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Corporate Reactions to the Fracturing of the Global Economy

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Introduction

This paper postulates a deep and long-term fracture in the global economy. It concentrates on policy-induced changes in the world economy and abstracts from "natural" imperfections that prevent the world from being 'flat'. The policies analyzed here include the tariffs and 'trade war' begun under ex-President Trump and the consequent Chinese retaliation, the Brexit withdrawal of the UK from the EU, the widespread manifestations of anti-globalization sentiment of the 'gilet jaunes' in France, "illiberal democracy" in the Visegrad nations of the EU, and voter disillusionment with established political parties, institutions, and governments in many Western democracies. This paper examines the impact of the fracture on corporate strategies. Corporate reaction to this fracture has been muted, uncertain and piecemeal. This paper argues that a corporate response is overdue and that it will herald new modes of international management.

Fracturing the World Economy: Theory

Several stages of escalation of national strategies to fracture the world trading system can be conceptualized. It should be emphasized that the fracture affects not just trade, but also international investment, including foreign direct investment by multinational firms (FDI) and their alliances, foreign licensing, and information flows, the latter disrupted by policy induced changes to the internet and other means of communication, affecting global value chains (GVCs). Flows of labor, and migration patterns are also altered by the fracture.

Actions may be undertaken by a single nation (unilateral action) or by several nations. Such actions can provoke retaliation that further disrupt the global economy. These actions include the following:

1) Introduction of tariff or non-tariff barriers (on imports)
2) Measures to reduce both trade <u>and</u> inward investment (usually Foreign Direct Investment)
3) A 'trade war'
4) Comprehensive targeted national competition against given foreign nations

5) A systems war – opposition expressed in policy aimed at disabling a different 'system'
6) A cultural war – 'clash of civilizations' (Huntington 1996)

A trade war implies more than regulation against inward FDI and imports. It implies rhetoric against the competitor, measures to disrupt the target country's trade and investment relation, sanctions against nationals, firms and institutions of the target country and attempts to induce others ('allies') to follow similarly targeted policies. Action 4 involves identifying the target country as a comprehensive competitive threat including its government institutions, that will be alleged to be its driving trade and investment and its political institutions that are the driving intelligence behind the competitive threat. Action 5 is a deeper version of action 4 where the target nation is identified as a different (alien) system that is designed to achieve dominance, even hegemony, globally and must be attacked as a holistic 'system' seeking this end. Finally, in action 6 the foreign competitor is identified as a cultural (even existential) threat to the home country's way of operating (its culture) and deeper forces are alleged to underpin that competition.

This is far more than an upscaling of the 'level of analysis' from firms to systems. These deeper actions involve a characterization that pulls all institutions and modes of living into a single 'culture' or 'civilization' identified as inimical to the "home" system. Cooperation at any level of operation is ruled out (possibly as treachery) and complete and overt opposition at all levels results as the culmination of these policies. Empirically, it is arguable that US (or "Western") competition against Japan escalated in the 1980s and 1990s up to and including action 5 but rapidly de-escalated. It is further arguable that US (Western?) competition against China has reached action 6 at some points, but this has not been sustained or systematic so that the fracture has settled between actions 3 and 5.

The fracture cuts across global value chains. Routing of intermediate products through third countries could circumvent some regulation but smart regulations will be aware of this (and of false location indicators – "made in Vietnam" labels for Chinese products, for instance). Cooperation thus is not only restricted or prevented in direct relationships (imports/exports and foreign direct investment) but also in indirect relationships, so that all value chains across the fracture are jeopardized. At the limit, this could result in value chains being restricted to one side of the fracture or the other ("never the twain shall meet"). The replacing of foreign competition for 'internal' cooperation is a key feature of trade warfare.

The key source for theories of economic nationalism is Frederick List's (1841) treatise "The National System of Political Economy". In contradistinction to Adam Smith's (1776) "Wealth of Nations", List compared the increase in global wealth through free trade with the potential loss of wealth at an individual national level. List regarded a tariff on imports as an investment in a nation's future productivity and advocated the creation of a "national system of innovation" behind protective tariff walls. List believed in a long run conception of national growth, even at the expense of short-term gains. Lubinski and Wadhwani (2019) suggest that List offers a clear conception of the means by which nations and nationalism shape economic calculations. This is most useful for the analysis of multinational enterprise strategy. List also conceptualizes national identity as inherently aspirational - pointing to the long-term goals that need to be incorporated into a coherent response by MNEs. The upshot of this is that MNEs need to take a wider view of stakeholder interests in a situation of rising nationalism, including the social aspirations of natural communities.

Farrell and Newman (2020) draw attention to the limitations of government policy in producing a clean break fracture of the global economy. Using the term "chained globalization" they note "Instead of liberating governments and businesses, globalization has entangled them" (Farrell and Newman 2020 p70). The vulnerability, competition and control that comes with globalization cannot be completely eliminated by deliberate policy. Complete "decoupling" would cause losses because of interlinked networks of global supply chains, financial networks and information sharing through the internet. The control of risks in flows of money, goods, services and information has become a key source of international power. The building of parallel networks by China – notably Huawei's communications network, represents a massive challenge to US dominance of the global economy. The use of government fiat in "chained globalization" is fraught with dangers – attempting to interdict flows of rival networks can have severe unintended consequences for the perpetrators from damage to the domestic economy and provoking retaliation. Smashing links in international chains can have unintended consequences resulting in the loss of economic welfare for the perpetrator as well as the intended target. Policies designed to fracture the world economy have costs – for the target, for the instigator and for the global economy.

The approach to the national and international economy, under the generic title "mercantilism" assumes that international trade is a zero sum game. National power is paramount and this is achieved by accumulating "treasure" via a surplus on visible trade (as a war chest to fund armies). As Milgate and Stimson (2009, p35) say "Although mercantilism is customarily presented as essentially a view of state policy towards the economy, it also embodied an idea of civil society". This can be contrasted with the classical tradition from Adam Smith and David Ricardo to modern trade theories where comparative advantage leads to the maximization of world welfare. J.S. Mill argued that commerce caused mutual dependence and thereby was a force for peace (Mill 1844). This notion of extreme independencies induced by trade led Norman Angell (1910) to argue that the mutual benefits of trade were too great to spurn by war (or by a trade war). Angell's "rational pacifism" and belief in international rules and institutions was tragically disproven by the outbreak of the Great War of 1914-1918. Angell's argument was based on trade and financial flows ("credit and commercial contract"), and it is arguable that the modern international economy faces even greater costs of disruption through the fracturing of global value chains. The flows not only of trade but of direct investment, portfolio investment, financial and data flows across national boundaries have grown massively, particularly in the post -World War II period of rapid globalization. Nevertheless, the arguments for national sovereignty are frequently adduced to be positive, even in the face of the costs of fracturing international intercourse. Hirshman (1945. xvi) asked the pertinent question – "Is there in the trading system some inherent weakness which makes it vulnerable to the will of any government so minded to use it in the pursuit of power?" Such economic aggression depends on the structure of a country's trading pattern. If a country has a wide spread of its imports and exports equally among a large number of countries, then it can be said to have "economic independence" (xvii). Where a country has a monopolistic or monopsonistic position, it can use its bargaining power to influence the terms of trade. This can be amplified if that country also controls trade routes and has the potential to interrupt trade routes. Countries with bargaining power can choose “the economics of welfare” or the “economics of power”. Hirshman (1945) argues that trade has a supply effect and an influence effect. The supply effect includes building stocks of strategic materials, directing trade to “friendly or subject” nations (p34) and securing control of trade routes. The influence effect includes strategies to make it more difficult for trading partners to dispense entirely with the trade or to make it difficult for trading partners to shift trade to other countries. These policies increase national power at the expense of competitors. It is notable that these arguments apply with even more force to foreign direct investment, and to higher order trade and investment in technology, services, strategic products and certain vital raw materials such as “rare earths” essential in “green” technologies, clean energy and digital technologies (Pitron 2020). These strategies might be applicable to the underlying aims of the Belt and Road Initiative (BRI), “Dual Circulation theory” and “Military –Civil Fusion” of the People’s Republic of China. Momentum is building in both the US and EU towards carbon border taxes targeted at imports from countries that are lagging behind on climate action. Failure by China to make tougher commitments raises the risk that Washington and EU capitals will conclude firmer action on trade is the only way to ensure progress (Financial Times 2021). Carbon border taxes may have laudable aims but still have mercantilist outcomes.

It is notable that the fracture of the 2010s and 2020s is double sided in terms of policy. President Xi Jinping has not only sought to challenge the current world order via the Belt and Road Initiative but also the “Made in China 2025” campaign seeks to challenge US strategic industries such as semiconductors, robotics and Artificial Intelligence – even mandating all State Departments to remove foreign made computer equipment, within three years from 2019. It is notable however, that the Beijing Artificial Intelligence Principles (BAIP) 2019 are regarded as a best practice governance framework for AI research, development and usage that clearly aligns with commonly held international best practice. The picture globally is mixed but it is arguable that a “tech cold war” with

Listian and Mercantilist underpinnings is becoming a salient narrative in many centers of power over economic policy.

The Fracture and Chinese Narratives

Much of the debate on policy has taken a “Western” viewpoint**.** Lee and Lee (2020) point out that China has been successful in controlling and manipulating narratives about its “peaceful rise”. Three sets of narratives are evident. The first is the narrative aimed at neighboring countries in Asia. This narrative portrays China as rising from a vulnerable and unthreatening state to a comprehensive regional power. This narrative proposes a benevolent hierarchy of power and the inevitability of Chinese success. (This can be set against Deng Xiaoping’s emphasis on the depth of challenges facing China). This builds on the reclamation of “Middle Kingdom” status for China, emphasizing the permanence, longevity and greatness of Chinese “civilization”. For Asian consumption, the USA is portrayed as a distant power, but distance can be portrayed as a virtue. The US can argue that it enters when needed and that it is obliged to negotiate terms to “enter” Asia (as in two World Wars) and that it seeks consensus to do so. The second Chinese narrative is aimed at “the west” and centers on the mutuality of benefits arising from China’s growth, “win-win” scenarios and “special relationships” with favored states. The third, internal Chinese narrative is of unprecedented strength and the more assertive stance and policies combined with competence in execution. The “wolf-warrior” diplomats are agencies of this stance. The evidence is contained in the rapid growth and dominance of the Chinese economy. This is a high-risk game given internal structural imbalances, debt funded growth and high risk external adventures such as South China Sea claims (challenging the image of benevolence) and maneuvers and the exercise of unprecedented control on Hong Kong (the end of the one-country, two-systems, accommodation). Further, the narrative asserts that China does not need the West (USA). But China needs imports, markets, technology, knowledge and it is vulnerable to the West’s external policies. The Renminbi is not a global currency; it is not freely floating nor freely convertible. It has limits as a store of value. It is notable that BRI partners often demand payments in foreign currencies when partnering with Chinese firms. The Chinese State is described by the UK

Parliamentary "China Research Group" (CRG) as a giant venture capital fund, targeting areas deemed strategic by the State.

Three key policies define China's industrial strategy: The Belt and Road Initiative (BRI), "Made in China 2025" and" Civil-Military Fusion".

1 The Belt and Road Initiative

The BRI provokes "economic clientism" in host countries (Buckley 2020). The BRI is an attempt to install a China-centric business environment in host countries, allowing the entry of Chinese capital and influence on the back of loan financed infrastructure. For our purposes, it is a major contributor to the fracture in the global economy. The existence of a single "external environment" for all global operators can no longer be assumed.

2. "Made in China 2025"

While Beijing stopped publicly mentioning its "Made in China 2025" strategic industrial policy plan after its trade war with Washington started in 2018, the spirit of the plan lives on. One of China's main goals was to establish a number of world-leading multinational firms and industrial clusters in 10 cutting-edge technologies by 2025. In an interview with the state-run Xinhua (10 August 2020), Hao Peng, chairman and Communist Party secretary of the State-owned Assets Supervision and Administration Commission (SASAC), said state firms, particularly those owned by the central government, should team up with smaller firms to build up supply chains and form industrial clusters in sectors where China has a leading edge. The commission supervises the central government's state-owned assets, "Whether they are state-owned or private firms, they are all Chinese companies," Hao said. "The SASAC will firmly promote the integration of upstream and downstream enterprises with all types of ownership; and the integration of large, medium-sized and small firms; as well as coordinate the development of various market entities to jointly build a number of world-class enterprises." (Leng 2020)

More responsibility has also been given to the SASAC, a ministerial level organisation under the State Council, China's government cabinet. The commission's main job is to manage the 97 state firms owned by the central government, which had assets worth more than 80 trillion yuan (US$11.5 trillion) as of the end of 2018, according to the latest data available. "It is the inescapable responsibility of central government enterprises to take the initiative to build industrial chains and supply chains with enterprises of all types of ownership, and to jointly create a good industrial and economic environment," Hao said. Hao said that, in the first half of this year, collaborative investment between the central government's state-owned enterprises and the private sector totaled 110 billion yuan (US$15.82 billion) via various channels, including purchasing corporate shares and establishing new joint ventures, as well as through mergers and acquisitions. Hao also said that central state-owned firms planned to work with all types of companies "on a larger scale, and at a deeper level". It is unclear how the new mission for state-owned firms will work out. In the past, the government has been criticised for giving favourable treatment to state firms over private companies in spite of their low efficiency. The scale of insolvent state firms, known as "zombie companies", is still unknown. Foreign governments, particularly the United States and the European Union, have demanded that China cut back special treatment of state-owned firms to help create a "level playing field" for foreign companies to do business in China.

3. "Civil-Military Fusion"

The purported integration of civil institutions with the People's Liberation Army (PLA) in achieving greater mobilization powers is perhaps the most draconian policy of the PRC (Levesque 2017, Hamilton and Ohlberg 2020). It conjures images of China as a "campaign state" (Looney 2020)
The National Intelligence Law 2017 required all Chinese citizens to do "national intelligence work" (Hamilton and Ohlberg 2020, p97). The notions are not new in China, as Jenner (1992, p36) says, "All rights are only licenses held at the state's pleasure and revocable without notice".

The Military-Civil Fusion policy was written into the country's 13th Five Year Plan (2015). Its purpose was to modernize the military and to enhance its technological capacity by blurring the lines between civil and military research through an open sharing of science and technology. In practice, where a foreign company develops technology in collaboration with a Chinese partner, this can be re-purposed for a military use without the foreign company's consent. This "dual use" potential of technology require extreme due diligence on the part of non-Chinese companies and is a massive barrier to collaboration, especially after defensive (or retaliatory) measures by Western countries.

After the Fracture

Some commentators argue that the fracture is a simple, binary cut between "the US" (or "the West") versus "China" (e.g. Teece 2019). Others (e.g. Storper 2019) argue that a threefold "Triad" system is emerging where a "US system" based on innovation and the achievement of scale economies faces a system controlled by a centralized bureaucracy (China) and a "European" system of a regulated large market with thin capital markets that is not an innovation leader. Analyses that go beyond a simple bifurcation lead into "varieties of capitalism" type analyses (Hall and Soskice, 2001). In this paper, concentration is on the key fracture – between 'the West' and China. Similarly, Milanovic (2020) suggests that there are two forms of capitalism. The first is a 'liberal meritocratic form of capitalism…: a system that concentrates the vast majority of production in the private sector, ostensibly allows talent to rise and tries to guarantee opportunity for all through measures such as free schooling and inheritance taxes' (Milanovic 2020 p10-12). This he contrasts with "the state-led, political model of capitalism…This system privileges high economic growth and limits individual political and civic rights" (Milanovic 2020 p12). Both systems try to export their economic and political institutions – China through the Belt and Road Initiative, focusing on physical things whilst "the West" focusses on building institutions.

Analyses such as the above conflict with the radical unbundling of tasks in the global economy and the rise of "trade by wire" that enable MNEs (global factories) to coordinate activities remotely and allow geographically separate tasks to be integrated by a central intelligence - or by orchestration (Buckley 2018, Banalieva and Dhanaraj 2019). The development of technologies such as Blockchain are major aids to such strategies.

Multinationals therefore face two (new) conflicting pressures – political pressure to consolidate activities in one polity versus the ability to disperse activities through technological advances and managerial skill in a global orchestration of tasks. (Buckley and Casson 2020).

If we characterize the world economy as being divided by politics and protectionism into 'Listian polities', where commercial operations are intended (by politicians) to be confined to "their" polity by captive firms, the fracturing of the world economy means that captive firms within one polity are prevented from operating in other polities. This is more likely to be the case in technology intensive areas or activities where security (data security, technological security) is alleged to be involved. (The controversy on Huawei is a case in point). It is, however, possible that firms can contract across polities in 'neutral' (non-sensitive) activities that do not involve security issues. Thus, operations by captive firms (those domiciled in one polity) are largely constrained to be within that polity except where the firm can contract outside the polity without being subject to sanctions by government or by prejudice from ethnocentric consumers. Concealment of extra-polity activity may be a short-term option ("made in Vietnam" labels on Chinese-made goods) but is unlikely to viable in the long-run. Competitive advantage, under these circumstances, is derived by extracting maximum advantage from within one polity plus judicious exploitation of permitted outsourcing in other polities. Access to the resources of other polities may be licensed and thus may depend on the negotiating skills of firms – political advantages that may of course, veer into corruption. Corporate diplomacy (Henisz 2014) may be a veneer for political favoritism in cross-polity trade licensing. The dispersion of activities as mandated by technological advances may thus be constrained by political impediments.

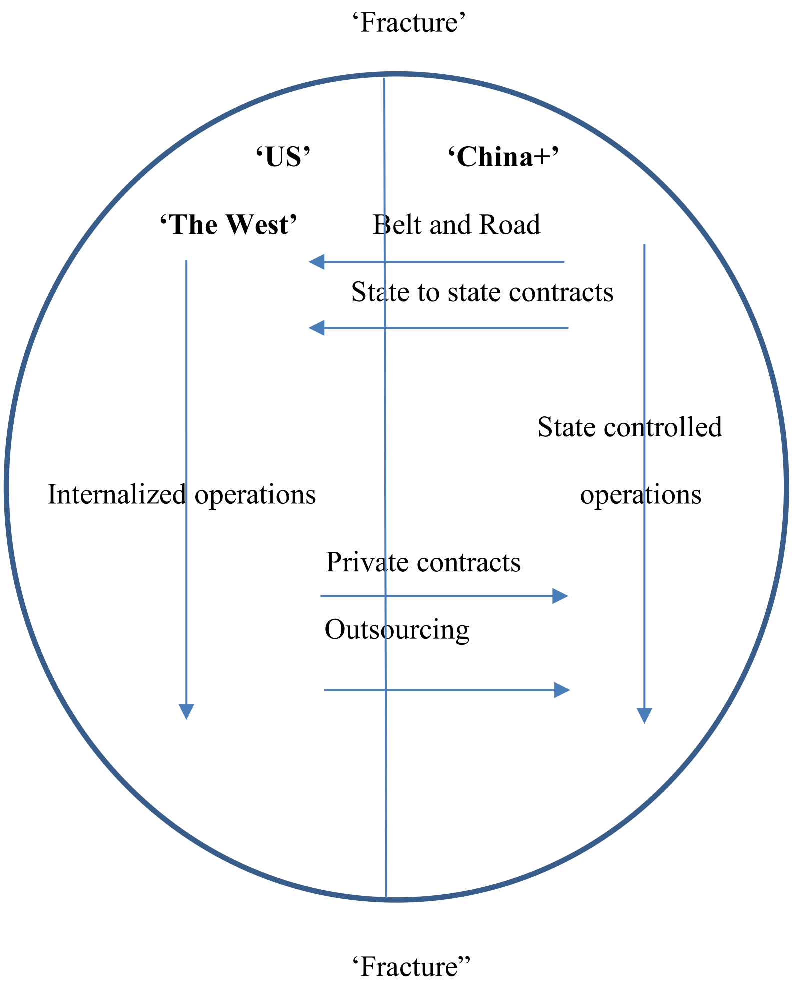

Figure 1: Schematic portrayal of bifurcated world economy (Two Listian polities).

A schematic portrayal of the bifurcated global economy is shown in Figure 1. The 'US' or 'the West' operates its economy by internalizing activities within firms and organizes its cross-fracture activities via private outsourcing contracts. This maintains internal control within private firms whilst minimizing risks from 'China+' (used as shorthand for China and its associated states) by arm's length contracting. In contrast, 'China+' operates by state directed activities and these are projected to the rest of the world under the Belt and Road Initiative (BRI), utilizing state-to-state contracts externally in infrastructure, resource and land acquisition. The external relations of both parts of the global economy enable congruence with internal activities – private contracting for 'the US' and state control via the BRI for China. External relations attempt to extend the home country's system of organization – private contracting or state driven operations - into other countries.

Exaggerating the Fracture?

This stylized picture may exaggerate the fracture. The DHL Global Connectedness Index (2020) examined four elements of global connectedness –flows of people, trade, capital and data flows. The trend for flows of people took an unprecedented dive, there was a modest decline in trade flows and a more severe fall in capital flows but information flows spiked following the COVID-19 pandemic.

The move of GVCs from China can be exaggerated. It is not easy to find locations that replicate the advantages of China. Japanese companies operating in China remain bullish about their operations in China and the prospects for the Chinese domestic market. Just 7.2% said that they were moving or considering moving production out of China in a September 2020 survey by JETRO, down from 9.2% in 2019. Naoto Saito, chief researcher at the Daiwa Institute of Research, said: "Japan Inc. is actually increasing its investment in China, while also seeking to set reasonable limits due to geopolitical risks, and remaining aware of avoiding overdependence." He added: "It's unthinkable for companies not to consider the Chinese market at all." (Obe 2021). Decoupling value chains from China has across a wide spectrum of industries, not been viable. Alternative locations with the myriad advantages of a Chinese location are simply not available, or only at prohibitive cost.

One important means of widening and perpetuating the fracture is for governments to attempt to ensure that their law have extraterritorial reach. Extraterritoriality of laws has become a major and growing barrier to cross-border trade and investment (see the International Chamber of Commerce

(2006)). In practice, only the USA is able to enforce the application of its laws extraterritorially. The Belt and Road initiative is an attempt to create a Chinese law and arbitration system in host countries. The fracture in the global economy is likely to accelerate these trends and to provoke international disputes on conflicting laws, regulations and jurisdictions. A potential crisis of legitimacy looms. One aspect of globalization that challenges the arguments for diminution of the fracture is the fracture (or fractures) of the internet that underpins global commerce.

The "Splinternet"

As O'Hara and Hall (2019) say, "the internet is open and interoperable, designed for growth. It is a network of networks, so we can talk about an "internet of internets". Technologies embodying different values can live in proximity, and several potential "internets" might together constitute the global internet. O'Hara and Hall (2019) posit four co-existing "internets" that have the requisite ethical vision, technological reality and sufficiently powerful institutional support to survive. They co-exist, in uneasy peace, each having ideals and engineering implementations backed by regulation and standards. The first may be termed the "Silicon Valley open internet", envisaging the free flow of data, as both a philosophical and engineering ideal. ("Open internet"). Second is the "Brussels bourgeois internet", also cherishing freedom, but within a framework of rights and good faith. The European Union is a prime mover, using the muscle of its Court of Justice to assert data-protection rights or copyright protections well beyond its jurisdiction. The third is the "District of Columbia (DC)" or "commercial internet", promoting data holders' property rights, and free-market co-ordination. The US Supreme Court has generally upheld this position, although it is under pressure from trustbusters in the US and elsewhere. The fourth is Beijing "paternal internet", a means of implementing social ideals. Most prominently, China's internet is a means not only of security and censorship, but also crowdsourcing social credit, and gathering data for effective artificial intelligence (AI) associated with Alipay (Alibaba) and WeChat Pay (Tencent). There is also a fifth model, which is less a vision, than a parasite, yet the extent of its disruptive power makes it influential on internet governance: the Moscow "spoiler model", encompassing the hacking ethic, and exploiting the free flow of data. Russia in particular has engineered an ideological space for cynicism and conspiracy theories. There is a dialectic between these models – all have their attractions, even the last, and none is held purely or exclusively by any nation or organization. They compete in courts, standards bodies and public opinion.

Data is an overwhelmingly important resource in the modern world. The control of data is a central target of Governments and corporations. The rise of the internet made data on private individuals a key battleground between companies and Governments. Much of this information was granted free to tech companies in the initial stages as a return for connectivity, privileged access to rewards, and price reductions. Now its value is recognized and possession has become much more contested. Access to the private data of one country's national by foreign companies and Governments caused political consternation and fueled protectionism. Political interventions, including "the Great Firewall of China", have splintered the previously largely globally integrated internet into several politically determined domains. However, cross holdings, the existence of shared interests, and information exchange are the beginnings of partial coordination across the fracture and the separated national hardware and software, and because overt ownership is not politically possible, cartels become optimal solutions (Buckley 2021, Buckley and Casson 2021). In view of the importance of an integrated internet for the internationalization strategy of companies, particularly "digital-first internationalizers", the fracture in the internet will inhibit future globalization (Banalieva and Dhanaraj 2019).

The splintering of an integrated internet will incentivize SMEs to internalize the imperfections created (Buckley and Casson 1976). In the West, large, well-endowed MNEs will be able to do this more easily than SMEs, thus increasing inequalities. Focal firms can offer their platforms as substitutes for an open internet, thus consolidating economic power. Costs of operating across splinters will increase and regional replication will create wasteful competition. In China, a separate internet consolidates State power. The fracture is thus exacerbated.

Mercantilism in Commodities and Data

Several exemplary cases illustrate modern mercantilism. In commodities, the case of rare earths essential for digital operations and for "green" technologies, in high-tech products and in data. Rare earths are largely sourced from China. They are not scarce, but the refining process is highly toxic and polluting and therefore is eschewed by many potential refining locations. (Pitron 2020). The use of export restrictions, even threatened restrictions, has many unintended consequences, most prominent among them the search by importing countries for substitutes. As early as February 2021, the Ministry of Trade, Industry and Energy in South Korea began working on an import source diversification plan to replace rare earth element imports from China. Canada and Australia are seen as alternative sources as more than half of Korea's rare earth imports were from China. New refineries will be opened and mothballed ones repurposed. Australia's "Modern Manufacturing Initiative" envisages increased production of rare earths with processing capacity in Australia (Thornhill 2021). Restrictions of supply bring forth substitutes. Only in situations of highly inelastic demand and restricted sources of supply are they likely to succeed (Hirshman 1945).

Similar sanctions are being brought to bear on China. China relies on the importation of high-tech components, biotechnology, life sciences, aerospace materials and applications, optoelectronics, and computer-integrated machinery. The response is predictable –increased investment in research and production in these fields and the search for substitute sources. In high-tech areas, sanctions may have short and even medium term effectiveness before "catch-up". Such strategies ratchet up the fracture, rivalry and tension between economic blocs.

Data is seen as a key commodity, barred from export. As shown above, the national capture and protection of data is a major cause for governments to implement policies to fracture the internet.

Covid-19 and the rise of the Biosecurity State

The role of national governments has become more salient following the large scale, almost universal action, to protect jobs and economic activity.

1. The conditionality of loans and grants (examples include provisions that corporations do not pay dividends and restrain executive pay, regional targets and "net zero" emissions).
2. Governments may continue to play an enhanced role in the economy. The conversion of loans to equity is a key possibility.
3. The issue of repayment conditions for loans and grants and its timing are crucial. This has implications for taxes (both corporate and individual), for public sector spending (which is unlikely to decline particularly in health and care services) and for Government budgeting.

Internationally, revenue authorities are likely to increase auditing and be stricter on compliance, Policies such as BEPS 2.0 and stricter rules on international transfer pricing were in place before the crisis and are likely to be tightened. All of this strengthens the primacy of national governments in the global system.

Many sovereign nations are operating on the precautionary principle with regard to the continued pandemic. Border closures and internal restrictions have interdicted GVCs. Individual nation state policies have taken precedence against globalist approaches to the supply of vaccines and medical supplies. Distribution channels have been centered on central or local state provision. State-controlled travel, migration, imports and exports, transport links, health authorities, public health and delivery (, laws, and regulations have become the norm. This has brought criticism in its perceived curtailment of human rights, including freedom of movement, assembly, education, speech, and the right to criticize the state. Individual states have accrued right to GVCs Ownership, Location, Governance and locus of innovation. This has posed threats to cross-border GVCs deemed to be sensitive to biosecurity including national export threats to "our vaccine". State bodies generally have played a deeper role in innovation and in strengthening intellectual property protection and in bringing together technologies in focused fashion to ensure biosecurity. These arguments are paralleled under concerns for food security.

Corporate Responses to the Fracturing of the Global Economy

The argument of this paper is that national mercantilist policies, the splintering of the internet and the rise of the biosecurity state mean that there is no longer a single "environment" for MNEs. This has profound implications for the strategy of MNEs in the long run. This section examines the responses of Western corporations to the policy-induced fracturing of the global economy. A later section examines non-Western companies.

The first response of corporations has to be the assessment of the degree and likely longevity of the fracturing of the global economy. If this is a temporary 'blip' in a generally upward trajectory of international cooperation and integration, then little needs to be done – small adjustments of strategy in location, outsourcing, governance and configuration of value chains and possibly branding (to adjust national identification) may be sufficient before 'normality' resumes. But what if the 'new normal' is disruption and fracture? Then strategy has to adjust and long term changes have to be implemented.

Following information gathering, one potential strategy is risk mitigation. Risk awareness and cultural/social sensitivity are increasingly important aspects of corporate strategy. Mitigation includes covering insurable risk, avoidance of high-risk countries as investment locations, breaking up large, salient investments into smaller units that may go under the radar, exiting sensitive industries, enhancing brand and IPR protection. Protectionist policies have reintroduced the notion of national sovereign risk. All of these strategies have negative economic consequences and are often inimical to corporate growth.

More fundamental changes will be to location strategy, to internal control versus outsourcing and to governance. Location strategy may have to be radically adjusted in order to effectively operate in the new fractured economy. Locations entirely within only one side of the fracture may be feasible. (It is unlikely that one company can manage two or more separate value chains on different sides of the fractures without becoming either two separate companies or being subject to punitive policies by one polity or the other). This may be complemented by judicious outsourcing of activities to ‘neutral’ or politically permissible locations. If foreign contract operation is not regarded as skeptically as foreign ownership (equity) by regulatory authorities, then outsourcing can give the flexibility in value chains to increase effectiveness in a fractured global economy.

Governance requires a great deal of attention and sensitivity to external circumstances in a fractured world economy. Working across the fracture may only be possible at arm’s length as ownership relationships and even joint ventures may be excluded on political grounds. If the fracture is not so severe, then globally integrated operations are likely to be ruled out, but not governance relationships that de-emphasize integration and emphasize autonomy in each territory –such as multi-domestic operations, where looser governance structures across fragmented territories.

The fracturing of the world economy does not mean that all (or even many) companies will relocate activities back in their home countries (“reshoring”) or even in nearby ones (“nearshoring). The normal rules of international business will still pertain. Companies will examine both their location strategy (“Where is the best location under current and predicted conditions?”) and their internationalization strategies (“What is the best means of carrying out this activity – ownership or outsourcing through contracts?”) and their interaction. If a low cost location is dictated for an activity - say one that is located in China – then it is highly likely that a new low cost location (Vietnam, Thailand or Malaysia for instance) will be chosen unless that activity can be automated, whereupon new location and internalization decisions will be mandated. Multinationals are constantly, and continually, monitoring location and internalization/outsourcing decisions so fractures, new regulations and changing technologies are key elements of these decisions.

Management of Global Value Chains

A McKinsey Global Institute report (2020) found that diversifying value chains –hedging and flexibility – was a more typical response than reshoring. Moreover, companies expected disruption to their value chains through external shocks and built in exposure to shocks as a key strategy. Shocks are defined to include financial crises, terrorism, extreme weather events, military conflict and pandemics. “Averaging across industries, companies can now expect supply chain disruptions lasting a month or longer to occur every 3.7 years, and the most severe events take a major financial toll” McKinsey Global Institute 2020, p3). It has to be remembered that GVC are complex, multi-tiered interconnected networks, so simple “one-size fits all” solutions cannot work. The corporate trend is towards scenario planning, attempting to created categories and likely magnitudes of shock and to reduce exposure where possible. This entails introducing “end-to end” transparency in value chains, minimizing exposure to likely shocks and building in rapid responses quickly when shocks hit. The fracture has ramifications for third countries throughout the world economy through GVCs. As an example, sanctions on Russia following the invasion of the Ukraine affect countries trading with Russia, who may be subject to “secondary” sanctions. This causes a forced reorganization of GVCs.

A return to multi-domestic organizations?

The trend away from global (or matrix) organizations back towards multi-domestic operations could be a reflection of the fragmentation of economies and disintegration in regional organizations such as NAFTA and the EU. The difficulty of coordinating activities across national boundaries is now increasing after a long period of decline in the increasingly fractured global economy. This is partly due to the increasing use of protectionism as an economic and political weapon (“trade wars”) but also because of heightened sensitivities about cultural differences and the protection of cultural identities at the “national” level. What is “a nation” has become contested. Independence movements such as Scotland and Catalonia co-exist with attempts to prevent “separatism” as in China, with Hong Kong, Tibet and Xinjiang as examples. Crossing “national” and “cultural” boundaries with a single uniform organization is becoming increasingly difficult. Doing so with a single brand name or corporate identity is even more problematic. Areas of heightened difficulty include products with cultural connotations such as film, television and social media.

As above with location and internalization decisions, so governance and internal organization have to be adapted to changing external conditions. Multi-domestic operations, more loosely coordinated at a global level, are an important step to managing a fractured global economy. So too are arm’s length dealing across the fracture, using contracts to substitute for contested foreign ownership. A revival of older style international business modes such as foreign distributors and agencies can traverse difficult political boundaries and regimes that restrict foreign ownership. Similarly, in high technology areas the revival of licensing is likely and in distribution/retailing, local franchises are an alternative to sales subsidiaries. In terms of “global factory” organization (Buckley 2018), looser forms of network structures are likely to gain prominence versus tighter ownership forms.

Multi-cultural operation may become increasingly difficult as the depth of the fracture increases and takes on cultural connotations. Restrictions on migration and the use of expatriates increases in difficulty and the use of technology as a substitute for the movement of people is likely to grow (Vahtera, Buckley, Aliyev, Clegg and Cross 2017, Vahtera, Buckley and Aliyev 2017). Virtual teams internationally can substitute for physical foreign operations – but only imperfectly because physical and real face-to-face contacts are hard to replicate in terms of operational efficiency.

The use of technology to cope with the fracture can be taken further via the use of “platforms” – transaction platforms to aid selling purchasing across borders, innovation platforms to empower innovation and information platforms for social exchange. Payment platforms facilitate this (subject to regulation). Platforms are important devices in the distribution of products and services. The use of platforms enables international connectivity but accessing the foreign location of a platform is not as sensitive as foreign direct investment location decisions. Routing access to the platform from ‘neutral’ or ‘third’ countries may reduce political sensitivities to foreign commercial links. “Opensourcing” rather than outsourcing can have similar effects. The digitization of commerce will certainly have short-term benefits in circumventing political barriers, but regulation will catch up.

The cartel as a strategic response

The multinational enterprise (MNE) and the cartel are alternative institutional arrangements for the exploitation of international monopoly power. (Buckley and Casson 2021). A cartel is an institution for implementing an agreement for the maintenance of prices or the limitation of outputs of independent producers (Casson 1985). The products have to be substitutes for such an arrangement to work. Cartels can be voluntary associations or Government mandated. They coordinate collusive behaviour and are particularly effective where there are obstacles to trade. Protection of national markets in whatever form--tariffs, quotas, bans, security concerns, prohibitions on inward foreign direct investments (including approval bodies such as CFIUS) all favor cartels over unified ownership MNEs. Where there is a high risk of expropriation, cartels reduce risks.

Cartels are most effective where there are few sellers and a high minimum efficient scale of operation. This includes manufacturing industries with economies of scale (microchips), mining industries where raw materials are geographically concentrated, transport including long-distance freight (volatile demand, rigid capacity constraints, long run economies of scale) and infrastructure. Cartels are least effective where products are varied, technology is rapidly changing, and where there is relatively easy entry from outside the sector. Cartels need to cope with costs of communication between the members and information costs. Cartels are likely to break up when innovation threatens their monopoly, and where integration into a global MNE is optimal following the end of obstacles to internalization.
In the short term, cartels can take the form of informal undertakings, price fixing quotas, pooling associations and associations for allocating contracts. In the medium term, cartels can take transitional forms such as sales syndicates, cartels with a dominant focal firm leader, or financial communities of interest. In the long term, trusts and holding companies mimic integrated multi-plant firms (Robinson 1941). Alliances between companies are sophisticated forms of the cartel, controlling "choke points"

in global product and service flows. Alliances too are flexible as regards longevity, and can be defined for a fixed period, or until a specified goal is achieved, or can be time-unlimited.

In the bifurcated world, cartels can take the form of local sales monopolies, organized systems of licensing and cross-licensing, and systemic contract allocation as well as new forms of holding companies. In the face of rising VUCA (volatility, uncertainty, complexity and ambiguity), collusion reduces unfavorable outcomes. International cartels link domestic multi-plant firms to replicate an MNE. Global dominance can follow a two-stage hierarchy of collusion – domestic monopolies colluding by entering a global cartel. This restores pre-fracture profitability by raising prices. Consequently, we may see tacit collusion and concealment to circumvent the fracture and avoid regulation. Working across political divides may result in new strategies and the science of business subterfuge may reach new heights. (Buckley 2021, Buckley and Casson 2021). Cartels thus present a negative, defensive mode of operation in the face of fragmentation of the world economy. There are also "positive" responses to these changes.

"Positive" corporate responses to nationalism

US multinationals have been criticized by politicians for 'kowtowing' to Chinese officials as they sought greater access to the Chinese market and to Chinese supply chains. Similarly, the social media platform TikTok is accused of carrying out Chinese government instructions, such as removing content based on Chinese sensitivities. This is in addition to the security concerns that have severely curtailed Huawei's international activities, particularly in the USA and Australia. Any companies operating across fractured political boundaries need to develop strategies to cope with clashing policy, security and other nationalist sentiments and sensitivities.

Nationalism is a major component element of anti-globalization. A recent piece, based on historical evidence, suggests several strategies that can be utilized to exploit host country nationalist sentiment (Lubinski and Wadhwani 2019). In analyzing colonial India, Lubinski and Wadhwani (2019) show

how firms can capitalize on the historical and aspirational attributes of national identity. Nationalism (in the host country) presents opportunities as well as risks for foreign entrants. One such strategy identified is "geopolitical jockeying" - political positioning to cultivate alliances with host-country stakeholders in ways that delegitimize rival multinationals from other countries. This is clearly a risky strategy as it risks retaliation from rivals (not just in the particular host country, but also around the world) and may conflict with the home country's political alliances and stances. Lubinski and Wadhwani's (2019) analysis suggests that specialized political capabilities are necessary including the gathering (and internal dissemination) of "intelligence" and engaging in symbolic and rhetorical communication to support the firm's political positioning. The following strategies are suggested:-

1) Discovering outsider opportunities
2) Developing politically motivated practices to accentuate differences vis-à-vis purported anti-nationalist entities including rival firms.
3) Negotiating pro-nationalist politics
4) Building political capabilities
5) Capitalizing on nationalism as a deliberate strategy

These strategies are evaluated in the summary section below.

Innovation and Industrial policy

Counterintuitively, rising tensions may stimulate investment and innovation and improve long-term prospects for innovating companies. Rivalries may stimulate innovation as in science and space travel in the "Cold War" between "the West" and "the Communist bloc". Investment may be stimulated in constructing diversified portfolios across the fracture by investment in uncorrelated stocks. Against this are ethical arguments and the fact that Chinese firms do not recognize the dividend paying culture and pay minimal dividends.

Human Rights

Vigilance on human rights is crucial for Western companies, It is essential that they "show their working" (to follow the advice of the China-Britain Business Council) across all aspects of operation and particularly their supply chains. Openness, honesty and transparency are vital. Companies must be prepared to vet all (potential) partners and publish complete lists of all associated companies. Advocates of a "broadband approach" to China have difficulty in finessing Uyghur oppression. Ultimately, attitudes to human rights could be the deepest fissure of all.

Non-Western Companies

Chinese firms do not have a choice – they are located in one side of the fracture. They are doubly threatened – by their own government's restrictions and by protectionist measures from foreign governments. The loss of the US market can be a severe blow as can restrictions on investment in US and allied territories particularly in tech-intensive sectors. The potential loss of dollar funding also requires a change of strategy. Inward FDI to China will also be impacted by anti-globalization policies. Some degree of forced decoupling will impede Chinese internationalization strategies. There is the limited possibility of doing business across the fracture via third countries and the intensive use of "non-market" strategies but more likely is retrenchment within the "Chinese" part of the global system or variants of multi-domestic and even cartel strategies to penetrate the divide.

Non-Chinese non-Western firms do have a choice. They can choose one part of the fracture or the other and regionalize their strategy within it, or they can attempt to do global business across the fracture. The latter approach may well involve separate regional Headquarters. Hybrid strategies may be possible if supplemented by careful non-market strategies and pro-nationalist strategies in separate locations. A separate international operation may be the solution. Nimble entrepreneurial strategies will be necessary for this class of firms caught in the middle of the fracture.

Implications for International Business Research

The fractured nature of the global economy (“chained globalization”, “slowbalization”, anti-globalization, protectionism and economic warfare) have an impact on the state of the art thinking in international business, both at the theoretical level and because of their implications for the practice of international management. As pointed out above, these political changes pull in an opposite direction to continuous advances in technology, enabling trade in tasks (an even finer level of fine-slicing (Buckley 2018)) and the increasing ability of management to orchestrate activities at a global level.

International Business Theory

Whilst there is a great deal of theory on international integration – across nations and industries – there is little theory of disintegration. It cannot be assumed that disintegration is a mirror image or inverse analogue of integration and so a fundamental re-thinking of theories of integration has to be undertaken leading to a theory of the dynamics of relations between nations and industries - to include both close relationships and fractures.

Fractures in internationalization require researchers to reinvent theories of protectionism including basic analyses, following List and variants of the “infant industry” approach (traditionally linked to Alexander Hamilton’s 1790 report on Manufacturers and List (1841)) where protected sectors are allowed to flourish behind tariff walls. Notably, this would apply to high-tech, highly research intensive sections particularly those with security implications (artificial intelligence for instance) or culturally sensitive areas (film, television).

A deeper issue than protectionism is a focus on the role of the state and the consequent “non-market” or political strategies of corporations. In the new fractured conditions, analysts cannot take “the environment” as fixed over time (dynamic changes) or across space (differences by country, region, territory) so simple analyses based on ‘internal’ (the firm) and an ‘external’ fixed environment must be avoided. The role of the firm as affecting and influencing the state is a key aspect of the interrelationship between firms and governments. Lobbying and all other aspects of non-market strategy reach a higher level of prominence and can no longer be taken as “theoretical add-ons” or optional choices – they are central to strategy and the modelling of strategy.

A further concept that is in need of theoretical restructuring is the ‘liability of foreignness’ (Zaheer 1995). In a simple sense, protectionism and trade wars make the liability of foreignness greater and make it weigh more heavily on foreign direct investment and internationalization strategies. However, smart strategies can mollify the burden of foreignness, and, as shown above, in certain cases can even make a virtue of particular types of foreignness. In these circumstances, liability if foreignness is a variable, a strategic target, not a fixed cost burden.

The fracture in globalization focusses research attention on distributional issues, that have been previously neglected in much IB theorizing. The protest against globalization and “populism” in general are fueled by increasing and salient mal-distribution in society – by income groups, age, region, gender and ethnicity. These elements need to be factored more carefully into IB theory.

International business research has focused largely on flows of capital, much less on flows of labour (except studies of expatriates). A key anti-globalization issue is that of international migration. Mass migration clearly has strong political effects. MNEs have generally favored international migration – at least those flows that provide (skilled) labor to favored locations. Conflicts around migration are neglected elements in IB theory.

In theorizing, international business researchers will no longer be able to assume a single external environment or single set of “exogenous changes” to which they have to respond. The fracture means that context matters more than ever and that a uniform global environment cannot be assumed for MNEs. Differentiated strategies are far more likely and careful distinctions will have to be drawn on “source” and “host” countries in the analysis of global business strategy and international management – the locations across which “international” business takes place will need to be more carefully specified in a post-fracture world.

In summary, the fracture in globalization and economic warfare urgently need to be added to those 'grand challenges' to which IB theory can contribute. (Buckley, Doh and Benischke 2017).

The Fracture and the Practice of International Management

This paper has shown that the fracture in the world trade and investment system is beginning to have profound effects on the practice of international management. Flexibility is needed in the responses of MNEs and therefore of individual managers. Corporate diplomacy becomes much more important because firms need greater identification with the countries in which (and with which) they do business. This requires a downplaying of ownership identity and positive identification of operations with their regional, national and local context. The balance between 'local' and 'global' shifts towards the former and issues of global coordination become much more complex and difficult, particularly any attempts at integration across the fracture.

New styles of management and governance are required. Partly this will come about by trial and error, but it could and should be informed by careful academic theorizing and the judicious application of the new theories. Management of 'global' value chains is the key to successful operation in a fractured and volatile global economy.

Summary - Corporate responses to the fracturing of the world economy

Multinational enterprises have learned to be flexible. Multiple panics, crises and downturns have been negotiated since the millennium. However, a rupture in the global trading and investment system creates a serious trauma in corporate international operations. Several strategies suggest themselves within the overall rubric of international operations.

1) The first requirement is keen intelligence on current and future developments. An information gathering and dissemination system is vital and with more diverse operations this needs to feed information to more levels in the corporation. Empowering “lower level” executives means that strategic information has to flow smoothly through the organization.
2) Location and externalization (outsourcing)/internalization decisions need to be thoroughly scrutinized. Some activities in the value chain will need to be relocated, others to be reevaluated in terms of mode of operation and some internal activities will need to be outsourced. An overall assessment of the interlocking of location and outsourcing strategies has to be undertaken regularly and thoroughly.
3) Governance structures have to be re-evaluated. Global operations become more problematic versus multi-domestic operations. Ownership modes become more risky versus licensing, franchising distributorships and agencies. Looser forms of operation require careful coordination. Although corporations do not need to own an activity to control it, contracts need to be fit for purpose and constantly reevaluated as circumstances change.
4) Digital and platform operations and virtual teams become more viable versus traditional methods such as ‘command and control’, the use of equity modes and expatriate operations. Again, this will have important consequences for holding corporate purpose together, for implementing strategy and coordinating geographically dispersed operations.
5) There are positive corporate responses to nationalism (as a component of anti-globalization). Building political capabilities is a key element but is fraught with danger from external political changes.
6) There is a need for corporations to revisit their international strategy to allow a long-term view of nationalist aspirations, including the social aspirations of host country citizens and the requirements of civil society in all the countries in which they operate. This requires a rebalancing of operations and considerations of reconciling the requirements of the host (and source) countries.
7) A wider-stakeholder conception of strategy is mandated as nationalism increases – this will have important implications for governance.

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