investment gaps of those countries that are not able to produce enough savings in order to support their rhythm of growth; secondly, multinationals can decrease the costs of international transactions (use of different languages, or of different rules) and they can facilitate the exchange not only of goods and services, but also of knowledge and technology. Besides, the presence of a foreign firm in the national territory can prompt local firms to improve their managerial, production and marketing techniques because they can have access to more sophisticated inputs and more skilled personnel, and also because they feel the competitive pressure[97].

Assessing the impacts of the activity of multinationals is far from being easy, because of the difficulty in stating a counterfactual situation: what would have happened if the investment was not made? Virtually every feature of the activity of MNEs has been given positive or negative connotations according to one's ideological point of view: MNE supporters see these firms as job creators, capable of expanding national economy, acting as a force leading to the economic development, through the

[97] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* pp. 80-81.

spread of new knowledge and new technology. MNE opponents, instead, see multinationals as exploiters of local economies and destroyers of workplaces. Additionally, things might change depending on the kind of investment (greenfield of brownfield investments), on the country in which the investment is made (developing or developed countries), and on the time-frame that is being considered. All these variables are responsible for eventual alterations occurring in the evaluation of the conducts of multinational firms, and so what can be true for a firm in one determined set of circumstances, may not be true in others.

In the next sections, first we are going to see the effects of the presence of a multinational firm in a host country (effects of inward investments); then we are going to value the consequences that the multinational has on its domestic base (effects of outward investments). Despite the fact that literature and the public opinion have for long focused the attention only on the impacts of multinational firms on host economies, relevance should be given also to the role that these actors play in their national context.

3.2 Impacts of multinational enterprises on host economies

The main point here is to identify which are the benefits and the costs for a country to be used as a host for multinational activities and to judge whether the benefits outweigh the costs. This represents a very important objective, especially for the governments of developing countries because, based on this evaluation, they will decide how much of their (few) resources they will spend trying to attract foreign investments. From a general point of view, it is undeniable that FDIs have represented a more positive, than negative, resource, since they have contributed to the economic development as a whole. In fact, "without the capital, technology, and access to markets that may be provided through involvement in transnational production networks, many places would be far poorer[98]". The effects that multinational enterprises can have on local actors can be distinguished into two kinds: direct and indirect effects. The former are easily identifiable: in the case of a greenfield

[98] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 460.

investment they include the transfer of capitals and the creation *ex novo* of workplaces from which all the host economy can benefit; in the case of a brownfield investment, the direct effects are more difficult to evaluate, and they are delimited to the boundaries of the firm acquired. The latter instead cover a vaster number of cases, starting from the fact that multinational enterprises own higher knowledge and higher technologies that can spread to other local firms. The idea at the base of this concept is that the foreign presence of a multinational firm does have positive spillovers, namely technological and monetary benefits, since multinationals possess deeper knowledge and more developed managerial techniques which local firms can use and from which they can learn. These include the transfer of technology, and the acquisition of professional competences; they encompass those externalities that may arise when the multinational uses components that are produced in the domestic market, strengthening the local production of factors, and generating quantitative and qualitative developments and costs reductions. When these positive spillovers affect the same sector in which the multinational firm operates, they are called intra industry spillovers, when they affect firms operating in the whole production chain of the multinational they are called inter industry spillovers. According to a study conducted by Gorg and Strobl (2005), positive spillovers take place especially when personnel who used to work in the multinationals stop working there and move to local firms, carrying with them all the experiences and the technological and managerial expertise they have learned.

3.2.1 Injection of capital

The first effect linked to the presence of multinationals in a host country is their capital injection, an action that represents an important resource particularly for those countries that lack capital availability. However, sometimes this injection can have other, and not completely positive, effects. For instance, in the long run the reverse flow of money towards the parent company generated by the first capital investment can happen to be bigger than the original investment itself, causing a loss in the host country. Other episodes saw that local firms were not bought thanks to a multinational's investment, but actually through local money, obtained by local firms

being squeezed out of their market because of the bigger attractiveness of the multinational enterprise[99].

As we said several times, multinational firms are the main resources of investments in the sector of research and development (three fourths of all civilian R&D[100]). First of all we need to remember that multinationals are very jealous of their knowledge, and so they can prevent local firms from accessing it, trying to keep their proprietary technologies secret. However, when the transfer of their knowledge and technologies to host countries do take place and knowledge is made available to other local users, this can actually represent the best way to move capitals, since the availability of new technologies can lead to an increase in productivity and possibly to the development of new innovation. Knowledge and technologies can spread to the local context thanks to the mobility of people: multinationals make use of resources and time for the training and formation of their employees, so when they leave the company they act as vehicles of knowledge from which local firms can benefit. Besides, when local labour force is employed in multinationals' affiliates, it gets trained and it is given specific skills and techniques that can then enrich the whole local community. Additionally, knowledge can be moved thanks to social interactions between people working on the same activities but in different companies.

3.2.2 Creation of new linkages

The best way through which knowledge can be spread is through inter firm linkages. The expression "linkages", introduced in 1996 by Andrés Rodriguez-Claire, meant the relationships being created between multinationals and local firms when the former turn to the latter in order to acquire intermediate or final goods, therefore establishing linkages with both suppliers (backward linkages) and customers (forward linkages). These relationships have positive repercussions on local actors: they have to face an increased demand of inputs originated by the presence of the multinational, that drives already existing local firms to increase the production (which in turn leads

[99] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 461.

[100] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 183.

to a reduction of costs), and that can also lead to the birth of new *ad hoc* industries, created expressly to meet the higher demand. Besides, multinationals' orders will need specific requirements, and local firms, in order to meet them, will develop more sophisticated knowledge and technical skills. Therefore, "the experience gained in new technologies by local firms enables them to compete more effectively in broader markets[101]". This expanded activity will have a positive propagating effect also for the industries of transportation and distribution, with the consequence of creating new workplaces, and finally contributing to an overall positive repercussion for the whole host economy. It was noted that, in some cases, the effects of interconnection created by the development of backward and forward linkages allowed domestic firms to become stronger than the multinational plant itself and finally they were able to remove it from the market[102].

3.2.3 Effects on local firms: stimulus or obstacle?

One main criticism that has often been addressed to multinationals is that they destroy local firms. Being bigger, better organized and more competitive, they drive out of the market especially those small national firms which cannot cope with foreign competition. The evaluation of the presence of multinationals' affiliates over the productivity of local firms is far from being easy. Factors that need to be taken into consideration are the kind of host country (developed or developing), its specific national economic context and also the size and the market power of the investing multinational firm. What has been noted is that there is far less difference between a foreign firm and a domestic firm that both belong to developed economies than between a foreign firm with its home base in a developed country and a domestic firm of a developing country. Dicken (2007) noted potential negative effects: in the long run the presence of a MNE in a host country will very probably lead to an increase in the level of firm concentration, a situation in which the number of enterprises will be reduced and fewer but bigger firms will dominate the market: the weakest domestic

[101] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 464.

[102] M. Hobday (1995) *Innovation in East Asia: Diversity and Development,* in *Technovation,* vol. 15, n° 2, p. 56.

firms are likely to be squeezed out of the market. Positive outcomes instead seem to be predominant in those countries or sectors in which the technological gaps between the investing and the domestic firm are non-existent or very small, and therefore the latter is capable of absorbing the positive spillovers: the two firms have a technological proximity. Empirical evidence has demonstrated that spillovers have bigger and long-lasting effects when domestic enterprises invest considerably in research and development, in the formation and training of their labour force, and when the local environment in which they act is active and competitive. Put another way, spillovers have the best outcomes when they find a fertile ground, that is to say when there are domestic firms that are capable of absorbing, elaborating and using everything that overflows from the multinational firm in terms of knowledge and technology[103]. Positive effects for the local economy can be possible also when foreign enterprises create linkages with domestic firms, enabling them to increase and develop their business activity, and also when, as we saw before, the increased production demand and the mobility of employees, especially of managerial personnel, stimulate the birth of new and of spin-off enterprises[104].

3.2.4 Jobs and wages

The most controversial problem related to the presence of foreign affiliates in host countries is definitely the one linked to jobs and salaries: we are going to see if multinationals stimulate the creation of new workplaces or if they destroy already existing ones, if the quality of jobs they offer is bad or good, if they pay higher or lower wages and if the salaries they pay have positive or negative overall effects. The issue of jobs has always been central for host companies and governments at the moment of deciding investment attractive policies. The main questions being asked to value the impact of MNEs on jobs are summarized by Dicken[105]:

- Does the presence of a foreign affiliate create new jobs?

[103] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 88.

[104] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 468.

[105] Ibidem.

- What type of jobs are they?
- Do MNEs pay higher or lower wages compared to local enterprises?
- What effects do higher salaries have on the local economy?

Before answering these questions we want to highlight that there is a considerable performance differential between multinationals and domestic firms. Most empirical evidence shows that multinational enterprises, compared to national firms, register better performances in the home base as well as abroad in the controlled affiliates. Different data analysis put together by Navaretti and Venables (2006) over the performances of firms for the UK, Italy and other developed and developing countries, shows that the productivity of the foreign-controlled affiliates in a host country is far higher (30%-70%) than the productivity of a domestic firm and, additionally, it is also 30% higher than the productivity of the MNE in the home base[106]. This happens because multinationals are bigger, they have the availability of greater capitals, they can invest more in research and development and they can make use of more skilled and better trained labour force. Therefore, making a new comparison that takes into consideration these differences, we can see that the productivity discrepancy between domestic and multinational firms still exists but it reduces consistently to a gap that goes from 1 to 7%[107]. If a domestic firm becomes controlled by a foreign multinational through a process of merger or acquisition, very probably that means that it has been chosen because it has displayed better performances than its national peers. Similarly, when it is a domestic firm that becomes an international investor acquiring other foreign firms, it is able to do so because it already owns optimal performances. Several studies have focused their attention on the control of productivity of firms starting to invest abroad or becoming controlled by a foreign multinational, asking the following question: what would have been the performances of these firms if they did not invest abroad or if they were not acquired by a foreign firm? Once again these studies confirmed the existence of a productivity gap: even if some works did not notice any significant positive effects, none of them observed negative effects, coming to the

[106] G. B. Navaretti, A. J. Venables (2006) *Le multinazionali nell'economia mondiale,* p. 56.

[107] Ibidem.

conclusion that multinational enterprises never display performances that are worse than the ones of domestic firms. Therefore, policy makers should be reassured by the empirical evidence: whether a domestic firm becomes transnational by investing abroad, or it is acquired by a multinational firm, its performance is going to improve. Besides, generally speaking, multinational firms have some specific characteristics (such as size, major investments in research and development and so on) that are highly desirable because they enhance the performance and the productive structure. Below it is reported the table with the different studies that Navaretti and Venables took into account to reach the conclusions described above.

Table 3.1. Multinational affiliates and domestic firms: who is more efficient?

Bibliographic references	Country and period	Who is more efficient?
Blomström and Wolff [1994]	Mexico, 1970	MNEs
Sjholm [1999]; Okamoto and Sjholm [1999]	Indonesia 1980 and 1991; Indonesia 1990-1995	MNEs in 26 out of 28 sectors. MNEs
Kokko, Zejan and Tansini [2001]	Uruguay, 1988	MNEs
Haddad and Harrison [1993]	Morocco, 1985	MNEs in 12 out of 18 sectors
Chuang and Lin [1999]	Taiwan, 1991	MNEs
Ramstetter [1999]	5 East Asian countries for 15-20 years	MNEs
Criscuolo and Martin [2002]; Griffith and Simpson [2001]; Harris [2002]; Harris and Robinson [2002]	United Kingdom, different years	MNEs
Benfratello and Sembenelli [2006]	Italy	MNEs

Source: Navaretti and Venables (2006) *Le Multinazionali nell'Economia Mondiale.*

When multinational firms engage in FDIs in a foreign host country, they do create a number of extra jobs, that can be divided into direct and indirect jobs. The former are those jobs being created by the multinational and its investment themselves, while the latter include also all the other workplaces being created throughout the domestic economy. If multinational firms act in a sector in which there is unemployment, they will increase the total number of jobs in that sector, and this represents a direct effect. Therefore, the number of jobs created directly depends mainly on the scale of the

investment and on the kind of activity: if it is labour-intensive, rather than capital-intensive, the number of jobs generated will be broader[108]. Regarding the indirect jobs, the stronger and vaster the local linkages established with domestic firms, the bigger the number of them being created.

3.2.5 Quality of jobs

The natural question that follows these considerations is: what kind of jobs are they? Which is the quality of them? The general perception is that jobs created by a foreign investment are less stable and durable than workplaces offered by domestic firms. This perceived volatility stems from the fact that people see multinationals as more exposed to the risks associated to international shocks, such as prices or technology shocks, that would have repercussions on occupation. Additionally, the costs of geographic reallocation of multinational firms are lower compared to the ones of national firms, and this allows multinationals to be less responsible towards national authorities and rules. However, according to the empirical evidence, the prediction that multinationals provide more volatile workplaces is wrong. In fact, after a shock implying the variation of salaries or of the demand of products, multinational firms are quicker to respond to these shocks, and they do so with the least alteration of labour demand. Therefore, employees of a multinational firm are less likely to lose their jobs, compared to employees of a domestic firm.

As we have already seen, as a general trend we can say that multinational firms distribute their high-level decision-making processes and their R&D laboratories in developed countries, while developing economies are basically used as bases for productive units and low-skill assembly occupations, showing an inclination to concentrate more sophisticated activities in developed countries. However, things are changing and there is evidence that also in developing economies multinational enterprises are increasingly employing better-formed and higher-skilled workers[109]. Besides, multinational firms tend to invest consistently in the formation and training of their workforce, and they have started providing this education, that was not available

[108] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 468.

[109] Ivi, p. 469.

before in the domestic firms, also to workers in developing countries, supplying with benefits the whole host economy.

Among the most recurring and shared accusations addressed to multinational firms is the fact that they behave immorally towards their workers, especially in poor countries, exploiting them and paying them salaries that have been defined as "unfair", "low", "inadequate" and sometimes not even "sufficient to live". Do these critiques represent the true reality or do multinationals pay, in fact, higher wages than the ones paid by national firms? Accusations directed towards globalization and its main actors are too often based on bad specific cases that, in themselves, are devoid of any statistical relevance. It is well-known that in the past decades some multinationals took advantage of lacking regulations to exploit child labour, a fact that has been abundantly proclaimed and condemned. In today's world, the probability of episodes like these happening again has considerably decreased. First of all because in many countries democratic forms of government have gained the upper hand, and also because in our era of television and the internet, such events would have a bigger significance that would damage or destroy the reputation of the firm[110]. As investigated by Khanna, the Business and Human Rights Resource Centre supervises the activity of 3600 enterprises in 180 countries, reporting any violation of human rights and updating their websites with this information every hour. Such operation of transparency forces a company to behave accordingly to rules, labour and environmental regulations in order to avoid damages to its balance and reputation[111].

Nowadays, all the available empirical evidence is unmistakable and it agrees on the fact that multinational firms, both in developed and developing countries, using more sophisticated technologies and so being more productive, pay higher salaries compared to domestic firms. The term *wage premium* is used to point out how much more money do multinationals pay to workers. As reported by Cohen (2007), regarding developed countries, Edward Graham and other scholars found out that the salary paid by American affiliates was 1.4 times larger than the one of domestic firms in high-

[110] J. Bhagwati (2005) *Elogio della globalizzazione.* Bari: GLF Editori Laterza, p. 231.

[111] P. Khanna (2011) *Come si governa il mondo.* Roma: Fazi Editore, p. 190.

income countries, 1.8 times bigger in medium-income countries and two times in low-income economies[112]. Navaretti and Venables (2006) reported a study conducted by Conyon *et al* that took into consideration UK firms after undergoing a change of property. It showed that, when a domestic firm is acquired by a foreign investor, a 3.4% increase in workers' wages took place. Conversely, when a foreign-controlled firm is acquired by a national firm, wages underwent a decline of 2.1%[113]. Generally speaking, evidence based mostly on data available for the United States and the United Kingdom shows that multinational firms from these countries pay higher salaries, with a premium wage going from 6 to 26%[114]. Evidence concerning developing countries is even more striking. According to a study by Linda Lim, reported by Goldstein and Piscitello (2007), foreign affiliates of American multinationals in Bangladesh, Mexico, Shanghai, Indonesia and Vietnam pay to their workers a wage premium that goes from 40 to 100% of their current salaries. Other scholars, namely Aitken, Harrison and Limpsey, as reported by Navaretti and Venables, stated that in Cote d'Ivoire, Morocco and Venezuela multinational affiliates provide to their workers consistently higher salaries. In these cases the wage premium ranges between 10 and 260%. Again, other works showed that in Indonesia salaries remitted by foreign-owned affiliates are between 12 and 50% higher than domestic firms' wages[115]. How can we explain this fact? Looking at things from the multinational perspective, one very important factor to take into account is reputation. By offering higher salaries to local workers, multinational firms can improve their network of linkages and relationships, and also their reputation in the markets. When it was discovered that some companies did not respect adequate occupational standards, and that they directly or indirectly exploited child labour force, multinationals had to face damaging repercussions. Besides, multinational firms have to keep rather homogeneous standards of working conditions and wages in all the different locations in which they operate, therefore not

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[112] S. D. Cohen (2007) *Multinational Corporations and Foreign Direct Investment: avoiding simplicity, embracing complexity.* Oxford: Oxford University Press, p. 293.

[113] G. B. Navaretti, A. J. Venables (2004) *Le multinazionali nell'economia mondiale*, pp. 57-58.

[114] Ivi, p. 57.

[115] Ivi, p. 164.

taking full advantage of the different labour cost differentials in the distinct countries. Another important reason why multinationals offer higher wages is to solve their problem of informative asymmetry: they need to attract the most skilled and better-trained workers, but they come from abroad and so they do not have the same network of contacts and connections as local firms do, and they do not know the local market as well as the latter do. Therefore, to reach these workers they offer them a higher remuneration than the one offered by domestic firms[116]. Finally, multinationals have to consider the turnover of workers: since they invest much in the formation and training of their employees, they offer them higher salaries to prevent them from leaving the company and dissolving internal knowledge. In fact, as we already said, the mobility of workers represents the main way through which knowledge and information can be spread between firms. For many years academics have feared the possibility of a downward race in the price of labour force, meaning that multinational firms would have moved wherever the labour could be paid less. However, recently an increasing number of companies have undertaken an upward race, teaching the employees new competences, continuously training them and offering them better salaries.

Scholars have then tried to see whether these higher levels of remuneration provided by multinational firms have led to positive spillovers (such as an increase in the salaries given by domestic firms), or to negative spillovers (when multinationals employ all the available better-skilled labour force, leaving to local firms only less skilled workers). Even if the results from the empirical evidence can be ambiguous, as a general trend the effects can be seen as more positive than negative: corporate restructuring and the cut of workplaces can happen in the short time, but then, in the long run, increase in productivity and in employment do take place. Generally, multinational firms employ skilled workers more intensively than domestic firms, but this is true almost exclusively for developing countries, while for developed economies a significant difference in the intensity of skilled-labour was not observed. These results are consistent with the idea that the more retarded the country of destination,

[116] G. B. Navaretti, A. J. Venables (2004) *Le multinazionali nell'economia mondiale*, p. 126.

the more important the difference in the level of technology between multinational and domestic firms[117].

3.2.6 Labour and human rights

Multinationals have also long been accused of being responsible for the violation of the labour rights of host countries and sometimes even of human rights. First of all it is very important to point out that, contrary to what is usually believed, multinational firms tend not to invest in those countries where human rights violations take place regularly. The vision of many people, who assumed that multinationals and rights violations would go hand in hand, has long persisted; but actually this issue needs to be considered more deeply. In fact, recent studies have shown that the respect of human rights can actually act as a stimulus attracting the foreign investment. According to Blanton and Blanton, "developing countries that respect human rights are more successful in attracting foreign direct investment than those characterized by abusive human rights practices[118]". This is due to the fact that countries where such violations take place are also places inclined to see frequent subversions and where the political stability is continuously threatened; therefore in such locations the foreign investment is going to be risky and the investor himself would feel too vulnerable to external conditions that he cannot control. Conversely, the "respect of human rights creates an environment conducive to the development of human capital and encourages a more open, well-trained and economically efficient society[119]", characteristics that are all very important for a firm deciding to invest abroad. It follows that multinationals have developed the trend that sees them privileging those countries where civil and political liberties are protected and respected. When multinationals make investments in countries where there are violations of labour rights, they can seek the help of organizations, such as Human Rights Watch (HRW), that can give assistance to them in order to manage better such situations. What is

[117] G. B. Navaretti, A. J. Venables (2004) *Le multinazionali nell'economia mondiale,* pp. 126-127.

[118] S. L. Blanton, R. G. Blanton (2007), *What Attracts Foreign Investors? An Examination of Human Rights and Foreign Direct Investment,* in *Journal of Politics,* vol. 69, n° 1, p. 143.

[119] Ivi, p. 144.

usually suggested is to keep investing and working in these places, trying to improve employees' conditions, in such a way that the private sector, and not the public sector, would be responsible for fixing higher standards that then can be followed by others[120]. Besides, it is difficult to believe that multinational firms do not respect labour rights in developing countries, because in these areas the national requirements are not particularly high and demanding. For all these reasons that we have observed, multinational enterprises and the respect of labour and human rights must started to be seen not as elements at odds with each other; rather, the latter has to be seen as a condition necessary to attract the activity of the former.

More and more frequently empirical studies have demonstrated that the activity of foreign multinationals in host countries has brought more positive than negative effects. The presence of foreign multinationals has acted as a stimulus for exports to the country of origin of the multinational, as well as to other markets. Goldstein and Piscitello reported that as far as 1999, 90% of exports in Ireland, 44% in Canada and the Netherlands, 15% in the United States, 80% in Hungary, 50% in China were accountable to the activity of multinational affiliates situated in each country. As for developed countries, empirical evidence also showed that foreign multinationals have a positive effect for the exports of domestic firms, because they have access to new information regarding distant and unknown markets and so they acquire the capability of evaluating the feasibility of accessing enlarged and international productive networks[121]. The increase of foreign direct investments for a developing host country speeds up its development and it reduces its level of poverty (provided that it already has a sufficient level of education). Therefore, the negative positions of no global people towards globalization and towards the "imperialistic" behaviours of multinationals have to be reassessed: for developing countries the presence of multinational affiliates and their investments represent a catalyst factor in the process of growth and catching up. People should stop believing that foreign investments in the poorest countries increase inequalities. As it was said by Ulrich Beck, "there is only

[120] P. Khanna (2011) *Come si governa il mondo,* p. 190.

[121] A. Goldstein, L. Piscitello (2007) *Le multinazionali,* p. 89.

one thing worse than being overrun by multinationals, and that is *not* being overrun by multinationals[122]", since multinationals allow even poor countries to be part of the global economy.

3.3 Impacts of multinational enterprises on home countries

Historically, little attention has been given to the effects that foreign direct investments could cause in the home country of a multinational firm. Only in the last decades this topic has received a strong push, focusing particularly on the relationship between the productive activity of the firm abroad and the levels of employment in the home economy. For pessimists in countries of origin, the main concern is represented by the fact that foreign investments imply resources that could have been spent in the national economy. This diversion in the use of resources is believed to cause a reduction in the domestic economic activity of the firm and therefore in its level of occupation. However, if this could be true in the short period, the effect of a foreign investment in the long run is far more complicated and needs to consider many more variables. The positions of critics are mitigated when the foreign investment is made as a defensive strategy, that is to say as a preventive step. In this case the firm invests abroad because otherwise it would lose part or all of its market share and workplaces would be dissipated anyway. The necessity of this kind of investment derives from the erection of new barriers to international trade and from the emergence of new competitors in the international market[123].

Additionally, when studying the effects caused by a foreign investment in the home economies, it is very important to consider another crucial problem: the fact that we do not know the counterfactual situation, that is to say that we cannot know for sure what would have happened to employment, production and exports in the home country if the foreign investment was not made. If those resources were kept in the home base, would the national firm have been able to maintain, or even expand,

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[122] U. Beck (2005) *Power in the Global Age: A New Global Political Economy.* Cambridge: Polity Press, p. 52.

[123] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy*, p. 457.

its market share? Or would other foreign competitors have driven it out of the market[124]? These questions are particularly hard to answer but, anyway, the results of these studies seem to go in the direction of a reinforcement of the national economy.

3.3.1 Effects on employment

According to Dicken (2007), the effects that a foreign direct investment can have on the occupation in its home country can be distinguished and divided into four categories[125], in three of which employment is strengthened by the investment, while in the remaining one it is weakened:

- *Export stimulus effect:* employment is strengthened thanks to the fact that the foreign investment has prompted the production of goods for export (this situation would not have been possible without the FDI).
- *Supporting firm effect:* employment is benefited because the investment increases the production of goods and services in other firms supplying the domestic company which made the investment, since it has expanded its activity.
- *Home office effect:* an increase in the occupation takes place in those functions that are not linked with production, such as control and administrative functions, because of the need to coordinate expanded foreign activities.
- *Production displacement effect:* employment is damaged by the fact that the new foreign affiliates serve directly those local markets in which they produce, causing a reduction of the exports from the home base plants.

Therefore, Dicken came to the conclusion that the net benefit for employment stems from the sum of the first three effects, to which the last effect must be detracted.

A common belief is the one according to which an enterprise that moves or expands its production abroad, especially in those countries with low costs of labour

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[124] M. Blomstrom (1999) *Internationalization and Growth: Evidence from Sweden,* in *Swedish Economic Policy Review,* n° 7, p. 191.

[125] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 458.

force, tends to substitute workers in the home base with new workers in the foreign affiliates in the host countries. In order to analyze carefully this issue, we need to make a distinction between vertical foreign direct investment and horizontal foreign direct investment. Considering the first category, firms change the structure of their own production chain, fragmenting it and reallocating those parts that are intensive in low-skilled labour wherever the costs of unskilled labour force are lower. However, simultaneously, this process of transfer implies a reduction in the costs of production, an increase in the competiveness of the firm, and therefore an increase in its market share, that, in the long term, would bring benefits to the size of the domestic activity as well[126]. The effects of a vertical offshoring can be seen not only in the level of employment in the home country or in the foreign affiliates, but also in the relationships of supply and in the demand of specialized inputs (such as services, managerial skills and so on) activated by the firm. In fact, production conducted in foreign affiliates can have *substitute* effects on national employment, when previous supply contracts are cancelled and so local demand of goods and services decrease; or it can have *complementary* effects, when the firm that becomes multinational improves its capability of innovation, generating a new demand of specialized inputs locally available.

A different argumentation needs to be done when we consider horizontal foreign direct investments. This kind of investment mainly indicates the willingness of a firm to grow and expand, and reflects its interest in the foreign local market. Horizontal investments are substitutive of exports going from the home base to the foreign country and so, in the beginning, they determine a reduction of the domestic output[127]. Nevertheless, if the foreign plants utilize complementary products that are created by the home base firm, in the long term the size of the activity of the domestic firm in the national market is going to increase. Several mechanisms can operate in the direction of an increase of labour intensity in the home base as well as in the foreign affiliate. In particular, international expansion implies the multiplication of tasks such

[126] G. B. Navaretti, A. J. Venables (2004) *Le multinazionali nell'economia mondiale*, p. 129.

[127] Ibidem.

as supervision, coordination and control of geographically scattered activities, it determines a qualitative and quantitative growth of the functions of research and development, of marketing, and of all those functions that are usually conducted in the home base. Consequently, there is an increasing need of those workers who are not directly employed in the production, namely managers and white-collars, in the multinational's original plants in the home country[128]. This effect can be amplified to the economic network of interactions of the home base when a renovated demand of specialized and skilled labour-intensive inputs generates positive externalities. The level of employment in the home country can be increased also thanks to complementary activities produced by the foreign investment, that can act as a compensatory force that can fix the eventual effects of substitution of the exports from the home base with the production abroad. To summarize, studies that focused their attention on employment showed that, generally, vertical FDIs are complementary to the activities conducted in the home base, while horizontal FDIs tend to substitute them. Indeed, the former operate a process of fragmentation of the production chain, leading to an increase in the exports from the home countries; the latter, conversely, cause a contraction of these exports. These results contrast with what is commonly believed, namely that the vertical kind of investments towards countries with a low cost of labour force weakens the activity in the home countries, while horizontal investments towards developed economies lead to an increase of the national presence in the international markets. What actually happens is that through a vertical investment a firm is able to decrease its costs altogether, therefore production can grow and also employment in the complementary activities can increase, or at least it can avoid a decline.

3.3.2 Effects on labour force composition

Navaretti and Venables (2004) go on with their analysis to consider also the composition of the inputs of the activities carried out in the country of origin. When a horizontal investment takes place, there are no precise predictions that can be done over the effect that it would have on the production factors. Conversely, a vertical FDI

[128] A. Goldstein, L. Piscitello (2007) *Le multinazionali*, pp. 91-92.

predicts that there will be an increase in capital and in the demand of qualified labour force in the domestic environment, since the activities intensive in low-skilled labour force are moved where this factor is abundant and cheap. This process represents the main reason why an increase in the demand of well qualified workers has been observed in developed countries. Besides, the two scholars investigated also the effects that foreign direct investments can have on the process of technological development of the firms. Indeed, foreign affiliates can represent an important channel through which a firm can acquire new knowledge and new technologies and transfer them in the home country to develop domestic activities. This happens especially when foreign affiliates are located in areas where high technology-intensive activities take place.

Many works have focused their attention on the relationship between domestic and foreign production. They demonstrate that these two elements are complementary, that is to say that an increase in the sales of foreign affiliates usually correspond to an increase in the exports of the domestic firm (which in turn implies an increased level of production). A study confirming this positions is the one conducted by Lipsey and Weiss, focusing on the activity of American multinationals: complementarity prevails at the firm's level as well as at sector's level. This reinforces the opinion according to which international production and trade act in unison: the foreign investment allows the firm to strengthen its market share, which in turn enables it to improve its learning capabilities in new markets, sustaining its exports performances.

The debate over the impacts of multinational activities on the labour force focused mainly on two aspects: to see if the nature of the production conducted in the foreign affiliates is substitutive or complementary to the production of the home base; and to see which are the impacts of the foreign activity on the composition of the national occupation and on the differentials in salaries. Considering the former issue, we saw that empirical studies have demonstrated, almost univocally, the existence of a relationship of substitution when the foreign investment is made in a developed economy. Conversely, when a vertical FDI takes place, the foreign activities of the affiliates in host countries tend to be complementary to those operated in the home

base. Under this point of view, outward investments have acted as a strengthening force for domestic activities since they have led to an increase in employment, outputs and production. Goldstein and Piscitello studied the Italian case, and they came to the conclusion that the reduction of the number of workplaces in those industries that underwent a process of internationalization through foreign investments is not only not very significant, but often this reduction is smaller than the one that would have taken place if the investments were not made[129]. These conclusions seem to offer a quite encouraging perspective, and they are in countertrend with the negative view over multinational activity. Often multinational firms have more positive than negative repercussions, both in the country of origin and in the host economies. As we reported above, also the common worry according to which investments made in developing countries, where labour force is cheaper, would decrease the activity in the home countries is basically unfounded. In fact, investing in countries where the cost of labour force is low can actually be a good strategy to safeguard national employment. Besides, considering the second issue, that takes into consideration the eventual changes in the composition of the national labour force, managing new productive activities abroad can lead to a skill-upgrading in the functions of the home country plants, namely an increase of qualified workers. In particular, this happens with vertical investments: they determine a rise in the average level of skills of the employees in the home base, since there all the qualification-intensive functions are located (R&D, marketing, finance...). The transfer of activities in foreign locations can have repercussions also on the general economic environment of the firm, namely on its suppliers and customers. The local system will be positively affected by the internationalization of the firm if its workplaces and its supply activity are safeguarded. Horizontal investments, that are made mainly because of the willingness of the firm to follow its strategy of expansion and growth, lead to a multiplication of the national production thanks to its increased volume of dealings and to its deeper experience of penetration of the markets. The transfer of the activities to countries where the labour force is cheaper can have, as a consequence, also the relocation of supply firms that otherwise would be negatively affected by their substitution with foreign supply

[129] A. Goldstein, L. Piscitello (2007) *Le multinazionali*, p. 93.

companies. When an important client moves and expand internationally, supply firms that have close supply relationships with it are prompted to follow it in the foreign countries where it moves, locating their establishments close to the foreign affiliates of the client. In this way, the downstream producer can guarantee a certain coherence of products at the international level, and simultaneously it can enjoy some benefits regarding the management of the supply chains: it can count on well-known and reliable partners, with which there are strong and long-lasting relationships based on trust, confidentiality and reliability for what concerns the exchange of information. Lastly, we want to report the effects that the internationalization can have on the levels of productivity. The question is: does a firm that becomes multinational enjoy benefits in terms of efficiency and productivity? The answer is not easy and straightforward and needs to take into account many different aspects. First of all it is important to analyse the relationship of causality: does an increased productivity represent the cause or the effect of the internationalization? Scholars need to work out whether multinational firms become more productive, or whether they are able to become multinational precisely because they are more productive. Then, it is necessary to discover an adequate counterfactual: what would have happened if the firm did not become a multinational[130]? Theory and research in these fields are still incomplete, but the few existent studies demonstrate that the effects are more positive than negative.

Then, what conclusions should we reach? The widespread idea that sees globalization and firms' internationalization as a misfortune, rather than an opportunity, needs to be faded away. All the empirical evidence assembled so far shows that the presence of multinational enterprises (both national firms in foreign countries and foreign firms in the national territory) can offer the concrete opportunity of gaining some benefits. However, do these advantages always take place? The answer has to be no. Therefore, we can conclude by saying that the positive effects represent a central trend, that is to say that they come about not always, but in most cases. The impacts that a foreign direct investment can have need to be studied on a

[130] A. Goldstein, L. Piscitello (2007) *Le multinazionali*, p. 98.

case-by-case basis, taking into consideration the characteristics of the home base, of the host country, and the characteristics and strategy of the firm itself[131].

Finally, we are going to report a recapitulatory table, provided by UNCTAD, of the direct and indirect effects of foreign direct investments on the employment in host economies:

Table 3.2 The potential effects of inward FDI on quantity, quality and location of employment in host countries.

Area of impact	DIRECT		INDIRECT	
	Positive	**Negative**	**Positive**	**Negative**
Quantity	Adds to net capital and creates jobs in expanding industries.	FDI through acquisition may result in rationalization and job loss.	Creates jobs via forward and backward linkages.	Reliance on imports or displacement of existing firms results in job loss.
Quality	Pays higher wages and has higher productivity.	Introduces practices in, e.g. hiring and promotion that are considered undesirable.	Spillovers of "best practices" work organization to domestic firms.	Erodes wage levels as domestic firms try to compete.
Location	Adds new and perhaps better jobs in areas with high unemployment.	Crowds already congested urban areas.	Encourages migration of supplier firms to areas with available labour supply.	Displaces local producers, adding to regional unemployment, if foreign affiliates substitute for local production.

Source: UNCTAD, *World Investment Report,* 1994.

And in home countries:

[131] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy,* p. 399.

Table 3.3 The potential effects of outward FDI on quantity, quality and location of employment in home countries.

Area of impact	DIRECT		INDIRECT	
	Positive	**Negative**	**Positive**	**Negative**
Quantity	Creates or preserves jobs in home location, e.g. those serving the needs of affiliates abroad.	Relocation of "job export" if foreign affiliates substitute for production at home.	Creates or preserves jobs in supplier/service industries at home that supply foreign affiliates.	Loss of jobs in firms linked to production/activities that are relocated.
Quality	Skills are upgraded with higher value production as industry restructures.	Lower wages to keep jobs at home.	Support sophisticated industries.	Downward pressure on wages.
Location	Some jobs may depart from the community, but can be replaced by higher-skilled positions, developing local labour market conditions.	The "export" of jobs can worsen regional/local labour market conditions.	The loss of blue-collar jobs can be offset by greater demand in local labour markets for high-value-added jobs relating to exports or international production.	Demand spiral in local labour market activated by layoffs can lead to employment reduction in home country plant locations.

Source: UNCTAD, *World Investment Report*, 1994.

3.4 Impacts of multinational enterprises on the environment

Since the movements and political activism in favour of sustainability have increasingly developed and gained influence, Occidental countries have been somehow forced to venture on the tough field of environmental regulations, and a great deal of attention has been given to the effects that the activity of multinational firms can have on the environment. It is a common opinion to believe that multinationals are responsible for causing environmental damages because they are thought to relocate some of their most environmentally harmful operations in those countries (almost exclusively developing countries) where environmental standards are not particularly high and

stringent. This point of view supports the idea of the so called pollution haven hypothesis, which implies that foreign direct investments are attracted in these areas thanks to their absence of environmental protection.

3.4.1 Pollution havens

A considerable number of studies have focused their attention on this topic, starting from the premise according to which multinational firms are prompted to relocate their activity by the fact that their home countries present too high costs of environmental protection. Research on the issue has to follow two steps: first, it has to demonstrate that, consequently to changes and enforcement in environmental regulatory mechanism, a firm tends to relocated those activities that produce more pollution. Secondly, it would also need to prove that, after this multinational investments, the export of pollution-intensive products from the pollution haven in the host countries has spread and, at the same time, the imports of the same products to the home country has increased as well[132]. What was, and partly still is, presumed is that multinational enterprises take part in a race to the bottom concerning the pollution standards at the international level. Basing our assumptions on the available empirical evidence, we can say that this worry is unfounded. For sure, if we look to the past, we can find examples of firms taking advantage of laxer foreign environmental standards to increase their profit. One example is provided by the behaviour of fruit companies such as Dole and Chiquita, which continued to use a worm-killing chemical pesticide in their plantations even after its harmful effect on health were discovered[133]. However, beyond the fact that these companies then had to face legal action, we can also state that this kind of behaviour is not the one systematically adopted by multinationals. In fact, all the different studies over the issue, considering different countries and different periods of time, are able to find only weak, if any at all, evidence that multinational investors relocate mainly those activities that are pollution-intensive, and even smaller evidence that places with moderate

[132] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 312.

[133] K. A. Reinert (2012) *An Introduction to International Economics: New Perspectives on the World Economy*, p. 399.

environmental regulations are more attractive for foreign direct investments. We report the words of Arik Levinson:

> "The conclusions of both the international and domestic studies of industry location are that environmental regulations do not deter investment to any statistically or economically significant degree. Most authors are careful to note the limitations of their individual research and to place caveats on their counterintuitive conclusions that stringent regulations do not deter plants, nor do lax regulations attract them. But the literature as a whole presents fairly compelling evidence [...] that regulations do not matter to site choice[134]".

In literature, many reasons why pollution havens have not worked as a sufficient stimulus to move multinationals' production have been found. First of all, in many cases the benefits that would have stemmed from an increased environmental freedom would have not been sufficiently high as to push the firm towards relocation. In fact, these advantages would have not been enough significant as to counterweight other factors, such as the costs of raw materials, the proximity to determined markets and the presence of fiscal facilitations[135]. Additionally, a more relaxed and moderate environmental context can be linked with other forms of bad governance, to which higher political risks can be associated. This situation can represent a danger for indigenous resources and infrastructures, building up an environment that multinationals always seek to avoid. We need also to consider the fact that multinationals tend to manage all their different establishments in the same way: they are adapted to the highest standards with which multinationals have to deal in the distinct locations in which they operate. Put another way, multinational firms decide to operate with the same technology in all the places in which they are present, since this have positive repercussions on efficiency and leads to an upward race for what concerns environmental standards.

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[134] Arik Levinson (1996) *Environmental Regulations and Industry Location: International and Domestic Evidence,* in J. N. Bhagwati and R. E. Hudec: *Fair Trade and Harmonization: Prerequisites for Free Trade?,* p. 450.

[135] J. Bhagwati (2005) *Elogio della globalizzazione*, p. 203.

Multinational enterprises, being active in many different countries, experience different environmental standards as well. If they adapt to the regulations that are laxer, they would continuously risk operating processes of upgrading, whenever these regulations become more stringent. This would imply considerable costs and waste of time, therefore multinationals prefer to pre-empt the events, and even in those areas with low standards, they go one step forward and apply more severe normative, as if the standard requirements were actually higher[136].

Another element that needs attention is the fact that multinational firms, operating in those countries with more rigorous environmental standards, tend to innovate more. They develop many innovations based on technology that has a low environmental impact, which is usually more productive and whose use brings more benefits. Since multinationals' purpose is to increase their productivity and profits, they will certainly use this environment-friendly technology wherever their affiliates are situated, even where the respect of high standards is not needed. In fact, using the old technology can represent a way of taking advantage of these laxer regulations, but it prevent the firms from exploiting the increased productivity made available by the state-of-the-art technology[137].

Last but not least, another factor that needs to be taken into consideration is reputation. Multinational firms that use environment-unfriendly technologies, taking advantage of the limited environmental legislation of the host country would risk damaging or losing their reputations. This element acts as an important inhibitor at the time of choosing whether or not to exploit this normative deficiency[138].

Thanks to the action of non-governmental organizations (NGOs), activist groups and the public opinion, multinational firms are starting to adopt the so-called "balance of the three Ps" (introduced by SustainAbility, a think tank and strategic advisory firm[139]) in which they consider equally people, profit and the planet. This model has

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[136] J. Bhagwati (2005) *Elogio della globalizzazione*, p. 204.

[137] Ibidem.

[138] Ivi, pp. 204-205.

[139] SustainAbility website, www.sustainability.com.

the purpose of explaining to firms how to evaluate their performance not only in terms of profits, but also considering their social and environmental impacts. According to Parag Khanna, since we live in a world in which multinational firms can produce more emissions than single countries, the importance of convincing them to analyze their activity in these three terms is astonishing, and it is considerably more significant than any international convention on the environment[140]. Besides, several big multinational firms have already started to use their own resources and capitals in order to develop projects over renewable energy. Some of them are British Petroleum, General Electric, Toyota and Michelin[141]. Data available on the former, in particular, show that its willingness to reduce its emissions leads to a cost of about 20 million dollars each year, but it has allowed the company to reach savings equal to one and a half billion dollars. British Petroleum has so intensively invested in renewable energies that a new meaning for its acronym has been suggested: BP standing for Beyond Petroleum[142]. Another important firm that is able to exercise a great deal of influence on the global economy in general, and therefore also on the field of ecology is Wal-Mart. This multinational firm has set, among its main objectives, to be completely supplied by renewable energy and create zero waste. At the moment, Wal-Mart spends about 500 million dollars annually for the implementation of renewable energies, it has around 300 renewable energy projects going on throughout its network and sustainable energy now provides 21% of its total electricity needs at a global level[143]. Wal-Mart is moving towards a policy of zero waste, that includes also the acquisition of the documentation over the sustainability of its suppliers. In 2008 the company announced that all its suppliers would need to cut at least 20% of their power consumption in

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[140] P. Khanna (2011) *Come si governa il mondo*, pp. 298-299.

[141] Ivi, p. 299.

[142] Ibidem.

[143] Wal-Mart website, www.corporate.walmart.com, and Wal-Mart Global Responsibility Report 2013, available at <http://cdn.corporate.walmart.com/39/97/81c4b26546b3913979b260ea0a74/updated-2013-global-responsibility-report_130113953638624649.pdf>.

order to be able to renew their contracts[144]. NGOs stopped waging war to these multinational giants and started to collaborate with them because they have understood that the private sector can do more for the environment than national or international treaties with their vague objectives.

The actions of non-governmental organizations, the civil society and environmentalists, pressures and boycott operated by consumers have represented very important factors that had the consequence of convincing multinationals of the relevance of applying high standards for the safeguard of the environment. What we saw is that, as a general trend, multinational enterprises do not operate a race to the bottom concerning the environmental standards: they do not purposely seek locations where environmental regulations are absent or lax, because the benefits that they would obtain would not be enough to compensate other factors. Finally, there is another final consideration that needs to be taken into account. More and more frequently firms that produce cleaner energy are putting more pressure and exerting lobby activities on authorities, because they want them to make these technologies mandatory. Lobbies of multinational investors and lobbies of environmentalists are consolidating a relationship between them: even if the former for profits, and the latter for altruism, they are responsible for the increasingly high standards in the field of environmental protection throughout the world[145].

[144] P. Khanna (2011) *Come si governa il mondo,* p. 300.

[145] J. Bhagwati (2005) *Elogio della globalizzazione,* p. 205.

4. STATES AND MULTINATIONAL ENTERPRISES: THE RELATIONSHIP BETWEEN THESE TWO ACTORS

4.1 The state in a globalized economy

According to the visions of hyper-globalists and of other tenacious supporters of globalization, the world in which we live today is characterized by the absence, or irrelevance, of borders. Under this point of view, the state no longer represents the main and more meaningful actor in the international context; rather, it becomes politically irrelevant, losing also its economic power. What happens is a shift, a transfer of power from nation states to multinational corporations, which have gained influence and authority especially thanks to the developments taking place in the fields of information technologies, communications and transportation. In this sense, "the multinational corporation not only premises the most efficient use of the world resources, but as an institution it poses the greatest challenge to the power of a nation-state[146]". Globalization is believed to operate a process of de-nationalization, internationalizing the financial and natural resources of a nation state, and simultaneously creating a relation of interdependence between states, multinational enterprises and international organizations. This decreases the autonomy of states, weakening their will to use their political and economic power to act in the national and international arena. These elements pushed some scholars to speak of the "end of the state", a situation in which nation states, due to the increase of the issues that spill over national boundaries and require international attention, are detracted of the possibility of making decisions. Therefore, this is transferred to the international level, but also to local levels of governments, since big cities are becoming increasingly important and persistently demand their participation in decision-making processes.

[146] J. N. Behrman (1975) *Control of the Multinational Enterprise: Why? What? Who? And How?,* in P. M. Boarman and H. Schollhammer: *Multinational Corporations and Governments: Business Government Relations in an International Context.* New York: Praeyer Publishers, p. 33.

Some academics think that the state is becoming an obsolete institution, for others it is adapting to globalization, but cannot play an active role in it.

According to the study conducted by Genschel and Zangl (2009), there are three distinct modes in which a state can denationalize its prerogatives: internationalization, privatization and transnationalization[147]. Through a process of internationalization, the power and authority of the state are shifted to international actors, namely institutions found at the supranational level, such as the European Union. As a consequence, these actors become more powerful and active in a wider range of fields, that were before believed to be of exclusively national competence. Privatization instead takes place when the power is moved to private actors, namely non-state players, whose field of action is confined to the territory of the state, like associations and private enterprises. The areas in which these actors can operate have been increasing, and their organizational power can be exerted more broadly. As a consequence the state is no longer capable of controlling how and by whom certain assignments are carried out. Finally, the process of transnationalization consists in the transfer of power from the state to those private organizations and businesses that act crossing national boundaries, for instance multinational enterprises. In recent times they have notably increased their authority, and expanded the fields in which this authority is employed.

In other words, the state seems to be an entity whose power and authority have faded away in favour of new actors. But is it really so? Have nation states really stopped being a major player in international relations? There is evidence that the capacities and competences of the states are sometimes reduced, but many scholars oppose the idea that this process encompasses all the sectors in which the states can operate. The current situation is more complex than it is usually described in articles and books, simply stating that globalization has made the existence of the state insignificant and even unnecessary. In the view of many scholars, all these developments do not take away the fact that states still represent a very important actor, the key protagonist in the national as well as in the international context. States still exert their influence at the moment of shaping the global economy, and they are

[147] P. Genschel, B. Zangl (2009) *Transformations of the State - from Monopolist to Manager of Political Authority.* Paper presented at the ISA Annual Convention 2009, New York, p. 3.

essential for the economic development of countries. When they act and cooperate internationally, they exercise their state sovereignty; the creation of supranational organisms do not necessarily lead to the weakening of the state, instead, states can be reinforced by an international context that is more stable and secure, in which they can feel free and safe enough to expand their activities and exchanges. Besides, they remain important for implementing the decisions taken by international institutions. For decades governments have been responsible for building up that environment in which transnational actors operate, promulgating regulations and legislative measures that allow foreign firms to work within their own territories, and national firms to work in foreign countries[148]. The state still plays a decisive role at the moment of attracting private firms to enter certain markets and offering them incentives to do so; states promote welfare, they cooperate and come to agreements with other states. In the opinion of several scholars the prediction of the death of the nation state was truly exaggerated, and they see that the role of the nation, in the era of globalization, has actually become more important. In particular, the more powerful states can take advantage of globalization, and use it to expand their powers:

> "States actively construct globalization and use it to acquire greater power over their national economies. [...] The US and G-7's other dominant members design and establish the international trade agreements, organizations, and legislation that support and govern the trans-border investments, production networks, and market-penetration constitutive of contemporary economic globalization. Advanced capitalist states use these political instruments to shape international economic decision-making and policy in their interests[149]".

Considering all these different aspects, what we can see is that the state, as a domestic and global actor is not disappearing, and its importance is not vanishing. Rather, we can say that its roles have been changing, shifting from being a "monopolist of authority", representing the only legitimate power that can exercise authority, to a

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[148] S. Sassen (2003) *Globalization or denationalization?* in *Review of International Political Economy,* pp. 7-8.

[149] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 174.

"manager of authority"[150], in which it acts as a coordinator and as the entity allowing other actors to take part in the exercise of authority. According to the words of Khanna, "this isn't to say that the states have disappeared, or will. But they are becoming just one form of governance among many[151]". In a possible future world of the year 2030, envisaged by the National Intelligence Council in its Global Trends Report, it is said that in the next years we will witness a shift in power, that, especially thanks to the developments occurring in communication technologies, will move from nation states to a variegated network consisting of state and non-state actors[152]. In this time of globalization in which we live today and which will probably characterized our future, the states that will become more solid and powerful are the ones which will be able to take advantage of the activities of the private sectors, instead of excessively control or suppress them[153]. Alongside this chapter, we are going to see which are these other non-state actors, in particular focusing our attention on the relationship between states and multinational enterprises.

4.1.1 Key roles of nation states

As we have said, the role played by nation states has changed, but not to the extent of undermining its importance and its basic functions. Dicken (2007) identified four main roles in which states remain unchallenged[154], we report them below:

- States as containers of peculiar cultural features;
- States as regulators of economic activity;
- States as competitors with one another;

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[150] P. Genschel, B. Zangl (2009) *Transformations of the State - from Monopolist to Manager of Political Authority*, p. 20.

[151] P. Khanna, New York Times, October 12, 2013: <http://www.nytimes.com/2013/10/13/opinion/sunday/the-end-of-the-nation-state.html?_r=0>.

[152] National Intelligence Council (2012) *Global Trends 2030: Alternative Worlds,* p. 18.

[153] P. Khanna (2011) *Come si governa il mondo,* p. 60.

[154] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 175.

- States as collaborators with one another.

The first category identifies the role of the state as the depositary of all those cultural features and economic practices that make every state peculiar and different from the others. Of course, these characteristics are not invariable and can be modified by the contact with other cultures; nowadays this is particularly true if we think of the great possibilities of information made accessible thanks to the internet. However, the increased permeability of states does not necessarily have to lead to changes in the peculiar domestic "ways of doing things". In fact, there is a great deal of evidence showing that the distinctive features of a state are quite well established and deep-rooted in national structures and practices[155].

Additionally, Dicken asserted that the persistence of characteristic national features can be observed also concerning the conceptualization that each state has of the way in which the economic activity should be carried out. Therefore, a state embracing one kind of capitalism will very probably abide by its characteristics, and it will hardly change its mind and decide to belong to another type of capitalism. The author identified three main models of capitalism: in the neo-liberal variety, the mechanisms that are in use to manage the market are the same that are utilized also for nearly all the other aspects of the economy; the main purpose is the maximization of profits to enrich the investors. A state that typically embraces this capitalism are the United States. The second kind is social market capitalism, where collaboration between different actors is considered important, and where social aspects are also taken into consideration in the management of the economy; examples of this variety are Germany and Scandinavian countries. Finally, in countries such as Japan, we find developmental capitalism, in which the state possesses an increased and independent political power and it intervenes frequently in the regulation of the economy, actually paving the way towards the developmental objectives for its industries and citizens[156].

As a consequence of what we have said above, we can deduce that states, as regulators of the economic activity, can apply different strategies and adopt different

[155] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 176.

[156] Ivi, p. 178.

measures to regulate and control the dynamics of what takes place within their boundaries. The state not only intervenes in the economy as an external actor, but it actually represents the most important contributor to the foundation and constitution of the economy, providing the policies and physical and human structures within which the economy will work. In fact, states are responsible for the provisions of roads, railways, airports, of laws and regulations, and of educated workers as well[157]. They play a fundamental role also for what concerns the management of the policies connected to inward or outward foreign direct investments, but this is a topic that we will discuss in more detail further on.

We pass now to the point of view that presents the states as competitors with other states. According to this vision, these actors take part in an economic race to increase their share of the global economic power. This implies being engaged in a competition to improve their positions for what concerns trade, and also foreign direct investments. They compete in order to be the most attractive locations for these investments, since, very frequently, they do represent a concrete opportunity to enhance national productivity. Increasingly often states take part in what has been called "locational tournaments": they consist in contentions in which states boast of their favourable characteristics and try to seduce potential investors in order to be able to attract a bigger slice of foreign direct investments[158].

According to Dunning and Lundan (2008), the best way through which a country can result more attractive for foreign firms is by making the most of its Location-specific advantages[159], because the propensity of a firm to invest in one country and not in another can be affected by several factors: the endowment and availability of factors, the education and training of labour force, the degree to which domestic policies and regulations reflect the needs of the investor[160]. In literature we find

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[157] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* pp. 179-180.

[158] Ivi, pp. 184-185.

[159] See OLI Paradigm, Chapter 2, pp. 24-25.

[160] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 323.

manifold models that try to characterize which are the most favourable and distinctive features on which a state can count at the moment of attracting foreign direct investments. One of them is provided by Koopmans and Montias, as reported by Dunning and Lundan. They invented the model known as environment/systems/policy paradigm (ESP paradigm). They categorized states according to these three variables, where the factor environment includes the endowment and availability of resources, and the intangible assets; system encompasses the usual way in which a particular country organizes and manages its economic activities; and finally policy, which refers to the measures, laws and regulations adopted, and to the institutions created by a state in order to reach its objectives of government[161]. The framework created by Michael Porter in 1990 and explained in his book *The Competitive Advantage of Nations* is probably better-known. The scholar supported the idea that the set of competitive advantages that delineates a firm located in a particular country is determined by certain specific features that are characteristic of that country only and that have been created through a process that cannot be reproduced anywhere else because its developments and results are deeply rooted in the local environment. Therefore, according to this model, the competitiveness of firms is strongly linked to geographical and environmental peculiarities that are not reproducible. Porter identified four main determinants of the competitive advantages of a country[162]:

- Factors conditions, consisting in a mixture of natural resources and created factors, such as physical infrastructure, as well as the degree of skills and knowledge of workers, and the availability of financial capitals.
- Demand conditions, namely the level, composition and quality of the home country demand. Also the size and the level of internationalization of the national demand are considered important.

[161] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* pp. 323-324.

[162] A. Vanolo (2006) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 88

- The presence, on the national territory, of related and supporting industries with which to establish close working relationships.
- The structure and strategies of domestic firms, and the degree of rivalry among them. This encompasses how workers behave with regard to their employers, how firms behave with regards to authority and in the relationships with other firms. Porter highlighted that a high degree of rivalry is usually representative of a consistent and constant push towards innovation.

To these four determinants the author added also the role and the influence that the national government can exercise, and the role played by chance. The model of Porter is well-known as the "diamond" of competitive advantages because he saw all these four attributes as interacting and interconnected with each other, a system in which all of them can be reciprocally reinforced. Porter prospected the co-evolution of firms and the environment, a situation in which the processes for the creation of value and of competitiveness are highly specific and localized, linked to cultural and institutional conditions[163].

Finally, the last of Dicken's viewpoints is the one according to which states are collaborators with other states. This is a widely accepted view, and it sees states collaborating in order to reach their economic objectives. This collaboration among states is particularly evident when they decide to build up political and economic relationships with other countries, therefore engaging in regional integrations agreements[164]. As we said in the previous chapter, the feature of regionalism has been characterizing, and still distinguishes, the world in which we live. Regional areas are created with the aim of abolishing, or at least reducing, the barriers to trade and investments in order to facilitate commercial exchanges. They are particularly important under an economic point of view because they exercise a great influence over the flows of foreign direct investments made by multinational firms. What we did not do before was to describe the different kinds of regional integration that can be

[163] A. Vanolo (2006) *Geografia economica del sistema-mondo: territori e reti nello scenario globale,* p. 88.

[164] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy*, p. 187.

established among countries, so we are going to briefly do it now. We can make a distinction among four main typologies of agreements, characterized by an increasing degree of economic and political integration:

- Free trade areas, which involve the abolishment of barriers among the states that take part in it.
- Custom unions, in which, beyond the establishment of a free trade area, there is also the creation of a common trade policy that member states have to apply towards non-members.
- Common markets, which encompass the features of free trade areas and custom unions, and additionally they allow the free circulation of the factors of production, namely capital and labour.
- Economic unions, which represent the highest possible form of regional economic integration, are agreements in which states accept the abolishment of their internal barriers, the creation of an external common policy, the free circulation of the factors of production and, besides, they also accept the coordination and harmonization of their economic, fiscal and monetary policies, and the shift of their control to a supranational level.

In this section we wanted to highlight how the importance of the state as a major actor in the global economic scenario has continued to be significant, keeping its considerable role as a container of peculiar cultural features, as a regulator of the economic activity, as a competitor and a collaborator. We have also underlined, however, that this fact does not mean that the role and functions of states have remained the same. Quite the opposite, the state had to adapt to a new international system in which it no longer has the sole power and authority to regulate the economy and other aspects of everyday life. It has become one of several other actors, such as multinational firms, with which it has to share the coordination of policies.

4.2 Relationships between states and multinational enterprises

As we have seen so far, nation states, in their transition process from the unique legitimate authority holders to one, among many, of the global economic actors, have increasingly had to intensify the relationships with multinational firms. These relationships have never been, and probably will never be, particularly easy and untroubled. Globalization has led to an increased interdependence between these two actors, but not always to a harmonization of their objectives. While sometimes they show common interests and so their aims may be in harmony and correspond, when, for instance, they work together to react to the challenges that globalization can pose[165], when they want to develop local resources and capabilities and they collaborate to open new markets; some other times instead they have also potential fields in which their interests diverge, paving the way to possible conflicting confrontations. On the one hand, multinational firms try to obtain policy concessions from the states and they seek to influence the state's policy making process in their favour; they also try to take advantage of the differences that are present at the national level in the creation and management of domestic measures and regulations; on the other hand, states try to limit such an arbitrary choice, seeking simultaneously to maximize their national objectives.

Consequently, we arrive to a situation which is characterized by a difficult and complex interrelation between these two actors, who use their power to try to further their own respective causes. The result has been described as a triad of relationships or as a triangular nexus of interactions between firms and states, which encompasses relationships between states, relationships between firms, and relationships between states and firms. Therefore, "the new geo-economy is essentially being structured and restructured not simply by the actions of either firms or states alone but also by complex, dynamic interactions between these two sets of institutions[166]". This new diplomacy needs to consider that, while in the past the only competitor that a state could have was another state, nowadays the situation has changed and also non-state

[165] C. M. Dent (2003) *Transnational Capital, the State and Foreign Economic Policy: Singapore, South Korea and Taiwan*, , in *Review of International Political Economy*, vol. 10, n° 2.

[166] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy*, p. 19.

actors such as the multinational firms can represent a contender: they can interfere in trades and investments using their power to manipulate home and host countries. Consequently, these three factors have to be taken into account when analyzing the current situation: bargaining happens between states to increase their power and influence, contention among multinational enterprises takes place when they try to increase their share of the global economic market, and finally negotiations between states and multinational firms are inevitable for the creation or control of the resources capable of increasing their respective wealth, since in today's world they share economic and political interests.

This growing interdependence somehow obliges both actors to behave with respect of each other, also considering the fact that, for certain issues, they respectively need each other. States need multinationals because they represent possible conveyors of wealth, supplying jobs for the citizens and increasing national productivity. If we look the other way round, multinational firms feel the necessity of states because of the services they provide, such as infrastructures and educational institutions able to form skilled and qualified workers. In the perspective of the OLI paradigm, studied earlier in this dissertation, the relationships and interactions between these two parties are likely to be dependent upon the relations that are established between the Location-specific assets of the country and the Ownership-specific assets of the multinational firm: the more the L-specific conditions reflect the requirements of the firm to exploit at the maximum level its O-specific assets, the more the relationship between the country and the firm is going to be intense and filled with negotiations.

In the study of the interconnections and games of power between these two parties, very often the size and profits of nations and multinationals have been compared. Sentences like the following can be found often: "Of the 100 largest economies in the world, 51 are corporations; only 49 are countries (based on a comparison of corporate sales and country GDPs)[167]"; or even "The 1999 sales of each of the top 5 corporations (General Motors, Wal-Mart, Exxon Mobil, Ford Motor, and

[167] UNESCO (2010) *Corporate Power Facts and Stats*. Available at <http://www.unesco.org/education/tlsf/mods/theme_c/popups/mod18t04s01.html>.

DaimlerChrysler) are bigger than the GDP's of 182 countries[168]". Put this way, these statistics are quite outstanding, but they are misleading as well. In fact, as it was highlighted by several scholars, the two values (a nation's GDP and a multinational's sales) cannot be directly compared. Indeed, the first is a measure of valued added, a sum of all the values added of the activities of a country, while the second is a measure of sales, considering gross prices. The two academics that were the first to observe this discrepancy, namely Paul De Grauwe and Filip Camerman, were also the first who tried to correct these statistics, measuring the value added, and not the total sales, also for multinational firms. The result gave a very different picture of the situation, where the numbers that were earlier characterizing sales are reduced of a measure going from 70 to 80%[169]. The table below reports such corrections:

Table 4.1 Sales and value added (billion $) of the top 5 corporations in 2000.

Company	**Sales**	**Value added**	**Value added/sales (%)**
General Motors	184,632	42,175	22.8
Ford	170,064	46,802	27.5
DaimlerChrysler	162,384	44,438	27.4
Royal Dutch/Shell Group	149,146	36,294	24.3
British Petroleum	148,062	33,536	22.6

Source: P. De Grauwe, F. Camerman (2003) *Are Multinationals Really Bigger than Nations?*

Therefore, when the two measures are made truly comparable, it becomes evident that nations' economies are still considerably bigger than multinational corporations. Among the 50 largest economies, only two are multinational firms, and out of the first

[168] S. Anderson, J. Cavanagh (2000) *Top 200: The Rise of Corporate Global Power*. Available at <http://www.ips-dc.org/reports/top_200_the_rise_of_corporate_global_power>.

[169] P. De Grauwe, F. Camerman (2003) *Are Multinationals Really Bigger than Nations?,* in *World Economics,* vol. 4, n° 2, pp. 25-26.

100 economies, multinationals are only 37[170]. Nevertheless, it is undeniable that they still occupy a powerful and dominant position, but this does not justify the fear, resentment and aversion that is very often felt towards them in general, and in their relation with states.

In a superficial analysis of the relationship between multinational enterprises and states, it would seem clear that the former would try to abolish all the possible barriers and constraints of the latter towards their activity. They would like to be completely free in the choice of their location, in the measure of their exports, in the measure of their imports of components and intermediate goods and so on. Since states' regulations are seen to be obstacles in the activity of multinationals, it is widely believed that the latter would always overthrow or circumvent them. However, things are slightly more complicated than it is usually believed. Actually, since one of the multinationals' abilities is to switch their operations according to where the regimes for carrying out certain activities are more convenient, the national differences in the regulation of the economy can represent, in fact, true opportunities, and a way through which multinational firms can engage in what has been defined as regulatory arbitrage[171]. Multinationals, putting states one against the other in the effort to attract their activity, stimulate competitive bidding and bargaining power.

4.2.1 Bargaining process, competitive bidding and locational tournaments

As we have observed so far, the relationship between transnational firms and states is very complex, intricate and ambiguous. Ultimately, it is based on the relative bargaining power of the two parties, that is to say the degree to which each of them is able to apply the strategies and policies that are more convenient to them. Considered the possibility of multinationals to move in and out of countries quite easily, it follows that, exploiting this locational mobility, their degree of bargaining power is likely to be high. The concerns for countries are many, and they include the fear that multinationals would relocate their activity where it is more convenient, and the fear

[170] P. De Grauwe, F. Camerman (2003) *Are Multinationals Really Bigger than Nations?,* p. 26.

[171] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 235.

that they might maintain in the state's territory only the operations implying low-skill and low-technology levels[172].

In the model proposed by Vernon in his thesis called "Sovereignty at bay"[173], he stated that the bargaining power is totally on the side of the multinationals. In fact, there is hardly anything that states can do to contrast the great flexibility and mobility of multinational firms, because they lack enough domestic resources and technological capabilities and enough developed entrepreneurial capacity to be able to free themselves from multinational activity and count only on their national production. However, nowadays this thesis cannot be considered valid anymore, because states own a certain degree of bargaining power, making the bargaining process a very complex phenomenon, highly dependent on each specific situation. Generally speaking, the multinational firm holds a considerable power when its activities and its contribution to the host economy are considered fundamental by states; conversely, the position of states is likely to be preponderant when they are able to offer a unique set of resources, technological assets and market volume to the multinational enterprise, and especially when they are able to obtain the same contribution of a multinational anyway, even if from other sources[174]. When a multinational firm is looking for resources and assets that are present and abundantly available in a number of different locations, they hold more bargaining force, and they have the power and the possibility to take the final decision, engaging in an active embeddedness[175]. Instead, when the resources or assets they want to have access to are highly localized in certain areas and/or are strongly controlled by the state, the latter would have the power to impose the rules of the game. In this case the multinational firm would be the one who needs to adapt and abide by the terms imposed by the state, engaging in a obligated embeddedness. Two different requirements have to be present in this

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[172] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 236.

[173] R. Vernon (1971) *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises,* , in *International Business Review,* vol. 13, n° 4.

[174] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* pp. 670-671.

[175] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 240.

case: the existence of assets considered essential for a multinational firm in order to be able to achieve its business objectives and the fact that these assets are strongly localized; second, the fact that a state determines the access to and exercises its control over such assets[176]. Additionally, both actors can exercise their power to impose their respective maximum restriction: while for multinationals it is represented by non investing in a particular location, for countries the ultimate restriction consists in completely forbidding a particular inbound foreign investment[177]. Given these general considerations, then, anyway, it seems obvious that the real outcomes of a bargaining process will largely depend on the abilities of negotiation of both the nation state and the multinational firm. These abilities are likely to vary according to the degree of knowledge that each of the two parties has of the other actor's possible options.

When the bargaining power is mostly in the hands of the multinational firm, the price that a state is disposed to pay to attract a new investment or to maintain an existing one will depend upon these factors[178]:

- How many foreign enterprises are struggling for that particular opportunity of investment;
- How important and unique will be the contribution of the foreign investment for the national economy;
- How much deep is perceived to be the need for that particular foreign contribution.

Depending on these considerations, states with similar situations and sharing similar sets of assets are likely to engage in locational tournaments and competitive bidding against each other, putting on the table increasingly large incentives in the effort to attract the foreign investment: a process that, in the end, is going to weaken their bargaining power. Competitive bidding is a phenomenon on the rise, in fact in recent

[176] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 240.

[177] Ivi, p. 242.

[178] Ivi, p. 241.

years it has seen a considerable intensification. The more states are involved in this process, the more multinational firms will improve their bargaining positions, because they can play off one state against the other and therefore they are likely to obtain those conditions thanks to which their investment can be more profitable. Besides, multinationals, to further even more their power, have tried, often successfully, to lever on threats of leaving the state's territory or of reducing their investments to reach even more favourable conditions.

On the other hand, when governments exercise more bargaining power than the multinational firms, the decision of the latter on whether or not to accept the terms and conditions of the states is based on these considerations[179]:

- How much deep is the need of the firm for an investment outlet;
- How attractive is the specific investment opportunity offered by that particular state when compared to other investment possibilities in other states;
- How important was the degree of previously existing commitment of the firm to the state and its market.

We need to remember, anyway, that the bargaining process is dynamic, and the bargaining power of both states and multinationals might change over time. One theory suggested that, after a multinational firm gains access to a host country and to its market, its bargaining power would start to obsolesce, increasing the relative bargaining power of the country. This happens because the ownership-specific assets of the firm would start to erode, and technology, knowledge and managerial skills that were before only available for the firm, spread and become more commonly available in the host market due to competition or involuntary leakages[180]. This theory, however, has not proved to be completely true, especially for those cases in which the transfer and integration of skills and capabilities take place customarily. In conclusion, contrary to what is usually believed, states do not represent always the weakest part in the bargaining process, and the bargaining power of each actor does not remain

[179] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy,* p. 241.

[180] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 672.

always unchanged. Besides, the bargaining condition of states is likely to improve when states collaborate with each other, applying consistent policies towards multinationals that, in the end, would probably surrender to such terms.

4.2.2 The evolution of the relationship between states and multinational firms

In the course of time the relationship between countries and multinational firms has not remained unchanged. It underwent periods of strong disharmony, and periods when, instead, their similar priorities made various forms of collaboration possible. Their connection and interdependence should always be studied bearing in mind that they take place in the context of the world's economy and politics, which are characterized, as we all know, by a certain degree of volatility. It naturally follows that, with the changing economic and political conditions, a unique and perfect set of rules and behaviours to adopt in order to make the relationship work at its best, cannot exist. Policies that worked in the past might not work presently, and measures that did good for a particular country in attracting foreign investments or in spurring domestic activity towards outward investments might not be suitable for other countries, even at the same time. There is not something that can be considered valid for all countries at all time.

Helped by the work of Dunning and Lundan (2008) we are now going to see how the relationship between these two parties has developed in the last 50 years. Actions taken by the states concerning the activity of multinational firms have been related to the perceived degree of contribution that the latter can make in helping the state reach the economic goals that it has set. The range of policies adopted throughout these years has gone from a total *laissez-faire* to the total prohibition of inward investments; however, nowadays, none of these extreme attitudes are still applied by states[181]. Since states differ in their needs and in their resource availability, the behaviours that they adopt will vary accordingly: while they can allow liberal policies for certain issues, they can apply restrictive measures for other areas. Starting from the 1950s, Dunning and Lundan identified three main and quite different periods in the

[181] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 674.

interactions between multinational firms and states: the first phase, going from the 1950s to the middle of the 1960s was called the "honeymoon phase"; the second period, lasting from half of the 1960s to the late 1970s was referred to as the "confrontation phase"; and finally, starting from the late 1970s to the present days goes the period known with the name "reconciliation phase"[182].

As it can be easily deducted from the name, the first period under examination represented a phase in which the relationships between the two parties were basically positive and prolific. This is particularly due to the fact that many countries, as they were exiting the war considerably weakened and ravaged, looked favourably upon the resources, capital, technology and managerial skills that the multinational enterprises could bring to these countries thanks to their investments. In this period American multinationals were exercising their technological dominance, and foreign investments were seen as a way through which to find new markets abroad and to discover new resources to increase domestic production and satisfy domestic demand. In this period in fact, multinational firms were still quite small, and their affiliates abroad were functioning as almost independent units[183].

As we pass to study the second period, we see that things start to change consistently in the direction of a deterioration of the relations. This was a phase characterized by the fact that many developing countries became increasingly independent and they started trusting in themselves in their path towards the achievement of their developmental objectives, such as an increase in their technological and managerial capabilities and an improvement in the conditions of local producers. Therefore, the activities of the multinationals began to be evaluated in these terms, and the result was that it was discovered that inward investments did not always lead to the best possible outcome for host countries. Multinationals started to be seen as the conveyors of a way of life that was not appreciated, as an obstacle to the creation and entry into the market of new local firms, an enemy for already existing indigenous enterprises that, at best, cannot develop and compete, at worst,

[182] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 675.

[183] Ibidem.

are driven out of the market. They were perceived as powerful players whose interests needed to be fulfilled even at the expenses of the host country, with which they were believed to share a minimum part of their rents[184]. These were years in which the environment for international business became harsher: the dollar was devaluated, the oil shocks caused by the huge increase in the price of oil by OPEC took place, and developing nations were exacerbated by the fact that international institutions and developed countries did not want to help them reduce their debit. This led to a deep fracture between developed and developing nations, and consequently multinational firms coming from the former were increasingly under attack since they were seen as the main manifestation of an international economic system that started to be felt as unacceptable[185]. From this moment on host countries began to take very restrictive measure concerning the inward investments, starting from the complete expropriation of the foreign assets of multinationals, to tougher limitations to the size and direction of the investments, to generous assistance towards domestic firms in order to help them compete more efficiently in the markets[186]. We do not have to wait for long to see the reaction of the multinational firms: where their activity was already well-established and functioning they were able to face the additional costs posed by the new host policies and they continued the production; however, very often they limited their involvement to the degree of the investments that they had already made, without investing any new capital. In other cases they menaced host countries to move their production elsewhere, in an attempt to convince them to mitigate their positions. Frequently, the result was that host nations felt even more outraged, and they applied even stricter policies or sought help in regional unions or in the international organizations for advices on how to best exploit inward investments[187].

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[184] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 676.

[185] Ivi, p. 677.

[186] Ibidem.

[187] Ibidem.

Finally, in the period of reconciliation, things started to work out better. Multinational firms became more aware of the fact that their activities did not always lead to the best possible outcomes for host countries, concerning their social and cultural situation. Therefore, they started to provide a more profound and more sensitive education and training to their managers, and subsidiaries abroad tried to establish more durable and reciprocally beneficial relationships with host countries and host countries' firms, abandoning the objective of gaining the maximum benefits in as shorter a term as possible[188]. Simultaneously in these years, knowing the effects that multinationals could have, the creation of more pertinent and properly-working institutions and organization took place. They committed themselves in the introduction of more precise and stricter rules and codes of conduct that multinationals should follow. All these facts happened in a period that, politically speaking, was characterized by a switch towards more right wing national administrations, that were evidently more favourable to the adoption of market-oriented policies[189]. The 1980s and 1990s represented a period in which the interdependence between multinational firms and nations became more intense and intricate; in this relationship each of the two parties knew quite well the benefits and contribution that the other could make in helping it reach its goals, but they also knew at which costs[190]. This learning process acted as an aid in the moulding of new attitudes of national authorities concerning foreign direct investments, moving in the direction of a more relaxed and opener position. Countries increasingly saw multinationals in a good light, perceiving them as a way through which, the right conditions provided, they could develop their institutions and improve the competitiveness of their resources. According to data made available by UNCTAD in 2005, in a study of the changes of the regulations concerning FDI that took place between 1991 and 2004, it was observed that the great majority (87%) of these

[188] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 678.

[189] Ibidem.

[190] Ivi, p. 679.

transformations went in the direction of making the investment environment more congenial[191].

However, this was also the period in which nation states started to give more importance to social issues, such as environmental protection and security. Such priorities are likely to determine additional costs to the multinational firm and its affiliates. Therefore, the more these non-economic factors influence the strategies of governments, the more conflicts and disagreement with multinational firms might arise. This fact has to help us remember that even though today we can speak of an international environment which is generally favourable to international investments, nonetheless there are instances in which the interests of the two actors diverge, and therefore possible areas of conflict still remain.

Nowadays we can say that the investment regime is still characterized by the same reconciliation atmosphere what was typical of the previous decades. However, one of its typical features in the 21st century is the presence of a discrepancy between developing and developed nations. The former are the ones more in need of the benefits, such as technology transfers and knowledge and capabilities spillovers, that can be brought by the multinationals' investments. Still, they are also the ones that display those features that will hardly attract such investments. In fact, as we already reported in chapter 3, developing countries are more likely to be characterized by an unstable political regime, where rules, regulations, institutions are barely respected, and where high levels of corruption and the non-protection of the norms of property very probably act as a disincentive for inward investments. On the other hand, a good governance, a deep respect of rules and of institutions and low levels of corruption seem to be necessary requirements for attracting foreign investments. For what concerns developed nations, their intrinsic characteristics make it quite easy for them to be able to draw investments; however, they need to face different consequent concerns. For instance, they need to deal with the uncertainty that stems from the fact that part of the production that was once considered national, now belongs to foreign hands. Additionally, governments of developed countries have also to develop plans

[191] UNCTAD (2005) *World Investment Report 2005: Transnational Corporations and the Internationalization of R&D*.

and projects in order to upgrade their national firms, their resources and capabilities to enable them to possess and manage standards high enough to compete and enter successfully in the networks of multinational firms[192].

In order to face these concerns and these obstacles in the attraction and management of foreign investment, there is a quite vast set of policies that host governments can adopt. We are going to study them in the next section.

4.3 States' regulations: policies directed to affect inward investments

Governments can take important measures in the regulation of both outward and inward investment activities. The majority of the policies concerns the attraction of inbound investments, and this is the kind of measures that we are going to study in this section. However, states also engage in policies for the administration of outbound investments: often they pose restrictions on the export of capital, since this type of investment is still largely associated with the export of jobs and technology, and they force multinationals to pass through an approval process before their investments are actually allowed.

From the point of view of governments, it is very important to make the most of inward investments, while simultaneously minimizing their costs or negative impacts on the domestic economy. While several distinct levels of openness might exist towards inward investments, today we can say that only very few nations execute completely closed policies. The degree of openness can vary considerably also according to the level of development of the country: on the one hand, more developed countries have always tended to apply more liberal policies, while developing governments preferred to adopt a more cautious behaviour, opting for more restrictive stances. However, at the broadest level, generally speaking in the last two decades there has been a trend converging towards liberalization[193]. The increasing convergence of national policies has pushed governments to offer fiscal and

[192] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 679.

[193] P. Dicken (2007) *Global Shift: mapping the changing contours of the world economy*, p. 182.

non-fiscal incentives and to apply more and more streamlined measures to abolish administrative constraints to the economic activity. With regard to inward investments, the policies that states can apply have been divided into four main categories[194]: first, the conditions of entry into the market; second, the performance requirements that have to be adopted while the multinational firm is already active in the host economy; third, the conditions for the exit from the national market for foreign investors; and lastly the fourth category which includes all the previous three and additionally it tries to implement all the policies and institutions to attract inward investments.

4.3.1 Market entry conditions

This first category encompasses a broad range of requirements that foreign multinational firms need to respect to be allowed to access a national market, and it includes also a series of pre-entry conditions for the inward direct investment. Governments operate a screening of all the investment offers and then, with these conditions, the first action they take is to determine the level of control that foreign multinationals can have over domestic firms. Rarely a 100% foreign ownership is allowed. Besides, through these conditions it is also usually established which are the national sectors and activities in which the foreign multinationals can participate. Even countries adopting quite liberal policies have always been unwilling to enable foreign firms to take part in those sectors considered culturally or strategically delicate[195]. Additionally, the presence of foreign multinationals has been seen under a bad light when the kind of products or services they provide are perceived to be harmful or undesirable. Entry conditions also dispose how the initial inward investment should be financed: it is probable that developing countries with financial deficiency would prompt multinationals to take charge of the total initial capital investment. As for the locations, national governments are likely to do their best to convince the foreign firms to direct the investment in those areas that are less developed or where the rate of

[194] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 681.

[195] Ivi, p. 682.

unemployment is higher[196]. Finally, this first category encompasses also the different kinds of incentives that countries can offer to attract inbound investments. These include fiscal incentives, such as tax reductions, and reduced rates in the contributions for social security, financial incentives and other general incentives, for instance protection from import competition, subsidised infrastructures and services[197]. As we already saw before, the boasting of the more advantageous features by different countries has led to the creation, and nowadays increasingly frequent presence, of the so-called "locational tournaments".

4.3.2 Performance requirements

The second category includes those that are called performance (or operating) requirements: they are applied on the behaviour of the foreign firm in the host territory, and demand to the foreign investors to meet certain specific objectives while carrying out their operations. According to UNCTAD, there are several reasons why governments try to impose performance requirements: they do so with the aim of generating new opportunities of employment, of promoting development at a regional level, of benefiting from technology transfers, and of fostering linkages[198]. These requirements are usually applied in the areas of training, of the transfer of technology, of exports, of local research and development. Examples of these requirements are: the need to involve, by hiring and training, local personnel, in particular in managerial positions, the insistence on purchasing locally raw materials, intermediate goods and services, the demand of a minimum degree of exports, restrictions on where to locate the foreign establishments, and other requirements linked to the transfer of technology and to research and development. Sometimes countries have been trying to adopt these policies, offering to multinationals, in exchange, a preferential treatment, for instance providing to them the protection from foreign competition.

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[196] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 682.

[197] Ivi, pp. 683-684.

[198] UNCTAD (2003) *Foreign Direct Investment and Performance Requirements: New Evidence From Selected Countries.*

UNCTAD adopted a subdivision of the performance requirements into three categories: in the first class we find those requirements that have been explicitly prohibited by the WTO Agreement on Trade-Related Investment Measures (TRIMs), such as local content requirements and export controls; the second category encompasses those demands that are prohibited, conditioned or discouraged by International Investment Agreeements (IIAs) at a bilateral or regional (though not multilateral) level, for instance employment requirements and requirements linked to the location of the foreign activity in specific areas or regions; and finally all the other requirements that have not been restricted[199].

Performance requirements have been used almost indiscriminately by developing and developed countries. However, it is still not clear whether the adoption of these requirements have led to more positive or negative repercussions. According to some scholars, they have been effective, and represent a fundamental instrument in the hands of governments to exploit at the maximum level the potential benefits of inward investments. According to others, by using these requirements, governments have reached very poor results, and sometimes they only led to costly and counter-productive effects.

4.3.3 Exit conditions

This third category includes those requirements that imply the divestment of the foreign firm from the national territory. Nowadays they are not very common anymore, but governments made quite consistently use of them in past decades, especially in the 1960s and 1970s. This was particularly true especially for developing countries, which "viewed the role of inward investment as that of a tutor to indigenous firms and considered that as soon as the tutoring had been successfully accomplished, the tutor should gracefully withdraw[200]". These requirements are more likely to be

[199] UNCTAD (2003) *Foreign Direct Investment and Performance Requirements: New Evidence From Selected Countries*.

[200] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 686.

used when the Ownership-specific advantages of the multinational are easy to be moved and then absorbed by the host economy.

4.3.4 Reaching productive foreign direct investments

As we already said before this last category includes all the three previously mentioned groups, and, additionally, it is conceived to implement those policies and institutions as to create the general conditions thanks to which the potential benefits of the inbound investment are totally exploited. It represents the modalities through which all the policies adopted, the incentives given and the performance requirement demanded can work consistently with each other. Indeed, while governments were making offers and giving incentives to multinational firms in order to attract their investments, they engaged in policies that posed a burden on the shoulders of the public sector[201]. A country can consider its actions as completely positive and successful not when it achieves its goal of attracting foreign investments, but when these inward investments actually pay off their initial costs. It has been observed that in recent times almost all governments increasingly engage in the attraction of FDIs as one of the means through which the public policy is performed, but simultaneously it is rising also the perception among scholars that these policies have negative effects. In fact, they state that if the incentives and favourable policies were not applied, the overall benefits of the inbound investment for the host economy would have not been much less consistent. Therefore, what is really important in order to make all these aspects function consistently, is to give multinational firms a chance to become really integrated with the domestic economy, by offering them logical incentives, institutional quality and working infrastructures, education and the provision of precise information, thanks to which the multinational can take conscious choices[202]. In the absence of such conditions, the multinational firm is likely to be involved just superficially, and to remain on the alert and receptive to other incentives and offers coming from other locations.

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[201] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy*, p. 687.

[202] Ivi, p. 688.

As the regulators of the economic activity, states can adopt a vast set of measures that are very likely to influence the extent and quality of its economic operations within its territory and also across its boundaries. As we have just seen, the nature of the measures adopted can vary considerably according to which are the main objectives of the state and to which position it already occupies, or would like to occupy, in the economic system.

4.4 The increasing importance of multinational firms as political actors

All the aspects studied along this dissertation lead us to think of multinational firms as not only economic entities, but also as actors exercising some influence on the cultural and political spheres. Evidently, the main effects can be observed in business-related issues, such as managerial and organizational skills, work methods and so forth. However, in the long period, such issues are likely to have repercussions on wider aspects, influencing the (business) culture more generally: effects can stretch to the ethos of work, attitudes towards the authority, notions of respect, justice and correctness, and the role of the government[203]. Clearly these issues refer to the business regime in the first place, but then they apply also to the general cultural and political environment of the states. Rules and practices are transferred from the home-based headquarters to the foreign affiliates, which in turn apply them in their activities and in their relationships with domestic firms and with the national governments. The importance of the impacts that investments made by multinationals can have on the local culture becomes even more evident when we see that countries, also the more liberalist, decide to limit or exclude the possibility of accepting inbound FDIs in those sectors that are considered to be culturally delicate and sensitive.

Multinational firms have acted as the transmitters of new ways of life, of new rules of work and they have introduced new forms of respect and new institutions. According to some scholars, they have also played an important role as promoters of peace and stability at the international level. In fact, their activity has helped link

[203] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 647.

reciprocally the economic prosperity of different nations: the more a state's welfare is dependent upon the well-being of other nations, the more clashes and unfriendly behaviours are avoided. For having increased interdependence among nation states, multinational firms are also seen as institutions fostering security. At the international level, since we saw that multinationals usually seek locations that display a well-functioning and determined governance, where standards on the environment and labour regulations are high and respected, multinationals are likely to encourage the spread of correct measures and policies. Generally speaking, in the last decades there has been an advancement in the policies regulating the environment as well as the labour standards and working conditions. Multinationals have developed new and up-to-date technologies for reducing the pollution produced by their activity, and often they have prompted governments to make these environmental-friendly innovations compulsory. They do so for their own advantage, but the result is that higher standards are imposed and the issue of environmental protection becomes higher in the political agendas of both states and corporations. Besides, they have also given their contribution for the improvement of workers' conditions, first of all by offering opportunities of employment, then by paying higher salaries and especially by giving workers education and training, supplying them with knowledge and capabilities that would then be used even outside the multinational firm, partly contributing to the enhancement of the qualification of the domestic economy in general. Therefore, we can conclude by saying that "attacking MNEs as the source of environmental and social problems in many cases amounts to targeting the wrong enemy[204]". Multinationals need to care about the general environment in which they operate, and they are increasingly adopting the motto conceived by Moody-Stuart, managing director of Royal Dutch Shell, in 1991: "If it is a problem for society, it is a problem for business[205]". Following this principle, this multinational firm was the first energy company to combine together its financial and social reports, carrying on a process

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[204] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 656.

[205] International Institute for Sustainable Development, available at <http://www.iisd.org/pdf/2006/pr_bg_sir_mark_moody_stuart.pdf>.

that takes into consideration the impacts that the activity has on people, socially, environmentally and economically speaking. In 2009 Shell supplied the Nigerian government with 3 billion dollars to help it cover huge budgetary holes, and it also provided investments towards education, the building of new schools, the purchase of new course books, and programmes for the literacy of adults and for the formation of teachers[206]. Multinationals are now aware of the fact that their operative stability strongly depends on the well-being of local communities. When states are poor and weak, or corrupted, they are not able to manage properly their own national resources, and multinational firms have tried to do their best to substitute them and take charge of their responsibilities. Therefore, sometimes, multinationals prove themselves to be more reliable political actors than the governments in office, and in some countries, for instance in Bolivia, it is already a common habit to directly address the multinational firms to obtain those services and assistance that the government is unable to provide[207].

The importance of multinational firms as non-state political actors can be observed also considering another aspect. In recent years and more and more increasingly, they have been engaging in non-traditional partnerships and collaborations with NGOs. These two actors together have sometimes behaved as one sole personality in addressing the problems that governments were not able to face. When they act properly, they do not ignore the policies of foreign developing countries, nor do they try to subvert the situation according to their interests. Rather, they give them resources and try to make them adopt higher standards in order to put them on the right way towards development. When politicians such as the former South African president Thabo Mbeki denied not only the problem represented by, but even the mere existence of AIDS, a collaboration among domestic firms, foreign multinationals and NGOs took place to provide HIV tests directly on the work place[208]. In many circumstances multinational companies finally saw that NGOs do not

[206] P. Khanna (2011) *Come si governa il mondo,* pp. 221-222.

[207] Ivi, p. 224.

[208] Ivi, p. 252.

represent their natural enemies; conversely, they can be a good help to foster a good picture of the multinational, and consequently they can be useful for the balance sheet. When companies respect the standards imposed by the NGOs, the latter can help the former build a credibility among the local communities. More and more frequently multinationals voluntarily seek help in these organizations: in the sector of environmental protection, the World Business Council for Sustainable Development, which has more than 200 members, is consistently considered an important tool for firms, that address it for suggestions in the reduction of energy consumption and for custom-made advices[209]. An active partnership between multinationals and NGOs can be useful also when the latter is called to measure the overall impact that the former can have on the host country. If the multinational firm has a good behaviour, the continuous publications of reports by NGOs can help it reach a sufficient degree of transparency allowing it to be considered a correct and reliable actor not only economically but also socially and politically.

In recent years, in order to improve their public image and to underline their determined commitment to the respect of social and political issues, multinational companies have started to equipped themselves with codes of self-regulations, at an individual as well as collective level. One of the most famous voluntary initiatives is the UN Global Compact, a world agreement which was introduced in the World Economic Forum in Davos in 1999, and signed in 2000 by more than 50 multinational firms. It is formed by 10 principles which reflect the essential aspects of other fundamental declarations, such as the Universal Declaration of Human Rights, the ILO Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development and the UN Convention against Corruption[210]. By signing this pact, multinational firms commit themselves to follow, with practical actions, principles such as the respect of human rights, the abolition of child labour, the elimination of

[209] P. Khanna (2011) *Come si governa il mondo*, pp. 293-294.

[210] UN Global Compact, www.unglobalcompact.org.

discrimination in employment, the diffusion of environmentally friendly technologies and the struggle against corruption[211] .

It is in this context of deep commitment to the respect of social issues that multinational firms have decided to engage in what has been called corporate social responsibility (CSR), a concept consisting in associating social responsibility with big multinational enterprises: they take charge of the impacts they have on society. This process of self-regulation takes place mainly as the consequence of external pressure, particularly from NGOs and it sets its objectives just to the level in which these external demands are satisfied. However, sometimes multinationals engage in CSR activity because they really mean their social commitment, they want to be a step ahead of the regulations and also to preempt future measures. Studying this context of active engagement in social issues, very recently two scholars, Michael Porter and Mark Kramer, invented the concept of Creating Shared Value (CSV), which we are going to analyze in the next section.

4.4.1 Creating Shared Values – a new social approach

Creating Shared Value (CSV) is the idea developed by Porter which starts from the assumption that today capitalism is being considered an evil for society, and companies are believed to create profits at the expense of the community. As a result of this perception, governments have increasingly seen companies as a source of problems, often adopting the mindset according to which the right thing to do is to regulate, control and tax. Political leaders seem to be unable to pursue business-friendly public policies. In Porter's opinion, it is fundamental that we come to see that at a deep level, society and business do need each other, and that actually what is good for the society is also good for business. The idea of the creation of shared value implies "creating economic value in a way that *also* creates value for society by addressing its needs and challenges[212]". Capitalism needs to be reassessed as a way through which jobs can be created, wealth can be built and human and societal needs can be met.

[211] UN Global Compact, www.unglobalcompact.org.

[212] M. E. Porter, M. R. Kramer (2011) *Creating Shared Value*, in *Harvard Business Review,* p. 4.

Nowadays we are all very aware of the problems that afflict the world: poor nutrition, access to water, climate change, pollution, lack of skills and so on. Still, this awareness was not sufficient to put us on the right path to the their complete solution, in fact we still have much troubles in dealing with these issues. NGOs, governments and philanthropists are the actors who are usually associated with the process of handling of these social problems, but they are not making progress quickly enough because, according to Porter, they lack resources to be able to reach solutions on a large scale. And this is exactly where companies can make the difference: businesses create wealth when they meet needs out of profit, they are the only actor that can create resources, that can then be utilized by other parties. That profit created by businesses allowed the solutions to social problems to be put on a vast scale. The conventional wisdom sees the existence of an incompatibility between the social performance and the economic performance, accusing business of making profits by causing social problems. Typical examples are pollution and labour regulations: it is generally believed that if a firm pollutes, it makes more money, because reducing pollution is expensive; it is more profitable to have an unsafe working environment because making it safe would be excessively costly. Porter, instead, sees that the reality is exactly the opposite: businesses do not make profits by causing social problems, rather, they do so by solving them. As for pollution, he observes that, actually, reducing the emissions is generating profits for the companies, because it makes the business more productive and efficient, and it prevents the business from wasting resources. As for the working environment, making it safer and avoiding accidents makes the business more profitable because they represent signs of good processes. He recognizes that the damages or social problems that a firm causes to its environment will have a negative repercussion on the firm itself: the deterioration of the physical and social environment outside the company will make its business less competitive and less able to create value. The scholar has come to see that there is no trade-off between social development and economic efficiency; on the contrary, there is a deep synergy between these two aspects, especially if we think in long-run terms. Companies can operate in different levels of shared value: by meeting societal needs through products, by utilizing resources, suppliers and employees more productively and by improving the local business environment, building local supportive clusters.

The concept of shared value wants to be completely different from the simple idea of redistribution of profits: it is not "about sharing the value already created but it is about expanding the total pool of economic and social value[213]". It also considerably distances itself from the concept of corporate social responsibility, which implies programs that are just very partially linked to the scope of the business, and that consequently are hard to maintain and justify in the long period. While CSR is discretionary and usually takes place as the consequence of external pressures, a process in which companies place value in doing good, but this doing good is separate from profit maximization, in the concept of CSV businesses create societal benefits because this actually increases their profit maximization, therefore the two aspects are integrated: companies adopting the CSV concept need to figure out what their product is, and understand where it touches important social needs and problems. The classic example that Porter gives to explain this difference is considering fair trade. According to fair trade, the farmer, or the small vendor, does not receive enough high compensation for his products, while distribution channels and the marketing companies have far bigger shares. So, the concept of fair trade says that we need to give better prices to the farmers to help them have a living wage. This is also a typical CSR idea, in fact it is mostly about redistribution: there is a fix amount of wealth, and what companies have to do is just to share more of their wealth with the farmers, to have a fair behaviour. Instead, according to the idea of CSV, the real opportunity is to extend the amount of wealth and to create more value, where the farmer can be rewarded by participating in this creation of more value. Companies are understanding that if they train farmers better, improving growing techniques, if they give them access to fertilizers and better seeds, if they strengthen the local cluster of suppliers, farmers can become far more productive, the quality of their products can increase and therefore the price to be paid to them can be higher. This would benefit farmers as well as the companies that buy from them[214]. While the approach of CSR can increase the farmer income by 10-20%, the approach of CSV can increase it by 200-

[213] M. E. Porter, M. R. Kramer (2011) *Creating Shared Value,* in *Harvard Business Review,* p. 5.

[214] Ibidem.

300%[215], by creating economic value but also social value at the same time. CSV acts in the self-interest of the company, mobilizing the business itself, and not engaging in more or less random charitable giving.

In order to do so it is important to change the image that companies have of themselves. In fact, in Porter's view, many companies are still trapped in the conventional wisdom that they should not worry about social problems because they are being managed by other actors. But this is now changing. Besides, the author acknowledges that businesses can take this important step alone, but their action would be far more effective if they establish partnerships and collaborations with governments and NGOs. According to him, the NGOs that are really making a difference are the ones that have reached these collaborative relationships, and the governments that are making the best progresses are the ones that have found a way to enable share value in business, rather than seeing the government as the only player. If they can break down this tension, and this sense of divide that impedes them to fundamentally collaborate in addressing these social problems, all these actors together will finally be able to reach large scale solutions. NGOs and governments are the actors that would allow companies to rebuild their legitimacy in the eyes of the communities in which they act. The concept of shared value will enable them to use their skills, capabilities and resources to tackle those social issues that governments and social organizations alone do rarely solve.

[215] M. E. Porter, M. R. Kramer (2011) *Creating Shared Value,* in *Harvard Business Review,* p. 5.

CONCLUSIONS

Throughout this dissertation we have tried to find an answer to some crucial questions concerning the existence, the conduct and the effects of multinational enterprises. We focused on the development of foreign direct investments as the fundamental vectors through which the multinational activity is carried out, and thanks to which the economic integration at the international level has been reached. Through a brief history of the multinationals we were able to see that they do not represent just a recent or sudden phenomenon, but they have developed since remote times, going through more or less favourable periods, and remaining alive also when national barriers and constrictions seemed to be an insurmountable obstacle to the full integration of the markets. Important technological or organizational progresses, but also actions taken by governments, have been turning points in the development of multinational firms, putting to test their capabilities to manage operations in different and faraway areas. Nowadays they represent an irreplaceable actor in the process of globalization, whose products are present in our everyday life and whose conduct has increasingly become the object of research by scholars and academics. Therefore, as Dunning and Lundan put it, "the history of MNE activity is the story of a series of political, social and cultural events that have fashioned the ownership, organisation and location of international production[216]". The influential and preeminent position that they have come to occupy in the contemporary world can be seen as the consequence of their capabilities, efforts and eagerness to manage transnational production better than any other institution. The relevance of the multinational phenomenon is confirmed also by data provided by UNCTAD and OECD: latest reports show that in 2012 all the global foreign direct investments were worth 1.35 trillion dollars. Nowadays there are about 82000 multinational enterprises, with around 810000 foreign affiliates throughout the world. They create sales corresponding to 26

[216] J. H. Dunning, S. M. Lundan (2008) *Multinational Enterprises and the Global Economy,* p. 197.

trillion dollars, giving employment to 72 million workers, and being responsible for about one third of the global exports of goods and services.[217].

In this thesis we focused mainly on three aspects characterizing the phenomenon of the multinational enterprises: in the first part we studied this actor in a merely economic context, describing its principal features and providing an analysis of the already existing contributions made by several scholars in literature; the second part consisted in an examination of the economic impacts that the multinational activity can have on host countries and on domestic bases, and, broadening the field of study, also on the environment and on the policies directed towards its protection. Finally, our last concern was to identify the political role of the multinational firm as an important actor in international relations and as a significant player in the global governance.

More specifically, in the first part we underlined that, when we speak of multinational firms, we indicate a broad and general category, within which firms differ according to their size, their operational mechanisms, their business culture, and so on. There are differences in the motivations pushing them to start international production, and these very distinctions have prompted scholars to adopt not a single explanatory model including all the possible variables, but four distinct categories of investment explanations. We studied their modalities of entry into foreign host markets and we also saw which are the principal factors influencing such decision. Attention has been given also to the transnationality index, showing the perceived and real degree of territorial rootedness of firms. We observed that, while it is true that a widening of the productive locations has taken place, it is also undeniable that some activities, especially those more technology-intensive, have remained deeply rooted in multinationals' domestic bases. Knowledge, culture and level of technology can pose limits to the actual relocation of the activity of multinationals.

In the second part, as for the different kinds of effect that multinational firms can have on the host countries and on their home bases, we considered factors such as the

[217] UNCTAD (2013) *World Investment Report: Global Value Chains: Investment and Trade for Development.*

procurement of employment, possible spillovers, linkages and relationships with domestic firms, and effects on the quality and composition of jobs and wages. Even if the difficulty arising from the counterfactual problem makes it hard to reach a 100% certain evaluation, the overall sum of these effects showed that engaging in foreign direct investments can actually lead to positive repercussions for the host country as well as for the home base. Becoming a multinational firm is likely to represent a step towards increased productivity both in the case of a national firm becoming controlled by a foreign possessor, and in the case of a national firm becoming multinational and engaging in FDI. In fact, studies demonstrated that if investing abroad cannot always lead to an improvement in the firm's situation, at least it does never lead to a deterioration. Additionally, we investigated the effects that multinational activity can have on the environment: empirical data have discredited the theory of pollution havens and, rather, they demonstrated that multinational companies can actually play a fundamental role in developing new environment-friendly technologies and in exercising pressure to force governments to adapt their policies and regulation to the use of these technologies, *de facto* raising the general standards. Similarly, when we consider the field of human rights and labour rights, we noted that multinationals do not consider as ideal locations those places where these rights are violated on a regular basis and where practices of corruption and bad governance are particularly widespread. In fact, the possible benefits that the firm can gain thanks to lower levels in human and labour standards, do not pay off the risks and vulnerabilities associated with an investment made where poor regulations make the political situation very instable and subjected to episodes that stand outside the investor's control. However, the mere fact that a country possesses an environment safe enough as to be able to attract the multinational activity, does not represent a guarantee of economic development. Countries that make the most of the multinational presence are the ones that invest in the formation and training of their labour force and that engage in technological innovation and in research and development, creating a fertile ground which is able to absorb and productively use spillovers produced by the multinational firm. We want to stress this important conclusion: in the investor's point of view, the existence of institutions with the aim of protecting workers rights is even more important than the incentives that developing countries give in an attempt to increase

their attractiveness: where civil and labour rights are violated, then probably also the risks for the investors increase. Therefore, perhaps one of the unexpected effects of the economic globalization can be the expansion and strengthening of the democratic institutions.

In all these fields we have just mentioned, the data and empirical evidence provided contrast with what is usually believed by the conventional wisdom. In fact, for a long time the latter has strongly supported the view according to which the impacts generated by multinational firms are causing more harm than good in all aspects of the economy related to the host and home economies. Under this point of view, multinational enterprises have been accused of operating "extraction" activities, namely of exploiting and taking advantage of the resources (physical or human) that they need without really caring about the destiny of the territories in which they act. They have been blamed for not paying sufficiently high salaries to allow workers to live, for the reduced domestic activity in host nations and for driving local firms out of the market, for exporting workplaces from their countries of origin, and for causing too many environmental damages because of their highly polluting processes. To those who sustained the negativity and wickedness of foreign investments in poor developing countries, other scholars answered by saying that the only thing which is worse than a foreign investment is no foreign investment at all[218]. In this dissertation we provided evidence that these assumptions are often wrong and too frequently based on prejudices. Of course, throughout history there have been famous examples of unfair behaviours and violations of rights, and still nowadays there are multinational firms that do not care about rules and regulations. However, in today's world, with the tools at disposal of the media, the spread of internet and information, multinational firms pay far greater attention to their behaviours, since just one wrong action can destroy their reputations and cause considerable damages to their business. Therefore, we think that it is particularly important to distinguish between single cases and the general trend: often the latter has demonstrated that the benefits that can derive from the activity of multinationals generally outweigh the disadvantages, for host economies, countries of origin and for the environment. As a result, the most

[218] P. Khanna (2011) *Come si governa il mondo,* p. 208.

evident consideration to be done concerns the necessity of, if not attributing a completely positive judgement to the conduct of multinationals, at least of operating a completely new, clear and free of any prejudice re-evaluation of their conduct, to allow a requalification of their activity among scholars, decision makers and the public opinion.

In the last part we dealt with the issue of the political relevance of multinational firms in the context of the global governance. We studied the delicate topic of the relationship between states and multinational firms: while nowadays a significant part of the scholars sustains that the state has lost its importance in shaping the economic destiny of the world, we sided with those academics who, conversely, think that it still plays a fundamental role as container of cultural values and as the regulator of the economic activity. However, we could not say that its role has remained unchanged in the years in which globalization has gained the upper hand, in fact, some modifications have taken place. Nation states have continued to exercise their influence over many aspects of life, including the economic one, but since throughout the years the presence of the multinational firms has become overwhelming, states somehow have been forced to increase the interactions with this actor, and to share with it part of their power and authority on the control of economic issues. As we saw in the chapter, the relationships between these two parties have gone through periods of harsh confrontation and through periods in which collaboration prevailed, but still in today's world this relation is very complex and ambiguous, characterized by a divergence of interests in some aspects, but also by a convergence of objectives in some other issues. Multinational firms, in their global expansion, have started to affect also cultural and social aspects of everyday life, widening their sphere of influence outside the economic environment, and becoming true political actors. Their contributions can be so important that, often, states engage in "locational tournaments" to be able to attract the foreign investment. Nevertheless, states can also apply a number of measures and policies to limit or direct the investment in those areas where it is most needed, therefore making the most of it.

The complexity of the global context can be deduced from the difficulty of reconciling all the interests of these different actors, to which we must add also NGOs,

whose role is becoming more and more fundamental in solving social issues. Among the many accusations addressed to multinational firms there is the one that sees them as an obstacle to the solution of social problems, if not even the main cause of them. The model of creating shared value by Porter and Kramer tries to reconsider this issue, noting that, actually, the resources that multinationals have are increasingly being used in favour of the community, not at its expenses, and that what is good for society is good also for the multinational firm.

A re-evaluation of the role, the conduct and the effects of multinational enterprises is needed in order to have a clearer picture of the situation at the international level. Now the relationship between multinationals and states seems to go in the direction of a reciprocal acceptance. Governments are increasingly evaluating positively the presence of these firms within their boundaries, since they have recognized that they represent an unavoidable resource that enables them to maintain or improve their competitiveness in the global markets, to have access to the most up-to-date technologies, and to benefit from the organizational and managerial skills and spillovers that might help them develop the local economy. Besides, recent theory is demonstrating that multinationals can have positive impacts also on the addressing of social problems. However, while partnerships have already started to be established between multinationals and NGOs for the tackling of social issues, collaboration in this sense between companies and governments is still poor and superficial. While many scholars continue to insist in finding and respecting the limits of action of all these actors, we believe that sometimes the boundaries among them have simply being blurred, and this does not necessarily imply bad consequences for the whole society. In the world there is no need for more international organizations or institutions; rather, what we think to be really fundamental is the birth of new combinations among the already existing parties: they need to establish among them new forms of collaborations and partnerships, and to coordinate better their respective policies. They should stop seeing each other as enemies and start behaving like partners. All these actors together would have at their disposal a great deal of money and resources to solve problems and reduce iniquities, but what they still lack is a profound willingness to reciprocally respect each other's power and values. In a world that

changes so quickly, interconnection can no longer be considered as an option but it must start to be seen as a necessity, and in this interconnected network, the most important characteristic would be flexibility. The importance and relevance of the phenomenon of multinational firms is nowadays undeniable, and as we saw, its different aspects are increasingly positive. Therefore, it is worthwhile to accept them and involve them in the management of the international governance.

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