Multinationals and NGOs amid a changing balance of power

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Contemporary debates about international economic governance confront something of a puzzle. In one sense, global economic governance is in crisis: global financial reform proposals remain divisive and the WTO negotiations are moribund, a state of affairs in which a lack of corporate interest is strongly implicated.[1] At the same time, private regulatory regimes run by and for multinational firms appear to be proliferating and, in spite of a deep global recession, we have not seen international commerce collapse into beggar-thy-neighbour protectionism. We are confronted with what appears to be a disregard for the regime responsible for regulating much international commerce precisely at the time when firms are more involved than ever in regulatory affairs. In addition, in many developing states corporate interest in market opportunities has outpaced the ability of these states to properly regulate multinational activity. Thus, concerns about the growth of privatized regulation arise both from the incompleteness of the international system and from the inadequate governance structures in many states. Firms can and do exploit these governance gaps to their advantage; but the extent of this activity can be exaggerated. Firms tend not to like the uncertainty associated with inadequate regulatory structures, and much of their corporate political activity is directed towards the creation of firm-friendly regulation. Nonetheless, the fragmentation of the contemporary international political economy and the increasing multiplicity of actors present policy-makers with a significant regulatory problem. In the absence of robust international regimes, Abbott and Snidal have called for 'orchestration' to become the organizing principle of transnational regulation, with states mobilizing support for regulatory goals rather than seeking to impose their own or accept ad hoc, privately created solutions.[2] Orchestration, in this context, speaks to some of the themes raised in this issue of *International Affairs*, in that the performance of international regimes hinges on the ability of states to work with non-state actors in pursuit of policy objectives.

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1 Aaditya Mattoo and Arvind Subramanian, 'From Doha to the next Bretton Woods: a new multilateral trade agenda', *Foreign Affairs* 88: 1, Jan.–Feb. 2009, pp. 15–26.

2 Kenneth Abbott and Duncan Snidal, 'Taking responsive regulation transnational: strategies for international organizations', *Regulation and Governance* 7: 1, 2013, pp. 95–113, DOI:10.1111/j.1748–5991.2012.01167.x.

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Corporate interests, global governance and the rise of the BRICs

The rapid growth of emerging markets presents firms from the developed world with significant opportunities to gain new markets and develop new products and services. A dominant narrative of the past 20 years has considered the development of rising powers as an economic opportunity for western multinationals, keen to tap abundant low-wage labour and lightly regulated economies in the pursuit of profit.[3] While this is part of the reality, it is also an incomplete picture of the contemporary corporate landscape, as more and more firms from developing states become key economic actors internationally. There is a notable tendency to exaggerate the political power of western multinationals and ignore the emergence of firms from the rising powers. The development of competitive emerging market firms has been under way for several decades. Domestic policy reforms in many emerging markets replaced discredited development policies in the 1990s.[4] This domestic process both capitalized on and informed European and American efforts to liberalize world trade. The development and expansion of the GATT agenda owed a great deal to corporate political activity, as American multinationals organized an effective lobby in support of the Uruguay Round negotiations. So effective was this lobby that some observers suggest that the Round is best understood as a complete triumph for corporate interests.[5] Corporate interest in the WTO has continued, though activity has centred more on expanding coverage than on renegotiating substantive details of the agreements. European and American firms played important roles in encouraging the integration of several states, notably China, into the world economy. American multinationals, for example, mounted a concerted effort to gain China's entry into the WTO, and business pressure was also important in assisting Russian accession.

This business pressure has been to an extent exceptional, with observers noting the relative lack of business interest in the Doha negotiations.[6] To the extent that this is true, it arises for a complex mix of reasons, not least the increasing attractiveness of 'mid-range' trade and investment agreements in preference to multilateral approaches. The globalization of production has also affected western multinationals' protectionist preferences. As goods become more a collection of intermediate inputs from a wider range of suppliers, firms have become more circumspect about using traditional trade tools such as anti-dumping rules.[7] The growth of intermediate goods trade has vastly outstripped growth in finished products in recent years, even leading the WTO to shift the basis for its methodology for

[3] McKinsey Global Institute, *Manufacturing the future: the next era of global growth and innovation*, Nov. 2012, http://www.mckinsey.com/insights/manufacturing/the_future_of_manufacturing, accessed 13 April 2013.

[4] Zdenek Drabek and Sam Laird, 'The new liberalism: trade policy developments in emerging markets', WTO Staff Working Paper, ERAD 9707, July 1997.

[5] Sylvia Ostry, 'The world trading system: in the fog of uncertainty', *Review of International Organizations* 1: 1, 2006, pp. 139–52.

[6] Mattoo and Subramanian, 'From Doha to the next Bretton Woods'.

[7] Steven McGuire and Johan Lindeque, 'Diminishing returns to trade policy in the European Union', *Journal of Common Market Studies* 48: 5, 2010, pp. 1329–49; Uri Dadush, Shimelse Ali and Rachel Esplin Odell, 'Is protectionism dying?', Carnegie Endowment for International Peace, international economics paper, May 2011.

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calculating world trade data to value added (trade in tasks), relinquishing the increasingly outmoded assumption that finished goods constitute the bulk of imports and exports.[8]

There is also a notable reluctance by western firms to complain about their treatment in the emerging powers, for fear that they will lose out in the fast-growing consumer markets in these countries. For all the attention rising powers receive as locations for western investment, it is arguably their emergence as significant markets for goods and services that gives them leverage with western governments and firms alike. For example, in spite of widespread concern about China's extensive subsidization of its solar panel industry, galvanizing industry support for a trade case has been difficult.[9] US Commerce Secretary Gary Locke has noted this reliance on China—and also drawn attention to the progress China has made in placing its domestic economy on a more institutionalized footing. He further made clear that day-to-day involvement by US firms in the Chinese market may well serve them better than using the available disputes processes: 'The importance of the Chinese market to the global strategy of US exporters and companies operating in China grows daily. The interaction between those US businesses and their Chinese partners, suppliers, and customers has improved dramatically as Chinese businesses have adopted more international business practices and as the commercial legal environment has improved.'[10] This reliance is not confined to manufactured goods but also extends over a vast array of commodities: 25 per cent of all soybeans grown in the United States are exported to China, and as mass affluence spreads in countries such as China and Brazil the market for everything from foodstuffs to cars to insurance is enormous.[11]

Services trade is another matter, as this is an area—perhaps soon to be the only area—where western multinationals have significant competitive advantages over firms from rising powers. Services also constitute a much greater share of national economies in the developed world, though even in developing countries they account for half of GNP.[12] There is thus a significant market opportunity. In both the United States and the European Union there are active corporate coalitions pressing for extensive liberalization of services under the General Agreement on Trade in Services (GATS). Aside from lobbying for renewed progress at the multilateral level, corporate coalitions such as the Coalition of Services Industries and European Services Forum have pressed the European Union and the United

8 WTO, *Trade patterns and global value chains in East Asia: from trade in goods to trade in tasks* (Geneva, 2011).

9 Keith Bradsher, 'Sitting out the China trade battles', *New York Times*, 23 Dec. 2010, http://www.nytimes.com/2010/12/24/business/global/24trade.html?_r=0, accessed 13 April 2013.

10 Gary Locke, US Commerce Secretary, 'The US–China trade relationship: finding a new path forward', Statement to the Senate Finance Committee hearing, 23 June 2010, http://www.commerce.gov/news/secretary-speeches/2010/06/23/testimony-senate-finance-committee, accessed 14 April 2013.

11 Paul Casper, President of the South Dakota Soybean Association, testimony to the Senate Committee on Finance, Sub-committee on International Trade, Customs and Global Competitiveness, 18 April 2012, http://www.finance.senate.gov/hearings/hearing/?id=608e6840-5056-a032-521b-eb6a46c4c9dd, accessed 14 April 2013.

12 European Commission, 'Economic sectors: services', http://ec.europa.eu/trade/creating-opportunities/economic-sectors/services/, accessed 13 April 2013.

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States to undertake a new round of bilateral transatlantic trade negotiations.[13]

Increasing frustration with the WTO's Doha process has produced a notable shift in lobbying activity in both the US and the EU towards a complex mix of regional trade agreements and sectoral liberalization among a smaller subset of countries. The great recession of 2008–2009 has provided a further stimulus for EU–US corporate activity, as lobbying in favour of greater transatlantic integration can now be sold as having the added benefit of assisting economic recovery.[14] Regional trade agreements have multiplied over the past 20 years: there are now over 300 in force around the world, with another 200 in varying stages of implementation.[15] American and European firms have increasingly opted to support regional initiatives, in some cases for the pragmatic reason that some liberalization might be better than none. Firms may also feel that they can more easily dominate smaller regional trade agreement (RTA) negotiations, particularly as WTO membership has expanded and there has been a notable decrease in the resource and expertise asymmetries that used to be exploited by European and American policy-makers. Finally, the growth of regional trade agreements reflects the fact that the world is actually less globalized than we think. Production networks might be more complex, but there remains a powerful need for timely delivery of intermediate goods—the essential inputs for a finished product. This leads to an uneven globalization process, where many suppliers are located in the same region as final assemblers.[16] Ghemawat has coined the term 'semi-globalization' to describe the contemporary international economy. He notes, for example, that in spite of surging foreign direct investment (FDI) in the past decades, about 90 per cent of fixed investment worldwide is domestically generated, and that stock ownership and venture capital financing show similar 'home base' effects.[17] For many developing states with inadequate domestic savings, the problem is insufficient investment from abroad, not too much. Semi-globalization affects the political activity of western firms by making national and regional institutional arrangements relatively more important than multilateral initiatives even if, in principle, the latter should reduce the transaction costs associated with differential regulation.

Western multinationals have thus sought to engage with emerging powers through a mix of strategies. They have sought to encourage the liberalization of these markets, bandwagoning with the prevailing support for pro-market policies. FDI has given many western firms direct access to policy-makers in emerging markets, so creating another channel of potential influence. The rapid growth of

[13] European Services Forum, 'Regulatory cooperation component in the services sectors to an EU–US economic agreement', joint statement of the European Services Forum and the Coalition for Services Industries, 21 Nov. 2012, www.esf.be, accessed 14 April 2013.

[14] Robert Lawrence, 'How can trade policy help America compete?', Peterson Institute for International Economics Policy Brief no. 21, Oct. 2012.

[15] WTO, 'Regional trade agreements gateway', http://www.wto.org/english/tratop_e/region_e/region_e.htm, accessed 13 April 2013.

[16] Elisa Gambenoni, Rainer Lanz and Roberta Piermartini, 'Timeliness and contract enforceability in intermediate goods trade', WTO Policy Research Working Paper 5482, November 2010.

[17] Pankaj Ghemawat, *World 3.0: global prosperity and how to achieve it* (Cambridge, MA: Harvard Business Review Press, 2011), p. 28.

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key markets—notably China—has made western firms wary of appearing protectionist in their domestic markets.

Emerging market multinationals

The appearance of firms from rising power economies as significant competitors in a range of industries has been one of the more obvious manifestations of change in the global economic order. Though most of the world's large firms have home bases in the established economies of western Europe, North America and Japan, emerging market multinationals have been carving out strong competitive niches in sectors as diverse as food processing, generic pharmaceuticals, IT consultancy services, household appliances, iron ore, copper and cement. The *Financial Times* annual report on the world's largest multinationals shows that China (22 firms with a combined market value of US$1.63 trillion), Brazil (12; $764 billion) and India (12; $367 billion) are home to a significant number. China is arguably an exceptional case, as the number of large multinationals based here has grown far more dramatically than those in any other emerging economy.[18] With its 22 companies on the *FT* list, China's 'market share' is exceeded only by the US (173 companies), the United Kingdom (38), Japan (36), Canada (25) and France (23).[19] Many emerging market firms are not publicly quoted companies, but rather are controlled or owned outright by the state, and this shift away from stockholders to private or state ownership is a signal feature of the contemporary international economy. According to one study, of the 14 largest Chinese firms, 12 are state-owned enterprises that span the banking, construction and natural resource sectors.[20] For many people, 'Big Oil' is manifest in large western multinationals such as BP, Exxon or Shell, and these companies are indeed large; but, big and influential as they are, they are tiny when compared with the state-owned oil companies around the world. Based on proven reserves, the Big Four of western oil—Shell, Exxon, BP and Total—barely make the top 20 firms. In the twenty-first century, Big Oil is a story of the 'Big State'.[21] And both 'ends' of the production scale—commodities like oil and agricultural goods at one end, and banking and finance at the other—currently have significant numbers of emerging market firms competing for market share.

The rapid growth of emerging market firms cannot, however, be ascribed simply to state patronage and ownership of natural resources. Rather, emerging market firms have become well-run, competitive and successful business enterprises, able to compete with European, Japanese and American companies. As Goldstein notes, this growth is a story of the development of complex organiza-

[18] Mike Peng, 'The global strategy of multinationals from China', *Global Strategy Journal* 2: 2, 2012, pp. 97–107.

[19] All data from the *Financial Times* 'FT 500 2012', http://media.ft.com/cms/a84bc84c-ca80-11e1-89f8-00144feabdc0.pdf, accessed 14 April 2013.

[20] Vale Columbia Center, 'Chinese multinationals gain further momentum', April 2010, http://www.vcc.columbia.edu/files/vale/documents/EMGP-China-Report-2010-Final-07_Dec_10_0.pdf, accessed 14 April 2013.

[21] Ian Bremmer, 'State capitalism comes of age: the end of the free market', *Foreign Affairs* 88: 3, May–June 2009, pp. 40–55.

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tions headed by sophisticated and capable managers who possess skills and attributes that once seemed to be the monopoly of western multinationals.[22] One of Europe's and America's most successful exports has been, through various channels, business education. The dominant narrative in international political economy in the past 20 years has viewed liberal policies in developing states as accommodating western economic interests; what has been overlooked has been the role liberalization played in the creation of competitive domestic firms within emerging economies. These firms, while extensively studied in the management studies literature, remain notably absent from International Relations analyses.

Academic work on emerging market multinationals suggests that, in potentially important ways, they are—for the moment, at least—different from their developed country competitors. Broadly, there are two areas of differentiation. The first relates to the markets served by emerging market firms; the second concerns their internal organization and ownership structures. In respect of the former, it has been suggested that firms from emerging economies, lacking the deep capital and intellectual resources of western multinationals, have tended to opt for products and services that work in other developed markets, that is South–South investment.[23] Firms based in emerging markets are particularly good at adapting a wide range of products for consumers in less developed states, where purchasing power and the lack of customer support services require relatively simple, cheap and robust products well adapted to emerging economies. Modern communications technologies have also assisted the growth of emerging market firms. The advent of widespread mobile telephony, internet and logistics services allows firms to globalize at a much earlier stage in their development than in previous eras. Overall, in other words, emerging market firms have particular advantages in terms of speed to market and general familiarity with other emerging markets that allow them to compete—or outcompete—firms based in the 'Triad' of the US, the EU and Japan.

Modern communications and logistics allow the disaggregation of supply chains: not merely of goods, but also of ideas and information. Gereffi and colleagues write about the fragmentation of the global economy, as more and more products are the result of the interactions of a complex but dispersed network of suppliers. The vertical integration of the traditional multinational enterprise—where all important business functions were internalized within the firm—has given way to a differentiated network structure, where a given firm may, in fact, effect very little direct control over upstream suppliers.[24] This pattern is now well accepted by commentators, but its impact on global governance is only now being appreciated. As international trade becomes more and more concerned with trade in intermediate goods, corporate interests change. When a firm exports a finished good, market access issues are indeed important; but, if that firm's business is part

[22] Andrea Goldstein, *Multinational companies from emerging economies: composition, conceptualization and direction in the global economy* (Basingstoke: Palgrave, 2009).
[23] Goldstein, *Multinational companies from emerging economies*.
[24] Gary Gereffi, John Humphrey and Timothy Sturgeon, 'The governance of global value chains', *Review of International Political Economy* 12: 1, 2005, pp. 78–104.

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of a complex supply chain, the firm's interests are likely to be governed by adherence to international standards, such as those developed under the International Standards Organization. In a networked, multinational supply chain, it is difficult to discern a 'national interest' to bring to the WTO negotiating table.[25] For many firms from emerging markets, convergence towards accepted operational standards is more important than participation in large, transnational corporate political activity. Büthe, in his discussion of the power of the International Electrotechnical Commission (IEC), articulates the power of industry-based standards:

> IEC standards control market access, as consumers or businesses rely upon them for interoperability, and purchasing managers from industry and retailers incorporate them into purchase orders. Producers may also comply with them because insurance companies use them to gauge the risks that a manufacturer poses, or because courts look to them as an indication of best practice in product liability law suits. In addition, governments not only use IEC standards for public procurement but also and increasingly incorporate or reference them in health and safety regulations, which render the 'voluntary' IEC standards literally mandatory.[26]

Emerging market firms have benefited from the liberalization of global trade in the past few years. In the first place, the reduction of tariffs and concomitant opening up of markets has allowed the emerging market firms that are able to grow outside their home markets to do so. Consistent with economic theory, as domestic economies become more competitive as a result of pro-market reforms, the best-performing domestic firms become more competitive and are then able to internationalize successfully.[27] Pro-market reforms thus provide a spur to improve and internationalize.[28] Emerging market firms have also become very active investors. Cemex, the Mexican cement producer, went on an acquisition spree in the 1990s, using FDI as a mechanism to build an international presence. Indian multinationals—notably Tata—have been successful at replicating the diversified business group model at the international level. A recent report by A. T. Kearney noted that, particularly after the start of the great recession, the volume and value of mergers and acquisitions by emerging market companies began to converge rapidly with developed country levels, and a significant feature was the use of mergers and acquisitions to acquire established brands with existing customer bases.[29] What is also noteworthy, however, is how aggregate investment figures hide significant clustering of investments on a few firms. In Brazil, for example, Vale (mining) and Petrobras (petroleum) accounted for two-thirds of Brazil's

[25] Michael Hart, 'Breaking free: a post-mercantilist trade and productivity agenda for Canada', CD Howe Institute Commentary 357, July 2012, http://www.cdhowe.org/breaking-free-a-post-mercantilist-trade-and-productivity-agenda-for-canada/18501, accessed 14 April 2013.

[26] Tim Büthe, 'Engineering uncontestedness? The origins and institutional development of the International Electrotechnical Commission', *Business and Politics* 12: 3, 2010, article 4.

[27] Steven McGuire, 'No more Euro-champions: the interaction of European trade and technology policies', *Journal of European Public Policy* 19: 6, 2006, pp. 887–905.

[28] Luis Alfonso Dau, 'Pro-market reforms and developing country multinational companies', *Global Strategy Journal* 3: 2, 2012, pp. 262–79.

[29] A. T. Kearney, *Emerging and established markets converge*, Aug. 2012, http://www.atkearney.com/en_GB/paper/-/asset_publisher/dVxv4Hz2h8bS/content/emerging-and-established-markets-converge/10192, accessed 14 April 2013.

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outward stock of FDI in 2009.[30] Similarly, in Argentina, two firms account for 85 per cent of the foreign assets held by Argentine firms.[31] This pattern holds broadly across emerging markets; though more and more firms are internationalizing, a small number of firms are particularly successful.

Another feature of emerging market firms has been the regional focus of their investment and sales. Brazil's most popular FDI destinations among developing states are Argentina and Uruguay.[32] While consumers and the popular media often fasten upon the exceptions, such as Tata or Huawei, when observing the march of emerging market firms, in fact most multinationals from rising economies, rather like their counterparts in Europe or North America, tend to locate most of their international activities close to home. This enables them to capitalize on relative similarities in consumer culture, lower transport costs and, more recently, the increasing number of RTAs. Many emerging market firms still lack the technological, marketing and regulatory skills necessary to overcome their liability of foreignness in western markets.[33] Ramamurti notes that the bulk of FDI from emerging markets into developed markets has been in sectors that are mature in developed countries but experiencing fast growth in rising powers. Buying mature western firms in expanding industries adds economies of scale and scope to service expanding markets in countries such as India and China.[34] Emerging market firms operate best where there are country-specific advantages (linguistic, cultural and political similarities) that compensate for a lack of firm-specific advantages (such as research and development capability or brand recognition).[35]

Ownership is another area of differentiation between developed and developing country multinationals. To a much greater extent than in developed economies, large firms in the rising powers feature state ownership or private ownership structured along family lines. The latter category, the business group, has been largely overlooked by the IR literature in spite of its ubiquity in developing economies.[36] The state ownership of many firms from emerging markets has raised political concerns in western capitals that FDI is part of a broader geopolitical strategy—

[30] Luiz Carvalho and Álvaro Cyniro, 'Brazil's global players', in Karl Sauvant, Vishwas Govitrikar and Ken Davies, eds, *MNEs from emerging markets: new players in the world FDI market* (New York: Vale Columbia Center on Sustainable International Investment, 2011), p. 25, www.vcc.columbia.edu/files/vale/.../EMGP_-_eBook_PDF_2_11.pdf, accessed 14 April 2013.

[31] Vale Columbia Center, 'Argentine multinationals remain industrially diversified and regionally focused', Nov. 2011, http://www.vcc.columbia.edu/files/vale/documents/EMGP-Argentina-Report-2011-Final-30_Nov_ 11.pdf, accessed 14 April 2013.

[32] Luis Afonso Lima and Octavio de Barros, 'Brazil: the growth of Brazil's direct investment abroad and the challenges it faces, 2009', in *Inward and outward FDI country profiles* (New York: Vale Columbia Center, Jan. 2011), p. 239, http://www.vcc.columbia.edu/files/vale/content/Profile_eBook_PDF_2_11.pdf, accessed 14 April 2013.

[33] Steven McGuire, Johan Lindeque and Gabriele Suder, 'Learning and lobbying: emerging market firms and corporate political activity in Europe', *European Journal of International Management* 6: 3, 2012, pp. 342–62.

[34] Ravi Ramamurti, 'What really is different about emerging market multinationals?', *Global Strategy Journal* 2: 1, 2012, pp. 41–8.

[35] Elitsa Banalieva and Charles Dhanaraj, 'Home-region orientation in international expansion strategies', *Journal of International Business Studies* 44: 2, 2013, pp. 89–116.

[36] Tarun Khanna and Yishay Yafeh, 'Business groups in emerging markets: paragons or parasites?', *Journal of Economic Literature* 45: 2, 2007, pp. 331–72.

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particularly on the part of China.[37] This view, of course, is given more weight by the support that the Chinese state provides for its firms—even private ones—to acquire western companies.[38] More direct economic concerns have also been raised, namely that state-owned enterprises, lacking the market discipline of competitors, overpay for investments and, in doing so, distort the market for corporate assets.[39] They are also regarded as inefficient and, to varying degrees, corrupt. Business groups are a common form of corporate arrangement in rising powers, ranging from giant Korean *chaebols* to smaller, diversified companies such as Indonesia's Salim Group. Business groups, conglomerates of loosely connected businesses, are prevalent in emerging markets because the structure offers a number of advantages in weakly institutionalized environments. First, familial bonds substitute for robust contracts and legal systems in respect of ownership. Diversification also allows for the spreading of risk across a portfolio of businesses. Though diversification is widespread in western economies, the volatility of many emerging economies makes diversification an important risk mitigation tool. What is not yet understood is the extent to which the institutionalization of the rule of law in rising powers will affect the business group structure.

The close relationships that state-owned enterprises or business groups might have with domestic political authority are often thought of as symbiotic, but the reality is more complex. In authoritarian regimes, privately owned business groups can use political activity to maintain good—and hence lucrative—relations with political authority. However, Dieleman and Boddewyn have documented how firms diversify their political activity just as they do their business interests—and for precisely the same reason: insurance against adverse change in the political environment.[40] As China develops, there is evidence of an increasingly complex relationship between political authority and entrepreneurs, where the latter require political support for their businesses but also engage in mitigation strategies to prevent politicians from appropriating economic rents.[41] In Russia, the adoption of corporate governance arrangements borrowed from the US and UK have the effect of erecting a barrier to domestic political interference in the firm's operations.[42] There is another reason to suppose that emerging market firms will engage in political activity, and this is directly linked to the enhanced international presence of many of these firms. Adherence to international regulatory standards requires that firms engage in a learning process, and this new knowledge can shape and inform their subsequent interactions with domestic political authority in the home country.

37 Deborah Bräutigam and Tang Xiaoyang, 'Economic statecraft in China's new overseas Special Economic Zones: soft power, business or resource security?', *International Affairs* 88: 4, July 2012, pp. 799–816.

38 A. T. Kearney, *Emerging and established markets converge*.

39 Antonio Capobianco and Hans Christiansen, 'Competitive neutrality and state-owned enterprises', OECD Corporate Governance Working Paper no. 1, Oct. 2011.

40 Marleen Dieleman and Jean Boddewyn, 'Using organization structure to buffer political ties in emerging markets: a case study', *Organization Studies* 33: 1, 2012, pp. 71–95.

41 Pei Sun, Kamel Mellahi and Guy Liu, 'Corporate governance failure and contingent political resources in transition economies: a longitudinal case study', *Asia–Pacific Journal of Management* 28: 4, 2011, pp. 853–79.

42 Stanislav Markus, 'Corporate governance codes as political insurance: firm-level institutional creation in emerging markets and beyond', *Socio-Economic Review* 6: 1, 2008, pp. 69–98.

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Corporate political activity and emerging market firms

It is common to talk about the increasing heterogeneity of the international political economy, with the expansion of the number of players, the expanding role for private regulation, and the greater activity of social media and non-governmental organizations (NGOs) as key participants. As Bernstein and Cashore argue, our understanding of how actors influence politics lags behind the reality of how policy is made.[43] In terms of the theoretical framework underpinning this special issue of *International Affairs*, the available evidence suggests that emerging market firms are not framing their policy preferences in terms of opposition to the developed world. Rather, they are adopting postures that indicate bandwagoning, and an effort to join and integrate into the international economy and its governance. Emerging market firms have been active in the domestic political arena for many years in ways recognizable to observers of western corporations. Business group pressures did push Mexican policy-makers to seek free trade with the US, and Indian firms seeking to internationalize supported extensive liberalization in the 1990s.[44] The growth of 'new protectionism'—the use of procurement and R&D policies—in aid of emerging market firms appears to be increasing. In 2012, the government of India passed the Preferential Market Access policy, which requires that government agencies source security-related electronics technologies from Indian firms. Complaints have been made for similar reasons about China's policies for the wind energy and solar industries.[45]

When most observers comment on corporate involvement—for good or ill—in the construction of global economic governance, they often have in mind the extensive firm-level lobbying activity associated with the WTO's Uruguay Round negotiations from 1986 to 1994.[46] But the success of corporate political activity in this Round was arguably exceptional and has not been repeated since.[47] The problem now is, as Narlikar has noted, corporate indifference to the WTO.[48] Another popular example is the vast expanse of international financial regulation, ranging from banking supervision to securities exchanges to international accounting standards. What all instances of successful corporate political activity share is a coalition of like-minded, resourceful and motivated firms that succeeded in galvanizing political support for their preferred policy preferences. The case of international accounting standards (IAS), for example—the role of the major professional service firms, all with US or European origins, in developing agreed IAS rules and persuading the EU to act as a key political conduit—has been well

43 Steven Bernstein and Benjamin Cashore, 'Global governance: pathways to influence', *International Affairs* 88: 3, May 2012, pp. 585–604.

44 Khanna and Yafeh, 'Business groups in emerging markets'.

45 Vinod Aggarwal and Simon Evenett, 'Industrial policy choice in the crisis era', *Oxford Review of Economic Policy* 28: 2, 2012, pp. 261–83.

46 Thomas Lawton, Johan Lindeque and Steven McGuire, 'Multilateralism and the multinational enterprise', *Business and Politics* 11: 3, Aug. 2009, DOI: 10.2202/1469-3569.1274.

47 Richard Sherman and Johan Eliasson, 'Trade disputes and non-state actors: new institutional arrangements and the privatization of commercial diplomacy', *World Economy* 29: 4, 2006, pp. 473–89.

48 Amrita Narlikar, 'New powers in the club: the challenges of global trade governance', *International Affairs* 86: 3, 2010, pp. 717–28.

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documented.[49] Strong coalitions like this, however, may be less common and more fleeting than our public concern about them indicates.

If successful coalition-building requires a shared conception of the nature of the policy problem, then there is reason to expect firm-level coalitions to be more difficult to develop in the future—but not because emerging market firms frame their demands in opposition to established players. The ownership structures of emerging market firms may well exert a considerable influence on their willingness to expand their political activity at the global level. Moreover, as noted above, the multiple pathways to influence that any business now enjoys—both legislative and regulatory—mean that much political activity goes unnoticed. Emerging market firms are thus part of a political feedback loop: as they internationalize, they learn about and adapt to international regulatory standards and arenas, and this in turn affects their interactions with their home governments.[50]

Firms from rising powers are already taking advantage of existing institutional structures and using non-market strategies in an effort to expand. First, the existing regime on inward investment has proved no obstacle to emerging market firms seeking assets abroad. The convergence of developing and developed country merger and acquisition activity does not suggest the existence of regulatory or political obstacles in any but the most unusual cases. The WTO's disputes process is a case in point, with more and more activity in the process from rising powers. Though governments take the cases to Geneva, behind each one are domestic firms seeking to expand their international markets.[51] Brazil has been particularly successful in developing a 'third pillar'—a private sector network of firms, trade associations, civil society and academia—to assist in the prosecution of trade cases and the more general diffusion of knowledge about the international economic system.[52] Firms from other member states are following this lead and are increasingly using the WTO disputes process. Brendan Vickers notes that the area of greatest growth in Dispute Settlement Understanding (DSU) cases has been in those between developing countries. This is consistent with the observed pattern of internationalization of emerging market firms: they still concentrate on expansion in other developing markets.[53]

Second, we would expect these firms to concentrate on regional initiatives that reflect—at least for now—the regionally dominant pattern of their investment and sales. Moreover, as successive WTO negotiations become larger and more unwieldy, the attractions of bilateral or plurilateral approaches increase. In the

[49] James Perry and Andreas Nolke, 'The political economy of international accounting standards', *Review of International Political Economy* 13: 4, 2006, pp. 559–86; Karthik Ramanna and Ewa Sletten, 'Why do countries adopt international financial reporting standards?', Harvard Business School Working Paper 09–102, 24 March 2009, http://www.hbs.edu/faculty/Publication%20Files/09-102.pdf, accessed 14 April 2013.

[50] Capobianco and Christiansen, 'Competitive neutrality and state-owned enterprises'.

[51] Vinod Aggarwal and Simon Evenett, 'The financial crisis, "new" industrial policy, and the bite of multilateral trade rules', *Asian Economic Policy Review* 5: 2, Dec. 2010, pp. 221–44.

[52] Gregory Shaffer, Michelle Ratton Sanchez and Barbara Rosenberg, 'The trials of winning at the WTO: what lies behind Brazil's success?', *Cornell Journal of International Law* 41: 2, Oct. 2008, pp. 383–501; Rogerio de Souza Farias, 'Sowing the seeds of leadership: Brazil and the agricultural trade negotiations of the Uruguay Round', *Journal of World Trade* 44: 3, 2010, pp. 661–85.

[53] Brendan Vickers, 'The role of the BRICS in the WTO', in Amrita Narlikar, Martin Daunton and Robert Stern, eds, *The Oxford handbook on the World Trade Organization* (Oxford: Oxford University Press, 2012), pp. 254–74.

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case of regional agreements, the gains and costs of concluding the pact are more concentrated, thus providing firms with powerful incentives to participate.[54] As noted above, firms are not nearly as global as is often suggested; most have an identifiable home region where most of their sales are generated. Ghemawat called regional strategies the 'forgotten strategy' because of the lack of attention to RTAs by management studies communities.[55] This observation is particularly important in respect of emerging market firms which, as noted above, often remain comparatively regionally focused. It thus makes sense for these firms to direct their political activity towards the creation of a viable regional market.

Third, in a world of disaggregated supply chains, activity in standard-setting bodies becomes significant both to gain important information about the demands of other firms in respect of the operational performance expected of a component enterprise and also as a signalling device to potential clients and customers. ISO compliance, for example, is a classic instance of a regulatory process into which firms enter, knowing that the lack of ISO certification is a commercial death sentence. The same holds true for environmental and social standards, though this may be affected to some extent by a firm's position in the supply chain. Supply chains aside, international regulatory bodies offer firms from emerging markets an opportunity to 'borrow' regulations and institutional structures lacking in their home markets. For example, less developed economies actively adopted the accountancy standards of the International Accounting Standards Board while richer, more developed economies were less willing to cede authority to the board. Interestingly, Ramanna and Sletten noted a clear regional or network effect where the adoption of IAS by one country was emulated by neighbours.[56] This strongly suggests that domestic corporate constituencies work to lower transaction costs through regulatory harmonization.

The decline of the NGO?

As emerging market firms become more important players, is this taking place at the expense of NGOs? For the past 20 years, the increasing prominence of NGOs in the development and delivery of public goods and development assistance has been notable. NGO growth has been spurred by globalization, as international policy coordination prompted political activity at the international level. But NGOs were not merely the vehicle for the transmission of private political preferences; they also played significant roles in the development and delivery of services in weakly institutionalized states. In Africa, for example, one study suggested that several thousand NGOs—mainly based in developed economies—were working in Africa across a range of activity areas.[57] NGOs and firms are often treated more

[54] Kerry Chase, 'Economic interests and regional trading arrangements: the case of NAFTA', *International Organization* 57: 1, 2003, pp. 137–74; Mark Manger, 'Competition and bilateralism in trade policy: the case of Japan's free trade agreements', *Review of International Political Economy* 12: 5, 2005, pp. 804–28.

[55] Pankaj Ghemawat, 'Regional strategies for global leadership', *Harvard Business Review* 83: 12, 2001, pp. 98–108.

[56] Ramanna and Sletten, 'Why do countries adopt international financial reporting standards?'.

[57] Firoze Manji and Carl O'Coill, 'The missionary position: NGOs and development in Africa', *International Affairs* 78: 3, May 2002, pp. 567–83.

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or less identically in some of the literature, both types of actor being conceived of as outsiders bringing about significant change to the state-centric political order that has dominated international relations since the Treaty of Westphalia.[58] Esty noted that a key role played by NGOs was to act as intellectual counterweights to governments in international forums, articulating views that would otherwise go unconsidered.[59]

However, changes in the international political economy have worked to the detriment of some NGOs, notably those concerned with development and the provision of public goods in weakly institutionalized states: those that Teegan, Doh and Vachani have called 'operational' NGOs.[60] Even before the arrival of the BRICs and the broader phenomenon of emerging markets, western policy elites came to embrace market-based solutions to a range of development issues. Jenkins notes the extent to which multilateral organizations have seen corporate social responsibility (CSR) initiatives as merely development policy delivered by the private sector.[61] Corporations offered two things. First, at a time of the dominance of neo-liberal conceptions of economic progress, it became useful to turn to the market on development as much as on any other issue. Poverty appeared intractable in many states, and it was time to let an alternative, market-focused policy regime take the lead. Aside from being favoured for ideational reasons, firms also offered resources, both financial and in personnel and expertise.[62] Thus international agencies such as the World Bank began to broker relationships between development NGOs and companies, attempting to use the public acceptability of the altruistic motives of many NGOs with the cash and technical know-how of the corporate sector.

The success of the BRICs has, however, undermined a key argument about the development trap that faced emerging markets, and to an extent justified NGO involvement in countries. Trade liberalization—albeit combined often with more economically nationalist policies—has proved spectacularly successful for many states. Suggestions, for example, that the agreement on trade-related aspects of intellectual property rights (TRIPS) trapped developing states into becoming permanent consumers of western-based technology have proved wide of the mark.[63] Emerging market firms have established themselves in a range of

[58] Stephen Kobrin, 'Globalization, transnational corporations and the future of global governance', in Andrea Georg Scherer and Guido Palazzo, eds, *Handbook of research on corporate citizenship* (Cheltenham: Edward Elgar, 2008).

[59] Daniel Esty, 'Non-governmental organizations at the World Trade Organization: cooperation, competition, or exclusion', *Journal of International Economic Law* 1: 1, 1998, pp. 123–47.

[60] Hildy Teegen, Jonathan Doh and Sushil Vachani, 'The importance of non-governmental organizations (NGOs) in global governance and value creation: an international business research agenda', *Journal of International Business Studies* 35: 6, 2004, pp. 463–83.

[61] Rhys Jenkins, 'Globalization, corporate social responsibility and poverty', *International Affairs* 81: 3, May 2005, pp. 545–60.

[62] Nicco Graf and Franz Rothlauf, 'The why and how of NGO–firm collaborations', Working Paper no. 04/2011, Johannes Gutenberg-University Mainz, July 2011.

[63] Shyama Ramani, 'Who's interested in biotech? R&D strategies, knowledge base and market sales of Indian biotechnology firms', *Research Policy* 31: 3, 2002, pp. 381–98; Clemente Forero-Pineda, 'The impact of stronger intellectual property rights on science and technology in developing countries', *Research Policy* 35: 6, 2006, pp. 808–24.

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industries rich in intellectual property, both by investing in indigenous research and development and through acquisitions of western firms. The latter route almost certainly had not occurred to many of the WTO's critics when TRIPS was being implemented—but it is a reminder of the adaptability of corporations and the multiple means they have to attain their business objectives. Criticism of CSR as a development tool has often focused on developed world multinationals and their activities in emerging markets, emphasizing the lack of long-term commitment by these investors: as firms could, in theory, relocate anywhere, they naturally had little incentive to make poverty alleviation a key objective.[64]

Over the past 20 years, numerous multilateral bodies have sought to give NGOs a greater voice. For some, this was in response to a perceived legitimacy crisis and an effort to reduce the informational and resource deficiencies that adversely affected the ability of developing states to involve themselves in the multilateral trade negotiations. The WTO, for example, sought to develop greater and better institutionalized links with NGOs in response to the anti-globalization backlash it experienced in the years following the successful conclusion of the Uruguay Round. Steffek notes that NGO involvement in the WTO is, on some measures, the equal of business groups. However, influence on the process is more difficult to discern. While NGO representatives are more welcome in Geneva than formerly, they have not been able to gain direct access to the WTO's procedures, notably its disputes process.[65] Van den Bossche notes that NGOs share many of the characteristics of firms in respect of formal access to international organizations: they lack a clear mandate and hence legitimacy, and are not accountable.[66]

Some NGOs have adopted a pragmatic approach and increasingly sought to align themselves with firms across a range of issue areas. To some extent, this adaptation was necessitated by multilateral organizations that had, previously, used NGOs to deliver policy outputs in individual countries. Multilateral agencies such as the UN increasingly use firms in preference to NGOs in the delivery of some development assistance, arguing that firms possess greater resources (both financial and material) and expertise to target assistance and fill governance gaps in emerging markets.[67] NGOs also came to prefer private regulatory governance structures out of frustration with the seeming inability of states to develop robust international regulation in areas such as environmental protection.[68] Firms, of course, can benefit from this arrangement to the extent that it confers on them greater legitimacy and social acceptance.[69]

[64] Jenkins, 'Globalization, corporate social responsibility and poverty'.

[65] Jen Steffek, 'Awkward partners: NGOs and social movements at the WTO', in Narlikar et. al., eds, *Oxford handbook of the World Trade Organization*, pp. 301–19; Martina Piewitt, 'Participatory governance in the WTO: how inclusive is global civil society?', *Journal of World Trade* 44: 2, 2010, pp. 467–88.

[66] Peter van den Bossche, 'NGO involvement in the WTO: a comparative perspective', *Journal of International Economic Law* 11: 4, 2008, pp. 717–49.

[67] Steven Kobrin, 'Private political authority and public responsibility: transnational politics, transnational firms and human rights', *Business Ethics Quarterly* 19: 3, 2009, pp. 349–74.

[68] Erika N. Sasser, Aseem Prakash, Benjamin Cashore and Graeme Auld, 'Direct targeting as an NGO political strategy: examining private authority regimes in the forestry sector', *Business and Politics* 8: 3, 2006, article 1.

[69] Carola Kantz, 'The power of socialization: engaging the diamond industry in the Kimberley Process', *Business and Politics* 9: 3, 2007, article 2.

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Conclusion

In his analysis of Canadian trade policy, Michael Hart argued that 'traditional trade negotiations have become much less important, in part because the trade negotiations of the past created a solid framework of rules and commitments by all major traders to keep their markets open'.[70] Hart's argument reminds us that the WTO impasse is not unambiguously a sign of failure. Emerging market firms have thrived in the past 20 years: they have entered new markets, exported successfully, purchased rivals and other firms as part of an acquisition strategy, and have developed brands and proprietary knowledge to enable future growth. The disaggregated global economy may well be a problem for policy-makers—and it could be a problem for firms—but for now, the liberalization set in train by Europe and the United States has proved remarkably accommodating to new corporate powers. Rather than seeing private regulatory regimes as instruments of oppression, these emerging market firms have recognized that adherence to these standards, far from locking them into a subordinate position, can be a means to full engagement in the international economy.

It is true, nonetheless, that emerging market firms often come from domestic political systems that emphasize economic nationalism. Many do successfully organize against further liberalization measures and support the broad negotiating agenda of BRIC countries in the WTO. They may yet find deeper integration into the global economy more difficult, especially if mature markets in Europe and the United States remain locked in post-crisis slow growth. For now, however, the disaggregated nature of global economic governance suits many emerging market firms. They have little reason to put resources into what might be corporate political activity that yields few gains.

Whereas some policy-makers in the West always viewed the rise of new powers as a zero-sum game, this was never true for multinationals. Corporate interests have always focused on the opportunities offered by emerging economies as well as the potential for competition they represent. Firms from developed economies have sought to engage more at the sectoral and regional levels, partly out of frustration with the multilateral process. EU and US firms no longer 'call the shots' in international negotiations, though clearly they remain influential. At a time when the developed world is recovering from an economic crisis and, in the longer term, facing financial challenges from demographic change, the emerging affluent middle class in rising powers represents an opportunity not to be missed. Political activity must be carefully calibrated.

For NGOs, the heterogeneity of the current environment presents a problem. The success of liberalization has presented a challenge to those whose *raison d'être* was economic justice. Even on environmental issues, there is some evidence that firms are responding to market-based incentives, though NGOs will claim a key role in shaping consumer expectations about the environmental impact of modern capitalism. The current pattern of selective alliances between NGOs and firms

[70] Hart, 'Breaking free', p. 25.

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looks set to continue. Firms, for all their success, see their legitimacy as social actors as highly contingent, and NGOs provide useful socially acceptable partners in pursuit of policy preferences.

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