Abstract.

This chapter examines the ways in which transnational companies (TNCs) combine the advantages and power asymmetries conferred by transnationalization with opportunities generated by differences in regulatory regimes that stem from governance systems of the nation states. This allows them to develop strategies that further increase the asymmetries of power. The main regulatory regimes considered are: laws, customs and regulations related to the labour market and social security system; fiscal regimes; and regimes of incentives towards the attractions of inward foreign direct investment. It is argued that cross-country differences in these regulatory regimes provide special advantages to the TNC as the company that can truly plan, organize and control across different countries. Most advantages of transnationalization and regulatory regime differences are towards actors who – so far – have been unable to plan, organize and control across frontiers to the same extent as TNCs and in particular labour. With regard to the latter the chapter considers possible companies’ strategies of fragmentation: both geographical – by nation-states - and organizational fragmentation and their impact on labour and its bargaining power. The chapter considers also the impact of different governance systems on the following: (i) the bargaining power of TNCs vis-a-vis national governments; and (ii) the advantages towards rival companies that transnationality confers in the following areas: the acquisition and development of knowledge and innovation as well as the spreading of risks.

1 I am grateful to Mehmet Ugur and David Sunderland for useful comments on an earlier draft of this chapter.
1. Introduction

The transnational or multinational companies (TNCs or MNCs)\(^2\) are much talked about as if they were a totally different type of institution from the normal company or firm. Are they? And if they are, what makes them so? The distant antecedents of the transnational company can be dated back centuries to the Medici Bank in Renaissance Florence or to the seventeenth and nineteenth centuries trading companies from Northern Europe. Many business historians (Cox 1997; Jones 2002) agree that the main factor that led to the development of the TNC was the formation of joint stock companies.

Nonetheless a TNC is not just another joint stock company. What are the key elements that make a company a TNC? The defining element is operations across frontiers. But not just any type of cross-border operations. Imports and exports on their own are not operations that identify a company as a TNC. The specific characteristics that identify the TNC are: (a) ownership of assets abroad leading to (b) direct business operations; and (c) the ability to control those operations.

Control has two main connotations in the context of a TNC. The first connotation is the equity stake in the foreign enterprise. What percentage of the foreign assets must be owned by the main company for the latter to have control? The International Monetary Fund (1977) guidelines set a minimum of 10 per cent. Equity control is a necessary condition but not a sufficient condition to ensure control of operations and directions of the foreign concern. Equity control by itself does not lead to strategic managerial control if the means of exercising such control are not available. In particular, if the system of communications and the organization of the business across countries are not suitable for the exercise of such managerial control. This was indeed the case of much foreign business prior to the First World War when there was a considerable amount of foreign investment. There were, in fact, many enterprises whose assets were owned wholly or in large part by person or groups or companies in foreign countries (such as Britain or Holland). However, though the owners had controlling stakes in the businesses, they were not in a position to exercise managerial control because of the large distance between home and host countries and the poor transportation and communication systems. Wilkins (1988) has termed these businesses as ‘free-standing enterprises’ to highlight the fact that, though they were owned wholly or partially by foreign nationals (whether individuals or groups or companies), they were managed and developed as independent concerns.

The modern transnational corporation is characterised by having both equity control and ability to manage the foreign affiliates at a distance. In the last few decades the latter ability has been greatly enhanced by the following two key developments. (a) Improvement in the systems of transportation and communications; and (b) improvement in the system of internal organization of companies. These two developments are interlinked: easier transportation and communication – particularly via the information and communication technologies (ICTs) – led to changes in the internal organization of companies and the latter affected the increase in ICT intensity of companies.

---

\(^2\) The term transnational is used by the UNCTAD who had a specialized department/division dealing with TNCs since 1972. I prefer this term because it best conveys the fact that these companies plan, control and manage across several countries and not independently in each of them.
The relevant type of management in our context is the one related to the setting of strategic goals and the monitoring of performance, rather than the day-to-day operational management. The issue of strategies and strategic behaviour by TNCs is key to the approach taken in this contribution. It is argued that the existence of different governance system in different countries allows companies with operations across different nation-states to develop strategies that enhance the asymmetry of power between them and other actors with which they interact in the course of their business.

The chapter is organized as follows. First, we shall consider issues of transnationality, power and strategic behaviour (Section 2). In Section 3 three key dimensions of nation-states are identified. One of them is of particular relevance for the strategies of TNCs. Sections 4 analyse how TNCs may exploit the differences in governance/regulatory regimes to develop specific strategies for enhancing their asymmetry of power in relation to other actors such as labour, governments and suppliers. Section 5 discusses some of the advantages towards rival companies given by transnationality and specifically: acquisition and diffusion of knowledge and innovation and risk spreading. Section 6 consider the wider context and boundaries of the theory put forward in Sections 3 and 4. The last section summarizes and concludes.

2. Transnationality, power and strategic behaviour

In section 1 we mentioned how developments in the internal organization of companies contributed to their ability to grow and internationalize. In the relevant literature, developments in the internal organization of companies have been analyzed under several paradigms and particularly: the ‘strategy’, the ‘efficiency’, and the ‘institutionalist’ paradigms. Penrose (1959) sees the boundaries of the firm and its internal organization changing as the firm grows. Growth and growth strategies lead to changes in the internal organization and the latter facilitates further growth. On a similar vein Chandler (1962)’ historical narrative sees the internal organization of corporations evolving mainly in response to strategic objectives, in particular growth strategies. Chandler’s line is taken up by Stephen Hymer, the pioneer of the theory of international firms. Hymer (1970) analyses the relationship between the evolution in the internal structure of the firm and multinationality, in particular, how the former facilitated the latter.

Williamson (1975, 1981 and 1984) sees changes in the internal organization as driven by efficiency objectives; specifically, by the desire to economize on transactions costs, as well as to minimize the pursuit of individual goals and opportunistic behavior within the organization.

The institutionalist school sees the internal structure of companies - and of organizations in general – as evolving in response to the institutional environment in which they operate. The relevant institutional environment is delimited by the organizational field(s) of the company. The organization field of reference is loosely defined to include all agents who have some form of business interaction with the company, from suppliers to consumers to rival firms to regulatory agencies (DiMaggio and Powell 1983). Companies may straddle different organizational fields (Westney 2005). This is the case of diversified companies as well as of transnational companies. The former straddle several fields.

---

3 Many of the issues considered in sections 2-5 are developed in greater details in Ietto-Gillies (2005: chs 1, 2 and 15).
because of the different products they are involved in; the latter straddle different fields in relation to the different countries in which they operate. Diversified TNCs will have scope for interaction with a variety of fields connected with both their different products and the different countries in which they operate.

Operating across different organizational fields generates conflicts. Of particular relevance are the ones between a given subsidiary and the headquarters of the company to which it belongs and/or the same subsidiary and other units of the company located in various countries.

The management literature has dealt with the impact of institutional environments and organizational fields on the internal structure of firms including multinational companies (Westney 2005). What has received less attention is the impact of the institutional environment and related governance systems on companies’ strategic behaviour. The last topic is the subject of this chapter particularly with reference to the locational strategies of TNCs.

Strategic behaviour has many connotations and can be analyzed in relation to two specific dimensions: strategies towards ‘what’ (a) and towards ‘whom’ (b). Regarding (a), the ‘what’ is seen in relation to the activities of the firm such as: its products’ range; the markets it seeks to penetrate; its production processes; the technologies used; the organization of the production process; and the geographical configuration of its production activities. As regards (b), the analysis of strategic behavior is in relation to specific actors such as: rival companies; consumers; suppliers, distributors and sub-contractors; the labour force; and governments.

Closely linked to the latter issue is the relationship between strategic behaviour and power. Zetlin (1974: 1090) argues that power “…is essentially relative and relational: how much power, with respect to whom?” Following Fred Hirsch, Pagano (2003) sees power and prestige as positional goods, a view that echoes Zetlin’s characterization. It follows from this view that: ‘…power and status are zero-sum goods and the increase in the positive consumption of positional goods by some individuals brings about an increase in negative consumption by some other individuals.’ (641)

In the economics/business literature companies’ power has usually been analysed mainly in relation to market power and therefore with respect to rival firms. However, power may also relate to other players in the economic system and specifically to labour, governments, suppliers/distributors, subcontractors or buyers/consumers.

A strategic use of power can aid the resolution of conflicts between the specific company under analysis and other agents. The conflicts are usually over distributional issues arising from production or market conditions. In the case of conflicts with rivals the distribution relates to market shares; in the case of labour, the conflict is over distribution between profits and wages; in the case of conflicts with governments the issue is distribution over the overall surplus and how much should go to the private or public sphere (via taxation or financial incentives or subsidies).

In the next three sections we shall analyse how transnationality generates opportunities for strategic behaviour by firms operating across nation-states. The strategic behaviour considered will focus on labour, governments and suppliers and, to a lesser extent, on rival companies. This is not because the latter is not considered important but mainly because many aspects of it have been well covered in the literature. In fact, in the international business literature the strategic behaviour towards rivals has been considered by many authors in the context of developing theories of why companies operate across...
frontiers and which modalities they employ. The strategic behaviour towards rivals is considered in Hymer (1960), Vernon (1966), Knickerbocker (1973) and Cowling and Sugden (1987).


3. TNCs and the nation-states.

In this section we shall consider the relevance of national frontiers and their different dimensions for the strategic behaviour of companies. At the semantic level transnationalization implies the existence of national borders. In this sense we can say that in a world with no nation-states there would be no TNCs meaning that we would not characterize a company as a TNC just as we do not currently attach a special label (such as ‘trans-regional’) to companies that operate in many regions of the same country.

But the issue is much deeper than the attribution of labels. We do specific studies of companies that invest across nation-states but not of companies that invest across regions of the same nation-state. In other words we attach relevance to the origin/nationality/identity of the investor in the case of trans-national operations but not in the case of trans-regional operations. There is one area of economics, within the confines of the nation-state, in which, traditionally, the identity of the investor has been considered important: the case of public v private sector investment. The main reason for this is the fact that public sector investors are supposed to have different aims from the private sector one: social aims versus profits aims. However, this does not apply to investment across frontiers versus investment within the same nation-state. In both cases we are talking of private companies motivated by profits. The objectives remain the same whether the company invests within a single nation-state or across several of them. What differs is not the aim but the strategies and opportunities for strategies. Operations across nation-states give opportunities for specific additional strategies that do not exist – or not to the same extent – within the confines of a single nation-state. These opportunities arise from the specific governance systems of nation states.

This raises the wider issue of the relationship between nation-states and companies and of the importance of the nation-state for companies. Is there something specific to the nation-state (and of relevance to corporations) which is not to be found at the level of regions within a country?

In order to tackle these issues it is helpful to consider the key dimensions of nation-states and of operating across national frontiers. They are: spatial or geographic dimension; cultural dimension; and regulatory regimes dimension.

The spatial/geographic dimension has to do with distance between locations and its relevance is largely linked to transportation and transaction costs. The distance between

---

4 All the theories cited in this chapter – as well as others – are summarized and critically analyzed in Ietto-Gillies (2005: Part III).
locations in different nation-states is often greater than the distance between locations within the same nation-state. But this is not always the case. For example, the spatial distance between Turin and Palermo is greater than the one between Turin and Geneva. Similarly, the distance between New York and Montreal is less than the one between New York and San Francisco.

The **linguistic/cultural dimension** - particularly the business culture element - affects the operations of companies in terms of transaction, organizational and managerial costs. The cultural distance is usually greater between nation-states than between regions of the same nation-state. But again, this is not always the case. Regions close to the border of two nation-states often have more similar business cultures than distant regions within the same nation-state.

The **regulatory regimes dimension** encompasses the sets of laws, regulations and customs governing the economic, social and political life of a country. It includes the regulations governing production, markets and the movement of resources across countries. These regulations stem directly from a country’s system of economic governance\(^5\) and related institutions. Countries differ in their system of governance and specifically with regard to the sets of regulations just mentioned. These differences often have historical as well as political roots. Regulatory regimes tend to differ – sometimes substantially – between different nation-states. However, they tend to be more homogeneous and consistent within each nation-state.

In this perspective the nation-state can be seen as the locus of a set of ‘regulatory regimes’. These comprise the set of specific rules and regulations – emerging from the overall governance system and related institutions - which affect people, firms and wider organizations directly and in terms of their business relationships. Some of these rules and regulations stem from the legal or institutional system, some from government policies; several have more than one connotation, i.e. they incorporate legal, institutional and/or policy elements. In relation to the business world, the following nation-states’ regulatory regimes are of particular relevance: (a) rules and regulations regarding the social security system and in particular different regimes regarding labour and its organization; (b) fiscal regimes; (c) regime of industrial policy with regard financial and other incentives to business; (d) currency regimes; and (e) rules and regulations regarding environmental and safety standards\(^6\). In the next section we shall concentrate on the first three only of these regimes.

All three regulatory regimes dimensions (geographical, cultural and regulatory) discussed here have **cost implications**. A company operating across frontiers may face additional costs and risks ranging from transportation and transactions costs to managerial and organization costs. They include also costs specific to the third dimension such as: costs of insurance against risks of currency fluctuations; additional costs of acquiring information about fiscal, social security and environmental standards regulations in other countries as well as information about their labour market conditions; costs of mastering – and managing in the context of - different laws, regulations, customs and their institutions.

---

\(^5\) The term and concept of governance are rather fuzzy and wide-ranging (Dixit 2008) and the Oxford English Dictionary gives several definitions. The ones relevant to this chapter relate to governance as: ‘the manner in which something is governed or regulated; …system of regulations;…’

\(^6\) On the latter issue The Guardian (2010) reports that Transocean, the owner of the rig leased by BP in Gulf of Mexico disastrous oil exploration, was registered in The Marshall Islands and possibly responsible to their governmental institutions for environmental and safety standards.
However, there are also advantages of operating across frontiers and these advantages can – to a large extent – explain the huge increase in FDI since WWII. Erturk (2011) points out how globalization increases the asymmetry in power relations. The TNCs are in such a position because they can truly plan, organise and control across frontiers. They can also develop strategies to take advantage of differences in regulatory regimes across frontiers. The asymmetry of power emerges because many of the agents with which they interact cannot plan and organise across national frontiers, or not to the same extent as the TNCs. These agents at the other end of the TNCs’ asymmetric power relation are: labour; governmental agencies; suppliers; and rival firms. The asymmetry derives from the advantages that transnationality gives them in terms of bargaining with labour, in negotiations with suppliers and in dealings with national and regional governments.

In addition to these, transnationality can give companies advantages also with regard to the following: acquisition of knowledge and innovation; and risk spreading. These advantages can lead to – or further enhance - the asymmetry of power towards rival firms.

4. Transnationality enhances asymmetry of power

As already mentioned most international business literature on companies’ strategic behaviour has concentrated on strategies towards rivals rather than on strategic behaviour towards other actors. Yet companies face other relevant actors in connection with their business activities, particularly labour, governments and suppliers. From the perspective of the company and its profitability the best position to be in is one in which it has power over its rivals as well as other actors.

Transnationality and power towards labour

The power relations of companies towards rivals and towards labour are affected by two different aspects of the organization of production: specifically, the market concentration and the internationalization of production activities. Both market concentration and internationalization have increased in the decades immediately after WWII. However, the last quarter of the XXth century saw considerable changes in the companies’ strategic behaviour with respect to the organization of production and the production process. Specifically, changes in the organization of the production process within and between firms and changes in the companies’ strategies towards the geographical location of their activities. In the late 70s, 80s and to some extent also the 90s many large companies have been downsizing i.e. outsourcing the production of part of their activities, usually the non-core part but, at times, some core activities as well. This means that whereas the decades following WWII have seen an increase in the internalization of production activities, the later decades of the century have seen the opposite process: many large firms have subcontracted part of their activities to smaller firms who are usually independent in terms of ownership though, often, dependent in terms of strategic control of their activities (Cowling and Sugden 1987). The same late decades of the XXth century have also seen acceleration in the expansion of activities abroad by large companies some on an internalized basis and some outsourced to smaller firms in foreign countries.

The explanation of these historical patterns can be aided if we see them in the context of possible strategies of companies towards labour. The concentration of production leads to oligopolies and thus to market power. However, it may - at the same time -
strengthen the power of labour because labour employed within the same ownership unit – that is within business enterprises all belonging to the same company - may find it easier to organise and take action compared to a situation in which it is dispersed across units belonging to different owners.

As regards the international location of production, labour has, traditionally, found it easier to organize and resist when working within the same country. Spatial proximity, shared condition of labour and shared contractual obligations lay the foundations for easier organization and resistance. Moreover, shared historical, cultural and social environments give labour a stronger feeling of solidarity. On the whole, the differentials in the actual and potential for labour organisation and for bargaining power are higher between countries separated by institutional, political, cultural, legal and governance borders than within each border. We can characterize areas of ‘labour organisation regimes’ as those geographical areas within which – ceteris paribus - labour finds it easy to organise itself effectively due to shared cultures, institutions, legal framework and working conditions.

This discussion leads to the identification of two main dimensions in the organization of production: (a) an ownership dimension by which we mean to capture whether or to what extent the firm internalizes its production activities or uses external, arm’s length transactions with other firms for part of its value chain activities; and (b) a geographic dimension which captures the extent to which production activities take place within the same (or near-by) locations or the extent to which they are dispersed in several locations. In the latter context of particularly relevance is whether the activities are located in different nation-states for the reason explained below; or (c) a mixture of ownership and geographic dimension. The latter is a combination of dimensions (a) and (b).

Companies within a sector may – ceteris paribus – face a more powerful labour force when the same is employed: (i) within the same company/institution rather than being dispersed into many; and (ii) within the same country. It is in the interest of companies to develop strategies that increase their power towards labour while not diminishing – and possibly increasing – their power over rivals. Possible strategies in this direction involve the segmentation/fragmentation of labour while retaining their market power. Two specific types of fragmentation strategies are possible and have been followed: (i) organisational fragmentation through the externalisation of some activities; and (ii) geographical (by nation-state) fragmentation through the location of production in various countries characterized by different regulatory regimes.

The organizational fragmentation can involve various degrees of externalisation of production: from full out-sourcing and use of market transactions to varying degrees of control through sub-contracting and similar arrangements; from the employment of labour full time and on permanent contracts to the casualization of labour (Ietto-Gillies, 2002: ch. 3). Some of the externalization routes – such as sub-contracting – allow the company considerable control of production without the added responsibility for the labour employed.

The second strategy involves the spread of production in countries/areas not linked by common labour organisation regimes i.e areas that have different trade unions and/or different labour and social security laws, regulations and standards. These elements make the organisation of labour and its resistance to the demands of capital more difficult. In this case fragmentation takes a geographical (by nation-states) route. This involves the dispersion of production over many nation-states, albeit within the internal, hierarchical organisation route. Some degree of both geographical and organisational dispersion and
fragmentation is also possible for example through cross-countries externalization such as international sub-contracting. The two fragmentation strategies reinforce each other in the labour fragmentation potential and therefore in the difficulties they generate for the organisation and resistance of labour in its bargaining with capital.

Two consequences derive from this analysis, both relevant for TNCs’ strategic decision in terms of the location of international production. First, that *ceteris paribus* companies may seek to locate in areas of weak labour organisation regimes; thus foreign direct investment would flow *ceteris paribus* from areas of strong labour organisation regimes towards areas of weak regimes (i.e. areas where labour is in a weak position).

Second, even if the differentials in labour organisation regimes across nation-states are not high, the *dispersion* of employment across many countries - though within the same company – *fragments/segments the employed labour force* and thus makes its organisation more difficult and its bargaining position weaker. Such dispersion gives a stronger position to companies *vis-à-vis* labour compared to a situation in which the growth of production within the same company were to occur all or most within a single country. Thus, we have a situation in which the *internationalization of production per sé may give companies advantages towards its labour force.*

The organizational pattern of production that arose from the late 70s onwards – outsourcing and increased international location – can be seen, partly, as a strategic reaction by companies to the increased power of labour in the decades after WWII. The latter being aided by the concentration of production into large units (often developed in the same site or in spatially close sites).

Our analysis goes some way towards explaining why (a) the largest share (69.6%) of the stock of inward FDI is directed towards developed countries as well as originating in the same group of countries (84.3%)7; and (b) large amounts of FDI are horizontal8. Companies keen to source foreign markets can produce most of their output in the home country and source foreign markets via exports or they can produce directly abroad near their foreign markets. In the first case they would be likely to face a stronger workforce – *ceteris paribus* – than in the second case, for the reasons explained above. The large amounts of horizontal FDI in countries with large markets – other developed countries – is therefore taken as a sign of a possible geographic fragmentation strategy.

Strategies that are successful in enhancing bargaining power of companies towards labour are likely to affect the distribution between wages and profits.

*Transnationality and power towards suppliers*

Let us now consider the issue of asymmetry of power towards other actors. Operations across different nation-states can enhance the bargaining power of companies towards suppliers and governments. The existence of multiple sourcing channels (whether actual or potential) in the various countries gives the TNCs a powerful bargaining position towards suppliers. This is particularly the case because many suppliers have specific characteristics which makes them liable to low bargaining power with large TNCs. In particular: (a)

---

7 Data refer to 2009 and are from UNCTAD (2010: Annex table 2, p. 172).

8 There is also a large amount of intra-industry FDI world wide (Dunning and Norman, 1986; Alfaro and Charlton 2009). However, it should be noted that intra-industry FDI is connected to both vertical and horizontal FDI.
suppliers are often smaller companies operating in a more competitive environment than their customer; (ii) they are often located in developing countries; (iii) they cannot easily develop alternative international networks. In this situation it is not difficult to see how a big TNC with a large transnational network and which can rely on several actual or potential suppliers will use its international position to enhance its bargaining power towards specific suppliers.

Transnationality and power towards governments

Having production locations and business activities in several nation-states can also give the company a strong bargaining position towards governments of the nation-states and their regions. Transnational companies can – and do – play governments of different countries or regions against each other with the objective of raising the offer of incentives for the location of inward FDI (Oman, 2000; Phelps and Raines, 2002). For example, the lack of fiscal harmonization within the EU has led to competition by governments for attracting foreign companies – sometimes only nominally rather than with jobs and capital relocation – via lower and lower rates of corporation tax\(^9\). Moreover, if a company has production facilities in many countries its threat of relocation (Kogut 1983) becomes very credible and can be used as bargaining power with governments to gain high incentives.

There are further advantages to be gained by a company with direct business activities in different nation-states. The latter, as loci of different governance systems and regulatory regimes are also loci of specific taxation regimes. Operating across several such regimes puts the company in a position to minimize its world-wide tax liability via the manipulation of transfer prices, i.e. prices charged for the exchange of goods and services within the firm but across national frontiers\(^{10}\) (Ietto-Gillies 2005: ch. 20).

In the last analysis all these strategies aim to shift the distribution of the surplus from the social sphere (of government and taxpayers) to the private sphere of companies.

5. Advantages of transnationality towards rivals

The various types of strategic behaviour we have discussed in Section 4 increase power in bargaining with labour or governments or suppliers. Are there also advantages to be gained towards rivals? A better bargaining position towards these actors puts the company in a stronger position also vis-à-vis rival companies. Any advantages towards labour and/or governments deriving from location strategies and leading to higher profits can be turned into indirect advantages towards rivals as it increases the potential for higher market shares.

There are, however, other specific elements of transnationality that may enhance the TNC’s power towards rivals, particularly in terms of innovation acquisition and development and of risk spreading. The locational diversification of technological and production activities allows the company to learn from its environment and thus to increase its overall ownership advantages (Cantwell 1989; Castellani and Zanfei 2006). Various units within the company – be they the headquarters or subsidiaries – form an internal network within which there is exchange of knowledge, innovation and technology.

\(^9\) See the case of Ireland where very low rates of corporation tax have upset other European governments while not being much benefit in her unfolding (as I write) economic and political crisis.

\(^{10}\) OECD (2010) gives detailed guidelines on how to detect transfer prices manipulation
The exchanges are often facilitated by movements of highly-skilled personnel whose flows have been increasing worldwide (Salt 1997; OECD 2002). Moreover, each company unit will be in contact with the innovation context and system of the country in which it operates. The unit learns from these locational contexts and then transmits the acquired knowledge to other parts of the company via the latter’s internal network. Often the learning from the locational context and system is heightened by formal innovation-based collaborative agreements leading to external networks (Frenz and Ietto-Gillies 2009). Other external networks can also lead to learning and acquisition of knowledge such as the networks linking subsidiaries to their local suppliers and customers. The two types of networks, internal to the company and external to it, operate together to facilitate the diffusion of knowledge and innovation, with significant effects for the local businesses, the TNCs and the various countries (home and hosts) in which they operate. Thus the geographically-fragmented configuration of production activities increases the scope for diffusion of knowledge and innovation. This advantage in knowledge acquisition can be turned into a competitive advantage towards companies which are less internationalized and, therefore, less able to tap into international sources of knowledge and innovation.

A further advantage is connected with risk spreading. A strategy of dispersion of production and multiple sourcing can also be a diversification strategy which allows the spread of the risks of disruptions to production due, for example, to political upheavals or industrial disputes in any one country. Disruptions to production can come about also through other problems such as natural disasters. Most risks linked to the latter are not nation-specific but are more likely to be specific to the physical and geographical environment. However, the ability of countries to cope with them and to minimize risks and costs for business is, to a large extent, nation-specific and thus specific to the social, economic and governance environment and not just to the physical environment. Thus a strategy of fragmentation by nation-states may become also a strategy of geographical diversification in order to spread risks deriving from the social and political as well as the physical environment. This enhances the TNC’s advantages towards those rival firms which are not internationalized or not to the same extent.

6. Wider context and boundaries

Sections 4 and 5 developed a theory of the TNC that emphasizes the advantages that transnationality confers to companies in terms of enhancement of power towards labour, suppliers, governments as well as rival companies. From a simple reading of such a theory one might conclude that transnationality is all a bed of roses. In other words that the higher the level of internationalization the higher the advantages for companies. I would now like to discuss the boundaries and limitations of such an extreme conclusion.

In general, do companies derive only advantages from a strategy of fragmentation of production across different nation-states? The answer is certainly negative. First of all,

---

11 Rugman (1979) suggests that the international spread of activities may be a risk diversification strategy on the part of the company.
because the fragmentation strategy may lead to higher unit costs if it requires operating below the most efficient size in some, if not all, the locations. Moreover, the diversity of regulatory regimes across which TNCs operate may, in itself, generate extra costs and uncertainties. For example, different currencies generate transaction costs; exchange rates fluctuations may bring losses as well as gains; operating across different cultures, governance and institutional contexts may result in higher transaction, organizational and managerial costs.

But there are wider caveats and limitations. First with regards to labour. Are outsourcing strategies and international location of production to be interpreted only in terms of strategic behaviour towards labour? The answer is emphatically: no. There are many other reasons why companies want to outsource (such as the achievement of more flexibility of supply to demand conditions or the lowering of fixed costs) and want to locate abroad (such as proximity to markets or sources of materials or of labour). However, whatever the reasons – and there are likely to be several – one of the outcomes is that both outsourcing strategies and international location of production lead to a weakening of the employed labour; it therefore increases the asymmetry of power between the company and its workforce.

Another caveat arises from the assumption on social security regimes or the tax regime or that of incentives towards inward FDI. In the real world some countries are fully centralized and their governance system with respect to social security, fiscal regimes and industrial policy apply throughout. In others there is regional decentralization and the regulatory regimes differ from region to region of the same country such as regions of the UK or States within the US. This is sometimes the case with regard to fiscal regimes and with regard the possibility of specific regional development institutions offering attractive packages for inward investment. However, the degree to which regions’ regulatory regimes differ tends to be not as high as that between nation-states. To the extent that they differ, TNCs can bargain with regional governments – and play one against the other – as well as with national governments.

In the last couple of decades we have seen increasing calls for decentralization and more fiscal and labour markets autonomy for the regions. This has been – and is – very much in evidence at the political level for example in Italy. But similar sentiments have also been voiced in more academic circles. Ohmae (1995) strongly argues for the formation of strong regions free to bargain with TNCs directly without having to go via the institutions of the nation-state of which they are part. He advocates the formation of region-states oriented towards the global economy rather than the national economy. He writes:

‘Region states…are economic not political units, and they are anything but local in focus. They may lie within the border of an established nation state, but they are such powerful engine of development because their primary orientation is toward – and their primary linkage is with – the global economy. They are, in fact, among the most reliable ports of entry.’ (pp. 88-9)

According to my analysis the region-states advocated by Ohmae would lead to competition between different regions of the same nation-state for the attraction of inward investment. This is a situation which favours the TNCs in their bargaining for special concessions. Reliable ports of entry yes, but for whom and in whose interest?
A last point to make is that there have been attempts at forging cross-country links between trade unions (The Guardian, 2007). However, the aftermath of the 2008 financial crisis is not likely to foster international cross-countries solidarity of the workforce. Quite the contrary as each labourer, union and indeed government wants to protect jobs in their own country.

The latter point is illustrated by the case of FIAT, the Italian motor car manufactures in its bargaining with the workforce in Pomigliano, Southern Italy in the winter and spring 2010. The company management had put two alternatives for their investment strategies: investing in Pomigliano or in Poland. The first alternative was conditional on the Italian workforce accepting a new contract which offered much worse conditions than the existing one, including clauses deemed unconstitutional by some lawyers. In this case asymmetric power towards Polish and Italian workers was being used to further the asymmetry of power towards the Pomigliano workforce. As far as I know the Italian trade unions negotiated to secure the investment in Pomigliano at the cost of jobs in Poland. They could hardly do anything else. Their bargaining power was reduced by competing with the Polish workers as well as by division within the three main negotiating unions, allied to different political parties.

7. Summary and conclusions

The paper starts with a discussion of ownership and organizational control within companies. This leads to a discussion of organizational structures. The focus then moves on the links between governance, institutions and strategic behavior of companies. A discussion of different dimensions of nation-states leads to an analysis of the opportunities and scope generated by nation-states for companies that can plan, organize, manage and control across frontiers. The nation-states are considered in terms of spatial, cultural/linguistic and regulatory regimes dimensions.

It is argued that differentials in regulatory regimes between different countries create scope for advantages and for strategic behaviour by TNCs. The strategic behaviour is seen in relation to other actors: labour, suppliers, governments as well as rival firms in relation to elements such as knowledge acquisition and risk spreading.

Why do we need a special study of the TNCs? Because nation-states differ in their governance, institutions and specific regulatory regimes. These differences allow companies operating across different nation-states to take advantage by developing specific strategies. Assume for a moment a hypothetical world in which nation-states did not exist and the whole world were governed from one centre with the same type of institutions and governance system. In such a world we would not need to develop special studies and theories of the transnational corporations. We would, instead operate within the parameters of location theory and economic geography to explain why firms invest in a specific locality.

In our real world we have nation-states characterized by different dimensions - as argued in section 3 - and, in particular, by different governance systems, institutions and related regulatory regimes. I refer in particular to: systems of governance and institutions regarding taxation or labour markets. On the latter a big role is played by the governance system related to trade unions, by those that regulate the social security system in a country and by the wider governance that affects the labour market such as immigration controls or obstacles to the emigration of skilled labour.
Different regulatory regimes in different nation-states put the TNCs in an advantageous position in their bargaining with other actors such as labour, suppliers and governments (Section 4). Transnationalism gives companies also additional advantages in terms of acquisition of knowledge and of risk spreading (Section 5). These overall advantages can be used to develop strategies that further widen the asymmetry of power between TNCs and other actors who do not have transnational power - or not to the same extent – such as labour, governments and uninalational (or not very internationalized) companies. The boundaries and wider context of the theory are discussed in Section 6.

The enhanced asymmetry of power, derived from strategies linked to transnationality, has distributional implications: with regard the distribution between wages and profits and the distribution of the economic surplus between the social and private sphere. Our analysis has also strategy and policy implications for other actors. In general labour and governments should avoid strategies that generate scope for further fragmentation such as collision between trade unions and/or workers in different sectors or countries. There should be caution in embracing political moves towards regional fragmentation of regulatory regimes. Though decentralization of power to the regions does bring some benefits, it may also result in stronger bargaining power for TNCs in their dealings with local or regional governments. At the level of the EU, harmonization of social security and fiscal regimes would strengthen the power of labour and governments. In general, labour and governments should work towards strategies leading to the development of what Galbraith (1957) labelled ‘countervailing power’.

References


Knickerbocker, F. T. (1973), Oligopolistic Reaction and Multinational Enterprise. Cambridge, MA: Division of Research, Graduate School of Business Administration, Harvard University.


The Guardian (2010), ‘Congress raises safety concerns over rig’s marshall Islands flag’ May 31st.


