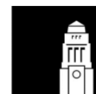

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Towards a theoretically based global foreign direct investment policy regime*

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Keywords

Multinational Enterprises

Foreign Direct Investment

Institutions

Investment Policy Regime

International Business Theory

ABSTRACT

Towards a theoretically based global foreign direct investment policy regime

This paper seeks to derive rational policies towards multinational enterprises (MNEs) from extant international business theory. It examines the impact of national institutions and policies on both inward and outward direct foreign investment. It adopts a theory-based perspective utilising internalisation, transaction cost and institutional approaches to the operations of MNEs. It contrasts the received policy process by which MNEs react to policy initiatives with a potential "direct" policy model whereby strategic decisions of MNEs embody policy goals. The paper suggests that transparent national policies with robust supranational monitoring are the best solution for world economic welfare.

TOWARDS A THEORETICALLY BASED GLOBAL FOREIGN DIRECT INVESTMENT POLICY REGIME

INTRODUCTION

"The most effective method of control (of multinational enterprises (MNEs)) is for governments to agree upon a new industrial policy which can be policed on a supranational basis" Buckley & Casson (1976: 1). …. "However, a prerequisite of an effective policy is an understanding of the behaviour of MNEs" Buckley & Casson (1976: 1-2).

This paper seeks to derive rational policies towards MNEs from existing international business theory. The contention of this paper is that public policies towards MNEs are best conducted at national level, policed firmly at supranational level. Policies have to be based on an understanding of the behaviour and strategies of MNEs. This paper is therefore an unashamedly "thought – polemic" piece involving both analysis and advocacy. The following section analyses the modern MNE and highlights those areas of strategy that are relevant to effective policy making. Then the importance and efficacy of national policies towards MNEs are presented, together with the deficiencies of purely national policies. It is then argued that deficiencies of national policies are best addressed by supranational monitoring. Questions are thus raised about what body (or bodies) is to carry out the monitoring of national policies and how this is to be achieved. The national and supranational policy set is then revisited in order to see if public interest goals are met by the proposed regime. The conclusion suggests that the optimal global regime for monitoring and controlling MNEs that is feasible is a transparent set of national polices declared in advance and systematically adhered to, under a global policing regime. Each substantive section ends with a short review of relevant theory.

NATIONAL POLICY TOWARDS MNES: THE GOALS

The modern nation is "a territorial relation of collective self-consciousness of actual and imagined duration" (Grosby (2005: 11-12)[i]). National power arises from the modern state which "may be loosely defined as a structure that, through institutions, exercises sovereignty over a territory using laws that relate the individuals within that territory to one another as members of the state" (Grosby, 2005: 22). The 1934 Montevideo Convention (Montevideo Convention on the Rights and Duties of States 1934) sets a standard for statehood. It lists four criteria: a permanent population, defined territory, a government and the capacity to enter into relations with other States. Crucially, the modern nation state has the legitimacy to raise taxation. The fiscal power of the state also gives it the power of coercion, in that taxation supports the police function and funds defence. Thus citizens indirectly pay for protection through tax revenues.

The economic interest of governments of states is to appropriate a share of rents from MNEs. This is made up of rents from foreign MNEs that are domiciled in a particular country plus appropriating rents from their home country MNEs wherever they are located. This 'struggle for a share of the world's appropriable rents' (Buckley, 1996) is at the heart of potential conflicts of government policies with the policies of other governments and therefore of the need for supranational monitoring.

The rational economic case for government policy intervention rests on two aspects of market failure: these are (1) monopoly and (2) externalities. The case for intervening in monopolistic markets is to enforce a price equal to marginal costs and thus to eliminate private rents. This may not be a complete argument because a monopoly (by reinvestment of rents) may enable more rapid innovation than other types of market structure. The innovation aspect of monopoly is disputed, but nevertheless, the ability of monopolists (multinational enterprises) to spread the results of R&D (even if not undertaken by them) over the largest potential market may present a case for toleration of a monopoly (Buckley & Casson, 1976). In order to justify government intervention, market failure in the form of externalities must have information problems because otherwise a market solution on the lines of the Coase

theorem (1960) correcting the real or potential externalities ("the polluter pays") is possible (Buckley, 1996) because trade in externalities would eliminate inefficiencies. Information constraints and restrictions are the key problem for the effective implementation of government intervention. Smit, Pennings & van Bekkum (2017) divide external uncertainty into two – transactional uncertainty that stems from institutional voids and increases transaction costs, and economic uncertainty that arises from the business environment. This paper envisages national policies as having an impact both on transaction costs and on market imperfections (Figure 1).

Addressing transactions costs – particularly those imposed by governments – is a suitable way, both theoretically and in practice, to identify the most effective policies. Governments have sovereign rights to implement national industrial policies, but the negative externalities of such policies can only be ameliorated at the international level in a globally interconnected world economy. A review of policies towards outward foreign direct investment (OFDI) concluded "We have not yet been able to present a holistic policy framework – but then, neither, so far, has any government" (Buckley, Clegg, Cross, & Voss (2010:272)). This paper attempts to provide a theoretically based, holistic approach to both inward and outward FDI. Issues that successful policy has to address are the creation or sustenance of monopoly or quasi-monopoly positions (unless explicitly an object of policy as in national champions or public national health services) and the imposition or increase of non-natural transaction costs.

As well as transactions costs, policies also affect other costs too, notably they can increase or decrease prices throughout the economy, either by tax-equivalent price increases or subsidies that reduce certain prices. Examples of the first case are wage increasing social provisions (e.g. minimum wage legislation). Examples of the second are subsidies for growth-increasing purposes (subsidies to R&D) or to "merit goods" (Marglin, 1967) such as education. These policy-induced changes feed into increasing or decreasing location costs and therefore discouraging or encouraging inward FDI. Their effects on outward FDI are more complex but, in principle, predictable. Whilst the price and cost effects of national policies are important, and their unintended consequences can also be significant, it

is the transaction cost and market imperfection effects that need to be comprehended by international regulators, because these transcend national boundaries, arising from of their effects on the existence and strategies of MNEs.

In addition to market constraints and policy regulation, ethical and cultural values provide restraints on the behaviour of MNEs. It could be argued that, ultimately, this is the most important aspect of restraint on excessive rent-seeking strategies by powerful corporations (and institutions in general). This issue is revisited immediately before the Conclusion.

Four dimensions to this analysis are considered, namely (1) domestic institutions and government administration, (2) domestic government-business linkages, (3) international government relations, and (4) international business and socio-political networks. Each of these dimensions has the potential to interact or impinge upon market imperfections, transaction costs, and the internationalisation processes of multinational firms (Buckley, Voss, Cross & Clegg, 2011). This leads to a theoretically grounded approach to policy. A schematic narrative of the argument is shown in figure 1.

Figure 1 goes about here

Configuring this argument in terms of 'the eclectic paradigm' (Dunning, 1977, Dunning & Lundan, 2008); national policies represent an important component of location factors (L) encouraging or dissuading inward foreign direct investment and affecting OFDI; the response to policy is an influence on the internalisation decisions of firms (I) as delineated below; and the third explanatory leg "ownership advantages" (O) are explicated in the section on innovation below.

The Governance Triangle

In practice, governance of market activities is not direct. Abbott and Snidal (2008) describe a 'governance triangle' which attempts to illustrate the interaction between 'the state', 'civil society' and

'the market' as governance mechanisms (Figure 2). This is useful because it integrates governance through coordination (the role of the state), governance through competition (the market) and governance through argumentation (civil society) and allows discussion of their interaction – through 'regulatory capture', lobbying and the role of pressure groups.

Figure 2 around here

We can add to this the role of international organisations as orchestrators of international governance mechanisms (Abbott, Genschel, Snidal & Zangl, 2015). Such orchestrators include both national Non-Governmental Organisations (NGOs) and international NGOs (Abbott, 2017). In practice therefore international production and service activities are subject to multipartner governance. MNEs are subject to a complex web of governance, regulation, rules and norms transmitted through a range of official, semi-official and unofficial institutions. Regime theory (Oye, 1985, 1993) approaches this problem from the actors' point of view as planned adaptation in the face of pervasive uncertainty. Cooperation under Anarchy (1985) provides a theoretical framework for the realisation of mutual interests in the absence of a centralised authority (Oye is referring to states, but this framework fits MNEs as well). It is possible to present these issues in a game theoretic setting but Oye goes beyond this to emphasise the role of evolving ideas and interests. In Economic Discrimination and Political Exchange (1993), Oye illustrates the internalisation of policy externalities through ad hoc negotiation and formal international regimes in researching inter-state disputes. This process is exactly analogous to the analysis of regulation of MNEs presented in this paper. This issues of compliance and uncertainty are at the forefront of the neoliberal institutionalist analysis of Keohane (1984 Chapter 6) again focusing on the reconciliation of state-to-state conflicts, but also picking up the importance of transaction costs.

Institutional design and its interaction with transaction costs are central to international political economy and international relations (Acemoglu & Robinson, 2012). This paper seeks to utilise these approaches in the analysis of a global foreign direct investment regime.

Analytical mechanism

Two analytical mechanisms might be employed in examining policies towards FDI. One is game theory where the actors seek to gain returns at the expenses of other players. The second is to suggest convergent norms, where repeated actions result in a convergent equilibrium from which there is no incentive to move. Cooperative games (Axelrod, 1984; Buckley & Casson, 1988) would result in a similar convergence. This paper adopts the second approach.

Non-economic Goals of Policy

It is clear from an examination of current national policies that they do not conform to any idealised notion of rational economic welfare maximisation. Partly, this is because they reflect sectional interests – producer interests, regional powerbases, elite interests and "state capture" by particular interest groups. In addition, other objectives than purely economic ones are embodied in policies – primarily "security". Security typically means national security and policies that are intended to protect national assets from foreign control. These protected assets may variously include defence related industries (electronics, shipbuilding, aerospace manufacture), transportation related industries (ports, airports), communications industries (telecoms), extractive industries (exploitation of "national" natural resources) or manufacturing and service industries with particular resonance for the "national interest" that can include iconic brands, industries that embody innovation (software, high-tech manufacturing) and language related activities (education, publishing). "National security" can represent an extremely wide set of activities that need special protection from foreign ownership and control. Exceptionalism can easily become the norm, undermining policies based on economic benefits. Non-economic goals can be adduced as a protectionist measure and can be used to subvert optimal policies.

The Societal goals framework of Policy

Many observers are sceptical about the societal goals of policy objectives. Attempts to introduce 'codes of conduct' for MNEs (for instance by the UN 'Group of Eminent Persons' in the 1970s (UNCTAD, 1973)) have foundered on differences of opinion as to what the moral basis of policy should be. However, if we accept that policy is not simply about static efficiency criteria, then introducing objectives such as 'development', 'equality', 'fairness', 'transparency' and 'sustainability', requires codification of objectives and establishing the relationship between policies and outcomes. The UN has made concerted attempts to introduce societal goals into economic policies and actions. Its Millennium Development Goals (MDGs) followed by its Sustainable Development Goals (SDGs) represent frameworks intended to guide policy, the actions of firms and indeed of civic society and welfare outcomes.

The societal goals set by the UN are not the only international mechanism promoting corporate social responsibility. The OECD Guidelines for Multinational Enterprises contain a grievance and promotion mechanism – the National Contact Points (NCPs) for Responsible Business. These are not legally binding and can be characterised (e.g. Nieuwenkamp 2018:1) as "international soft law". NCPs are mandated to promote corporate responsibility and to impartially problem-solve. They incorporate ILO labour standards and the UN Guiding Principles on Business and Human Rights and – in 2011 – were revised to include global value chains. The grievance mechanism impacts on all global value chains with a link to any of the 48 adherent governments (Nieuwenkamp, 2018). Case law by the NCP covers hundreds of business operations including ending forced and child labour, improving health and safety, improving human rights through due diligence and actions to secure compensation for indigenous peoples. From his review of NCPs Nieuwenkamp (2018:2) concludes "Responsible business conduct is no longer voluntary in the sense of being optional, even though it is still not legally binding. There is an increased uptake of corporate responsibility and due diligence standards in legal instruments".

Consequences do follow from non-observance of the guidelines and national governments do have tools to incentivise companies to behave responsibly. Export credit agencies can withdraw support for irresponsible ventures. Institutional investors can use their agency to promote better behaviour and activist stakeholders can access the decisions.

It can be argued that such multilateral frameworks have little effect on policy or outcomes. However, there is substantial and increasing evidence that MNEs do take account of societal goals and are increasingly constrained to do so by their stakeholders. One example is Nestle, who in the Foreword to their Stakeholder Community Survey 2017 said:

“Stakeholder perception of the development of our societal commitments in five areas with the UN’s Sustainable Development Gods is promising, however, and comes as a reassurance that we are going in the right direction” (Nestle, 2017: 1).

The increase in shareholder activism, stakeholder pressure, the importance of confirming to (global) standards, the increase in ethical consumerism and public and social pressure in general requires MNEs, in particular, to pay increasing attention to moral standards in business behaviour, not just in “Corporate Social Responsibility” or “Shared Value” but as a means of long term sustainability and survival.

The societal goals of policy at both international and national levels provide a set of constraints and incentives to corporate behaviour that cannot be ignored. The complex web of hard, legally binding and “soft” law overarches international business conduct and transcends the ‘governance triangle’. These “moral” effects on inward and outward FDI are concrete and operate through markets, governments and civil society.

INSTITUTIONS AND INTERNATIONAL BUSINESS

Institutions coordinate aspects of an economy by determining the 'rules of the game' and influencing 'how the game is played' North (1990); Brewer (1993). To do so, institutions contain an element of enforcement and sanction. Institutions that are characterised by codified and rule-based enforcement and sanction procedures (that is, formal institutions) comprise government structures such as legislature, judiciary and bureaucracy, as well as market mechanisms. Informal institutions lack such rigid structures and are based on conventions and norms of behaviour as exemplified by socio-political networks (North (1990)). Such formal and informal institutions can create two types of market imperfection: (i) structural market imperfections (for example, government intervention, market concentration, and collusion) and (ii) endemic market imperfections (for example, information problems and heightened uncertainty). Both types of market imperfection have the potential to influence the level of transactions costs in an economy – in other words, they give rise to costs that prevent perfect competition. Such imperfections can be created by home country governments and their agencies with intent and do not necessarily evolve by accident (North, 1990; Dunning, 1992; Hämäläinen 2003; Acemoglu & Robinson, 2012). This is done to achieve certain political, economic or social goals and is reflected in different aspects of inward and outward FDI activities. Likewise, some institutional arrangements can be created to circumvent the transactions costs caused by a misalignment of an existing configuration of other parts of the institutional environment, but without removing them. Extant work on inward FDI and institutions identifies four dimensions which are used in the following sections to structure the assessment of the institutional regime within which FDI takes place.

Domestic Institutions and Inward FDI

The influence of host country institutions on inward FDI and the business strategies of foreign multinational enterprises (MNEs) are well documented, especially in the case of investments to emerging markets (see, for example, Dunning, 1992; Meyer, 2004; Lipsey, 2002; Makino, Beamish & Zhao, 2004, Lundan, 2016). Generally, host country institutions support its national locational advantages for the attraction of inward FDI by putting emphasis on policies that target, *inter alia*,

foreign exchange liberalisation, international trade and domestic market liberalisation, and that support private ownership (for example, Bevan & Estrin, 2004; Gastanaga *et al.* 1998; Sethi *et al.* 2002; Globerman & Shapiro 1999; Taylor, 2000). Especially in the case of emerging markets, transparent and accountable institutions are seen by investors as an insurance against those political and commercial risks that MNEs generally do not encounter when investing in more advanced economies (see for example, Drabek & Payne, 2002; Loree & Guisinger, 1995). Such institutions are intended to remove those market imperfections which were put in place by an emerging country government for political and industrial policy reasons and which have the effect of increasing the costs of establishing and operating a business in that market for foreign firms. Likewise, domestic institutions can cause strategic and operational problems to MNEs due to unexpected nuances and unforeseen changes (Henisz and Swaminathan, (2008) which raise transaction costs for MNEs and have the potential to jeopardise their profit-maximising strategy. China is a good example. China became one of the most attractive locations for inward FDI, not least because, since 1978, it has undergone an institutional transformation that has helped to release its potential as a production base for exports and for the servicing of a growing domestic market by foreign firms (for example, Henley *et al*; 1999; Ng & Tuan, 2002; Zhang, 2001; Ng & Tuan 2002; Buckley & Lessard, 2005). Meyer and Nguyen (2005) extend the scope of analysis by demonstrating that host country institutions at both the national *and* sub-national levels influence the strategy of MNEs, and that both levels should be considered when seeking theoretical explanations for the inward investment behaviour of foreign firms. This is the *domestic institutions and government administration* policy dimension of FDI.

Advanced, rich countries also seek to regulate inward FDI. The rise of neo-protectionism has strengthened arguments in various national economies on concerns such as unfair competition, security issues and culturally sensitive areas of activity. The Committee on Foreign Investments in the United States (CFIUS) has been strengthened, plans for a new regime on inward foreign investment in strategic European targets for takeover are underway (CFIEU), the German government is implementing steps to tighten administrative procedures on foreign investment control (Cornett, Link and Becker 2017) and the UK is re-examining its inward investment policy. The UK is considering a

‘public interest’ criteria including media plurality, financial stability and national security as a means of blocking international takeover of UK companies (Economist 04.03.2017 p 60).

Host country governments sometimes actively seek to exploit the potential benefits from inward FDI. These benefits include an increase in the competitiveness of domestic firms through spill-over and demonstration effects, as well as through the establishment of domestic value chains which may attract further foreign investors and thus lead to positive agglomeration effects. At the same time, the government may work to minimise the possibility of crowding-out effects arising from inward FDI that might be caused by the higher productivity of MNEs vis-à-vis domestic firms. This alignment of objectives between the government and the business sector for mutual benefit falls into what can be described as the *domestic government-business network* policy dimension.

In instances when domestic formal institutions are weak, at either the national or sub-national level, informal institutions - such as personal networks and relationships- can be used by MNEs as a substitute in order to provide channels for obtaining business intelligence, securing greater investment certainty, and other benefits. When the formal institutions are perceived to work well, informal institutions may supplement rather than replace them (Li *et al*. 2004; Wang, 2000; Gao, 2003). Such considerations are encapsulated in the *international business and socio-political* policy dimension.

Following a similar line of argument, international investment agreements (IIAs) based on bilateral or multilateral contacts and negotiations between governments and between governments and international organisations can support FDI flows by lowering institution-derived transaction costs (Buckley *et al.* 2008a; Bandelj, 2002; UNCTAD, 2004). WTO membership provides foreign firms with a tool for dispute settlement through an independent entity. Such interactions are embraced by the *international government linkages* policy dimension.

This review of how institutions affect inbound FDI provides a theoretical foundation for understanding that institutions have the potential to influence the scale of inward and outward FDI and the

investment behaviour of firms. In the following section, we discuss this framework under each of the four dimensions identified above – accounting for both inward and outward FDI policy effects.

Table 1 goes about here

Domestic Institutions and Outward FDI

Domestic institutions and government administration

Countries introduce economic policies and regulatory frameworks with a clear goal in mind, namely, to advance national economic development. Intentionally or not, this can have negative effects on OFDI. Amongst the measures that may have negative side effects on OFDI are those actions that target the international economic interaction of domestic businesses (for example, balance of payments controls, international investments approval processes, and foreign exchange controls), while other measures have a domestic policy focus such as domestic investment promotion and control, and the identification and support of industry sectors considered to be important for the economic future of the country. The intention of these types of policies is to ensure that there is sufficient long-term capital for domestic investment that will create employment and economic growth. However, by curbing the international investment possibilities of domestic firms, their competitiveness potential may be diminished because they cannot develop and exploit their resources and capabilities to the fullest possible extent.

On the other hand, the domestic institutional framework may have positive effects on some indigenous firms and can augment their ownership advantages. Companies that originate from a restrictive institutional framework will gain substantial experience of how to cope with such an environment and, indeed, how to exploit those imperfections associated with the local market which may assist them in being successful in countries with similar institutional conditions. Of itself, this can constitute a firm-specific advantage, and one that may enable firms to internalise even the smallest changes and opportunities provided by the governance system – regardless of whether it is a 'rules-based' or

'relations-based' system. By extension, such firms are likely to exploit these advantages in a similarly structured host country – a notion that accords with the spirit of the 'Uppsala' model of incremental firm internationalization (Johanson & Vahlne, 1977). These are the advantages of home country embeddedness, and they can include the ability of firms to cope effectively with (rapidly) changing institutional settings and discretionary policies, to economise on the use of scarce capital and other factor inputs, to exploit domestic and international network capacities to circumvent market imperfections, and to scale products and production systems to suit foreign market needs and conditions. In fact, companies might feel more comfortable investing in a country with a similar institutional setting and governance system to their home country as they can better appreciate it, utilise existing operational leeway, and better foresee any political developments and administrative decisions that might ensue (Wells, 1983; Lall, 1982; Lecraw, 1977; Johanson & Vahlne 1977; Cuervo-Cazurra & Genc, 2008). In contrast, the institutional environment may be designed in such a way that any international investment by domestic firms is prohibited: that is, when structural market imperfections are put in place (Hämäläinen, 2003). Companies operating in such an environment may find it costly and cumbersome to (illegally) circumvent investment barriers to take advantage of their international competitiveness (Khanna & Palepu, 2010). But firms with only a few short-term ownership advantages have to proceed with their internationalisation at a point in time when they are in possession of the advantage. If the foreign investment is delayed, their ownership advantage may become eroded before they are able to invest, and this may render the investment unfeasible (Rivoli & Salorio, 1996).

A case for subsidising OFDI can be made from arguments about reducing the uncertainty surrounding information gathering on a foreign country. In the absence of proven externalities, the correction of which can be shown to accrue to the home country, there is little theoretical support for actively subsidising OFDI.

A current example of coordinated policy initiatives is the Chinese "Belt and Road Initiative" (BRI). This involves various types of connectivity – of policy, of infrastructure, of trade, of financial flows

and of personal networks. Each of these connections involves the tying of international activities into Chinese domestic institutions and frameworks. This is less of international policy projection ('in to out') and more of an enmeshing of international (non-Chinese) bodies in the domestic Chinese nexus ('out to in'). As such it represents new policy challenges.

Domestic Government-Business Linkages

The character of the government-business networks of a country can exert considerable influence on the domestic and international development of companies. Economic systems which are built upon 'relation-based' governance systems may reward personal linkages between businesses and governments. This can be reflected in the protection of companies against internal and external competition through government-imposed market entry barriers and the preferential treatment of selected companies (Li *et al*. 2004). Such behaviour is more difficult to sustain in a 'rules-based' system, which tends to be more transparent and independent.

Close relationships and collusion between the government and domestic businesses can lead to structural and endemic market imperfections which are exploitable by companies that enjoy good relationships with the administration. 'National champion' policies, for example, favour a small number of companies in selected industries with the aim of raising these firms to national and, eventually, international excellence. Industrial policy which focuses on the development of certain business sectors can also be regarded as a structural market imperfection when government involvement leads to the artificial adjustment of factor prices in favour of companies that have preferential access to critical inputs (Dunning, 1992). Although such policies have been in place for a number of years in numerous European and Asian economies (see, for example, Hayward, 1995) they tend to be more commonplace in economies where state-ownership of firms dominates (and where these firms are an important pillar of the domestic social and economic security system) or in economies which are built on 'relation-based' governance systems. There are two reasons for this. First, within 'relation-based' governance systems, it becomes difficult to distinguish between formal

and informal institutions because they intermingle. Laws, regulations, and procedures are interpreted and applied in a discretionary way by certain actors in society to the advantage of a selected few. The informal, personal linkages between firms and government officials can lead to economically unjustified protectionism and favouritism (that is, regulatory capture and adverse selection problems) (Li *et al*. 2004). As a consequence, one important market imperfection that may manifest itself at the interface between government and businesses concerns the capital market. Capital markets evolve alongside the general economic development of a country and are therefore often underdeveloped in developing countries (cf. Freire & Petersen, 2004; Levine, 1999). This leads to an inefficient allocation of capital. Soft budget constraints are a form of domestic capital market imperfection (Buckley *et al*. 2007). Soft budget constraints arise, for example, when an organisation's spending is not restricted to the boundaries of an annual budget but can be extended with extra-budgetary funding from the supervising (government) authority (Kornai, 1986). This creates a semi-permanent disequilibrium in the capital market. Outward investors can potentially exploit this and obtain the necessary marginal funding to pursue an internationalising strategy. In particular, companies with excess capital may use it to: (i) invest internationally on a trial-and-error basis without putting the domestic business at risk, (ii) outbid competitors in a fight for resources (especially energy and raw materials, brands, and technology), or (iii) fund overseas investment in the first place. For this reason, capital market imperfections can become an ownership advantage for domestic companies facilitating internationalisation (Buckley *et al.* 2007).

International Government Relations

Companies in countries in which the government plays an important role in the domestic economy may benefit from the government taking an active role in establishing international ties with other countries (Bandelj, 2002). Such activities can be directed towards the conclusion of bilateral and multilateral agreements, the accession to supranational institutional arrangements which shape international business activities, and other less codified measures. The intention is generally to reduce both structural and endemic market imperfections in and about the host country in order to lower

transaction costs for domestic companies in the foreign market. The Chinese government is in the process of negotiating a number of bilateral and multilateral trade and investment agreements in order to support and strengthen the outward orientation of Chinese companies, amongst other things. It has concluded a growing number of bilateral investment agreements and double taxation treaties over the past two decades to protect Chinese investors and their interests (Wang, 2001), and to coordinate China's foreign affairs and official development aid policy for 'mutual' benefit (Chen, 2006). The impact of these activities on the international investment decision-making of Chinese firms depends largely on the perceived credibility of these government-led initiatives (Murtha & Lenway, 1994). Given the current high levels of government support, Chinese firms have to be certain that it is either sufficiently long-term or provides sufficient (monetary) short-term benefits to merit the internalization of market imperfections and that the long-term growth of the firm is not impeded. Below we discuss in turn these types of bilateral, multilateral and other government-led initiatives.

China's "belt and road initiative" (BRI) (previously One belt, One road) (Cheng, 2016; Huang, 2016; Blanchard, 2018; Chen, 2018, Oxford International Infrastructure Consortium, 2016) raises many issues for the international direct investment policy regime. The close alignment of loans, direct investment, (Chinese) MNE involvement, state policy and geo-political relations requires great attention in unravelling and analysing the issues for the global economy, beyond the scope of this piece (for instance does the BRI promote Chinese outward FDI? Provisionally, yes, according to Du and Zhang, 2018). The potential debt servitude imposed on host states and the dual penetration of foreign investment and state policy make BRI a prime candidate for international supervision and regulation. Market imperfections here shade into market exclusion. Transparency is compromised and individual nation states are incapable of overall supervision. Such initiatives strengthen the case for an international policing framework, and for future research by the international business academic community.

Bilateral agreements

International investment agreements (IIAs), especially bilateral investment treaties (BITs), double taxation treaties (DTTs) and trade agreements, are often seen as policy instruments which countries introduce to improve their locational attractiveness to MNEs (Mallampally & Sauvant, 1999). A BIT provides a legally binding situation in which investors from the signatory countries enjoy greater investment protection for their tangible and intangible assets than domestic laws would otherwise provide. A BIT is therefore generally argued to reflect a progressive and positive attitude towards economic liberalism on the part of contracting parties (Vandevelde, 1998). The conclusion of a BIT should ensure a relatively high level of investment protection which helps the internationalising firm to attenuate risk considerations in the investment decision and to focus more attention on commercial considerations. In other words, a BIT regulates a distorted market and dilutes those market imperfections created by inefficient and (potentially) hostile host country governments. A BIT can also help to mitigate the risk of them behaving opportunistically. Consequently, a BIT may trigger FDI since overall investment costs and risks are decreased and business opportunities are widened (Egger & Pfaffermayr, 2004; Ramamurti, 2001).

Similar to a BIT, a DTT is concluded between two countries to avoid the duplicated taxation of companies operating in both countries for the same activity. Host country attractiveness is increased because future tax rates on (profitable) foreign affiliates are made more predictable for the investing parent company (Davies, 2004). Regional and bilateral trade agreements, on the other hand, have the potential to help domestic firms establish themselves in a foreign market first through exports and subsequentially through FDI, especially as such agreements often include provisions concerning the liberalisation of the host country's inward investment regime and can therefore stimulate intra-regional FDI (Globerman & Shapiro, 1999; Jaumotte, 2004; UNCTAD, 2005). Under the sphere of bilateral agreements also fall aspects of foreign policy such as official development aid and state visits by leading politicians to and from the host countries concerned. State visits are generally intended to appease and befriend the visited country but bear no codifiable enforcement mechanisms like home country government action. Such visits may, however, be followed by the negotiation and conclusion

of bilateral arrangements between the governments and, as we have seen above, this can affect the foreign investment behaviour of domestic firms positively as transactions costs are reduced.

Multilateral agreements

The most important supranational organisation that shapes international business on a global scale is the World Trade Organisation (WTO). The WTO is responsible for administering around thirty international treaties and agreements, and these include the General Agreement on Tariffs and Trade (GATT), the agreement on Trade-Related Intellectual Property Rights (TRIPs), and the agreement on Trade-Related Investment Measures (TRIMs). These agreements govern much of the framework for international trade and investment (such as most favoured nation terms and equal treatment of domestic and foreign firms, trade dispute resolution, market access, reductions in preferential trading arrangements and so forth) (Sornarajah, 2004). Membership of the WTO signals to foreign firms that a country is likely to conform to its strictures and obligations with respect to international trade and investment, and signals to domestic firms that the home government is capable of supporting them legally in cases of, for example, dumping accusations and other unfair practises. The WTO thus constitutes an important supranational component of the institutional framework within which MNEs operate. National membership of other region-specific organizations such as the ASEAN, EU, MERCOSUR, and NAFTA can offer similar benefits to investing firms.[ii]

International Business and Socio-Political Networks

Access to an international socio-political or business network has the potential to increase investment flows between countries by lowering transaction costs and by pointing a company to existing business opportunities. Such a network exists between a potential outward investor and (i) an ethnically-close overseas community, (ii) established foreign trade and contract partners, (iii) international business facilitators (such as investment promotion agencies, consultancies and trade promotion organisations),

and (iv) a foreign business partner with whom the potential investor already collaborates in its home country (for example, in the form of a joint venture).

Overseas communities can take different configurations which range from recently emigrated nationals that study or work in the host country or region to communities that have lived in the host country for several generations and retain strong links to their ancestral homelands.

Moreover, 'inward internationalisation' (Welch & Luostarinen, 1993) in the form of strong buyer-supplier relationships and contract work for foreign MNEs (for example, original equipment manufacturing (OEM) and original design manufacturing (ODM) arrangements) are all channels of knowledge transfer to emerging market firms. These types of collaboration bring information about product and process standards, as well as technology and quality control mechanisms which help to upgrade the intellectual capital of domestic firms.

National and sub-national investment promotion agencies from a wide range of countries have internationalised over the past decade in order to identify and attract potential foreign investors. These agencies offer crucial first-hand business information and contacts, and provide professional services to businesses that are considering internationalising and, in so doing, they support the investment decision process. Interested firms can also take advantage of professional services firms operating internationally that disseminate 'best-practises'. A good example of a national investment promotion agency is the UK Trade and Investment (UKTI) and its twelve regional development agencies (RDAs) in Britain. The UKTI's mandate is to strengthen the international competitiveness of British firms and the British economy. To fulfil this mandate, the UKTI has investment promotion offices in Beijing, Chongqing, Guangzhou, and Shanghai that target Chinese businesses in their respective regions.[iii] Anderson and Sutherland (2015) show that the presence of Canadian provincial level investment promotion agencies in China increase the likelihood of Chinese firms locating in that Canadian province because they reduce the expectations of the liability of foreignness (Zaheer, 1995).

Local firms can also absorb knowledge through direct and indirect business linkages. Direct linkages involve both backward- (supplier) and forward- (customer) linkages, as well as any kind of business collaboration, such as license arrangements, outsourcing agreements and the purchase of factor inputs (Pack & Saggi, 1997). Indirect linkages, on the other hand, derive from 'watching' the business operations, functions and products of other firms and imitating them (Inkpen, 2000).

Socio-political and cultural networks therefore can decrease transaction costs for foreign firms entering a particular national market and enhance international knowledge transfer. On these grounds they are to be encouraged by policy support. However, such networks can have anti-competitive effects by excluding non-network members. Exclusive networks can be used by firms to achieve unfair competitive advantages (Buckley, 1996). Further, the social and political strategies of dominant firms through lobbying and more overt corruption strategies can 'capture' local and national policies. Thus the existence of socio-political networks represent a prima facie case for government policy intervention, but one that has to be balanced by attention to the welfare enhancing aspect of such networks. Where purely national distortions occur because of network imperfections, there is a case for international counterbalancing regulation.

THEORY-INSTITUTIONS AND INTERNATIONAL BUSINESS

This section has shown that the institutional configuration of the national economy and its international networks and agreements interact with market imperfections and that this affects transaction costs. Rational policy making has to take account of the incidence of these transactions costs in order to improve outcomes. (Table 1). Table 1 shows the theoretical impact of the four dimensions of interaction between domestic institutions and transaction costs and market imperfections. The following section examines regulation, taxation and investment incentives to show the potential efficacy of rational national policies towards MNEs.

THE POLICY NEXUS

Foreign direct investment and trade policies are enmeshed in a complex nexus of other national policies – economic policies, fiscal, monetary and competition (industrial) policies (Buckley, 1996) and non-economic policies. The MNE is central to this nexus as its decisions on the location of investment and its choice of modes of foreign market servicing (exporting, licensing or FDI) have an impact across all of these policies. Similarly FDI is at the core of MNE strategy and is the cement that holds together global value chains and "global factory" structures as it conveys MNE control of these networks. Therefore examinations of policy on MNEs have to account for other elements of the policy network that impinge on MNEs and FDI, both inward and outward.

Tax, competition and environment laws can be used to discriminate against "foreign" multinationals (inward investors) with favourable treatment being given to domestically owned firms. "National treatment" requires that all firms, irrespective of ownership are treated equally.

The principle of subsidiarity

The notion of subsidiarity comes from Pope Pius X1's 1931 Papal Encyclical *Quadragesimo Anno* – "the task of the state was to facilitate activity by other groups and persons within the community but not to supersede these if they were working with reasonable efficacy" (Kilgannon, 2016: 7). The principle of subsidiarity was examined by UNCTAD in the World Investment Report 1994 'Transnational Corporations, employment and the Workplace (UNCTAD, 1994: 315). UNCTAD's 1994 World Investment Report (1994) quotes Article 4.3 of the council of Europe's European Charter of Local Self Government (1985).

"Public responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy".

The principle has been developed by the Catholic Church to develop decisions taken as closely as possible to the citizen. Applying the principle of subsidiarity to policies implies that it can be used:-

negatively (a large group should not accomplish tasks that a small group is capable of accomplishing), positively (the large group must do everything possible to enable the small group to fulfil to the greatest extent it can the functions that it is capable of fulfilling), subsidiarily (the large group will intervene with respect to the small group only to provide functions or services that are beyond the possibilities of the latter).

It is arguable that subsidiarity reflects common management practices in MNEs where issues are not submitted to higher levels of the management hierarchy for decision unless they cannot be settled at a lower level. The principle of subsidiarity also supports the approach of this paper; that the closest competent body to the citizen – the nation state - should be pre-eminent in decision making, with supranational authority ameliorating conflicts between sovereign nations.

National Jurisdiction

The national level remains the most appropriate and effective unit at which to implement trade, competition and fiscal policy. In some cases – most notably the European Union (EU) - some of these sovereign powers have been assigned to European level bodies, most notably in exchange rate and some associated levels of monetary policy in the adoption of the Euro, but with this significant exception, policy and the associated statistics underlying policy, are implemented at national level. Self-governing nationhood and government accountability remain dominant in determining the vast majority of policy making in the areas relevant to FDI and the MNE.

Regulatory power over inward and outward FDI resides at the national level. In Germany the Economics Ministry has the power of veto if a foreign buyer (outside the EU) takes a stake of more

than 25% of a company. In the UK the government holds "golden shares" in (just two) security sensitive businesses (BAE Systems and Rolls-Royce) preventing foreign takeovers.

Linkages between firms – Global Value Chains and Clusters of Firms

Much of domestic and international policies towards MNEs is based on the analysis of unitary firms. In the modern global economy MNEs act as coordinators, or orchestrators (Hinterhuber, 2002) of global value chains (Gereffi, Humphrey & Sturgeon 2005) or as "global factories" using information and material flows to integrate constellations of independent firms (Buckley, 2007, 2009a, 2009b, 2010, 2011a, 2011b, 2012, 2015; Buckley & Ghauri 2004). In addition, spatial analysis of economic activity has identified clusters of firms, usually national, but often international, in which dense interlinkages between firms – flows of product, information, human capital – ties firms together. Policy that fails to recognise value chains and clustering will be inefficient, possibly ineffective and may have negative or counter-productive outcomes (UNCTAD, 2011, 2013).

Current antitrust legislation may not be fit for purpose in the digital age. The strategy of large incumbent firms is often to acquire promising start-ups that maybe potential competitors. Dominant firms make it difficult for consumers to move their data from one provider to another and control of platforms gives companies the possibility to privilege their own services over those of competitors.

International trade rules

The design of trade rules that respect different national preferences on matters such as state control, product standards, property rights and competition policy are at the forefront of current negotiations on trade and investment partnerships such as the Transatlantic Trade and Investment Partnership (TTIP). Trade in services is particularly fraught with difficulties as illustrated by negotiations on the Trade in Services Agreement (TiSA).

Regulation

Sauvant, (2016) argues that ‘macro-liberalization’ (reduction of barriers to international trade, investment technology and financial flows) has run its course and the focus should shift to ‘global micro-regulatory frameworks’; rules on the international operations of firms, including cross border mergers and acquisitions “Such international rules for the principal actors in international production and markets would complement (or replace) the unilateral rules that exist at the national level. International rules would set the direct parameters for certain aspects of the international activities of firms and hence provide the global governance for operating in the global production and trading spaces” (Sauvant, 2016:1). Sauvant advocates international rules for the principal actors engaged in international business to complement or replace the unilateral rules that exist at the national level. These international rules would set the parameters for activities such as cross-border M&As and international bankruptcies. This approach contrasts with the ‘transparent national regimes with supranational monitoring” approach advocated above. The proposal here is not entirely congruent with Sauvant’s views. Here the suggestion is that transparent declared and registered national policies should be policed by supranational authority. Regulatory harmonisation at regional or international level is an alternative.

Taxation

The 2016 controversy between Apple Inc, Ireland and the European Union illustrates the potential strength of the package of national control with international monitoring.

The essence of the case is that Ireland lobbied for preferential treatment in order to encourage foreign investment in what was a relatively poor part of Europe from the1970s on (Ireland joined the European Community in 1973). This has been continued with EU approval of a low corporation tax in Ireland which benefits inward investors. This low tax rate was the background to the ‘double Irish’ system used by multinationals to reduce their overall tax burden. MNEs channel all their European

sales through an Irish registered subsidiary. This subsidiary then pays out royalties to related companies (possibly in tax havens) and has minimal profits on which to pay the low rate of tax.

This case is alleged to show that there are no sanctions available against governments that violate treaties and provide subsidies to MNEs. They are indulging in beggar-my-neighbour policies, depriving other countries of legitimate tax revenues. The extent to which this behaviour (and the transfer pricing strategies that it encourages) is condoned by EU agreements is a secondary point to the issue that international monitoring is weak. Tax policies need to be transparent and registered with international authorities with arbitration powers.

The OECD's BEPS initiative (Base Erosion and Profit Shifting) is intended to end double taxation and non-taxation and to ensure "fair treatment" of intracompany loans, sales and leases. Legislation on this needs to be followed by MNEs being compelled to adhere to a code of transparency and disclosure.

Alternative strategies to BEPS include unitary taxation, where an MNE is treated as a single integrated entity for tax purposes, no matter how it is configured. Profit shifting is eliminated as all intra-group transactions are ignored. A second radical solution is to abolish existing business and profit taxes and replace them with a single tax on cash outflows from all corporate vehicles to individuals. Both systems still require internationally agreed rules on intra-company payments and intellectual property. Indeed, any system needs to recognise that investment in intellectual property needs to be rewarded and that damaging the potential for innovation is a massive risk for global welfare.

Competition and Innovation Policy

It was argued in the Introduction that innovation is a critical determinant of Government policy and that the argument for and against monopoly as an innovation-stimulating structure is at the core of the debate. The competition policies of individual nations (or regions in the case of the EU) can conflict with each other and become, like protectionism. 'beggar-my-neighbour' policies. Here there is a clear

role for supranational monitoring – and reconciliation. Policies on innovation will have an important effect on both inward and outward FDI. They act as an attractor for knowledge-intensive activities and can stimulate firms to invest abroad because they contribute to building what the eclectic paradigm (Dunning, 1988; Dunning & Lundan, 2008) articulates as "ownership advantages" (the 'O' in OLI).

Investment Incentives

Setting national incentives to attract inward FDI has often been described as a 'race to the bottom'. The danger is that by attempting to maximise inward FDI, investment incentives are self-defeating because competitive bidding transfers potential gains from host countries to mobile MNEs. There may also be a 'race to the top' where host countries vie to spend public funds on infrastructure, vocational skill building initiatives and supportive institutions (Moran, 2010).

Similar arguments apply to outward FDI although here policies sometimes attempt to restrict OFDI (in the hope of increasing domestic investment) and sometimes to encourage it – to encourage 'national champions', gain access to resources or markets, or to invigorate the domestic economy through globalisation (China's 'Go Global' policies, for instance).

Competition to attract firms is healthy when it encourages countries to improve policies and invest in public goods, such as infrastructure. It is less so when it is used by powerful firms to extract public subsidies which damage taxpayers and competitor firms. Investment incentives at the national level are frequently derided as self-defeating, wasteful and ineffective. Such comments are usually followed by calls for international regulation of national incentives or a global system to set subsidies and restrictions. Given that national (or regional bodies like the EU) are the sovereign institutions that cover 'industrial policy' including investment incentives, cognisance must be taken of their de facto and de jure powers – and of the ineffectiveness of intended regulation in these areas. Transparency and monitoring are the key elements of rational policy making and cooperative monitoring. Kobrin (2015) suggests that there is an asymmetry between MNEs market strategy – where an integrated

international economy makes global strategy possible, and its non-market strategy where a fragmented international political system renders a global non-market strategy infeasible.

Investment incentives are defined by the OECD, (2003: 13) as "measures designed to influence the size, location or industry of a foreign direct investment project by a affecting its relative cost or by altering the risks attached to it through inducements that are not available to comparable domestic investors". UNCTAD, (1996: 11) suggests "…measurable advantages provided by government to particular companies or group of companies with a goal to force them to behave in some way". Of critical importance is the specificity of the incentive – the extent to which it is targeted at certain investors or types of investors. This might be a particular sector or industry, location, technological content or value-added characteristic. Consequently, Tavares-Lehmann et al, (2016: 5) use the following definition "Investment incentives are targeted measures designed to influence the size, location, impact, behaviour, or sector of an investment project – be it a new project or an expansion or relocation of an existing operation". This includes measures to retain or encourage the growth of, extant projects. As noted in the theory section above, incentives cover not only financial, fiscal, and regulatory measure but also information and technical services.

The argument for investment incentives to encourage inward FDI rests on the beneficial externalities from that investment outweighing the cost of such incentives. The existence of unpriced 'spillovers' has been the source of much contention in international business research and development economics (Blalock & Gertler, 2008; Javorcik & Spatareanu, 2011; Tavares & Young, 2005; Gorg & Strobl, 2001; Buckley, Clegg & Wang, 2007).

Investment laws

As UNCTAD's (2016) Investment Policy Monitor: Investment Laws points out, at least 108 countries have an investment law as a core instrument to govern investment – often with provision for foreign investment. Currently, most of these laws are focused primarily on investment promotion

strengthening investment laws and increasing their coherence with other public policies (tax, trade, competition, regulation, social and environmental policies) would allow national treatments of investment to become more transparent. Eventually, a standard investment law with clear provisions could be produced as a template. It would then be up to individual nations to adopt, or modify, this standard set of provisions, making international monitoring of individual national investment laws easier.

Administrative Guidance

In some societies, laws are less important than 'administrative guidance' where companies both public and private take their lead from signals from governmental bodies on behaviour and investment. Japan (Johnson, 1982) and now China (Hildebrant, 2013) are often adduced to follow this paradigm. These issues have important implications for transparency as "private" policy signals often go unrecorded.

THEORY - THE POLICY NEXUS

The relationship between the myriad elements of the policy nexus and the theoretical analysis helps us to unpack the complexity of policy and policy impacts. Table 2 shows the links between the four dimensions of home country institutions, inward and outward FDI and the requirements of supranational monitoring. It shows that it is possible to decompose policies (regulation, trade rules, taxation, competition policy investment incentives, investment laws) into institutional impact, business government relationships, international government linkages and international business network effects. In decoupling these elements, the theoretical analysis enables us to show the direction of the effect of institutions and policies and to determine the need for supranational intervention and monitoring (column 4 of Table 2).

Thus we can trace the impact of policies in terms of the increase or decrease in transaction costs, the creation of structural market imperfections, endemic market imperfections, information costs and benefits and uncertainty (increase or reduction) as delineated in column 3 of Table 1. Supranational intervention then becomes the mechanism for the correction of, or mitigation of, these effects at international level. It is to this supranational monitoring that we now turn.

Table 2 goes about here

SUPRANATIONAL MONITORING

The design of rational policies towards inward and outward FDI can be derived from existing theory (Table 1). The policing and monitoring of such policies at the supranational level is institutionally more problematic but potentially implementable. Questions arise about who should do the policing and exactly what in national policies should be policed (Table 2). This applies to both inward and outward FDI. It is clear that national policies with international policing is a second best package where international harmonisation is optimal. However, no international institution exits with sufficient legitimacy and power to interfere in all the world's nationally based (or regionally based) policies, their implementation and unintended consequences. Far better to recognise this limitation, to press for rational national policies but to monitor and police their negative externalities.

It is easy to underestimate the extent to which supranational rules permeate seemingly national policies. Membership of the UN, the OECD, the WTO constrains, underwrites and determines 'national' policies. Membership of "economic unions" (EU) of trade blocs (NAFTA) and trade associations (EFTA) further writes supranational rules into national policies – on "the single market" for instance. These rules are transcribed into EU law and then into national laws. Rules are formulated like 'Russian dolls' nesting inside each other, with the global policy rules as the outmost doll.

Correcting the Negative Externalities of National Policies Towards FDI.

Direct policy conflicts between nations are resolvable by treaty. Multilateral agreements are possible for general issues –specific conflicts or unusual, context-bound anomalies can be addressed by bilateral agreements. The negative externalities of national policies, borne by those outside the host nation are the most intractable problems of international monitoring. An excellent example of transaction cost reducing multilateral agreements is the WTO's Trade Facilitation Agreement (TFA) which went live on 22 February 2017. The TFA tackles unintentional barriers to trade and problems arising because of outdated customs systems (Bianchi, Botwright & Doherty, 2017). Through the TFA, governments will publish a wide range of customs-specific information and will aim to standardise import, export and transit formalities and to reduce the number of different procedures businesses have to fulfil in order to move goods between countries. Measures will help to speed up the processing and clearance of goods including advance clearance of documents before goods arrive and options for electronic payment of import or export duties. There is a special provision on perishable goods that is particularly helpful for the world's rural poor who are often the exporters of perishable agricultural produce. The reduction of transaction cost, improvement of transparency and correction of unintended consequences of policymakers the TFA an ideal exemplar of multilateral amelioration of the policy consequences of national enactments.

Competition between countries to increase their national tax base at the expense of others is moderated by the OECD's BEPS rules (Base erosion and profit shifting). It has been adopted by more than 100 jurisdictions to challenge aggressive tax avoidance. BEPS requires MNEs to declare to the tax authorities where they generate revenues by country so their tax planning can be judged. Countries can however compete as tax havens by reducing corporation taxes. Transparency and monitoring will at least focus all countries on halting extreme tax avoidance and can introduce 'haven status by international consent' where individual countries or jurisdictions are allowed to compete with lower corporation tax rates. This may further induce harmonisation of rates across sovereign jurisdictions.

Such policies also have a strong regional element, as Chaisse and Jusoh (2016) say, the International Investment Regime is now one of the fastest growing areas of international economic law which increasingly relies on large membership investment treaties such as the ASEAN comprehensive investment agreement (CIA). This represents a move to regionalisation of laws and policies on FDI.

A further instance of regulatory oversight being hindered by international MNE links is the growing reluctance among regulatory authorities to intervene in the foreign actions of MNEs even when such actions have direct and substantial effects on consumer choice and pricing in their home market. The extraterritorial application of domestic antitrust law has long been an issue particularly in the case of US legislation (Griffin (1999), Kobrin (2009), Vernon (1971), Kobrin (2015)) but the foreign activities of MNEs can often be unregulated in the absence of extraterritorial actions of parent country law. This presents a strong case for international antimonopoly (antitrust, anti cartel) regulation. A recent case illustrates the difficulty of national antitrust legislation being effective in a global market. This concerns Minn-Chem Inc. v Agrum Inc. (2012). The defendants in the case were MNEs with potash mines outside the US (most of the world's reserves of potash are in Canada, Russia and Belarus) who allegedly operated a cartel that increased prices worldwide and therefore in the USA. The courts in the USA concluded that they lacked jurisdiction under the Foreign Trade Antitrust Improvements Act.

Finally, we should return to an issue raised in an earlier part of the paper – linkages between firms, particularly global value chains and cross-national clusters of firms. In these circumstances, disentangling external effects is critical. When links between firms are price related ("linkages") (Bellak, 2004) they can be dealt with by the normal policy processes above (taxation, regulation and the like). Where there are unpriced externalities between these firms, across borders, then there is a case for government intervention.

The inescapable conclusion of the logic of this paper is that there is a missing institution (an institutional void) at supranational level to mitigate the outcomes of national policy. This is not just about conflict

between national policies but reconciliation where transaction costs are imposed across national boundaries.

THEORY – SUPRANATIONAL MONITORING

Supranational monitoring is theoretically mandated by the need to correct externalities spilling over from one national jurisdiction to another. There is no Coasean property rights system in place (Coase, 1960) to allow a market solution to conflicts of national policies and therefore a supranational jurisdiction is necessary to correct the negative effect of unpriced spillovers.

DIRECT SUPRANATIONAL POLICY IMPLEMENTATION THROUGH MNE STRATEGIES

The conventional policy model for "global goals" (goals that are compatible with, or at least reconcilable with, global welfare), as articulated by bodies such as the United Nations is portrayed in Figure 2. Policies, purportedly for the global good (such as "sustainability" (UN, 2015)) arising from social or moral agendas is set at supranational level (1 in Figure 3, top half). These policies are then implemented in national government policies (stage 2 in Figure 3, top half). These policy initiatives (e.g. on climate change mitigation) then alter, or affect, the decisions of economic actors such as MNEs which has policy results and unintended consequences (the latter may lead to a further round of policy initiatives). This is the process that was envisaged for the Millennium Development Goals (MDGs) and their replacement at the United Nations by the 17 Sustainable Development Goals (SDGs), (UN, 2015), (Zhan & Karl, 2016).

Figure 3 goes about here

The potential backlash against 'global policy goals' (such as climate change mitigation) in the 'anti-globalisation' movements (including the election of President Donald Trump) suggest that the received policy process may not succeed if 'global policy goals' are not incorporated into national policy making processes. Such a potential failure suggests a more 'direct' policy implementation strategy. This implies that the overarching global goals are directly targeted at changing the strategies of MNEs, perhaps through altering the incentive structure of MNEs. Such a strategy by-passes, or eliminates, the role of national governments completely (Figure 3, lower half). This strategy is an enlargement of the argument treating (foreign) investment by companies as a substitute for missing domestic institutions (Boddewyn & Buckley, 2017; Boddewyn & Doh, 2011; Buckley & Boddewyn, 2015) or filling institutional voids (Khanna & Palepu, 2010).

In practice, many companies already incorporate "societal goals" into their operations and objectives. The Nestle Stakeholder community survey (Nestle 2017) quoted above, is an illustration of autonomous incorporation of the UN Sustainable Development goals (SDGs) directly into corporate strategy.

Witte and Dilyard (2017: 2)[iv] say "Whereas the mobilisation of the private sector is repeatedly emphasised as a prerequisite for successful implementation of the SDGs – including in the UN resolution – academic work specifically linking the private sector to the SDGs or the MDGs is sparse… little is known about how an MNE's practices affect development goals set by the international community, or about how firms incorporate international initiatives such as the MDGs or the SDGs in their strategies". These issues are among the important agenda items for JIBP (Kolk, Rivera-Santos and Rufin, 2018, Van Zanten & Van Tulder, 2018 forthcoming, Kolk, Kourula & Pisani, 2017).

This neglect arises because the 'conventional model' of Figure 3 does not require analysts to pay attention to how MNE practices incorporate international initiatives or policy goals. They are treated like any other external, environmental or locational factor. Foreign institutions, business practices and labour costs are treated in exactly the same fashion as policy initiatives. However 'direct'

implementation (as in Figure 4) requires attention to be paid to the precise manner by which policy objectives are embedded in strategic decision making within MNEs. This opens up a new policy agenda.

Transnational New Governance

Corporations, including MNEs, operate within a web of rules and signals. Only some rules emanate directly from Governments, others arise from compliance with standards, customer expectations, product accreditation, suppler demands and civil society norms. Signals that come from all of the corporations' stakeholders are not only expressed as price signals but also through means such as social movements, ownership changes and lobbying. Corporations are not passive receivers of rules and signals; they also make them. The fundamental conception of Transnational New Governance is of a combination of business, NGOs and private regulatory bodies in novel combinations creating innovative institutions that apply transnational norms through predominantly private, voluntary standards (Abbott & Snidal, 2009). The role of individual states and intergovernmental organisations is largely to act as orchestrators of an emerging international regulatory system. This implies a much more decentralised system of "regulation" and the use of "soft law" to complement mandatory "hard law" (Abbott & Snidal, 2009: 509).

There are an increasing number of concrete examples of New Transnational Governance involving MNEs. One example arises from the global reach of credit rating agencies and a second one on the global palm oil industry. Both examples show that the road to successful transnational governance regimes is not straight, nor easy, nor is its ultimate success inevitable.

The transnational financial credit rating regime relies heavily on private credit rating agencies (Moody's, Standard and Poor's, Fitch). These private, for profit, corporations produce ordinal rating systems that effectively regulate the pricing and availability of credit to both public and private organisations. The integration of cross-border financial markets has made rating of the credit worthiness of financial institutions more consequential. Increasingly detailed regulation is typically implemented by market

actors (Sinclair, 2005). Indeed rating has become a transnational form of private regulation as nation states have to take account of (private) rating agencies' decisions. Rating agencies "are changing the norms and practices of commercial and public life around the world" (Sinclar, 2005: 174), to the extent of altering policy choices even of national governments. This growth of nonstate authority is a challenge to global governance even though the services of credit rating agencies are enlisted on behalf of states to manage their own domestic capital markets "in order to increase transparency and cheapen the cost of lending" (Sinclair, 2005: 175). Such outsourcing of regulatory judgement (White, 2010) is an issue of policy that requires evaluation through the prism of the New Transnational Governance.

The palm oil industry suffers from problems of tropical deforestation, biodiversity loss, greenhouse gas emissions, disturbance of carbon-rich peatland, exploitation of workers and "land grabs". The principal producing countries have been reluctant to regulate production, despite pressures from NGOs. In 2004 a multi-stakeholder "Roundtable on Sustainable Palm Oil" was established and a comprehensive certification scheme with defined environmental and social standards (2007) provoked limited reforms (Nesdurai, 2017). The Palm Oil Innovation Group (2013) backed stronger standards prescribing deforestation, the use of peat soil and social exploitation guidelines to provide benchmark standards. Pledges of 'supply chain traceability' were given by lead producers as an industry norm. These are examples of voluntary governance schemes relying on the market in using downstream corporate buyers' demand for sustainably produced products to incentivise upstream producers to act responsibly. Official governmental policies have followed these developments. Tripartite (MNEs, governments, NGOs) agreements are difficult and are not a panacea, nor are they secure in results. However the introduction of ISO 26000, guidance on social responsibility, brings together the UN's SDG goals and operating standards (ISO, 2018) and represents a further step to transnational tripartite governance standards.

The emergence of Transnational New Governance as a conceptual approach and as a practical solution reinforce the analysis of this paper, presenting an alternative to the "received model" of Figure 3 and modifying the starker "direct" approach of Figure 4. Attention to the network of signals, rules, standards

and formal regulations presents the future of research on an international policy regime for FDI and MNEs.

THEORY – SUPRANATIONAL IMPLEMENTATION THROUGH MNE STRATEGIES

Building global goals into national policies has always depended on the willingness of national authorities to subscribe to those same goals. This has been a patchy and contested process. In a global political economy where some national governments clearly do not subscribe to a globalist agenda – on free trade, on climate change mitigation, on development goals – then an alternative is to by-pass national governments and implement a more ‘direct process’ whereby global welfare goals (e.g. as interpreted by the United Nations) directly influence the actions of economic actors, most importantly the decisions of multinational enterprises.

The theory behind this is that the goals of MNEs have to be ‘manipulated’ to conform to the globalist agenda. This could be through incentive effects on managers – building the SDGs into reward systems – or through a change in company culture. Influencing the decisions of MNEs to implement policy goals directly raises questions of public versus private power and any move away from the conventional policy model towards a transnational governance triangle needs widespread discussion. This discussion will reflect “public morality” as the views of civil society impact on regulation. Ultimately, ethical and cultural values at least influence, if they do not entirely determine, regulation and policy. The most usual current means of expressing societal goals is through national policies and this makes necessary some form of international coordination. The institutions to do this – international bodies such as the UN, treaties, MNEs, are imperfect; consequently implementation to achieve improvements in Pareto optimality has to be consistently revisited and re-evaluated.

CONCLUSION

The thesis of this paper is that public policies towards multinational enterprises are best carried out at national level with strict international policing. The authority of the nation-state is the only feasible countervailing power to that of global firms, although (as in the case of the EU) this may be delegated to a regional authority. However, the supervisory, regulatory and incentivising roles of the national state need to be transparent and policed to ensure fairness, transparency and efficiency. An optimal global regime is not yet in place, but is necessary.

The theoretical narrative here is that national policies affect transaction costs (positively or negatively) and market imperfections, which give incentives for firms to alter location decisions and either to internalise intermediate markets or to outsource previously internalised activities. The contradictions between these policies create conflicting pressures across national boundaries which results in a contested policy space within which there is scope for supranational monitoring and coordination to improve world welfare. Currently this policy space is vacant.

The potential for a more direct embodiment of policy initiatives in the decision making of MNEs provokes the need for a major research initiative in International Business. How could policy goals be built into MNE strategies? Are incentives the way forward or is this a question of modifying company cultures?

This approach is strengthened by the emergence of "Transnational New Governance" whereby companies, NGOs and private regulatory, standards and accreditation bodies come together to provide a means of furthering transnational norms in innovatory ways through largely private means. This reduces the demands on national states and intergovernmental organisations and meshes well with direct policy initiatives by MNEs.

The approach propounded here is firmly based on international business theory. It addresses the issues of transaction costs and negative externalities in the operation of the global economy. It respects the principle of subsidiarity and it recognises the complications of global value chains and agglomeration.

The rubric is feasible, tractable and would be a step towards improvements in world welfare. The argument for a supranational monitoring body is compelling.

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Table 1. The impact of home country institutions and policies on inward and outward FDI

Dimension	Characteristics	Theoretical impact	Examples
"Institutional Impact" Domestic institutions and government administration	Strong governmental/ administrative involvement	Increase of transaction costs Creation of structural market imperfections	Inward FDI approval systems. Monitoring and adjusting OFDI.
Domestic government-business networks	State-ownership Industry policy	Creation of structural and endemic market imperfections	Domestic capital market imperfections, State bodies' OFDI.
International government relationships	Alignment of foreign policy and aid policy	Creation of structural market imperfections Reduction of endemic market imperfections, especially transaction costs, information problems and uncertainty	'Tied aid' Preferential government – government loans. 'Commissioning' of OFDI.
International business and socio-political networks effects	International strategic alliances OEM, ODM and others. Ethnic Overseas communities	Decrease of transaction costs but anti-competitive effects Channels of knowledge transfer	Domestic encouragement and subsidies to local sourcing and joint ventures. Overseas networks.

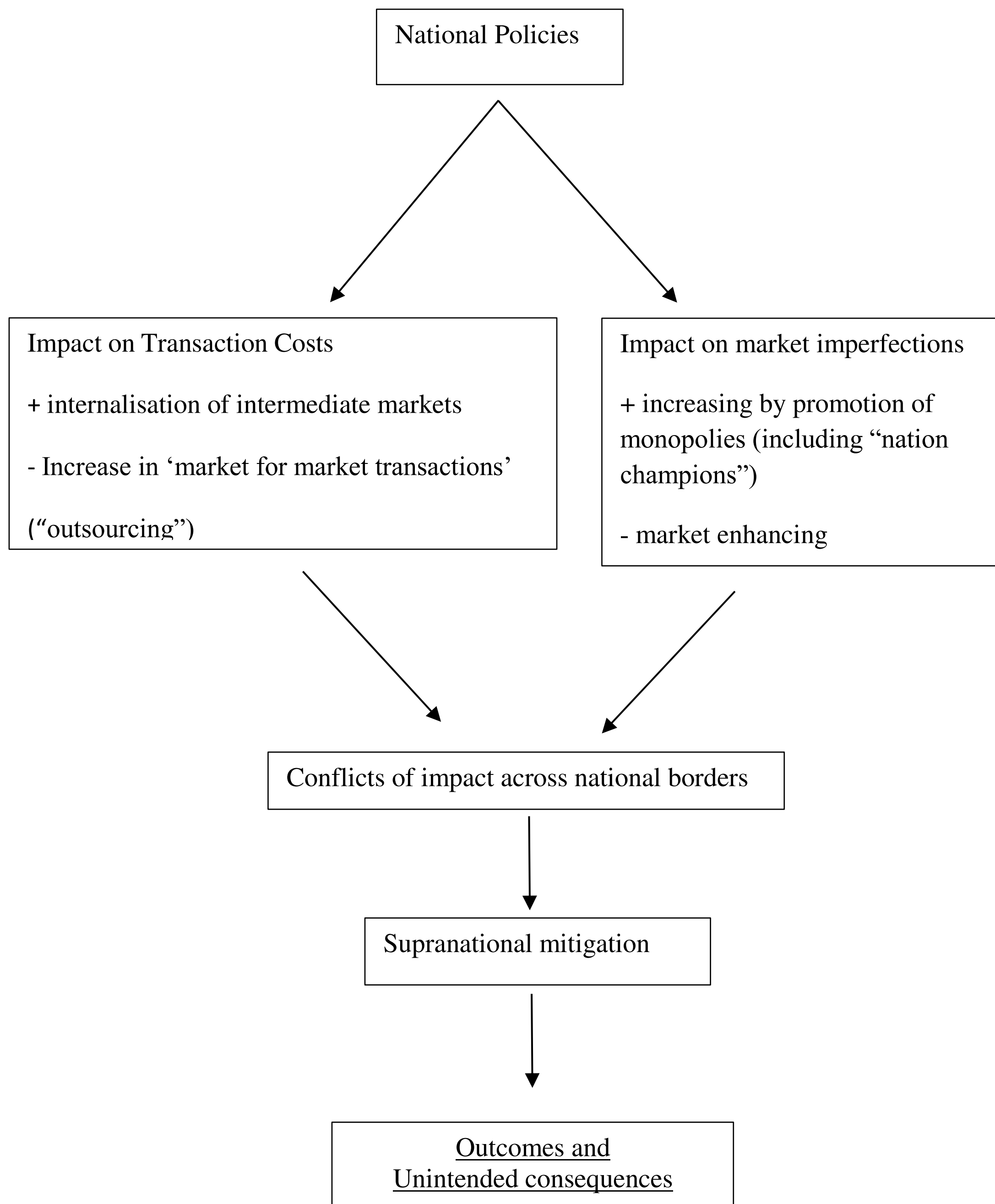
Source: Modified from Peter J. Buckley, Hinrich Voss, Adam Cross and Jeremy Clegg "The emergence of Chinese firms as multinationals: the influence of the home institutional environment" (in R. Pearce (ed.) China and the Multinationals: International Business and the Entry of China into the Global Economy. Edward Elgar: Cheltenham, 2011, pp. 144.

Table 2 The Policy Nexus: Home Country Institutions, FDI and International Monitoring

Dimension	Inward FDI	Outward FDI	Appropriate International Monitoring
"Institutional impact" Domestic institutions and government administration	Varied Policy Impact	Policy Impact may encourage or discourage OFDI	Agree Schedule of protected industries
Domestic government-business networks	Exclusion from protected sectors	Build "National Champions"	Global Anti-Trust
International government relationships	Discrimination Against Foreign Companies	Preference for Home Nation Firms Discriminatory	Anti-discriminatory (Most Favoured Nation) Policies
International business and socio-political networks effects	Aids inflow of capital, skills, technology	Aids OFDI by reducing transaction costs. Aids knowledge transfer if captured in firm	Monitor for abuse (anti-competitive) on ethnic basis

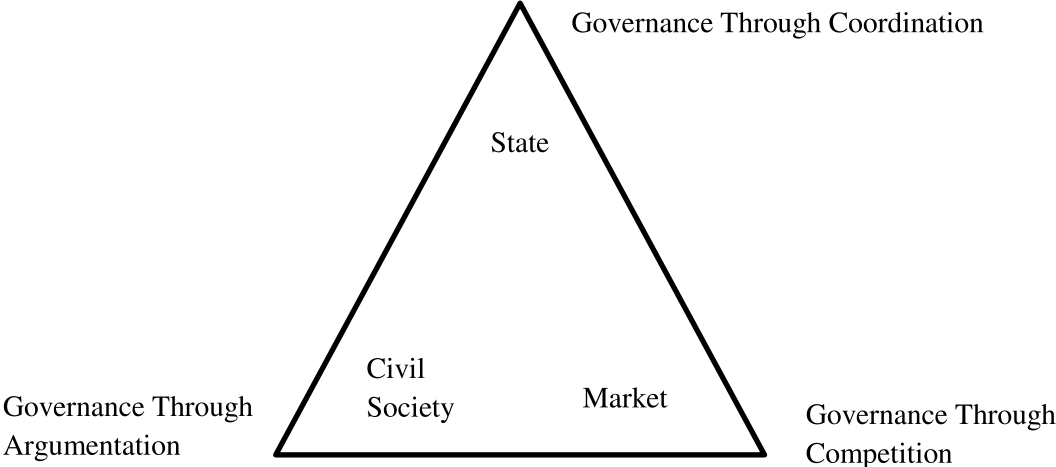
Source: Modified from Peter J Buckley, Hinrich Voss, Adam Cross and Jeremy Clegg "The emergence of Chinese firms as multinationals: the influence of the home institutional environment" in R. Pearce (ed.) China and the Multinationals: International Business and the Entry of China into the Global Economy. Edward Elgar: Cheltenham, 2011, pp. 144.

Figure 1: A Schematic Narrative of Policy Process Analysis



Source: Author

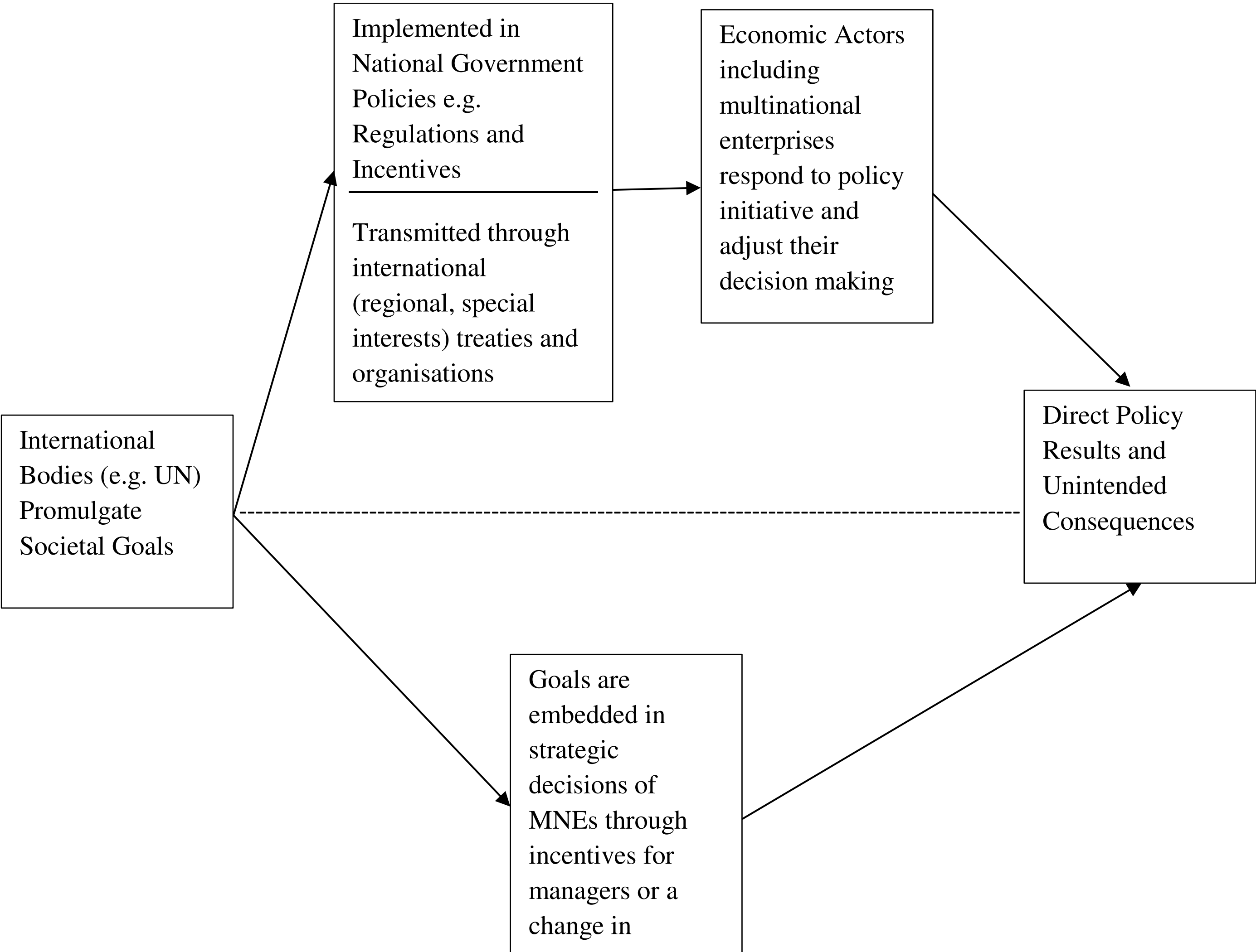
Figure 2 The Governance Triangle



Source: Adapted from Abbott and Snidal 2008.

Figure 3 Policy Models

1. The Received Policy Model



2. Potential "Direct" Policy model

[i] The idea that nations are "imagined communities" (Anderson, 1983) is not new. In 1796 Edmund Burke saw nations as a social construction "Commonwealth's are not physical but moral essences. They are artificial combinations, and, in their proximate efficient cause, the arbitrary productions of the human mind" (1796: 254). Quoted in Pollard (1971: 102).

[ii] The acronyms stand for: ASEAN: Association of Southeast Asian Nations, EU: European Union, MERCOSUR: Southern Common Market (from the Spanish Mercado Común del Sur), and NAFTA: North American Free Trade Agreement.

[iii] In addition, eight of the British RDAs have at least one office of their own in China to approach and attract Chinese firms that fit the particular business and development agenda of their respective region in the UK. These offices provide Chinese firms with an opportunity to learn about the potential of the British economy and help them to establish important business contacts.

[iv] Witte and Dilyard is an Introduction to a Special Issue of Transnational Corporations on "The Contribution of Multinational Enterprises to the Sustainable Development Goals".

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