Transnational corporations, nation-states and labour

Abstract

Following a brief review of the standard approaches to the explanation of transnational corporations (TNCs) and their activities the paper presents a theory based on the following building blocks.

(1) The approach is strategic rather than based on efficiency. The strategic behaviour is linked to TNCs' power towards other actors in the economic system such as rivals, labour and governments. While a good amount of literature has concentrated on strategic behaviour towards rivals, this paper concentrates on power and strategies towards other players and particularly towards labour and governments.

(2) It looks for explanations in the multi-nationality characteristic and therefore in institutional elements: the characteristics of nation-states and of operations across frontiers.

(3) Nation-states are characterized in terms of their regulatory regimes. TNCs operate across different regulatory regimes which are defined in terms of: labour and social security issues; tax regimes and currency regimes. By operating across many nation-states TNCs take advantage of the differences between different regimes in its conflicts with labour over the distribution (of profits versus wages) and with governments (over, for example, tax liabilities or the size of financial incentives to attract inward FDI).

(4) As regards labour, the hypothesis put forward is that TNCs follow fragmentation strategies towards the labour force. These strategies can take a locational (by nation-states) and/or an organisational mode (via outsourcing). In both cases they are likely to lead to the weakening of the power of labour towards capital.

Key words. Transnational companies; theories of international production; role of nation-states; strategic versus efficiency approaches

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Transnational corporations, nation-states and labour[1]

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1. Introduction

The study of transnational corporations (TNCs) and international production has, on the whole, remained outside mainstream economics teaching. Some material is taught usually as part of courses on industrial economics. However, most of the rest of economics largely ignores the literature on TNCs and the issues raised by the main actors in contemporary economic systems. In Business Schools there is a wider interest in TNCs and their activities though, on the whole, the approach tends to be from a more managerial than economics perspective.

However, a recent textbook by Giorgio Barba Navaretti and Anthony Venables (2004) may change this and is likely to lead to more teaching on the economics of TNCs in economics degrees. Should we be pleased about such a development? The book is developed on the basis of the tenets of the mainstream neoclassical economics paradigm: the international business solutions come out of the search for equilibrium in a context in which the actors' behaviour is profit maximizing and efficiency seeking.

This paradigmatic approach finds roots in a series of research works inspired by the so called 'New Trade' theories of the multinational companies (MNCs) [2] on which more in section two. The research on MNCs' activities within this approach is connected with the more traditional international business literature via its links to the internalization theory of the TNCs and – to a lesser extent - to Dunning's eclectic framework.

While the spread of interest in the study and teaching of international business to the wider economics community is welcome, the neoclassical paradigm is a straightjacket which may prove unhelpful in our understanding of the motivations and activities of TNCs and of their effects. In order to justify this statement I shall first consider very briefly the main theories of international production in historical perspective (section two). This will be followed (in section three) by an analysis of the role of the nation-state in explanations of international production; an analysis of strategic versus efficiency approaches to international production will be presented in section four. The last section summarises and concludes.

2. The main theories in historical perspective[3]

[1] A version of this paper is appearing in *Critical Perspectives on International Business,* 2007 (forthcoming).

[2] On the whole I prefer to use the term 'transnational' rather than 'multinational' because it better highlights the cross-countries reach and strategies of modern large companies. However the term 'multinational companies/corporations' will be used when referring to theories and authors who use it themselves.

[3] The various theories here touched on are summarized and critically analyzed to a greater detail in Ietto-Gillies (2005). See also the survey in Cantwell (2000).

Hymer[4]

The modern theories of the TNCs started with the seminal doctoral dissertation by Stephen Hymer (1960, published 1976) where he suggests that there are two main determinants of direct investment abroad. A key assumption in both these determinants is the existence of market imperfections; connected to this is the desire of the company's managers to further enhance its market power position.

The first determinant is the existence of *specific advantages* that – particularly once the domestic investment opportunities have been exhausted – put the firm in a favourable position to branch out in foreign production locations. The advantages are directly linked to market imperfections because the firm that commands market power through them has a competitive advantage over its rivals. Moreover, the exploitation of advantages in foreign markets enhances further the firm's market power and thus it increases the overall level of imperfections in the market.

Licensing is seen as a less profitable modality of involvement in foreign countries than direct production; the reason for this has mainly to do with the perception that licensing involves risks of debasing the quality of products and of losing the monopoly over specific knowledge and technology.

The second determinant is the *removal of conflicts* in foreign markets. Whenever several firms are already operating in a foreign market - or trying to get into it - a conflictual situation is likely to emerge. The conflict can be removed either via collusion in the sharing of markets between rivals or because a specific firm gets direct control of production abroad. The latter strategy leads to an increase in market power for our specific firm and thus, again, to the increase in imperfections for the market as a whole.

Hymer's main message is that, for direct investment to thrive there must be market imperfections that create both advantages and conflicts. By investing directly and by thus reducing competition, the firm aims to reduce or eliminate the conflicts while exploiting its own advantages.

The two main types of determinants (firm's specific advantages and removal of conflicts) are closely linked. The existence of advantages is part and parcel of the market imperfections that lead to conflicts. The competitive advantages of the firm allow the removal of conflicts via the acquisition of control over the foreign business. Both determinants have their roots in the imperfect market structure. The behaviour of the firm, in its desire to gain control over foreign operations, leads to the enhancement of its market power and thus to increased profits.

Vernon and the product life cycle

Raymond Vernon was working at Harvard up the road from the MIT in Cambridge, Massachusetts where Hymer was based when he developed a theory of internationalization based on the product rather than the firm as in the case of Hymer. Specifically, Vernon (1966) starts from an analysis of the life cycle of the product

[4] For developments and critical analyses of Hymer's work see Yamin (2000) as well as the various contributions to special editions on Hymer of: *Contributions to Political Economy* (2002) and *International Business Review* (2006).

originally developed by Kutznets (1953). Other antecedents to Vernon's approach are to be found in the technological gap theory of trade (Posner, 1961).

Vernon argues that the economic and social environment of a high per capita income and capital abundant country – the USA – creates the conditions for new products to be developed. The first firm to develop a new product acquires a monopolistic position; however, such position will gradually be eroded by competition as the product is imitated first by other firms at home and later in other developed and developing countries.

Within his theory Vernon analyzed developments in - and interactions between - the following elements: (a) the demand for the product; (b) the competitive environment; and (c) the location of production. As demand at home and abroad grows the following pattern emerges: the product is first produced at home and exported to other high income countries; later, as the product becomes mature, direct production in these countries follows. In the last phase of the product life cycle imitation becomes widespread. This leads the firm to try and compete via cost cutting and thus to locate production in developing countries.

Exports and imports of the product follow a pattern related to international production. The product is first exported from the US to European countries till direct production in Europe takes over as the main modality for sourcing the European markets. In the last phase, when direct production is located in developing countries, the product may be exported from these countries not only to Europe but also to the US itself, where the product and production originated.

The theory is therefore developed as an interplay of: market structure, from a monopolistic position in the new product and its technology to increasing competition; life cycle of the product: from innovation to maturity to standardization; development of demand for the product: in the USA and in Europe; location pattern of production: from the US to Europe to developing countries; trade pattern which is linked to the location of production and to the location of consumers.

The theory has had a tremendous success and has also given rise to very large number of critiques including some from Vernon himself (1979). More recently criticism has focused on the theory' ability to explain the innovation activities of firms and industries (Cantwell, 1995).

The Reading School

John Dunning had been working on international business research since the 1950s, well before he came up with his eclectic theory (1977). His approach is more in the nature of a theoretical framework to explain the 'why, where and when' of international production. This he does by analyzing three groups of advantages: *ownership advantages; location advantages and internalization advantages (OLI).* The first set of advantages (O) explains which firm is in a favoured position for investing abroad; the second set (L) explains why some locations are favoured over others for investment; and the third set (I) explains why the direct production route is preferred to externalization modalities of foreign involvement such as licensing.

It is on the latter type of advantages – internalization – that two other members of the Reading Economics Department – Peter Buckley and Mark Casson - concentrated in

developing their own theory, the seeds of which were in McManus (1972). Buckley and Casson (1976) use Coase's (1937) transaction costs theory to develop a theory of why direct production is a superior modality of international business for companies, particularly those involved in high levels of research and development (R&D) expenditure. It is the superiority of direct production – and thus of internalizing the various stages of production – over more external forms, such as licensing, that determines the choice of modality of operations. The superiority in terms of efficiency derives from the fact that operating internally to the firm rather than on the market saves costs of transactions; moreover, internalizing allows the firm to retain its proprietary knowledge from R&D activities.

The 'New Trade' theories approach[5]

The efficiency approach to corporate transnational activities has more recently been taken a step further by the so-called 'New Trade' theories. The 'new trade' theorists (Krugman, 1985; 1991; 1998) develop theories of trade based on equilibrium under monopolistic competition and on the assumption that there are economies of scale internal to the firm (the Chamberlinian type) and/or external to it (the Marshallian type). The resultant agglomeration tendencies have implications for the geography of production. Theoretical results predicting agglomeration patterns would seem to militate against the reality of spread of production into different countries via the foreign direct investment (FDI) activities of MNCs.

So how does production by MNCs come into the picture and be justified in the context of a theoretical approach that predicts agglomeration? The researchers make a series of assumptions to explain FDI in either developing or developed countries. As regards location in developing countries (Helpman, 1984 and 1985; Helpman and Krugman, 1985) the assumptions relate to internal economies; they can be considered to be at (a) the plant level and (b) the firm level. The efficient outcome from such a model leads to the prediction of vertical fragmentation of production across several countries: the location of labour intensive components will take place in developing countries while the developed countries will specialize in capital intensive components.

A different set of assumptions is made in order to explain international production of the horizontal type: a situation in which similar types of products/components are located in countries at similar stage of development i.e. in developed countries (Markusen, 1984; 1995). The assumptions made relate to fixed joint inputs particularly in the area of R&D as well as to high costs of transportation.

It should be pointed out that the theories of the MNCs have great difficulties in explaining the spread of production into many countries by MNCs. Krugman (1998: 15) while using cautious words can be read as fairly explicit on this. He writes: "… preliminary efforts… have found that such models are not at all easy to calibrate to actual data; in general, the tendency toward agglomeration is stronger in the models than in the real economy!" Whatever the assumptions that allow the compatibility of TNCs' activities with agglomeration economies, the key elements of the theories relate to the fact that TNCs are analyzed in terms of their efficiency and in the context of equilibrium: a standard neo-classical approach though developed in the context of monopolistic

[5] More on this approach in Ietto-Gillies (2000)

competition and economies of scale rather than in the context of perfect competition and constant returns.

Other approaches

Through the decades following the 1960s many other theories have been developed though none as influential on the community of international business researchers as the ones highlighted above. Among the many other approaches are the following.

In 1970 Aliber proposed a theory of movement of financial assets based on differences of currencies and fiscal regimes between countries. On the whole it did not have much follow up partly because the international business community was trying to explain production abroad and thus FDI, while Aliber's theory was considered more appropriate for financial flows due to portfolio rather than direct investment. Both type of investment have increased considerably since the 1970s; however, even if FDI may entail some movements of funds, its explanation must address the issue of why firms want to produce abroad.

An interesting follow up on Vernon was developed by one of his students: Frederick Knickerbocker. He starts from the product life cycle theory with the aim to develop an explanation for locational 'bunching up' of foreign direct investment (Knickerbocker, 1973). He noticed a tendency for FDI to be located in the same countries in industries characterized by an oligopolistic structure. He explains this as the result of 'attack and defence' behaviour by rival firms. More recently Edward Graham (1990 and 1998) has followed up the same lead.

The oligopolistic structure is key also to the work of Cowling and Sugden (1987) who emphasize rivalristic behaviour by TNCs and the effects of their activities on nations and communities. Sugden (1991) and Peoples and Sugden (2000) stress another element - already present in Cowling and Sugden: strategic behaviour towards labour and the advantageous position that TNCs are in because they can follow 'divide and rule' strategies towards labour. The theme of strategies towards labour as a key determinant of TNCs activities is further developed in Ietto-Gillies (2005: ch. 15).

One key element in Vernon's theory is the emphasis on innovation and technology and their diffusion/transfer to other countries. The innovation and technology emphasis is characteristic of John Cantwell's work (1989)[6]. Though based at Reading University, Cantwell has followed a different trajectory from Buckley and Casson; nonetheless, his developments have much in common with Dunning. Cantwell sees firms as generators of their own ownership advantages via innovation and technology strategies. He also emphasizes the spread of knowledge and innovation within the firm and across countries; this leads to an endogenous view of locational advantages as well as of the ownership ones. The emphasis on innovation gives the same starting point as Vernon's; however, the similarities end there and Cantwell (1995) clearly demarcates them in his critique of the International Product Life Cycle Theory.

The issue of knowledge transfer is taken up by the so-called evolutionary theory of the TNC of which the developments by Cantwell represent one strand. Another strand is more closely linked to the internalization theory. The latter sees TNCs as minimisers of

[6] Cantwell has developed his work since and presented it in many publication (see Ietto-Gillies, 2005: ch 12)

transaction costs and thus as efficiency driven organizations; the evolutionary theory of Kogut and Zander (1993) sees the TNC as a social institution in which congenial social relation among the workforce lead to efficiency in the development and transfer of knowledge within the company and across countries.

A different approach to international business has been developed by the Scandinavian School (Johanson and Wiedersheim-Paul, 1975; Johanson and Vahlne, 1977 and 1990). The antecedents to their work can be traced to Penrose (1959), Cyert and March (1963) and Aharoni (1966). The preoccupation of this school has been more with the stages in the internationalization process than with the underlying motives for international production per se.

In the next two sections the activities of TNCs and related theoretical approaches to their explanations will be examined from two perspectives: the first perspective considers the role of the nation-state in theories of the TNC; the second perspective looks at the underlying assumptions about firms' behaviour that inspired the theories. The relationship between the first and second perspective will also be analyzed.

3. The role of the nation-state in theories of the TNC[7]

Most economics texts ignore the TNCs and therefore ignore the domestic versus foreign character of the investor or producer, or more specifically, ignore the actual nationality of the investor. Instead, concentration tends to focus on such issues as the following: the firm in general or in relation to its size or organization; the market structure of an industry; the production, investment or trade of the macro economy independently of the nationality of the firm producing, investing or trading. This is exactly what we do when we study, for example, trade theory: we analyse the comparative conditions and advantages of the trading countries and/or the impact of trade on them independently of the national character/identity of the exporter firm. International business studies and theories take a different approach and consider important the nationality of the investor. It is time to have a discussion about this. Standard economic theory does not seem to bother about the nationality of the exporter or importer; why should we bother about national identity when we analyse investment? In fact, we do not attach much relevance to the identity of the investors when they originate from other regions within the same nation-state; for example when a Texan firm invests in California or a firm from Lombardy invests in Sicily. Why should we consider the origin of the firm as relevant when it is from a foreign country?

What I mean is that the case for a special study of the TNC is not obvious. Traditionally, economists have looked into the specific characteristics of the investor, when studying the investment by public firms versus private ones. However, the reason for this is clear: the public investor is assumed to have different *objectives* compared with the private one and thus the identity private/public does matter. But this is not the case when the investor is a TNC. Whether the firm is foreign or domestic, whether it is a transnational or a uninational firm, the objectives are not different; they are profit objectives.

In fact the reason why in our case the uni- or multi-national character of the investor matters has nothing to do with objectives but with *strategies*. In order to argue

[7] This section draws largely on Ietto-Gillies (2004 and 2005: ch 15).

for the relevance of cross-border elements in international production decisions, let us start by considering the following three main dimensions to operations across national frontiers:

1. *Spatial/geographical dimension*. The distance between locations in different nation-states is often greater than the distance between locations within the same nation-state, though this is not always the case. For example, the distance between Boston and San Francisco is far greater than the distance between Boston and Montreal. The spatial distance – whether within or across nations – affects the costs of transportation.
2. *Cultural and linguistic dimension*. The cultural distance is usually greater between nation-states than between regions of the same nation-state. But again, this is not always the case. The cultural distance between Milan and Geneva is probably lower than the one between Milan and Reggio Calabria. Cultural and linguistic distance affects the ease and costs of business operations.
3. *Regulatory regimes dimension*. By regulatory regime I mean the sets of all laws, regulations and customs governing the economic, social and political life of a country. It includes the institutional sets of rules governing production, markets and the movement of resources across countries. Each country has specific regulatory regimes and thus specific sets of rules and regulations which often have historical origins and connotations. Countries differ – often substantially – in terms of their specific regulatory regimes. However, the regulatory regimes tend to be fairly – though not completely – homogeneous and consistent within each nation-state. In particular, different nation-states have different:
   (a) currency regimes;
   (b) tax regimes;
   (c) rules and regulations regarding the social security system and specifically different regimes regarding labour and its organisation

Dimensions one, two and three all contribute to characterize the differences between states; they are also all important elements in decisions and strategies related to international business activities. Moreover, it is the third dimension that generates opportunities – as well as some costs – for taking advantages of economic activities across frontiers.

The existence of different frontiers may generate additional costs for business activities usually associated mainly with the first two dimensions, though the third dimension may also generate costs. For the TNCs, organizing and managing under different laws, regulations, cultures, may be costly; uncertainty over exchange rates may be a disadvantage of operations across countries.

However, the third dimension related to ‘regulatory regimes’ may also give rise to specific advantages of transnationality *per se*. Specifically, advantages:

- Regarding different currency and tax regimes
- Towards labour
- In negotiations with governments
- Related to risk spreading

Thus the existence of different *currencies and taxation regimes* may, for example, give TNCs the opportunity to develop strategies of production location and intra-firm transfers; such strategies allow companies to manipulate transfer prices [8], a technique by which they can achieve higher profits than they would otherwise have achieved.

The literature on large firms – whether TNCs or not[9] - gives some emphasis on strategies towards rival firms in particular in the context of oligopolistic market structures. The advantage of transnationality can be used – and has at times been used - to analyse advantages towards rivals. However, strategic behaviour towards other players in the economic system such as labour or governments has been given less weight. Yet it is with respect to these other players that the advantages of transnationality can be used most effectively.

It is particularly with regard to *labour* that the opportunity to develop advantageous strategies arises. Unlike the TNC, labour has, so far, been unable to organise itself across frontiers and, indeed, labour solidarity across frontiers tends to be much lower than within frontiers.

This means that whenever a TNC has production spread into many nation-states it faces a labour force working for it that is more fragmented/segmented and less able to organise and resist the demands of corporate capital. This situation should be assessed in comparison with one in which the same labour force were all to be employed by the same company to produce the same amount of output in one single country. The latter situation would make labour organisation and resistance much stronger. Thus a strategy of international location may also be a *strategy of labour fragmentation/segmentation*[10].

A strategy of locational fragmentation/segmentation weakens the power of labour to resist in any conflict with capital. This effect is compounded by another type of fragmentation strategy which has been pursued in the last two decades by large uni- and multi-national organisations in both the private and public sector. I refer to *organisational fragmentations* in which businesses (private and/or public institutions) outsource part of their activities thus forcing the labour force previously all working for the same organisation, to work for a variety of enterprises. This organizational fragmentation makes it more difficult for labour to organise and resist the pressures of capital for poor and divisive pay and conditions.

The existence of nation-states with their different regulatory fiscal regimes also gives scope to companies for the development of strategies towards governments. Transnational companies can – and do – play *governments* of different countries or regions against each other with the objective of raising the offer of financial incentives for the location of inward FDI (Oman, 2000; Phelps and Raines, 2002). The fact that the company operates with a large multinational internal network makes any threat of relocation of production very credible as it could be achieved with relatively low costs.

[8] On transfer prices and reason for their possible manipulation see Ietto-Gillies (2005: ch. 20)

[9] But, of course, most large firms are transnationals because operations abroad is part of growth strategies and often a condition for growth.

[10] See Ietto-Gillies (2002: ch. 6 and 2005: ch 15).

Thus the TNC with a production network spreading into many countries[11] has a strong element of bargaining power towards both governments and labour force.

Moreover, location of production in several countries will *spread the risks*, particularly those associated with political or labour unrest. It may also enhance the company's innovative power as it learns from different environments (Cantwell, 1989 and 1995; Frenz and Ietto-Gillies, 2007; Castellani and Zanfei, 2006).

The conclusion is that companies that can truly plan, organize, control activities and assets across frontiers can also develop strategies to take advantage of differences in regulatory regimes across frontiers. Thus the transnational company - by virtue of operating effectively across different nation-states and thus across different regulatory regimes - has wider opportunities for developing strategies designed to improve its position vis-à-vis other actors in the economic system who have been less able – so far – to operate across frontiers as effectively as the TNC. In this approach the spread of production into many countries becomes one of the strategies to increase profits.

So the reason why the nationality of the company matters is not due to its having different objectives from other firms (as in the case of private versus public institutions) but to its having different and wider *opportunities for strategies* to pursue its profits aims. Two consequences derive from this.

First, a realistic approach to explanations of the activities of TNCs must take account of specific cross-border institutional elements. Unfortunately most theories of the TNCs' activities do not take adequate account of the trans-national nature of the operations; that is they do not take adequate account of opportunities[12] related to specific characteristics of the nation-states. In most cases the theories apply to different regions of the same countries as to different nation-states. This means that the specific characteristics of different nation-states – i.e. the differences in regulatory regimes – are not properly accounted for. Quite a few theories take account of differences in fiscal regimes and Aliber's theory takes account of different fiscal and currency regimes. However, no theory – as far as I know[13] – takes account of the different regulatory regimes regarding labour and the social security system. Yet even a superficial reading of the business press shows that this issue is at the forefront of firms' location decisions. Why else would the British and other governments in Europe oppose the harmonization of social security (the social charter) and of fiscal regimes across the EU?

Second, different regulatory regimes give rise to opportunities for companies' strategies. This makes a strategic approach to the explanation of TNCs' activities even more relevant than a similar approach regarding the firm in general.

4. Efficiency versus strategic approaches in theoretical explanations

When we are dealing with large and powerful organisations, a strategic approach is necessary for the understanding of their activities, their motivations and implications. This wider approach to strategic behaviour is particularly relevant when dealing with actors that operate across national frontiers because this element gives companies opportunities for additional strategies. However, we must move away from a strategic

[11] On the theoretical and empirical analyses of international networks of the world's largest TNCs cf. Ietto-Gillies (2002: chs 3, 4 and 5).
[12] However, account is more often taken of the additional costs that operating across frontiers may involve.
[13] Apart from Ietto-Gillies (2005: ch 15) and to some extent Sugden (1991).

approach focused only on strategies towards rivals, in the direction of an approach that considers also TNCs' strategies towards other players in the economic system such as labour and governments or supplier firms. It is in the context of dealing with other actors – particularly labour and governments – that operations across frontiers give rise to opportunities and advantages for companies. Success in the strategies towards labour and governments will also give the firm a competitive advantage towards its rivals.

There are many underlying similarities in the theories of international production developed through the decades. There are also considerable differences. One specific area of commonality or demarcation between theories can be the assumptions behind the driving forces in the behaviour of companies regarding their internationalization decisions; by this I mean the extent to which each theory sees the decisions of companies as led by the desire to utilize their resources efficiently and thus maximise profits via cost reduction – as well as increased revenues – or whether the decisions are strategy-led, that is whether the companies have an overall vision of where they want to be and how to get there.

It could undoubtedly be argued that all companies strive to maximise their profits and that therefore the dichotomy strategic versus efficiency behaviour is irrelevant. However, profit maximization is not a clear concept except perhaps in the very theoretical works of neo-classical economists. What costs do we consider when we set up our maximising models? Do we know much about costs and revenue patterns and curves? What are the underlying assumptions behind our precise, elegant curves? Do we maximise over the short, medium or long term? We can all agree that firms want profits or so called shareholders' value; however, the practical details of this are not clear. This is why I think that the distinction between theories that are inspired by strategy-led or efficiency-led behaviour by companies can be useful even bearing in mind the following; (a) that the demarcation is not clear cut and the borderline between the two approaches is often difficult to see; (b) efficiency is a precise concept in the context of an unrealistic framework while strategy is an imprecise concept in the context of a realistic approach, the reality of actual firms' behaviour.

Moreover, while an efficiency approach is perhaps easier to detect, when it comes to the strategy approach we are at greater difficulty: strategies in what respect and towards whom? The strategic behaviour can refer to production elements or to research or to market penetration or to a combination of these and other elements. It can also be directed towards rivals or towards other actors in the economic system such as labour or governments or suppliers.

The theories of international production that seem to conform more to the assumption of profit maximisation and cost efficiency are the following: Aliber's theory that relates the cross-border flow of funds to the differences in currencies and in taxation rates; the internalization theory that relates decision on internationalization modes to the minimisation of transaction costs; the 'New Trade' theories because they are largely based on the same principles as the internalisation theory.

Theories that are inspired by a strategic approach usually start from the realistic assumption that companies that are or become transnationals operate in oligopolistic market structures; this means that one of their main preoccupation is their rivals and how to deal with the competition from them. Market power then becomes a key element of strategies: market power affects behaviour and is affected by it, as we saw in Hymer's

theory. Innovation capabilities and innovation activities impact on market power – as in the case of Vernon's and of Cantwell's theories. In the case of Knickerbocker's theory the geographical pattern of FDI emerges from the rivalristic behaviour of companies wanting to get ahead of their rivals; attack and defence strategies by rival firms play a key role in Cowling and Sugden's theory. Dunning's framework being all embracing and eclectic contains elements of efficiency approach – in the internalization elements – and of strategic approach – in the ownership advantages elements.

In section three it was argued that the nation-states with their different regulatory regimes should play a (the?) main role in theoretical explanations. A theory of the TNC should be informed by issues related to firms and industries in general but, over and above that, we need to explain the inter-national dimension of the business; that is we need to explain why and under what circumstances a Texan firm might prefer to invest in Canada or Europe rather than in California. That is we need to embody into the theories specific trans-national elements in order to make them not only theories of the firm's behaviour but also theories of their behaviour in the context of trans-nationality.

This takes us to the distinctive character of nation states and how their specific characteristics may generate opportunities for strategies by firms. The strategies which become relevant in this context are not only those towards rivals but also those towards labour and governments. In other words, a realistic theory of the TNC must take account of opportunities for strategic behaviour offered by the different regulatory regimes of nation-states. Thus in the context of trans-national activities strategic behaviour becomes ever more relevant than efficiency-led behaviour; moreover, there arise a need to take into account a plurality of elements and actors relevant for strategies in the trans-national context. The latter point means that strategic behaviour towards rivals must be considered alongside strategic behaviour towards labour and governments if we want to reach some understanding of what motivates TNCs and what leads to their behaviour.

5. Conclusions

Following a brief excursion into the main theories of international production developed since World War II, the paper has considered why characteristics of the nation-state are relevant for understanding the behaviour of firms in their trans-national context. Different regulatory regimes offer the firm opportunities for the development of a variety of strategies. The paper then analyses the various theoretical approaches according to whether they are based on efficiency versus strategic company objectives. It links the need to give prominence to the nation-state to the need to consider strategic behaviour in the development of theories.

Transnational companies are complex institutions and their motivations and behaviour are not easily disentangled by simple theoretical approaches. Nonetheless, there seem to be two elements that make a theory relevant and realistic. First, the institutional context: the nation-state and the nationality of the investor must play a role in the theory otherwise it becomes unclear why we do not use standard economic theories of the firm in general and how and to what extent we can claim that our theories relate to trans-national activities. Second, once the role of nation-states is properly analyzed, it becomes clear that the existence of different regulatory regimes offer the firm scope for the development of a wide range of different strategies. Thus a proper trans-national

analysis, i.e. one linking the firm's behaviour to characteristics of the nation-states becomes also an analysis in terms of strategies. This means analysing the company's behaviour as inspired by attempts to develop strategies to cope with the threats and take advantages of opportunities: some of these opportunities are indeed offered by operating across frontiers.

Strategies can be developed with regards to rivals or to markets and consumers or to innovation or to workforce or to governments. While strategic behaviour towards rivals has been considered in the literature on TNCs, the strategic behaviour towards the labour force or governments has been rather neglected. Yet, it is specifically in the development of strategies towards labour and governments that the trans-national dimension of operations can be turned into a great advantage: operating in several nation-states with their different social security and fiscal regimes may put the TNC at a great advantage towards its workforce or towards its bargaining with governments.

There are strategic policy implications from this approach. If operating across frontiers gives companies specific advantages in dealing with labour and governments, then the answer may be to try and redress the balance for these actors. This can be done by a stronger inter-national focus and organization. As regards labour, the information technologies will increasingly make it easier to exchange information and cooperate across frontiers even if full trade union organization, solidarity and resistance across borders may require wider social and cultural shifts. A stronger push for the acceptance of the Social Charter across all EU member states or for more fiscal harmonization would be a move in the right direction. As regards governments, a higher degree of cooperation may reduce the practice of offering financial incentives to attract inward direct investment in competition with each other. It is worth pointing out that this practice is not only costly for taxpayers, it may also be ineffective: though TNCs will bargain with governments to get as high 'sweeteners' as possible, their location decisions are usually based on other elements such as availability of labour skills, size of markets, innovation environments or labour costs.

Finally, let us go back to the question with which this paper started: should we be pleased to see the study of international production and the TNCs become part of standard economics theory? My answer is that the interest of a wider community of researchers, teachers and students in the subject is to be welcome; however, a move towards a more efficiency-driven neo-classical approach is a step in the wrong direction[14]. This is because it will not contribute to an understanding of what is going on in the world of TNCs i.e. to an understanding of their motivations and behaviour and to an understanding of why firms branch out into the inter-national arena; of what role the nation-states play in making them trans-national; and of what effects their motivations, behaviour and activities have on contemporary economies and societies. This means that we may move further away from an understanding of the world of companies responsible for most of world production and trade.

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[14] These remarks are not meant to detract from the high value of the Barba Navaretti and Venables (2004) book. For a review see Ietto-Gillies (2007).

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