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Thanks but no thanks: State-owned multinationals from emerging markets and host-country policies

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Abstract

I study the impact of the internationalization of state-owned companies from emerging markets on host-country government policy. Whereas the literature commonly recommends that host-country governments design policies to attract foreign direct investment, governments instead question or block investments by state-owned firms from emerging markets. I address this conflict between theory and practice by separating the causes of this behavior into six types depending on the characteristics of the firm (i.e., state ownership and emerging market origin) and the logic (i.e., economics, politics, and psychology). I suggest the development of ex-ante rule-based policies that provide clarity, address concerns, and support the benefits of inward investments, while limiting state capture by domestic interests. Thus, I explain how economic concerns over national security sectors and strategic technologies can be dealt with via exclusion, the political worries over opacity and weak governance can be addressed through monitoring, and the psychological anxieties of unfriendly governments and loss of relative status can be ameliorated using controls.

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INTRODUCTION

In October 2005, Dubai Port World (DP World), an Emirati port development and management firm that was majority owned by the Dubai government, acquired the British competitor Peninsular and Oriental Steam Navigation Company (P&O) after approval by the British High Court and the US government's Committee on Foreign Investment in the United States (CFIUS). P&O had numerous international operations and, among them, it ran the management contracts of six ports in the US. However, in February 2006, Republican and Democratic politicians in the US Congress voiced security concerns, and an opposition campaign started in the media. This was despite the fact that the contract was only for the management of the ports, that the ports were already operated by a foreign firm, that U.S. Customs and Border Protection was in charge of screening cargo, that workers were US citizens and members of the International Longshoremen's Association, and that DP World was managed as a commercial enterprise with little influence from the government. After multiple attempts to address the voiced concerns, in December 2006 DP World sold the management contracts to the US asset management firm AIG Global Investment Group, even though AIG lacked experience in port management (Beisecker, 2006).

The challenges that DP World faced in the US are an illustration of the problems that state-owned firms from emerging markets confront in their global expansion. These trials are not just a crucial managerial issue, but also a theoretical one because they question our understanding of the development of host-country policies toward inward foreign direct investment (FDI). Substantial literature has explained the benefits for countries to design inward FDI policies to attract foreign investments (for an overview see entries in the book edited by Tavares-Lehmann et al., 2016). Following these suggestions, host-country governments go to great lengths to facilitate inward FDI because it is seen as bringing plenty of benefits to the country, such as capital, advanced technology, employment, and connections to global value chains. Not only central but also subnational governments compete for investments against other governments, providing financial subsidies like investments in infrastructure and employee development, and fiscal subsidies like tax reductions and tax holidays (Tavares-Lehman, 2016).

However, when the investments are made by state-owned firms from emerging markets, many host-country governments question and sometimes block them. State-owned firms are perceived as having unique governance characteristics (Cuervo-Cazurra, Inkpen, Musacchio, & Ramaswamy, 2014; OECD, 2016) that lead host-country governments to treat them differently. This clash between what the theory of FDI suggests and the reality that state-owned multinationals from emerging economies confront makes this topic a theoretically exciting and important one to analyze.

Hence, in this article, I study this theoretical and empirical contradiction between the development of policies to attract inward FDI and the constraints imposed on investments by state-owned firms from emerging economies. I propose separating the causes of host-country governments' concerns into six types depending on the characteristics of the firm (i.e., state ownership and emerging market origin) and the logic (i.e., economics, politics, and psychology). I suggest establishing ex-ante rule-based policies that clarify views, address concerns, and support inward FDI, while limiting state capture by domestic interests. Thus, I explain how: (1) the economic concerns over national security regarding state-owned investors and the purchase of strategic technologies by emerging economy multinationals can be dealt with through exclusion; (2) the political worries over the opacity of state-owned multinationals and the weak governance of emerging economy investors can be addressed via monitoring, and (3) the psychological anxieties of unfriendly government influence through state-owned firms and loss of relative status to emerging market firms can be ameliorated using controls.

STATE-OWNED MULTINATIONALS FROM EMERGING ECONOMIES

Many managers and scholars nowadays tend to associate the phenomenon of state-owned multinationals with the recent internationalization of state-owned firms from emerging markets in general and China and Russia in particular. This association may exist because state-owned multinationals from emerging economies have recently expanded and purchased some iconic firms in advanced economies, drawing attention through the novelty and boldness of their actions (Economist, 2012).

However, state-owned multinationals do not exist only in emerging economies. State-owned firms have a long history of operating across borders (Aharoni, 2018; Anastassopoulos, Blanc, & Dussauge, 1987; Cuervo-Cazurra, 2018; Vernon, 1979). They were prevalent in advanced economies in the past (Mazzolini, 1979) and nowadays continue to exist in all countries (Musacchio & Lazzarini, 2014; Sauvant & Strauss, 2012). For example, all countries belonging to the Organization for Economic Cooperation and Development (OECD), a club of mostly advanced countries, have state-owned firms (OECD, 2014); Table 1 summarizes the numbers. The analysis of firms in the Forbes 2000 list of top publicly traded firms whose state-invested sectors have a market value over US$100 billion reveals that there are publicly traded state-owned firms in advanced and emerging markets alike; Table 2 provides the numbers (OECD, 2016).

This gap between the perception and reality of the importance of state-owned multinationals from emerging economies seems to be the result of two

Table 1 Number of state-owned firms in OECD countries and selected economies

Country	Number of state-owned firms: all	Number of state-owned firms: majority-owned listed entities	Number of state-owned firms: majority-owned non-listed entities	Number of state-owned firms: statutory and quasi-corporations	Number of state-owned firms employees: all	Value of state-owned firms, billions of US$: all
OECD countries						
Australia	15	0	5	10	49,945	18.3
Austria	9	2	6	1	74,161	22.1
Belgium	8	1	7	0	88,476	10.2
Canada	47	0	0	47	86,588	28.3
Chile	34	3	7	24	48,900	22.2
Czech Rep.	125	1	89	35	140,300	40.3
Denmark	17	1	10	6	22,823	11.9
Estonia	57	0	30	27	25,661	5.4
Finland	39	3	34	2	84,760	44.2
France	48	2	25	21	781,643	70.3
Germany	72	0	71	1	349,203	47.3
Greece	52	5	47	0	45,258	12.9
Hungary	371	1	370	0	124,924	6.6
Iceland	37	0	26	11	4737	5.5
Ireland	24	0	24	0	39,582	31.9
Israel	34	0	34	0	54,959	48.9
Italy	17	7	10	0	526,911	226.1
Japan	13	0	8	5	64,173	339.3
Korea	57	8	49	0	129,235	200.9
Luxembourg	34	0	34	0	13,118	N.A.
Mexico	69	0	46	23	N.A.	83.2
Netherlands	26	0	26	0	50,313	107.2
New Zealand	18	4	12	2	33,424	8.1
Norway	45	3	25	17	221,045	243.7
Poland	326	6	295	25	159,730	61.6
Portugal	82	0	31	51	146,899	8.0
Slovak Rep.	73	0	37	36	N.A.	17.3
Slovenia	39	4	35	0	52,039	12.6
Spain	53	1	44	8	95,589	5.5
Sweden	54	0	51	3	135,608	85.6
Switzerland	4	1	1	2	101,098	39.7
Turkey	34	8	21	5	170759	69.8
U.K.	24	1	11	7	397,312	88.0
U.S.A.	19	2	1	16	599,010	13.5
Selected non-OECD countries						
China	147,000	286	N.A.	N.A.	35,947,000	N.A.
India	1097	68	N.A.	N.A.	N.A.	N.A.
Indonesia	141	16	111	N.A.	N.A.	147.0
Russia	1147	7	17	N.A.	14,305,100	N.A.
South Africa	512	N.A.	N.A.	N.A.	N.A.	N.A.
Malaysia	N.A.	57	N.A.	N.A.	N.A.	N.A.
Viet Nam	3239	14	N.A.	N.A.	1,606,400	116.3

Note Data for 2012, *N.A* not available.
Source OECD (2014).

Table 2 Distribution of state-owned firms among the largest 2000 publicly traded firms, ranked by a combination of sales, profits, assets, and market value

Economy	Number SOEs										Market value, US$ billion
	All	Banking	Electricity and gas	Manufacturing	Other financial	Metals and mining	Petroleum	Telecom	Transport	Other	
China	128	18	10	23	18	17	5	4	7	26	4004.3
India	34	16	4	2		4	4	2		2	330.5
Hong Kong	13	1	3	1	3	1			3	1	209.6
France	13	1	3	5	1			1	2		384.7
U.A.E.	11	6	1		2			1	1		123.5
Russia	10	2	3			1	3	1			188.1
Saudi Arabia	9	2	1	3	1	1		1			210.4
Qatar	9	5		1	2			1			110.1
Brazil	7	1	2	1		2	1				121.6
Singapore	6	2						1	1	2	143.7
Germany	6	1	2	1				2			290.0
Norway	5	1		1		1	1	1			141.5
Italy	5		3	1			1				128.5
UK	2	2									144.6
Japan	2							1		1	136.7
Others	66	25	11	2	5	2	11	8	2		788.4
Total	326	83	43	41	32	29	26	24	16	32	7456.3

Source OECD (2016) using Forbes Global 2000 and including only countries with state-invested firms with over US$ 100 million in market value.
Note Data for 2014.

influences: a large variety of types of state-owned multinationals, and the limited availability of information about these firms.

Defining State-Owned Multinationals from Emerging Economies

I start the clarification of the topic with a definition of the companies under study: An emerging-market state-owned multinational is a company that is owned by the government, has foreign direct investments, and comes from an emerging country. This definition seems to be straightforward, but applying it, in reality, appears to be less so because its three features are each themselves challenging to define: state-owned firms, multinationals, and emerging markets.

The first challenge is defining state-owned firms. The typical view of state-owned firms — companies wholly owned by the central government — is outdated. The pro-market reforms of the 1990s resulted in the partial and full privatization of many state-owned firms (Megginson & Netter, 2001; Ramamurti, 2000). At the same time, new investment instruments emerged, such as sovereign wealth funds that purchase small stakes in private firms (Gerard, 2007; Megginson & Fotak, 2015; Sauvant, Sachs, & Schmit Jongbloed, 2012). Despite their small investments, some of these funds have taken an active role in influencing private firms. For example, Norway's Government Pension Fund Global has promoted corporate responsibility in the companies in which it has invested (PWC, 2015: 13). State-owned firms are controlled not only by the central government, but also by sub-national governments, which results in significant differences in internationalization (Li, Cui & Lu, 2014). Moreover, there are further changes in the way governments influence the economy (Bremmer, 2010). Governments have used reverse privatization, in which they contract back with private and state-owned firms rather than going back to state-owned monopolies (Hefetz & Warner, 2004; Warner, 2008). Politicians have also recently nationalized firms (Nash, 2017). In some cases, this has been done for ideological reasons, such as the nationalizations in Venezuela in the 2000s. In other cases, it has been done for practical purposes to support essential industries, such as the US government's minority investments in major US banks and majority investment in the US automaker General Motors after the 2008 crisis.

All this has resulted in a large variety of types of state-owned firms (Bruton Peng, Ahlstrom, Stan, & Xu, 2015). Table 3 summarizes the multiplicity of ways in which the state can influence a company (Cuervo-Cazurra et al., 2014). Despite these definitions, the consideration of a firm as state-owned can also be subjective. For example, the telecom equipment manufacturer Huawei was barred from entering the US market because legislators considered it to be under the influence of the Chinese government. Although the founder had been an official of the People's Liberation Army, the firm was owned by its employees and not by the state (Sevastopoulo, 2014).

In this article, I concentrate on legally independent firms that are wholly or partially state-owned to keep the discussion manageable. Hence, throughout the article, I do not always make an explicit distinction in terms of policy regarding wholly and partially state-owned multinationals. However, it is important to acknowledge that partially privatized firms behave differently from wholly owned ones because of the influence of capital markets and private owners; for example, they show improved profitability (Boubakri, Cosset & Guedhami, 2004; Gupta, 2005; Megginson, Nash, & van Randenborgh, 1994). Moreover, a discussion of Sovereign Wealth Funds and their investments would require a different framework given that many of the investments are done in search of financial returns, the investments tend to be smaller than those undertaken by state-owned firms, and Fund managers rarely take an active role in the strategy of invested firms (Aguilera, Capape, & Santiso, 2016; Megginson & Fotak, 2015).

The second challenge is in identifying foreign direct investment. Foreign direct investment is commonly defined as investments with a lasting interest in the stock of a firm in a foreign country, usually being over 10% of the stock (UNCTAD, 2017a). Early researchers considered multinationals to be companies with production facilities in

Table 3 Types of state-owned enterprises

	Direct ownership				Indirect ownership		
	State entity/ agency	State (fully) owned firm	State majority-owned firm	State minority-owned firm	Sovereign wealth fund invested firm	State pension fund invested firm	State bank loaned firm
Legally separate firm	No	Yes	Yes	Yes	Yes	Yes	Yes
Budget	No separate budget	Separate budget	Separate budget	Separate budget	Separate budget	Separate budget	Separate budget
Ownership	Direct ownership	Direct ownership	Direct ownership	Direct ownership	Indirect via ownership by sovereign wealth fund	Indirect via ownership by state-owned pension fund	Indirect via convertible loan by state-owned bank
Level of ownership	Full ownership	Full ownership	Majority ownership	Minority ownership and/ or golden share in private company	Minority investment in private firm by Sovereign Wealth Fund	Minority investment in private firm by state pension fund	Minority investment in private firm via convertible loan by state-owned bank
Types of managers	Civil servants	Civil servants/ professional managers	Civil servants/ professional managers	Professional managers	Professional managers	Professional managers	Professional managers
Level of government influencing firm	Central/ federal	Central/ federal; province/ state; municipal/ city	Central/ federal; province/ state; municipal/ city	Central/federal; province/state; municipal/city	Central/federal	Central/ federal; province/state; municipal/city	Central/federal; province/state; municipal/city

Source Adapted from Cuervo-Cazurra et al. (2014).

another country (Dunning, 1977). However, this definition excluded service firms and many other activities that could be valuable to the firm such as supply or R&D. Some authors added size requirements before considering a firm to be a multinational, like more than 10% of foreign sales and investments in more than three countries (Rugman, 2009). However, such criteria are ad-hoc and have no theoretical basis behind them. I consider multinationals to be firms that own value-added activities abroad; this includes not only production and sales but other activities such as supply, technology development, financial management, design, et cetera.

The third challenge is agreeing on what an emerging economy is. There are multiple classifications of countries depending on the entity that does the classification (e.g., UNCTAD, World Bank, UN, UNDP, etc.). There are also various names given to countries that are not advanced, such as the Third World, developing, transition, least developed, emerging, newly industrialized, or frontier, that reflect different criteria (Economist, 2008). I follow the IMF classification of countries into two groups (advanced, and emerging and developing) (IMF, 2013) and consider emerging nations to be those countries that are not advanced. The IMF uses qualitative criteria to classify economies, which is less subject to sudden changes in the measures that underline other classifications.

Identifying State-Owned Multinationals from Emerging Economies

The next difficulty in analyzing state-owned multinationals from emerging markets is identifying them among all companies. This is complicated for three reasons: (1) lack of databases, (2) variation in the firms included in databases, and (3) biases in databases of publicly traded firms.

First, there are no databases of state-owned multinationals, because this is not data that is commonly collected. Some countries group state-owned firms under a holding; for example, in Spain, investments in firms by the central government are grouped in the SEPI holding (SEPI, 2016). However, such groupings exclude state-owned firms at the subnational level, which account for the vast majority of state-owned firms, even if many of them are not multinationals. For example, in Germany, there are 15186 state-owned companies, of which 89% are municipality-owned, while in Sweden there are 2563 state-owned companies, of which 69% are municipality-owned (PWC, 2015: 11). Although an implicit view is that centrally-owned firms are the ones that matter because they are the biggest firms, this is not accurate. For example, the German car manufacturer Volkswagen was in 2016 the second largest car producer in the world by the number of cars sold, and the state of Lower Saxony owned 11.8% of its shares and controlled 20.0% of its voting rights (Volkswagen, 2017). Likewise, the Chinese automaker SAIC Motor was in 2016 the top Chinese car manufacturer and 12th in the world, and Shanghai's Municipal Government owned 74.3% of it (SAIC, 2017).

The solution to the lack of databases on state-owned multinationals is to create them, relying on secondary datasets to study what state-owned firms are doing abroad. One approach is to do a multi-country analysis, for example, using the Forbes Global 2000 database and identifying the ultimate ownership of the firms listed there from other sources such as Orbis or companies' websites (e.g., OECD, 2016). Other approaches include single country studies, identifying firms in the country that are owned by the government and comparing them to private firms, using surveys to obtain data (Cui & Jiang, 2012); relying on databases that contain one type of foreign investment such as greenfields (Duanmu, 2014); focusing on firms that that are publicly traded (Meyer, Ding, Li & Zhang, 2014; Pan, Teng, Supapol, Lu, Huang & Wang, 2014); or studying one type of state-owned firm, such as research labs (Choudhury & Khanna, 2014). Another alternative is to analyze firms in one single industry, such as oil and gas firms (Bass & Chakrabarty, 2014).

Second, studies that rely on secondary databases may suffer from biases because the firms included in the dataset change over time; hence, the conclusions of the study may be influenced by the specific firms analyzed. For example, the study of the internationalization of state-owned firms by Kowalski, Buge, Sztajerowska, & Egeland (2013) used the list of firms in Forbes 2000 in 2010. To illustrate how the composition of firms changes widely over time, Table 4 provides the top 25 firms on their list, and Table 5 contains the top 25 in 2017. The comparison reveals significant changes in the firms included. These changes are primarily driven by the use of four criteria for ranking firms (sales, profits, assets, and market value) that can vary widely across time. One exception is the disappearance of the US automobile firm General Motors as a state-owned firm. General Motors was nationalized in mid-2009 (with the US government owning 60.8% and the Canadian and Ontario

Table 4 Top publicly traded state-owned firms, ranked by a combination of sales, profits, assets, and market value in 2011

Rank 2011	Forbes rank	Company	Country	Sales 2010, US$ billion	Profits 2010, US$ billion	Assets 2010, US$ billion	Market value 2010, US$ billion
1	6	PetroChina	China	222.3	1.2	251.3	320.8
2	7	ICBC	China	69.2	18.8	1723.5	239.5
3	8	Petrobras-Petróleo Brasil	Brazil	121.3	21.2	313.2	238.8
4	15	Gazprom	Russia	98.7	25.7	275.9	172.9
5	17	China Construction Bank	China	58.2	15.6	1408	224.8
6	21	Bank of China	China	49.4	11.9	1277.8	143.0
7	22	Sinopec-China Petroleum	China	284.8	10.9	148.7	107.7
8	25	Agricultural Bank of China	China	49.4	9.5	1298.2	134.0
9	29	GDF Suez	France	113.1	6.2	245.5	85.2
10	34	China Mobile	China	71.8	17.7	129.3	192.1
11	51	Banco do Brasil	Brazil	68.9	7.1	488.7	48.5
12	60	Statoil	Norway	90.4	6.5	110.3	83.8
13	61	General Motors	USA	135.6	6.2	138.9	49.8
14	68	China Life Insurance	China	48.2	4.8	179.6	96.6
15	77	Rosneft	Russia	46.1	10.4	93.9	85.0
16	95	Saudi Basic Industries	Saudi Arabia	40.5	5.7	84.3	81.2
17	100	EDF Group	France	87.2	1.4	319.9	78.2
18	136	State Bank of India Group	India	29.1	2.6	322.2	36.1
19	144	CNOOC	China	27.0	8.0	41.8	101.3
20	145	China Shenhua Energy	China	23.1	5.8	51.6	82.3
21	157	China Telecom	China	32.5	2.3	61.8	47.2
22	171	PTT PCL	Thailand	63.2	2.8	40.9	32.1
23	172	Oil & Natural Gas	India	22.6	4.3	44.6	53.2
24	178	Sberbank	Russia	32.3	0.8	234.4	74.4
25	179	Ecopetrol	Colombia	21.9	4.2	35.8	84.4

Source Kowalski et al. (2013: p. 51) based on data from Forbes and Orbis.

Provincial governments owning 11.7%) and privatized from 2010 until 2013 by the US government and until 2015 by the Canadian and Ontario governments (Vieira & Dummett, 2015).

Third, another significant bias in our understanding of state-owned firms is the outcome of using datasets of publicly traded firms. To be publicly traded, the state has to sell some shares in the stock market to create the free-float on which prices are quoted. As a result, studies of state-owned multinationals that analyze publicly traded firms end up basing their conclusions on partially privatized firms, which behave differently from wholly state-owned firms (Megginson & Netter, 2001). For example, partially and fully privatized firms have higher performance (Boubakri & Cosset, 1998). With such databases, we end up with a distorted view of the behavior of state-owned multinationals; the approach is akin to deriving recommendations on foreign market entry based on databases that only include partially owned foreign subsidiaries. This is an area in which studies of state-owned firms suffer from the lack of comprehensive databases. Nevertheless, this problem also affects studies of other types of firms such as family-owned, as many studies analyze publicly traded family-owned firms (e.g., Anderson & Reeb, 2003) and exclude fully owned family firms.

One illustration of the limitations of datasets of publicly traded firms is the identification of state-owned firms in the oil industry; this is a global industry in which all sizeable firms are multinationals. Table 6 provides a list of the largest publicly traded firms in the oil industry according to Forbes

Table 5 Top publicly traded state-owned firms, ranked by a combination of sales, profits, assets, and market value in 2017

Rank 2017	Forbes rank	Company	Country	Sales 2016, US$ billion	Profits 2016, US$ billion	Assets 2016, US$ billion	Market value 2016, US$ billion
1	1	ICBC	China	151.4	42.0	3473.2	229.8
2	2	China Construction Bank	China	134.2	35.0	3016.6	200.5
3	6	Agricultural Bank of China	China	115.7	27.8	2816.0	149.2
4	8	Bank of China	China	113.1	24.9	2611.5	141.3
5	22	China Mobile	Hong Kong	106.8	16.4	218.9	225.3
6	25	China Petroleum & Chemical	China	255.7	7.0	216.7	105.1
7	29	Volkswagen Group	Germany	240.3	5.7	458.7	72.9
8	34	Bank of Communications	China	53.0	10.1	1209.2	62.2
9	37	Nippon Telegraph & Telephone	Japan	105.0	7.4	180.3	92.2
10	40	Gazprom	Russia	91.4	12.1	265.4	51.8
11	42	China Merchants Bank	China	44.5	9.4	855.1	66.4
12	45	Japan Post Holdings	Japan	123.7	3.1	2522.1	55.1
13	52	China Life Insurance	China	82.8	2.9	388.7	98.1
14	55	Postal Savings Bank of China	China	48.0	6.0	1189.4	55.2
15	56	Sberbank	Russia	43.0	8.1	415.6	63.9
16	63	Industrial Bank	China	44.3	8.1	872.1	45.1
17	65	Shanghai Pudong Development	China	40.1	8.0	842.8	50.5
18	71	China State Construction Engineering	China	140.8	4.9	201.4	43.2
19	72	Citic Pacific	Hong Kong	49.1	5.6	933.6	41.4
20	77	Deutsche Telekom	Germany	80.9	3.0	156.6	80.0
21	78	China Citic Bank	China	39.7	6.3	853.5	43.1
22	82	Rosneft	Russia	74.9	2.7	193.2	62.4
23	99	Enel	Italy	75.9	2.8	164.1	47.5
24	102	PetroChina	China	214.8	1.2	344.9	204.5
25	108	SAIC Motor	China	112.7	4.8	85.0	43.5

Source Forbes (2017) and companies' websites.

Global 2000, while Table 7 lists oil companies ranked by reserves. The differences in the lists are stark. They not only rank the companies very differently, but many of the top oil companies are not included in the Forbes list, because they are wholly owned by their governments. Thus, a study on state-owned firms in the oil industry that only analyzes publicly traded firms would yield biased results because prominent wholly owned players would be excluded from the analyses.

Inward Foreign Direct Investment Policy and State-Owned Multinationals from Emerging Economies

Inward FDI policy tends to be designed to support and attract foreign companies to the host country. However, in the case of state-owned multinationals from emerging countries, governments tend to have a skeptical view and in many cases block their investments. This distinction between what the theory proposes and what state-owned multinationals from emerging economies confront in reality make this an exciting and essential issue to study. Hence, to clarify the positions I first review inward FDI policies and then the attitudes that governments have toward investments by state-owned multinationals from emerging economies.

Inward FDI Policy

The usual attitude of governments toward inward foreign direct investment since the 1990s has been to create policies that attract such investments. Previously, some governments blocked foreign investments as part of a drive to promote local

Table 6 Top publicly traded oil and gas companies, ranked by a combination of sales, profits, assets, and market value

Rank 2017	Company	Country	Sales 2016, US$ billion	Profits 2016, US$ billion	Assets 2016, US$ billion	Market Value 2016, US$ billion	State-owned
1	ExxonMobil	USA	197.5	7.8	330.3	343.2	
2	Royal Dutch Shell	Netherlands	234.8	4.7	411.3	228.8	
3	China Petroleum & Chemical	China	255.7	7.0	216.7	105.1	Yes
4	Total	France	128.1	6.2	231.0	128.1	
5	Gazprom	Russia	91.4	12.1	265.4	51.8	Yes
6	Rosneft	Russia	74.9	2.7	193.2	62.4	Yes
7	PetroChina	China	214.8	1.2	344.9	204.5	Yes
8	Reliance Industries	India	41.8	4.3	97.9	71.2	
9	LukOil	Russia	74.6	3.1	83.2	44.6	
10	PTT PCL	Thailand	48.7	2.6	63.4	32.4	Yes
11	Phillips 66	USA	71.2	1.5	51.7	39.9	
12	Valero Energy	USA	75.7	2.3	46.8	29.4	
13	Repsol	Spain	38.4	1.9	68.4	23.8	
14	Oil & Natural Gas	India	19.9	2.2	57.7	37.2	Yes
15	Indian Oil	India	54.1	1.7	37.3	30.0	Yes
16	Marathon Petroleum	USA	56.0	1.2	44.4	26.4	
17	Surgutneftegas	Russia	13.9	7.8	60.9	18.5	
18	BP	UK	183.8	0.1	263.3	114.7	
19	Chevron	USA	110.5	−0.4	260.1	206.1	
20	SK Holdings	South Korea	72.1	0.6	85.3	14.7	

Source Forbes (2017) and companies' websites.

Table 7 Largest oil and gas companies in the world, ranked by reserves

Rank 2016	Company	Country	Revenue 2015, US$ billion	State ownership (%)
1	Saudi Aramco	Saudi Arabia	478.0	100.0
2	NIOC	Iran	110.0	100.0
3	ExxonMobil	US	268.9	
3	CNPC	China	428.6	100.0
5	PDV	Venezuela	128.4	100.0
6	Rosneft	Russia	91.7	69.5
6	BP	UK	222.8	
8	Royal Dutch Shell	Netherlands	265.0	
9	Gazprom	Russia	106.3	50.0
10	Total	France	212.0	
11	Chevron	US	129.9	
12	Sonatrach	Algeria	76.1	100.0
12	Petrobras	Brazil	130.0	28.7
14	KPC	Kuwait	251.9	100.0
15	Adnoc	UAE	60.0	100.0
16	Lukoil	Russia	144.2	
17	QP	Qatar	37.0	100.0
18	Pemex	Mexico	117.5	100.0
19	Petronas	Malaysia	100.7	100.0
20	Sinopec	China	455.5	70.9

Source Energy Intelligence (2016), Energy Business Review (2016), and companies' websites.

industry under the import substitution development policy (Prebisch, 1950), but this attitude reversed in the 1990s (Bruton, 1998).

The logic behind attracting inward FDI is based on the benefits derived from such investments (see reviews in Blomström & Kokko, 1998; Ghauri &

Yamin, 2009; Görg & Strobl, 2001; Knoerich, 2017; Lim, 2001; Spencer, 2008): (1) Direct investment benefits, and (2) positive spillovers and externalities.

First, the direct benefits associated with foreign investments take several forms: (a) the capital transferred to the country to fund investments; (b) the technologies brought to the country to facilitate the operations of the subsidiary, which include not only product and process technologies, but also managerial and organizational knowledge; (c) the new employment that the subsidiary generates when it is a greenfield; (d) the integration of the activity in the global value chain of the foreign company and the facilitation of exports from the host country to the rest of the world; and (e) the increase in the economic activity and subsequent direct and indirect taxes that the government can collect.

Second, the indirect benefits of inward FDI in the form of externalities on the host-country economy take various dimensions: (a) technological spillovers from the foreign firm to suppliers, competitors, and distributors via demonstration, training, or employee mobility that help domestic companies upgrade their capabilities; (b) increased economic activity in the location and thus associated increases in employment among suppliers and distributors; (c) in some cases, investments in the development of infrastructure to facilitate the activities of the company, such as the creation of new roads or improvements in port and airport facilities; (d) the attraction of additional FDI from other companies that follow the actions of a competitor or customer; or (e) the promotion of the host country as an attractive location for FDI.

Most governments incentivize inward FDI. Unless the country has something unique that other nations lack that makes it attractive to investors (e.g., it has some absolute advantage such as some unique natural resource or an extremely large underserved market or production base), the government may end up in competition with other governments to incentivize inward FDI (Oman, 2000). To make the host country more attractive than alternative locations, and thus ensure that direct and indirect benefits are realized, the government may provide incentives to attract inward FDI (Tavares-Lehmann et al., 2016).

Inward FDI incentives can take four forms depending on the type of subsidy provided: (1) informational, (2) regulatory, (3) fiscal, and (4) financial. The literature commonly discusses fiscal and financial incentives (Tavares, 2016); informational and regulatory incentives are nevertheless important even if they have been mentioned less often.

First, with informational incentives, the host government provides quality information to potential investors to reduce their uncertainty and improve their perceptions of the prospects of the location; this is commonly done using investment promotion agencies (UNCTAD, 2008). Informational incentives can take the form of (a) facilitating contacts with government officials, (b) explaining requirements and expectations, and (c) assisting with the completion of paperwork and compliance with local regulations (UNCTAD, 2017b). Such informational incentives are highly beneficial for the country and come at low costs. There are initial costs of gathering information from multiple ministries and departments and organizing the information to explain the investment procedures and qualities of the country. However, once this has been documented, the marginal costs of providing such information to new investors are minimal, given that information has a non-rival nature.

Second, with regulatory incentives, the host-country government gives foreign investors special regulatory treatment that makes the host country more attractive. These regulatory incentives take multiple forms such as: (a) free trade zones that allow foreign investors to import and export more quickly and, in many cases, at a lower or no tariff level (Krugman, 1991); (b) exclusive monopoly rights over an area or a period that enable the foreign firm to increase profitability; (c) stabilization clauses that create a predictable environment by protecting foreign investors against future changes in laws that may harm their activities in the country (UNCTAD, 2016); and (d) low levels of regulation that make the location more attractive than others because it has higher property rights protection, less stringent environmental standards, or more moderate labor standards (FitzGerald, 2001). Regulatory incentives might have a limited cost to the government. Some require improvements in regulation, which can be economically and politically inexpensive and have high positive externalities in the country. Other costs are the forgoing of income to the government, in the form of tariffs and permit fees, and some incentives can even be free to the government because the costs are transferred to customers who pay premium pricing when foreign investors are given exclusive monopoly rights.

Third, with fiscal incentives, the host-country government provides foreign investors with a reduced tax burden. These take a variety of forms and are widely used across countries (UNCTAD, 2000): (a) reduced tax levels for particular investments, such as in R&D laboratories, employee training, or contributions to social security; (b) tax holidays, whereby the foreign company does not have to pay certain taxes over a period; (c) tax concessions, in which the foreign firm pays a lower level of corporate tax; or (d) duty reductions, in which the foreign enterprise pays no or lower import and export taxes. The cost of fiscal incentives might be high, but they are not always apparent because the government is not investing money in the development of the project, but rather relinquishing future income. The government may still benefit from additional tax revenues from the establishment of new suppliers and distributors.

Fourth, when providing financial incentives, the host-country government subsidizes investments that the company may need to incur in the location. These financial incentives take many forms (OECD, 2001): (a) direct subsidies for some of the costs of the project that reduce the total investment to the firm, such as purchasing and transferring land or paying for part of the construction; (b) investments in the development of complementary infrastructure that supports the development of the operations, such as new roads and utilities or the upgrading of utilities and transport infrastructure with the modernization of ports and airports; (c) financing of the project via direct grants that lower the investment made by the foreign firm; (d) subsidized loans or loan guarantees that lower the cost of capital for funding the project; (e) insurance at reduced rates to help lower financing costs. Such subsidies can prove costly to the government as they require using funds that could otherwise be used in alternative investments. Nevertheless, some subsidies, such as the development of complementary infrastructure, can have positive spillovers on the country and may not happen without a policy of attracting foreign investors.

However, when deciding on inward FDI incentives, the host-country government needs to do a realistic cost–benefit analysis. The case for providing incentives to specific companies, especially tax reductions or subsidies, may not be apparent (OECD, 2003). There are several concerns: (a) it is not always apparent that the foreign company needs incentives, because the location may be attractive enough; (b) the cost of incentives may be above the direct and indirect benefits that the country obtains from the investments; (c) investments may be driven only by the incentives, and once these are phased out, the foreign company may close down the operation or demand additional support to maintain it; and (d) the expected spillovers and transfer of skills to the country may not materialize, because local firms lack the ability to absorb them (Blomstrom & Kokko, 2003).

Concerns about State-Owned Multinationals from Emerging Economies

Many host-country governments view state-owned firms from emerging economies with suspicion. One reason is that politicians and government officials see state-owned firms as recipients of support by their home governments. This support can take multiple forms (OECD, 2016): (1) preferential financing from and for state-owned firms, state banks, and other state-backed financial institutions; (2) privileged access to information; (3) subsidies and tax concessions; (4) in-kind subsidies; (5) grants and other direct payments; (6) a privileged position in the domestic market; (7) explicit or implicit guarantees; (8) exemptions; (9) preferential regulatory treatment; (10) preferential treatment in public procurement; (11) price support; and (12) assistance in commercial diplomacy.

However, not all state-owned companies receive such support. There is a considerable variation in the relationships between governments and their state-owned companies across countries; some governments have very hands-off relationships with their state-owned firms (e.g., Norway), while other governments have much tighter connections (e.g., China). Also, many large private firms receive government support as well, especially those that are well connected to the government (Fisman, 2001; Ghemawat & Khanna, 1998).

The issue is not so much how state-owned firms are supported at home, but rather how such support may help the companies enhance their competitiveness abroad. It appears that on this topic there is an imbalance in the perceptions of government officials of host countries and officials of home countries. On the one hand, host-country officials worry about the behavior of state-owned multinationals abroad. For example, Table 8 summarizes the results of the OECD survey on opinions

Table 8 Host country officials' concerns about investments by foreign state-owned firms, ranked by degree of concern.

Concern	Degree of concern (%)		
	Low	Somewhat	Strong
Maintain a level playing field	8	38	54
Competition enforcement	31	31	38
National security	50	17	33
Ad hoc political intervention	8	59	33
Public Interest	33	42	25
Insufficient Information	46	31	23
Corruption Risk	58	25	17
Net economic benefits	41	42	17
Protect national champions	50	41	8
Re-nationalization	50	50	0
State-owned enterprise governance	42	58	0

Source Sultan Balbuena (2016).

Table 9 Home country officials' concerns about the treatment of state-owned firms operating abroad, ranked by degree of concern

Concern	Degree of concern (%)		
	Low	Somewhat	Strong
Administrative and regulatory procedures	10	30	60
Public procurement	30	20	50
Transactions with subsidiaries	30	30	40
Industry restrictions	20	40	40
Trade/investment agreements	10	60	30
Competition law and policies	60	10	30
Investment review	30	50	20
Institutional factors	50	30	20
Negative media coverage	50	30	20
Ideological/cultural/language barriers	30	50	20

Source Sultan Balbuena (2016).

about foreign investments by state-owned firms (Sultan Balbuena, 2016). The more frequently mentioned concerns are maintaining a level playing field, competition enforcement, ad hoc political intervention, and national security. On the other hand, home country officials are concerned about discrimination toward their state-owned multinationals abroad. Table 9 summarizes the perceptions of officials regarding discrimination of state-owned companies abroad (Sultan Balbuena, 2016). Their primary worries are administrative and regulatory procedures, limitations on public procurement and industry restrictions, and controls on transactions with subsidiaries.

Some of these concerns, and subsequent discrimination, seem to mix two distinct influences: State ownership and emerging market home country. To clarify these, Table 10 provides a two-by-two matrix with commonly-held views of the four types of foreign investors by their country of origin (advanced or emerging) and ownership (private or state-owned).

First, private companies from advanced economies are usually viewed favorably by host-country officials. They are assumed to be bringing new technologies and behaving with high governance standards. For example, in 2009 the Italian private automobile firm Fiat was welcomed by the US government to help acquire the US automaker Chrysler. Chrysler was the third largest US car manufacturer. It was bought by the German automaker Daimler-Benz in 1998, which sold 80.1% to the US private equity firm Cerberus Capital Management in 2007. As a result of the financial crisis of 2008, the US government nationalized Chrysler to save the jobs and manufacturing base, absorbed the debt, and sold most of the firm to the trade unions and Fiat (Rutenberg & Vlasic, 2009). The government, and later the unions, sold their stakes to Fiat, which took full control of Chrysler in January 2014 (Abrams, 2014).

Second, we have state-owned companies from advanced economies, which are viewed as having proper governance standards and behaving appropriately. For example, in 2007 the Italian state-owned oil company Eni bought the assets in the Gulf of Mexico of the US oil firm Dominion (Parker, 2007). This purchase drew little attention other than remarks about the price paid, US$4.75 billion, which was considered high (McAnelly & Sweeney, 2007).

Third, private companies from emerging economies are sometimes perceived negatively because they are assumed to contribute little to the host country in the form of advanced technologies and capabilities. For example, in 2013 the Chinese private pork producer Shuanghui International offered to buy the US pork producer Smithfield Foods for US$4.7 billion, a 30% premium over its market value. The purchase was presented as a way to increase pork exports to China, benefiting from the higher efficiency and safety of the US producer (de la Merced & Barboza, 2013). Nevertheless, the offer led some US lawmakers to express concerns about the acquisition. For example, Senator Debbie Stabenow, who headed the Senate Agriculture Committee, indicated that food was a strategic resource that should be as important to the U.S.

Table 10 Concerns of host-country governments on investments by foreign multinationals, classified by ownership and home country of the foreign investor

		Home country of foreign investor	
		Advanced	Emerging
Ownership of the foreign investor	Private	Most positive: Leading investors who bring new technologies and help upgrade local firms (We are delighted you are coming)	Negative: Companies in search of strategic assets that will hollow out local firms (You cannot trust them)
	State	Positive: Well behaved firms with good governance operating like private firms (I had no idea it was state-owned)	Most negative: Companies in search of strategic assets that are poorly governed and will take advantage of the host country (Those are not the investors we want)

government as oil, and ordered an investigation of the deal and potential involvement of the Chinese government in the acquisition (PBS Newshour, 2014). Despite this, the purchase was eventually approved by CFIUS in September 2013 (Reuters, 2013).

Fourth, state-owned firms from emerging economies tend to be viewed very adversely by host-country officials; they are assumed to threaten national interests. For example, in 2005 the Chinese state-owned firm CNOOC's offer to purchase the US oil firm Unocal drew sharp criticism from US lawmakers, even though it was offering a higher amount, in cash, than the US firm Chevron. To reduce concerns, CNOOC hired lobbyists, bankers, and lawyers, who stressed that 70 percent of Unocal's reserves were in Asia; Unocal's US reserves were only one percent of US consumption and did not supply the military; CNOOC was willing to sell assets if needed; and it would maintain its US employees and supplies in the US (Wayne & Barboza, 2005). However, lawmakers proposed changing the law that regulated the work of the Committee on Foreign Investment in the United States to include energy and oil supplies in the definition of national security (Lohr, 2005). CNOOC later withdrew the offer as a result of the political opposition to the deal (Barboza and Sorkin, 2005).

This last type is the most interesting, as it illustrates the tensions in policymaking. I clarify the sources of the very negative view of state-owned multinational enterprises from emerging markets by separating the influence of state-ownership from that of emerging home country, and analyzing their economic, political, and psychological drivers. Table 11 summarizes the arguments that I explain in more detail next.

STATE OWNERSHIP: CONCERNS AND POLICY

State ownership matters. Having the government instead of private investors as the owner changes not only the behavior and the reasons for the firm's existence, but also the attitude of the host-country government toward the company. To clarify host-country policy, I separate three distinct drivers: Economic, political, and psychological. The economic influence is driven by the non-business objectives of state-owned firms and the subsequent worries over national security that these firms create in host countries. The political impact is motivated by the multilevel agency problem and the associated concerns over opacity of their actions in host countries. The psychological effect is the result of state-owned firms being used to exert soft power abroad and how the host-country government deals with unfriendly governments.

Economic Concerns: Non-business Objectives and Exclusion from National Security Sectors

Non-business objectives of state-owned firms

State-owned firms are created with a different purpose than private firms, resulting in non-business objectives driving some of their investments. Private firms are founded by entrepreneurs to take advantage of market opportunities; the founders assemble resources and capabilities needed to generate products and services that fulfill some unmet needs of customers better than competitors (Barney, 1991; Penrose, 1959). In contrast, state-owned firms tend to be created by the government to address market imperfections that the private sector is not solving (Lawson, 1994; Levy, 1987; Lindsay, 1976). These market imperfections result in government-backed investments that: (1) have

Table 11 Concerns of host-country governments on investments by state-owned multinationals from emerging markets and policy responses

			Approach		
			Economic	Political	Psychological
Characteristic	State-ownership	Difference in behavior in comparison to other multinationals	**Non-business objectives**: State-owned firms are created to address market imperfections and follow non-business objectives abroad	**Multilevel agency**: State-owned firms suffer from multilevel agency problems that results in unclear governance of foreign investments	**Soft power**: State-owned firms are used to exercise soft power and influence abroad
		Host-country government concerns over their behavior in the host country	**National security**: Use of state-owned firms to threaten national security in the host country	**Opaque behavior**: Opacity in the ultimate decision making and behavior of state-owned firms	**Trojan horse**: Unfriendly government influence
		Suggested host-country government policy responses	**Exclude**: Exclude all foreign firms from areas considered of national security interest	**Monitor**: Force disclosure of information and monitor behavior	**Control**: Identify level of friendship and control firms from unfriendly countries, with reciprocity with firms from friendly governments
	Emerging market origin	Difference in behavior in comparison to other multinationals	**Acquire capabilities**: Emerging market firms suffer from underdeveloped innovation systems and invest abroad to obtain advanced technologies	**Weak governance**: Emerging market firms learn to operate with underdeveloped institutions and bring such learning abroad	**New competitors**: Emerging market firms are quickly catching up, combining low-cost production and foreign high-technology
		Host-country government concerns over their behavior in the host country	**Hollowing out**: Acquisition of advanced technologies may lead to the hollowing out of technological capabilities of the host country	**Unethical behavior**: Emerging market firms bring poor governance standards to the host country	**Status loss**: Emerging market multinationals contribute to the loss of the relative status of the host country
		Suggested host-country government policy responses	**Exclude**: Exclude particular technologies from being acquired and transferred abroad	**Monitor**: Require high governance standards of firms from emerging economies and monitor behavior	**Control**: Control rapid expansion of firms in technologies that will support future development

high positive externalities for the country, but from which private entrepreneurs may not be able to derive revenues to cover the costs (e.g., education, healthcare, etc.); (2) are public in nature as a result of non-rival consumption and thus require coordination by the state (e.g., infrastructure, defense, etc.); or (3) have natural monopoly conditions in which one provider can cover the needs of customers but will have a tendency to exercise monopoly power (e.g., utilities, etc.). Of course, the existence of market imperfections does not necessarily require the creation of state-owned firms. The government has other instruments at its disposal to incentivize the private sector to address market imperfections (Laffont & Tirole, 1993), such as taxes and subsidies, and regulatory mandates and prohibitions. Nevertheless, when the government decides to create firms, these state-owned firms will have non-business objectives as part of their mandate, in addition to the traditional business objectives of creating products that satisfy customer needs.

Although market failures explain the creation of state-owned firms, their foreign investments are more difficult to explain under this logic; this raises several concerns about their non-business objectives. First, state-owned companies are designed to address market imperfections in the home country and help citizens there. Thus, the solution of market imperfections in other nations should be the prerogative of governments there, not of a foreign government. Otherwise, state-owned companies may be perceived to be a tool of extraterritorial actions (Cuervo-Cazurra et al., 2014), generating worries about their non-business objectives. There seem to be significant differences in the industries and countries in which state-owned firms invest in comparison to private ones (Ramasamy, Yeung, & Laforet, 2012). Second, a prevailing view among politicians is that foreign direct investment is done at the expense of domestic investments and therefore should not be encouraged (Dutton, 1982; US Joint Committee on Taxation, 1991); however, such adverse effect has not been found (Desai, Foley & Hines, 2005; Stevens & Lipsey, 1992). Hence, foreign investments by state-owned firms could be questioned abroad as being driven by non-business objectives given that the home government should prioritize domestic over foreign investments. Third, foreign investment by state-owned firms may be made to address the solution of global market imperfections and the protection of global public goods (Kaul, Grunberg, & Stern, 1999). However, global market imperfections can be better addressed by the coordinated actions of multiple governments than by the unilateral actions of one government, or its state-owned firms.

Exclusion from national security sectors

Host-country governments may be suspicious of investments by state-owned firms for fear that these are driven by non-business objectives, rather than by the usual business objectives behind foreign direct investments, such as selling more in new markets, or buying better inputs, natural resources, factors of production, or strategic assets (Cuervo-Cazurra, Narula & Un, 2015). The investments may be made following a logic of facilitating the achievement of business goals that a private firm would have also followed. If this is so, there is little need to establish special provisions for state-owned firms.

However, such arguments may not apply to sectors that are considered sensitive to national security in the host country. In these cases, ex-ante policies that clarify the exclusion of foreign firms from such sectors may be appropriate. The identification of industries that pose national security concerns varies across countries and has expanded over time (Wehrle & Pohl, 2016). The typical sectors are defense and dual-use technologies, i.e., sophisticated industrial technologies with military applications and real estate near sensitive areas such as military facilities or national borders, because these are viewed as crucial for ensuring the military superiority of the country in case of conflict. These national security sectors have sometimes been expanded to include other industries that can support military operations, such as transportation and telecommunications, and even natural resources and food. For example, such worries over the control of natural resources were voiced in 2012 among Canadian policymakers over the US$15 billion acquisition of the Canadian oil firm Nexen by the Chinese state-owned oil producer CNOOC. Although the deal was eventually approved, as was the US$5 billion acquisition of Progress Energy Resources by the Malaysian state-owned oil firm Petronas, Canadian lawmakers indicated their willingness to change the rules to make future deals subject to additional scrutiny (Austen, 2012). An expanding list of industries that are considered relevant to national security may be driven by domestic companies in search of protection from foreign competition rather than by real concerns about the security of the country; hence, such a list requires moderation and careful assessment.

In sectors of national security, the host-country government may want to exclude foreign companies regardless of their ownership. This approach seems to be the policy in most countries (Wehrle & Pohl, 2016: 25). Even if state-owned firms are directly connected to their home governments, private firms can also be influenced by their home governments. If the host-country government considers the particular industry, location, or activity to be of national security importance for the country, the appropriate policy is to state this clearly with a list of sectors from which foreign investments are excluded. This will clarify which areas of activity are open to foreign investors and which are not, and can be applied consistently across all foreign investors rather than by subjecting state-owned investors to additional scrutiny, reducing the inclination of politicians to influence decisions. For example, in the US, the Committee on Foreign Investment in the United States is tasked with reviewing and approving foreign investments, but is still subject to pressure from politicians when they disagree with its rulings, and it has been compelled to be less balanced in its assessments (Byrne, 2006).

Limitations to exclusion from national security sectors
There are some limitations to the exclusion of foreign firms, especially state-owned ones, from sectors of national security. For many host governments, the exclusion of foreign firms, in general, and state-owned firms, in particular, may not be feasible. In such cases, the appropriate policy may not be one of exclusion but one of control of foreign firms' behavior.

There might not be domestic providers of the products and services that are considered of national security. In such cases, the host-country government may not have the ability to create a company that produces these. For example, weapons, especially advanced ones, are manufactured in only a handful of countries (e.g., US, Russia, China, UK, France, Israel, etc.) and a small country may have to rely on foreign firms, many of which are state-owned, for these products.

In some industries with national security characteristics, there is a limited number of providers without government ties, which restricts the ability of the host-country government to exclude foreign providers altogether. For example, a handful of firms manufacture airplanes (e.g., the US firm Boeing, the European company Airbus, the Brazilian firm Embraer, the Canadian company Bombardier, and the Russian manufacturer Tupolev), and many of these firms are either partially state-owned or have large defense contracts with their home governments, which may result in home governments influencing their decisions.

If natural resources are included as industries of national security that require the exclusion of foreign firms, another limitation that the host government needs to assess is whether the institutional framework it has in place would enable the country to develop domestic operators. Countries rich in national resources can build their development on these resources when they have appropriate pro-market institutions in place (Easterly and Levine, 2003; Engerman and Sokoloff, 1997).

Political Concerns: Multilevel Agency Problems and Monitoring to Reduce Opacity

Multilevel agency in state-owned firms
State-owned and private companies also differ in the agency problems they face: state-owned firms have a multilevel agency structure that results in more challenging governance, with politicians playing a significant and in many cases opaque role in their behavior.

Multilevel agency relationships create a complex conflict of interest (Aharoni, 1982, 1986; Shleifer & Vishny, 1997). Citizens are nominally the owners of state-owned firms. As such, they are the principals of politicians who act as agents for them to ensure that the state-owned firms achieve their objectives. Citizens have a multitude of objectives, in many cases conflicting ones, that they want the state-owned firm to achieve: the provision of subsidized products and services, the employment of locals, the development of a location or region, etc.

Politicians, in turn, are the principals of the managers who run the state-owned companies. Politicians have their own set of objectives to achieve, such as the support of the public and, in the case of democracies, reelection. Politicians may induce state-owned firms to invest in populist actions, even if these are not contributing to the objectives of the firm or its business activities (Shleifer & Vishny, 1994), such as redirecting investments toward preferred communities, or employing more workers than required for the normal operations of the firms. They may react to state capture by interest groups and pressure state-owned firms to support preferred causes and groups (Lopez-de-Silanes, Shleifer, & Vishny, 1997). As a result, state-owned firms appear to have more inefficient investments (Jaslowitzer, Megginson, & Rapp, 2018) and their losses are borne by the country's treasury (Boycko, Shliifer, & Vishny, 1995; Kikeri, Nellis, & Shirley, 1992). Politicians may also follow their ideologies and lead state-owned firms to expand their realm of action to achieve higher influence over the economy (Cuervo-Cazurra et al., 2014). Moreover, politicians with authority over state-owned firms and the managers that run them are not controlled by citizens, who lack mechanisms to ensure that state-owned firms follow their desires (Aharoni, 1982). Moreover, in the case of partially privatized firms, it is even less clear who is in charge because there is another group of principals whose objectives are likely to differ from those of politicians and citizens: diffused owners in the stock market (Gupta, 2005) and private blockholders (Shleifer & Vishny, 1997). This multitude of principals further complicates the identification of the objectives of the company and who is driving its behavior.

Finally, managers of state-owned firms have their own goals, which differ from those of citizens and politicians, such as ensuring a career within government or eventually moving to the private sector

(Aharoni & Lachman, 1982); these goals further complicate the agency problems. Managers may induce the firm to help politicians achieve their objectives by, for example, investing in areas of the government's preference. Alternatively, they may seek to ensure the independence of the firm from political influence to help managers establish credibility in the market for managers, for example by internationalizing (Choudhury & Khanna, 2014), and in the case of partially privatized firms, managers have to answer not only to politicians, but also to the stock market and private blockholders, complicating their decision-making and the direction they take the firms.

This complex multilevel agency problem affects how state-owned multinationals are perceived to behave abroad, creating concerns about the opacity in their decision-making because it is challenging to identify how they are managed and who is in charge. Politicians may lead state-owned firms to invest in preferred countries and activities that have a high value for them in terms of establishing relationships with host-country governments and promoting the image of the country and the political stature of the politicians abroad. Managers of state-owned firms may follow a different objective and aim to increase foreign involvement to achieve a degree of independence from the influence of politicians at home (Choudhury & Khanna, 2014). Managers of state-owned multinationals can leverage their connections with the home government in case of disputes in the host country (Duanmu, 2014). Thus, state-owned firms may end up benefiting from their internationalization (Benito, Rygh, & Lunnan, 2016). Additionally, as the firm becomes a multinational, it adds another agency relationship between headquarters and subsidiary managers (Roth & O'Donnell, 1996), with managers of the foreign subsidiaries following their objectives, aiming to ensure the success of their subsidiaries abroad and, thus, of their careers.

Monitoring to reduce opacity

Host-country government officials may face challenges in dealing with the opacity of state-owned companies with complex agency structures and a multiplicity of objectives, leading them to establish additional disclosure requirements and controls. It may not be evident for host-country government officials what the actual motives behind the foreign investments of the state-owned company are, because they are not able to disentangle who might be behind the actions and who is actually in power making the decisions. This opacity is a particular issue in state-owned firms because many tend not to disclose or follow governance practices common among private firms (OECD, 2010, 2015). Such opacity may create concerns for host-country government officials about the operations of the state-owned multinational in the host country.

To address these concerns, host-country governments may establish ex-ante monitoring rules that require the disclosure of the structure and operations of the company, the relationships among the different subsidiaries of the state-owned multinational and, especially, the structure of power and decision making within the company. Such monitoring and transparency efforts may be particularly useful when the foreign state-owned company uses pyramids or intermediate companies domiciled in offshore financial centers that have limited transparency requirements. Complex organizational structures, with a multiplicity of shell companies in tax havens, obscure the process by which the firms invest in the host country, including issues of internal transfer of payments and the subsequent loss of tax revenue (Desai, Dyck, & Zingales, 2007). These pyramids obfuscate relationships among subsidiaries and how the financing of deals are structured. The opacity of the structure of foreign companies has been mentioned as concern over some acquisitions of domestic companies by foreign ones. For example, the attempt by the Chinese conglomerate Anbang Insurance Group to buy the US hotel chain Starwood, in competition with a rival bid from the US hotel chain Marriott, was viewed as having a complex structure and unclear financing, even if the bid was superior to the one by Marriott (de la Merced and Picker, 2016). The monitoring in the host country is also useful for state-owned firms coming from countries with limited protection of minority stakeholders, which results in politicians controlling the firms with little oversight (Shleifer and Vishny, 1997).

Limitations on monitoring to reduce opacity

This policy of monitoring state-owned multinationals to reduce the opacity of their structure and behavior has limitations. Some state-owned firms have clear structures in their actions and relationships with the government, with the government having an arms-length relationship with the firm and politicians being constrained in their ability to mandate actions from managers; in such cases, there is limited need for additional monitoring. Partially privatized firms may have better monitoring systems, as private blockholders and stock market analysts keep track of the misbehavior of managers in their decisions. Hence, the level of monitoring of partially privatized firms may be lower, especially those with minority state ownership and those coming from countries with strong protections for minority interest shareholders.

Small countries may not have the ability to impose extra monitoring requirements on state-owned firms from large countries. This is especially true when the big country has an active policy of supporting its firms abroad and lobbies host-country governments. The unevenness in power between countries may limit the establishment of monitoring requirements, and some governments may not have the capacity to monitor the actions and follow the complex structures of large state-owned companies. In such cases, the host government may have to decide between some form of limited monitoring, or the exclusion of state-owned firms that are opaque in their structure and decision-making.

Psychological concerns: Soft Power and Control of Firms from Unfriendly Governments

State-owned firms as soft power tools

From a psychological viewpoint, the central issue of state-ownership is the particular government that is behind the state-owned company and the relationship between home and host-country governments. Host-country governments have varying relationships with the governments of other countries. The host-country government may be on amicable or hostile terms with a particular home country government depending on the interests being pursued. The 19th-century British politician Henry John Temple Palmerston captured this as "We have no eternal allies, and we have no perpetual enemies. Our interests are eternal and perpetual, and those interests it is our duty to follow."

Thus, an independent assessment of the level of friendliness or hostility among governments is challenging. One step could be analyzing the level of autocracy of the home country and how it compares with the host country, for example using information on the characteristics of the political system (Marshall, Gurr & Jaggers, 2017) and state fragility (Marshall & Elzinga-Marshall, 2017). Although democratic governments may dislike each other, the likelihood that this will escalate into outright hostility tends to be lower than with autocratic governments (Russett, 1994). Such assessment is essential as most of the state-owned firms that have undertaken cross-border mergers and acquisitions from emerging economies come from autocratic countries (Karolyi & Liao, 2017). Another way of identifying attitudes toward the home country is analyzing surveys of the positions of individuals towards the nation. For example, in the case of the US, the U.S.-Global Leadership Project conducts opinions of the views of US leadership in 130 countries (Gallup, 2013).

State-owned firms' investments can be part of the development of soft power by the home country (Nye, 1990, 2004). The home country government may direct the state-owned firm to invest in support of the development of the host country, even if it is not commercially viable or profitable to do so. The state can always soften the budget constraint of state-owned firms by subsidizing these investments (Kornai, Maskin, & Roland, 2003). The investment may help improve the perceptions among host-country politicians and citizens of the home country government, as the host country receives development and assistance benefits not provided by other multinationals and their governments. This might be more obvious in large infrastructure projects that tend to be visible and driven by government decisions, and this may be more prevalent in state-owned firms that are wholly owned by the state; in partially privatized firms, private blockholders or analysts in the stock market may question and in some cases block investments that are done purely for soft power reasons and have limited or no business logic.

Control of unfriendly government influences

The perception of the friendliness or unfriendliness of the home country government affects the attitude of the host-country government toward foreign state-owned firms; this may result in controls over their investments and strategies. Trade and foreign investment depend on political relations. Trade connections among countries are influenced by the political relations among governments (Berger, Easterly, Nunn, & Satyanath, 2013; Findlay & O'Rourke, 2007; Fuchs & Klann, 2013). Foreign investments by multinationals are also affected by political relationships (Murtha & Lenway, 1994; Ramamurti, 2001; Stopford & Strange, 1992).

State-owned companies controlled by friendly home governments may see their investments facilitated in the host country. The host-country government uses the support of investments by state-owned companies as one way to maintain and deepen the good relationships with the home country government. This type of investments might be highly welcome by the host government and may receive some preferential treatment. When state-owned companies undertake corporate diplomacy (Henisz, 2014), the question for the host-country government to consider is whether such investments come explicitly with some restrictions or requirements attached. On some occasions, the home country may decide to subsidize investments in the host country to maintain cordial relationships, and thus such investments may be more than welcome. However, on other occasions the home country government may instead ask the host-country government to pay for the investments, providing some preferential financing to help the host-country government fund them. The questions for the host-country government here are whether it needs and can afford such investments, and whether these investments are ultimately made to benefit the home rather than the host country. In the answer is yes to both, as appears to be the case of the construction in Laos of a railway connecting China to Southeast Asia (Janssen, 2017), for example, the host-country government may want to control and maybe not undertake such investments even if they have friendly relationships.

However, state-owned companies owned by unfriendly governments may be viewed with suspicion. Host government officials may have an inclination to control their investments and operations to limit their ability to exercise soft power. The host government may be concerned about the unfriendly home country government achieving economic or political influence in the affairs of the host country indirectly through the actions of the state-owned company.

However, controlling firms from particular nations tends to be constrained by bilateral and multilateral treaties, and the WTO can be asked to intervene in cases of discrimination by country of origin. Such controls on investments would be akin to the case of sanctions against unfriendly nations (Hufbauer, Schott, & Elliott, 1990). Nevertheless, sanctions have been critiqued for not being effective (Pape, 1997), unless the target country is small and the policy objective modest (Hufbauer et al., 1990: 92–93). Moreover, the control of investments from countries deemed hostile can result in a tit-for-tat retaliation; the host government blocks investments by firms from a particular nation and, in turn, their home government blocks investments by firms from the host country (Elliot & Bayard, 1994).

To reduce misunderstandings and improve the controls, the appropriate policy for dealing with hostile countries may be to provide ex-ante rule-based clarity on how host-country politicians deal with firms from unfriendly countries. This will help companies from the nation perceived as hostile to reduce misunderstanding and avoid wasteful investment attempts that may be controlled. This would also reduce the likelihood of retaliation by the home country government, such as establishing new constraints on firms from the host country.

Limitations to the control of unfriendly government influences

A limitation on the ability to establish controls over state-owned firms from unfriendly countries is that perceptions of friendliness may change quickly. Politicians in the home or host countries may be replaced through normal political processes of government rotation. Thus, a government that imposed controls over firms from another country that had a hostile government may suddenly encounter a friendlier government. Controls that were applied to nations that were considered unfriendly may need to be designed to be temporary, with a set of conditions for such constraints to remain. This temporary nature can allow for quick changes in the controls to provide flexibility to lawmakers, given the difficulty in predicting how the relationships among countries may evolve. Moreover, in the case of partially privatized firms, the capital markets and private blockholders may act as internal controls over the use of the state-owned multinational as a tool of soft power, thus requiring fewer controls by the host country.

EMERGING MARKET MULTINATIONALS: CONCERNS AND INVESTMENT POLICY

What makes emerging market multinationals different from advanced economy multinationals is the relative underdevelopment of their home country and how this affects their behavior (Cuervo-Cazurra & Ramamurti, 2014). The exposure at home to underdeveloped economic conditions and institutions influences the internationalization of emerging market multinationals (Cuervo-Cazurra & Genc, 2008; Cuervo-Cazurra & Ramamurti, 2017; Khanna & Palepu, 2010; Peng, Wang, & Jiang, 2008, see a review in

Cuervo-Cazurra, Luo, Ramamurti & Ang, 2018). It also affects the reaction of host-country governments to their investments depending on the type of influence: economic, political, and psychological. First, underdeveloped innovation systems and less sophisticated consumers lead emerging market firms to invest in advanced economies to obtain sophisticated technologies. This may be perceived by host-country governments as a hollowing out of strategic assets. Second, emerging market firms suffer from exposure to underdeveloped institutions that may lead these firms to have sub-par governance practices. Host-country governments may be concerned about the transfer of such practices. Third, emerging market multinationals have been quickly catching up and in some cases surpassing advanced economy firms. This is creating feelings of loss of relative status among politicians and citizens in advanced economies.

Economic Concerns: Acquisition of Capabilities and Hollowing Out

Acquisition of capabilities by emerging-market multinationals

Emerging markets are characterized by underdeveloped economies in which customers are more constrained in their purchasing ability because they have much lower average incomes (Prahalad, 2005); the infrastructure that supports company operations (e.g., transportation, communication) is less advanced as a result of lower investments by the government (Foster, 2008; Kirkpatrick, Parker, & Zhang, 2006); and there is a lower level of education and innovative ability (McMullen, Mauch, & Donnorummo, 2000; World Bank, 1999). An outcome of all of this is companies that are less able to create sophisticated technologies that support their global competitive advantage. Although emerging-market companies can benefit from lower costs of production, they are hampered in their ability to generate cutting-edge technologies and products (Awate, Larsen, & Mudambi, 2012) despite their progress in innovating (Bromfield & Barnard, 2010). The lack of widespread advanced education limits their ability to create highly innovative products (Wang & Cuervo-Cazurra, 2017) while the lower level of income of many customers reduces incentives to produce high-tech products that command a high premium. Hence, although some unique companies have been able to achieve high levels of innovativeness in emerging economies (Guillen & Garcia-Canal, 2012; Ramamurti & Singh, 2009; Williamson, Ramamurti, Fleury, & Fleury, 2013), many tend to focus on low to mid-level technologies developed in the home country, relying on imitation of foreign technologies (Chittoor, Sarkar, Ray, & Aulakh, 2009; Luo, Sun, & Wang, 2011) or alliances with companies from advanced economies in their home countries to obtain more advanced technologies (Luo & Tung, 2007). Some of the foreign investments of emerging market firms are made in search of state-of-the-art technologies from advanced economies, with emerging-market companies acquiring firms in developed countries that have technologies that complement the low-cost production base in emerging economies (Madhok & Keihani, 2012). In such cases, emerging-market companies use funds from their home country operation to purchase advanced economy firms and bring those more sophisticated technologies to the home country to help them upgrade their capabilities there (Elia & Santangelo, 2017). The newly acquired host-country operations are given a relatively high level of autonomy (Wang, Luo, Lu, Sun, & Maksimov, 2014) to ensure that critical employees that understand the technology remain in the subsidiary.

Hollowing out and exclusion of foreign acquirers

Investments by emerging market multinationals to obtain sophisticated technologies may be seen by the host-country government as potentially resulting in the hollowing out of the host country of cutting-edge technologies; this prompts the exclusion of these firms from assets that are considered strategic. The host-country government may fear that emerging market multinationals may be achieving a shortcut to the development of advanced technologies that its companies took a long time to generate. The government may want to exclude foreign companies' ability to acquire particular high-tech companies for fear of their hollowing out (Bloom & Grant, 2008).

However, it is not entirely clear that such exclusions should apply to firms from emerging economies only. Companies from advanced countries purchased firms in other advanced economies to access more sophisticated technologies long before emerging market companies started doing the same. This was the case, for example, of investments by Japanese companies in the US in computers, as well as investments by European and American companies in Japan in robotics and automobiles. Hence, a more appropriate host-country policy that addresses fears of hollowing out of the innovation base may be one that excludes all foreign acquirers in equal terms regardless of home country. If the concern is that some strategic technologies may be lost to companies from other countries, the appropriate response might be to limit their transfer to all other countries and not just emerging ones. Such ex-ante identification of strategic technologies from which foreign firms are excluded would help establish clear criteria on which technologies are open for purchase to foreign investors and which are not. Still, it is not clear that such hollowing out happens, as the acquisition of US firms by emerging market ones resulted in higher profitability of the target firms (Chari, Chen, & Dominguez, 2012).

Limitations on the exclusion from hollowing out

There are some limitations to this exclusion of foreign firms from advanced technologies in the host country. Although the primary concern is the hollowing out of existing technological capacity, foreign firms may contribute to the development of such technological capacity. For example, in greenfield investments, foreign firms hire local scientist and combine their expertise with the knowledge they transfer from their home countries and other operations, contributing to the continued development of advanced technologies in the host economy. Hence, the exclusion from strategic sectors may need to be applied only to the acquisition of local firms and simply questioned in the case of greenfield investments.

Another limitation on the exclusion of emerging market multinationals from acquiring high-tech domestic firms is the actual technological sophistication of the domestic firm being acquired. Unlike the case of national security in which whole sectors can be easily identified as being of security concerns, in the case of high-technology, there is a considerable variation in the technological capabilities of firms within high-tech as well as low-tech sectors. Thus, a company-by-company rather than a blanket sector-wide exclusion may be more appropriate. In many cases, emerging market multinationals purchase firms in advanced economies that are technological laggards and in financial difficulties. Such acquisitions are not only cheaper but also good enough for emerging market firms because their technologies are easier to absorb by acquirers that are not very technologically sophisticated.

Political Concerns: Weak Governance and Monitoring of Unethical Behavior

Weak governance in emerging market multinationals

Underdeveloped institutions characterize many emerging economies, and have received plenty of attention in the literature under the term institutional voids (Khanna & Palepu, 2010). Companies in emerging economies face the challenge that institutions (the laws, rules, and regulations that govern economic relationships (North, 1990)), may not be well developed and supportive of market transactions; the government and its agencies may not implement the rules and regulations in an effective and unbiased manner; and the specialized intermediaries that facilitate market transactions may not be up to par (Khanna & Palepu, 2010). In such conditions, poor and unethical governance may be prevalent. For example, corruption in government is more common in emerging economies because politicians and civil servants are not subject to stringent controls over their decisions and behavior, resulting in higher costs of operation and higher uncertainty for companies (Kaufmann, 2007). Fraud may also be more common in emerging economies as managers are less constrained in their ability to take advantage of business partners and can get away with defaulting on contracts because the judicial system is ineffective (Henisz, 2000). Theft of intellectual property may be more widespread in emerging economies because innovative companies find that they are unable to enforce intellectual property rights protection as courts are ineffective (Zhao, 2006). Companies establish close relationships with government officials to be able to navigate such environments. Ties with members of the ruler's family are the basis of much of the advantage of the companies, and when the ruler is replaced the companies suffer in their performance (Fisman, 2001). Emerging market firms learn to adapt to these weak governance conditions and develop a capability to manage under such conditions that proves useful when entering other countries with weak institutions (Cuervo-Cazurra & Genc, 2008). The exposure to political risk and corruption at home reduces profitability but helps improve profitability when investing in distant countries (Cuervo-Cazurra, Ciravegna, Melgarejo, & Lopez, 2018).

Monitoring of unethical behavior

Host-country governments may be concerned that emerging market firms bring with them lessons on how to deal with weak institutions and may apply unethical behavior and poor governance practices in the host economy. Learning how to deal with the weak institutions in the home country, which in many cases involves very deep connections with politicians (Ghemawat & Khanna, 1998), may in some cases morph into outright corruption or disregard for the law. Thus, for example, investors from countries with higher levels of corruption do not appear to be deterred by bribery in the host country but rather attracted by it, because they already know how to bribe officials to get contracts and permits (Cuervo-Cazurra, 2006); government representatives from corrupt countries appear to disregard parking laws in other nations because they are not used to following existing regulations (Fisman & Miguel, 2007). Host-country governments may be concerned about the potential misbehavior of emerging market firms as they may bring similar poor governance attitudes to their operations in the host economy.

To address this potential misbehavior, the government in the host country may need to implement strict monitoring of firms from countries with weak institutions to ensure that the companies do not transfer some of their poor governance practices to the host economy. This does not require the creation of additional rules for emerging market multinationals, but merely monitoring and enforcing existing laws and regulations. Countries with better governance attract more acquisitions and may help improve governance in acquirers (Rossi & Volpin, 2004). Such enforcement needs to be done in equal terms for all firms regardless of the country of origin. Although there might be a perception that emerging market multinationals are more likely to be unethical, this is not always the case. Advanced economy firms may also misbehave abroad even if they implement good governance practices at home. For example, the German engineering conglomerate Siemens did not bribe in Germany, but had a sophisticated organization to bribe politicians and regulators all over the world to gain contracts (Schubert & Millerdec, 2008).

Limitations on monitoring of emerging market multinationals

This monitoring of the governance of emerging market multinationals has some limitations. One is that not all emerging market multinationals are misgoverned. Many emerging market companies have strict governance and end up investing in countries with strong institutions to bond themselves and reduce the association with the weak governance standards of the home country (Coffee, 2002). There is also a substantial variation among emerging markets in terms of the quality of governance, and some have institutions that are better than those in more advanced economies. For example, Botswana and Chile have similar or better governance levels than Italy or Spain (World Bank, 2017). Also, it is not clear that advanced economies have more stringent governance standards and more transparency requirements for firms. Whereas the typical perception of offshore financial centers is that these are small emerging economies with lax governance, this is not always correct. For example, it appears that it is easier to open anonymous shell companies with bank accounts in many OECD countries like the US and UK than in small island offshore centers (Sharman, 2010), and when Alibaba was looking for a market to become listed, it ended up issuing its initial public offer in New York rather than Hong Kong, because the latter would not allow dual-class shares nor the founder and managers picking most of the board members despite controlling little more than 10% of the company (Davies, 2013).

Psychological Concerns: Loss of Relative Status and Controls over New Competitors

Loss of relative status

A third concern regarding the global expansion of emerging market multinationals is their rapid catching up to advanced economy competitors, and in some cases surpassing them (Cuervo-Cazurra, Newburry, & Park, 2016); this results in a loss of relative status for advanced economy firms and their countries. The traditional ranking of countries and their firms has changed dramatically in recent decades. After the Second World War, US firms dominated the global landscape; European competitors and later Japanese ones improved their positions as their economies recovered from the war. There were few changes in relative status, with the exceptions of smallish economies like Hong Kong, Taiwan, Singapore, and South Korea that became advanced by the 1980s. However, pro-market reforms in the 1990s led to a significant transformation of countries and companies as developing nations liberalized their economies and adapted many technological and organizational innovations from advanced economies (Amsdem, 2001). This led to a massive transformation of the relative ranking of economies, in which the traditional group of six (US, UK, France, Germany, Japan, and Canada) was superseded by the group of twenty as the relevant forum for discussion, and the BRIC (Brazil, Russia, India, and China) economies were branded as the economies of the future (O'Neill, Wilson, Purushothaman, & Stupnytska, 2005). Emerging market multinationals played an essential role in this transformation as they quickly grew not only in size but also in international competitiveness (Ramamurti & Singh, 2009; Williamson et al., 2013). A few emerging market firms started to question the dominance in global markets of advanced economy multinationals (BCG, 2006, 2016). Some of these emerging market challengers surpassed their advanced economy counterparts, and ended up purchasing iconic companies (e.g., the US brewers Miller and Budweiser, which dominated the US market, ended up being acquired by a South African and a Brazilian-led firm, respectively).

Controls on upcoming competitors

This rapid rise of emerging economies and the subsequent change in the ranking of the top countries and firms appears to concern government officials and citizens in advanced economies who fear of the loss of relative status; they may seek to control the continued growth of these firms as a response. Politicians and commentators in advanced economies increasingly see this rapid developmental process with suspicion or even outright fear that their countries would be taken over in development by nations that until recently were poor and backward (Friedman & Mandelbaum, 2011). Such concerns have increased as host-country governments perceive that emerging market multinationals are receiving preferential financing from their home governments, as has been the case of the Brazilian government financing the global expansion of private firms through the state-owned BNDES (Lazzarini, Musacchio, Bandeira-de-Mello, & Marcon, 2015), and the Chinese government mandating and supporting the global expansion of companies (Luo, Xue, & Han, 2010).

Host-country governments may try to impose controls that signal that they are doing something to stop the catching up by emerging market firms. For example, in the 1980s, the US government asked Japanese firms to voluntarily limit the export of cars to the US (AP, 1991). However, establishing a policy on the basis of perceived loss of status or fairness is challenging because there are no appropriate criteria to establish ex-ante rules that can be applied objectively. Without a rule-based logic, such policies can become tools for garnering domestic political support without a clear logic for applying them appropriately, and they can be challenged easily in existing multilateral agreements. This lack of a well-defined rationale appeared to be happening with the tariffs that US President Trump imposed against Chinese goods in 2018. Although the tariffs were imposed in the name of reducing the trade deficit, they seemed instead to target industries in which the Chinese government wanted to achieve future leadership, such as information technology products, electric vehicles, aerospace, and robotics (Wildau, 2018).

Limitations to controls on upcoming competitors

These policies of controlling emerging market multinationals to maintain relative status face a barrier in the ability of the host country to force emerging market firms, and implicitly their governments, to accept the policies. The acceptance of controls depends on the relative size of the countries and the importance of the host country for the companies and their governments. Governments of small host countries may not be able to unilaterally develop controls over emerging market multinationals, because the host countries are not sufficiently important as markets. Additionally, there is the challenge of deciding which industries the host-country government needs to protect because they will be the basis of its future development. It is challenging to pick winners and the industries of the future. Establishing controls to safeguard specific sectors may open the door for domestic competitors lobbying for protectionism, reducing competitive pressures that would spur innovation.

CONCLUSIONS: EX-ANTE RULES-BASED POLICY FOR STATE-OWNED MULTINATIONALS FROM EMERGING ECONOMIES

Most governments are eager to attract foreign direct investment because it is seen as helping the country receive the benefits of investments and spillovers that support its development. However, investments by state-owned firms from emerging economies tend to be viewed with suspicion and are subject to additional review and in some cases blockage. I analyzed this interesting tension between the theory and policy practice and proposed an ex-ante rules-based treatment of foreign investors that clarifies the reasons for the policy and its limitations. Specifically, I proposed a separation of the influence of state ownership from emerging country origin, and a separation of the concerns about these by three underlying approaches: economic, political, and psychological. This separation reveals that many of the discourses that use the economic justification to try to exclude these firms, such as national security and strategic industries, are in reality driven by the political issues of opacity and weak governance and, especially, by the psychological concerns of dealing with unfriendly governments and loss of status.

In the economic arena, governments are free to define what they consider to be sectors of national security or of strategic importance for the development of the country, and exclude foreign firms from these sectors if they deem it appropriate. However, there is an implicit cost of such exclusion in the form of domestic companies lobbying for their industry to be considered of national security or strategic interest to obtain competitive relief from foreign competition. An ex-ante definition of the sectors and assets that are indeed of national interest will reduce such lobbying and maintain continued pressure to innovate on domestic companies.

The political issues of opacity and weak governance can be better dealt with via monitoring of the practices and actions of foreign firms in the host country, and the requirement that they abide by existing local regulations and laws. This monitoring not only facilitates their investments, but also provides a level playing field to all foreign and domestic competitors. All have to follow continuously improving governance standards. Opacity and weak governance concerns can be easily dealt with by existing rules rather than being used as justifications for excluding firms.

The psychological issues of dealing with unfriendly governments and status loss are more challenging in the sense that it is more difficult to establish clear ex-ante standards of what an unfriendly government or a status loss is. They are also arduous to apply because the relationships among countries change over time, in some cases very quickly, and policy is tricky to develop and implement consistently when following attitudes rather than principles. Thus, controls over foreign multinationals, not only in terms of their investments but also regarding their trading behavior, may provide the needed flexibility. The caveat is that such ad-hoc interventions can not only be challenged in bilateral and multilateral trade agreements, but also may result in tit-for-tat responses in which all countries suffer.

In conclusion, open borders facilitate the transfer of knowledge and technologies across countries and the integration and development of nations. Foreign direct investment is perceived as bringing many benefits to host economies. Historical examples of countries that blocked foreign investments and exchanges, such as China and Japan in the 16th–19th centuries and Latin American countries in the middle of the 20th century, as well as recent ones such as North Korea or Venezuela, illustrate how such exclusions have resulted in a lack of development. Even if the host-country government has concerns about investments by state-owned multinationals from emerging economies, such worries need to be considered in light of the opportunity cost of missing investments. An appropriate host-country policy is one that provides an ex-ante rules-based framework by which the economic, political, and psychological concerns about the behavior of foreign firms can be addressed. Many of the economic claims that politicians make in the name of national security or protection of strategic assets seem instead to be driven by psychological conceptualizations, and by interest groups. An ex-ante rules-based framework can help limit state capture by such interests.

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