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# Home-country measures to support outward foreign direct investment: variation and consequences

Florian Becker-Ritterspach, Maria L. Allen, Knut Lange and  
Matthew M. C. Allen\*

The state, especially in emerging economies, plays a key role in influencing firm behaviour, including outward foreign direct investment (OFDI). Often literature on the state's influence on OFDI stresses direct state ownership. However, the state can influence OFDI in several ways, including policy support and subsidies; the literature has largely overlooked these effects. We build on key insights from the comparative capitalisms literature to put forward a series of propositions on how home-country measures – in both emerging and developed economies – to boost OFDI will influence, *inter alia*, the volume, location and mode of firms' investments abroad. We thus contribute to the literature by showing how government policies across a wide range of countries influence an important aspect of firm behaviour that has economic, social and environmental implications.

**Keywords:** multinational firms; international business; comparative capitalisms; investment policies; business objectives of the firm

## 1. Introduction

The international business literature has long recognized how the home country can influence domestic firms' outward foreign direct investment (OFDI). For instance, it has shown how home-country norms shape the location and timing of OFDI (Johanson & Vahlne, 1977), and how the state can influence the capabilities of internationally competitive domestic firms (Narula, 1993). However, although this body of literature has put home-country effects centre stage, it has so far paid limited systematic attention to how home-country measures that states implement to support domestic firms' OFDI vary and how this variation, in turn, affects OFDI.

This rise of emerging-market multinational companies (EMNCs) has led to a focus on the state's role in economic activity (Buckley, Clegg, Cross, Liu, Voss & Zheng, 2007; Ibeh, 2018; Peng, 2012; Zhang, Zhou & Ebberts, 2011). Much of the empirical

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\* Florian Becker-Ritterspach is at the Hochschule für Technik und Wirtschaft Berlin, Maria L. Allen is at Manchester Metropolitan University Business School, Knut Lange is at Royal Holloway, University of London and Matthew M. C. Allen is at Alliance Manchester Business School. The corresponding author is Matthew Allen (Matthew.Allen@manchester.ac.uk).

research has focused on how either the home country, in general, or direct state ownership, in particular, influences emerging-market firms' investments abroad (Buckley, Cross, Tan, Xin & Voss, 2008; Cuervo-Cazurra & Genc, 2008; Zhang et al., 2011).

Although some studies examine how home-country measures (HCMs) that the state implements to support companies' foreign investments shape OFDI (Luo, Xue & Han, 2010; Narula, 1993; Torres, Clegg & Varum, 2016), such studies are limited in number. In addition, these efforts focus on emerging-market firms, often Chinese ones (Jormanainen & Koveshnikov, 2012). However, there is no a priori reason to assume that it is only emerging-market states that support firms' OFDI strategies (Fiedler & Karlsson, 2016; Narula, 1993). Indeed, in an era of increasing nationalism and the questioning of international free-trade agreements, there may be a role for the state in developed economies as well as emerging ones to promote overseas investment for the purpose of accessing knowledge and other capabilities (Mathews, 2006; Welfens & Baier, 2018). Significant research gaps remain, therefore, related to how states – both developed- and emerging-market ones – vary in their support for OFDI and what effect this variation is likely to have on patterns of OFDI.

In this paper we seek to address these gaps conceptually through a range of propositions that combine recent advances in international business with longstanding insights from international policy papers and the comparative capitalisms (CC) literature. Drawing on policy papers from the Organization for Economic Cooperation and Development (OECD) and the United Nations Conference on Trade and Development (UNCTAD) that coined the term “home-country measures” (HCMs), we define and conceptualize home-country support for firms' investments abroad. We draw particularly on the work of Sauviant et al. (2014), which provides a comprehensive review of policy papers on HCMs. We combine that effort with insights from the CC literature to identify how HCMs differ across countries and, more importantly, how HCMs affect OFDI. Building on four crucial tenets of CC analysis, we illustrate how HCMs are likely to influence OFDI patterns.

Our work makes three contributions. First, we help to explain OFDI patterns by examining the variation and consequences of HCMs, a relatively neglected influence on firms' investments abroad. Second and building on the first point, our work demonstrates the importance of taking HCM variation seriously, both across and within countries. Third, we illustrate how HCMs (1) can fundamentally alter the strategic priorities of firms and (2) should be conceptualized as configurations of several measures rather than as individual ones, challenging best practice suggestions of the past (UNCTAD, 2001) and sensitizing policymakers and researchers to the need to assess – as well as the challenges involved in examining – the OFDI effects of HCMs.

The remainder of this paper has three sections. Section 2 reviews key strands of the international business literature: the country-of-origin perspective, important theories of OFDI and recent perspectives on the nature of EMNCs. While recognizing the important contributions of these three strands of the literature, we address their shortcomings in section 3 by introducing complementary insights from HCM policy papers and the CC literature. In that section, we put forward four broad propositions that set out the principles that are likely to shape the relationship between HCM variation and OFDI. We anticipate that more focused hypotheses will build on each of these propositions; to illustrate how the propositions can be used, we put forward one hypothesis for each proposition. Section 4 concludes, summarizes our contribution to the literature and sets out the implications for policymakers, managers and future research.

## **2. Review of the International Business Literature**

We focus on four important strands of the literature: country-of-origin perspectives, OFDI theories within the international business literature, the “double diamond” framework and recent perspectives on the nature of EMNCs. We show that, while all four propose relationships between some aspects of the multinational corporation’s (MNC’s) home country and its investments abroad, there is little systematic treatment of how countries differ in terms of HCMs and how this variation is likely to affect OFDI patterns.

### **2.1 The Country-of-Origin Effect**

The country-of-origin effect potentially explains a wide range of behavioural aspects of the internationalizing firm, such as MNCs’ product perceptions, knowledge transfer propensity, strategy and structure, and coordination modes, as well as the constitution of their work systems and production models (Elango & Sethi, 2007; Ferner & Quintanilla, 1998; Geppert, Williams & Matten, 2003; Harzing & Sorge, 2003). A substantial body of work shows that MNEs’ country of origin influences OFDI patterns (Tan & Meyer, 2011).

The theories underpinning country-of-origin contributions vary substantially. While some contributions use the home country as an explanatory variable with little theoretical grounding, others use theory extensively, with culturalist and comparative theories often dominating. These country-of-origin perspectives have taught us a lot about how the home country influences MNE behaviour (Buckley, 1996; Chen, 2015; Dunning, 1992; Young & Hood, 1992). We see country-of-origin perspectives that are based on the CC perspective and that build on seminal insights from the broader international literature, such as the importance of the state in explaining OFDI (Dunning, 1992; Stopford, 1994; Young & Hood, 1992; Zhan, 1995), as a

fruitful starting point for understanding the constitution and consequences of HCMs, because they have tended to focus on national institutional settings to explain firm behaviour. We therefore build our understanding of home-country support on institutional foundations and extend it to include the important role of HCMs.

## **2.2 OFDI Theories**

This section briefly assesses important OFDI theories, focusing on the extent to which they consider the home context in general and HCMs in particular to explain OFDI patterns. We will discuss the classical mainstream approaches first and then move on to more recent theories on EMNCs' OFDI.

### ***2.2.1 Hymer's Theory of the Multinational Firm***

Hymer's (1960) theory of the multinational firm seeks to explain why firms invest abroad. Drawing on industrial organization theory, Hymer (1960) asserts that MNCs have monopolistic advantages, such as privileged access to capital or other resources, economies of scale or government concessions (Forsgren, 2009). Consequently, firms may be able to invest abroad because they can exploit those monopolistic advantages internationally (Forsgren, 2009: 28). This early seminal work is not particularly concerned with the state's activities to promote OFDI. Importantly, proponents of internalization theory, who build strongly on Hymer's ideas of market imperfections, have focused on the role of home-market imperfections to explain EMNCs' OFDI (Buckley, 2018; Rugman, Nguyen, & Wei, 2016). They have not, however, examined HCMs.

### ***2.2.2 Johansson and Vahlne's Uppsala model***

Johanson & Vahlne's (1977) work seeks to explain OFDI processes through the lens of learning and contextual distance. Firms move gradually from more to less familiar foreign contexts and their foreign investments move from low to increasingly high commitment. Whereas the former involves moving first into neighbouring countries before entering more distant target markets, the latter is a process that starts with exports, moves into initial foreign investment in sales subsidiaries and ends in fully fledged production sites abroad. This approach has been criticized. For instance, contributions on EMNCs' OFDI (e.g. Guillen & Garcia-Canal, 2009) have argued that contemporary firms often venture almost instantly into radically distant environments and also choose high-commitment modes of entry early on. The Uppsala model (Johanson & Vahlne, 1977, 2009), therefore, tends to overlook the state's proactive promotion of OFDI and how that action can lead to investments in unfamiliar cultural contexts and that do not build on existing company strengths (Hennart, 2012; Mathews, 2006).

### *2.2.3 Dunning's OLI model*

Dunning's (1988) "eclectic paradigm", or OLI model, focuses on the necessary conditions for firms to engage in FDI, arguing that three conditions need to be met: firms need an ownership advantage (O), a locational advantage (L) and an internalization advantage (I). Ownership advantages can differ in kind and can involve, for instance, trademarks, production technique or entrepreneurial skills. The possession of ownership advantages is the most basic requirement for OFDI; without it, a firm cannot overcome its liability of foreignness in the foreign context. However, EMNCs' OFDI raises questions about the need for firms to have organizational advantages before investing abroad. Similarly, the OLI framework does not explain the emergence, development and maintenance of ownership advantages, consequently downplaying the institutionally conditioned creation, change and continuation of organizational capabilities (Whitley, 1999).

Responding to such criticisms, Dunning & Lundan (2008, 2010) incorporated institutional analysis into the OLI framework, suggesting a potential link between national institutions in both home and host countries and their influence on the kinds of organizational advantages firms are likely to develop. Despite these developments, the OLI model does not focus in detail on particular policies and HCMs and how they influence OFDI. This is different to Rugman's work, which focuses on the nexus between country- and firm-specific advantages.

### *2.2.4 Rugman's FSA-CSA framework*

The last major theory of OFDI is Rugman's (1981) FSA-CSA matrix or framework, which aims to explain the key drivers and sources of competitive advantages of the internationalizing firm. The starting point of the framework is a distinction between firm-specific advantages (FSAs) and country-specific advantages (CSAs). FSAs include, for instance, brands, managerial resources and skills, and systems integration, which are unique and idiosyncratic to the firm. CSAs can be advantages that have little to do with a firm's capabilities, but that benefit the firm because of its location. Such advantages may involve access to natural resources or low labour costs.

It is the interplay and recombination of CSAs and FSAs that drives OFDI and offers a key source of MNEs' competitive advantage (Rugman, 1988). However, it can be difficult to achieve. Focusing on China, Rugman, Nguyen & Wei (2016) have argued that the types of FSAs that Chinese firms develop stem from home CSAs, including low-cost labour, cheap financing, a large home market and privileged access to natural resources within China. They conclude that strong reliance on home-country and government support may have helped some Chinese firms to invest abroad but has not been sufficient to enable them to combine home-country

FSAs with host-country CSAs. Rugman's work, hence, highlights the difficulties that firms face when seeking to combine FSAs and home and host CSAs, but does not focus specifically on HCMs.

### 2.3 Extensions of Porter's Diamond

A further strand of the international business literature builds on Porter's (1990) diamond to develop a "double diamond" model (D'Agostino & Santangelo, 2012; Ghauri & Santangelo, 2012; Rugman & Verbeke, 2003), which can help to explain, inter alia, OFDI. Porter's diamond focuses on firm strategy, structure and rivalry; factor conditions; demand conditions; and related and supporting industries, to explain the competitiveness of industries in different countries. The double diamond model has two key elements that Porter's framework downplays (Rugman & D'Cruz, 1993; Rugman & Verbeke, 1993, 2003). First, to be successful abroad, internationally competitive firms do not rely only on their home country's strengths. Often the interaction between resources located in different countries can explain companies' international success (Rugman & Verbeke, 1993). Second and more specifically, companies often undertake OFDI to access knowledge, expertise and resources that their domestic market does not provide (Rugman & Verbeke, 2001).

### 2.4 Emerging-market multinationals and the role of the home country

The growing importance of EMNCs' FDI has led to analyses of home countries and their influence on domestic firms' investments abroad (Buckley et al., 2007; Buckley, 2018; Chen, 2015; Pradhan, 2016). Indeed, without examining the home country's role, it is difficult to explain such firms' OFDI. The global shift in OFDI patterns has led to two theoretical developments. First, proponents of classical theories of international investment examined the role of states and home-country institutions in greater detail (Buckley, 2018; Dunning, Kim & Park, 2008; Dunning & Lundan, 2008, 2010; Rugman, 2009). Second, recent work has put forward new theories and empirical analyses specifically tailored towards explaining emerging-market firms' OFDI (Chen, 2015; Hennart, 2012; Luo & Tung, 2007; Mathews, 2006; Ramamurti, 2009, 2012).

Although amended classical theories and new theories on EMNCs posit different drivers of OFDI and firms' competitive advantages in foreign markets (Buckley, 2018; Hennart, 2012), they share an emphasis on the *constraining or enabling* role of home-country institutions. These institutions are often seen as being directly linked to – if not equated with – the state's behaviour in the home country. Hence, the literature has increasingly focused on the importance of the state to explain emerging-market OFDI, but very few studies examine the policies that states have in place to promote OFDI in both emerging and developed economies.

For instance, a few studies focus on China and provide a comprehensive review of HCMs (Li, et al., 2013; Luo & Rui, 2009; Luo et al., 2010). Some of these cover a wide range of HCMs, including various fiscal incentives, such as tax rebates and subsidized loans, insurance against political threats, support from government agencies, treaties to protect investment abroad, and help to deal with host-country governments and to conform to free-trade agreements, such as WTO protocols (Luo & Rui, 2009; Luo et al., 2010).

In sum, OFDI theories have begun to acknowledge the home country's important role. However, there is little systematic understanding of how HCMs differ across countries and how divergent HCMs, in turn, affect OFDI (Buckley, 2018; Sauvant et al., 2014). This gap in the literature is all the more surprising as "HCMs can potentially influence, among other things, the volume, quality, mode of investment, type of investor, sector of investment, and location of OFDI" (Savant et al., 2014: 3).

### **3. Towards a framework of HCM variation and consequences**

#### **3.1 Classifications of HCMs**

International organizations, notably UNCTAD and the OECD, were among the first to acknowledge the importance of HCMs in explaining OFDI. The initial focus rested on the question of how to incentivize MNCs to invest in developing countries (OECD, 1983, 1993; UNCTAD, 2001). Consequently, UNCTAD published a range of papers defining HCMs and discussing their possible effect on FDI in terms of quality and quantity in developing countries. In general, UNCTAD (2001: 65) understood HCMs as

[A]ll policy measures taken by the home countries of firms that choose to invest abroad designed to encourage FDI flows to other countries. Their formulation and application may involve both home- and host-country government and private sector organizations.

HCMs can exist at the national, regional and multilateral levels and involve a broad variety of measures, ranging from information provision, technical assistance and capacity-building to financial, fiscal and insurance measures, investment-related trade policies, schemes to promote the transfer of technology and investment insurance (UNCTAD, 2001: 11).

Savant et al. (2014: 11–12) define HCMs as advantages provided by home governments that are "meant to facilitate, support or promote outward FDI". Drawing on a comprehensive review of policy papers, Sauviant et al. (2014) were among the first to examine how HCMs vary. They identified five characteristics to distinguish between HCMs. HCMs can be (1) direct or indirect, (2) provided by government and non-government actors, (3) grouped into broad categories of



support and the types of institutional actors that often provide them, (4) different in terms of their objectives and (5) different in their level of development, coherence and integration.

Sauvant et al.'s first distinction is between indirect and direct HCMs. Direct HCMs aim to support domestic firms' OFDI through information and other support services, financial measures and fiscal measures. Indirect measures are subsidies or measures that are related to trade and market access. Sauvant et al.'s second characteristic underscores that the private sector may have a role to play in stimulating OFDI; however, this is not the focus of their framework, which excludes non-governmental measures that aim to promote OFDI (Sauvant et al., 2014: 20).

The focus of Sauvant et al.'s third characteristic is on how government-related HCMs can be grouped into broad categories of support (information and support services, financial and fiscal measures, investment insurance measures and treaties) and the types of institutional actors that typically provide them (government departments and ministries, export credit agencies and development finance institutions, and investment and trade promotion agencies, as well as private organizations fulfilling government mandates).

Sauvant et al.'s fourth characteristic highlights how, apart from the obvious variation in HCM type, HCMs differ in their objectives. Such objectives can span a wide spectrum, ranging from more developmental goals for the host country to the promotion, primarily, of home-country economic interests. These objectives are typically reflected in the eligibility criteria and conditions that are often attached to HCMs, such as protecting the home country's economy as well as developmental, environmental, cultural or social considerations. Sauvant et al.'s fifth characteristic suggests that HCMs vary in their proactive promotion by the state, their transparency and, more importantly, their coherence and integration. This suggests that the interactions of HCMs are important.

In summary, Sauvant et al.'s (2014) work provides an extensive discussion of HCM variation. However, they do not provide a theoretical or analytical basis on which to assess how HCM variation influences OFDI. As we show in the next section, CC analysis is particularly useful for providing this basis, so that a more systematic analytical framework can be put forward to examine the effects of HCMs on OFDI.

### **3.2 Comparative Capitalisms and Home-Country Measures**

We rely on the CC literature to develop a better understanding of how HCMs vary and how that variance relates to OFDI patterns. Before discussing these antecedents and consequences of HCM variation, we outline why the CC literature is a valuable one to review.

There are different strands within the CC literature. Among the best known and most widely cited ones are the National Business System, the Varieties of Capitalism and the Societal Effect approaches (Hall & Soskice, 2001; Maurice, Sorge & Warner, 1980; Whitley, 1999). Although these approaches vary in a number of ways (Allen, 2014), they share the basic premise that firms' priorities, capabilities and behaviour can only be understood within their home-country institutional contexts (Jackson, 2010; Whitley, 1987). Hence, the predominant perspective on institutions has been to examine how configurations of formal institutions at the national level influence firms (Allen, 2013; Whitley, 2005a). On the basis of divergent institutional settings and, hence, dominant firm types and firm relations within different countries, CC approaches distinguish between various categories of market economy (Hall & Soskice, 2001; Maurice, Sorge & Warner, 1980; Whitley, 1999). Since its first expressions, the CC literature has seen some important revisions. Among the most important are that firms are not passive agents but influence institutions as much as they are influenced by them (Hancké, Rhodes & Thatcher, 2007). It has also been recognized that national institutional settings are neither static nor necessarily homogeneous within a national economy (Allen, 2013; Whitley, 2009).

Nevertheless, what has remained a constant in this body of literature is the importance of institutional configurations (institutions as interconnected combinations rather than collections of discrete entities) as well as firm-institutional relationships to explain firm behaviour. Hence, four elements within the CC literature are particularly important: the mutual constitution of institutions and actors, complementarity, sectoral heterogeneity and the role of the state. We discuss their implications for HCM variation and the consequences for OFDI in the following subsections.

### ***3.3.1 Mutual constitution of institutions and actors***

Rather than seeing institutions and collective actors, such as firms, as separate entities, the CC literature builds on key insights from sociological theory, such as those of (Giddens, 1984) and (Simmel, 1955), to argue that individuals define or shape the social groups to which they belong and social groups define or shape their members (Jackson, 2010). In other words, neither is more important than the other: each co-constitutes the other (Jackson, 2010).

This has profound implications for how we view firms and how we seek to explain their behaviour. For instance, important national institutions not only encourage or discourage certain actions by firms; they also shape the fundamental nature of firms, their objectives and their abilities to carry out particular actions (Jackson, 2010; Jackson & Deeg, 2008; Whitley, 2010a). As a result, the CC literature highlights how key national institutions, such as corporate governance and the role of the state, constitute as well as constrain or enable firm behaviour both at home and abroad (Jaehrling et al., 2018; Lane & Wood, 2009; Tüselmann, Allen & McDonald,

2015). Consequently, it shows that the nature of firms varies between institutional contexts (Hall & Soskice, 2001; Lange et al., 2015; Maurice et al., 1980; Whitley, 1999). For instance, corporate governance regulations influence who has a say in important strategic decisions, shaping the firm's priorities and its capabilities (Goyer, 2011; Hall & Soskice, 2001; Whitley, 2010a). In other words, key institutions do not exist separately from firms, but are part of them, fundamentally shaping the nature of firms and their priorities; institutions do not just act as incentives or disincentives for firms that are, generally, homogeneous (Jackson, 2010; Whitley, 2010a).

Applied to HCMs, this view suggests that the state, as the "group" in Simmel's terms, is constituted by and constitutes the firms and other organizations that enact its policies and that are its "members". Therefore, the state's priorities, as embodied in HCMs, become the priorities of those companies that are involved in, or wish to be involved in, trying to achieve the state's objectives. One corollary of this is that, depending on the role of the state in the economy, we cannot assume that firms in all countries are profit maximizers. If the state plays a dominant role in shaping economic development, those firms that are expected to contribute towards achieving the state's objectives are likely to have socio-political as well as commercial aims.

For instance, the Chinese word *lishu* signifies a sense of "belonging to" or "directly controlled by" (Buckley, 2018). Such a relationship exists between the Chinese state and some domestic companies; therefore, in those firms, the state can have a direct influence not only on senior management appointments but also on major projects, such as OFDI (Buckley, 2018). As a result, HCMs signal to firms the state's priorities. *Lishu* is likely to mean that the strategic priorities of some Chinese firms reflect political rather than solely commercial objectives, resulting potentially in investments abroad that would not otherwise have occurred. Of course, not all OFDI by Chinese or other emerging-market firms will be influenced in this way (Voss, Buckley & Cross, 2010), but some will (Ramamurti & Hillemann, 2018). For instance, the Chinese state has influenced the location of OFDI and the type of companies that invest in particular projects abroad. China's One Belt One Road initiative, which is related to a government-backed \$10 billion credit line to support Chinese investment (an HCM) (Tonchev, 2017), has led to an increase in OFDI in those countries that fall within the initiative, with state-owned companies playing a leading role in infrastructure sectors and private firms being more active in acquisitions not related to infrastructure (Du & Zhang, 2018).

This perspective suggests that political objectives associated with HCMs in some countries and variation, more broadly, in eligibility criteria and in conditionality – in terms of the host countries that attract, for example, funding or tax advantages associated with HCMs – in other countries will not just provide incentives to firms in general to invest overseas, but may inherently alter the strategic priorities of some firms. In other words, an HCM to promote OFDI into a particular country

or region may not only enhance the attractiveness of investing in that country or region for domestic firms, but also may fundamentally alter some domestic firms' strategic priorities, potentially influencing the geographical focus of their OFDI and, hence, both their spatially specific objectives as well as their overall priorities. Thus, HCMs and the conditions associated with them may encourage some firms (but not others) to invest in particular geographical locations or technologies (Sauvant & Chen, 2014). Conversely, eligibility and conditionality criteria may discourage some firms from using HCMs due to their constraining nature (Sauvant & Chen, 2014). We, therefore, put forward the following proposition:

P1: HCMs will influence OFDI patterns (types of actors, volume, location, technology area, mode of entry).

This broad proposition suggests that HCMs will encourage some firms to undertake investments overseas (either in particular countries or technologies) that they would not otherwise have carried out. One possible hypothesis that can be derived from this: HCMs will increase the volume of OFDI to politically favoured locations.

### **3.3.2 Complementarity**

The CC literature highlights how institutions interact with one another; they should be seen as systems rather than as discrete entities with individual and independent effects (Goyer, Clark & Bhankaraully, 2016; Jackson & Deeg, 2008), raising the importance of complementarity (Deeg, 2005; Wood, Deeg & Wilkinson, 2014).

Prominent analytical approaches within the CC literature rely on typological theories, arguing that firm behaviour differs as a result of variation in countries along a number of dimensions (Hall & Soskice, 2001; Whitley, 1999). Consequently, these approaches implicitly draw on Weberian ideal types (Weber, 1949). At the heart of ideal types are the dimensions along which a set of ideal types, which forms a typology, vary (Doty & Glick, 1994). Within the CC literature, some important dimensions along which different types of capitalism exist are the role of the state in economic activity, the degree of centralization of wage negotiations and the relative importance of stock markets in corporate financing (Hall & Soskice, 2001; Whitley, 2005a). Each ideal type should be an internally coherent and logical model that shows the combination of dimensions that are distinct to each ideal type (Weber, 1949). However, in a typology, the ideal types are interrelated, because they vary along the same dimensions, making them different to classification systems (Doty & Glick, 1994). In addition, typologies should provide a logical or theoretical argument to explain why each ideal type's dimensional patterns leads to a particular outcome (Doty & Glick, 1994). For instance, the Varieties of Capitalism framework relies heavily on, but differs from, transaction cost economics to explain how contrasting national institutional regimes result in patterns of comparative advantage (Allen, 2004; Hall & Soskice, 2001).

A corollary of this typological theorizing is that how one institution shapes firm behaviour depends on the other institutions that are present (Jackson & Deeg, 2008). This can lead to systems of institutions that may either mutually reinforce one another (Hall & Soskice, 2001; Whitley, 1999) or compensate for one another, so that one institution may overcome the “deficiencies” of another (Crouch et al., 2005).

When institutions reinforce one another in a country, their effects are greater together than the effects of the institutions individually (Hall & Soskice, 2001; Whitley, 1999). Applied to HCMs, this kind of complementarity suggests that the institutional complementarity in a country may translate into different levels of coherence among the different HCMs. Coherence may, in turn, have a strong effect on the scale and scope of OFDI. This echoes Sauvants et al.’s (2014) work on HCMs as more or less coherent and integrated systems. For instance, one HCM by itself may have only a limited influence, but when coupled with one or more other HCMs, its influence could be quite substantial. Theoretically, then, one HCM (say, information support) may increase OFDI a little but when coupled with another (such as loans) may increase it a lot. HCMs may also stipulate or at least influence the mode of OFDI (joint ventures or wholly owned subsidiaries). Again, if the foci of other HCMs reinforce a particular mode of OFDI, the effects could be substantial.

The alternative view of complementarity suggests that one institution may make up for the deficiencies of another (Crouch et al., 2005). For instance, in the CC literature, strong, active labour-market policies in a country may “compensate” workers for a lack of strong employment rights, enabling workers to maintain their skills, expertise and employment as they are able to find work with different employers (Kristensen, 2016). Applied to HCMs, this insight suggests that some HCMs may make up for the absence or inadequacy of other HCMs. Therefore, research should examine how particular configurations of HCMs – rather than individual HCMs – may lead to the same outcomes. In other words, different sets of HCMs may have equifinality or the same result. They may, of course, have different outcomes as well.

Instead of complementing one another, HCMs and the eligibility criteria and other conditions associated with them may work against one another or be incoherent. As a result, the configuration of institutions may in some ways be complementary but in other respects may be incoherent, making for a complex set of causes that lead to particular outcomes. For instance, China’s policy framework supports OFDI, but inefficient administrative procedures can impede investments abroad; despite these limitations, state-owned enterprises seem to benefit from HCMs more than other types of firms (Sauvant & Chen, 2014). In other words, although some institutions promote OFDI, they interact with unclear administrative remits to hinder OFDI; however, the impact of these interactions varies depending on the type of firm that is seeking to engage in investment abroad. Drawing on these two views of complementarity and incoherency, we put forward the following proposition, in broad terms:

P2: HCMs collectively and configurationally (rather than individually and additively) will influence patterns of OFDI.

One hypothesis that follows logically from this proposition is that, for example, government grants to firms to set up overseas facilities will moderate (enhance) the positive effects of tax deferral policies for income earned abroad on OFDI. Such a hypothesis highlights how HCMs are likely to interact with one another rather than act individually, with each having a direct effect on OFDI that is neither moderated nor mediated by other HCMs.

### ***3.3.3 The role of the state***

The third insight from the CC literature is the importance of the role of the state. Typologies of the state's involvement in economic activity are manifold, ranging from "predatory" states (Evans, 1995) to "segmented business systems" (Wood & Frynas, 2006) to "arm's length", "dominant-developmental" and "corporatist" states (Whitley, 2005a). As discussed in more detail below, any state's involvement in economic and commercial activities is likely to be sector specific, so these labels should be treated with care as they are unlikely to reflect the actual role of the state and its variation across economic sectors (Allen, Allen & Lange, 2018; Thurbon & Weiss, 2006; Wade, 2012).

Arm's length states, in their ideal typical forms, seek to achieve a level playing field for all firms, so that no firms are directly advantaged or disadvantaged by the state. This means that such states, as ideal types, do not intervene directly in any firm or firms' activities; they do not seek to shape investment decisions, for example, in favour of particular technologies or geographical areas. By contrast, dominant-developmental states, again as ideal types, pursue a strategic and active role in the economy, offering financial or other incentives to specific firms or sectors to encourage the growth of those firms and sectors and/or chosen technologies (Allen et al., 2018; Whitley, 2005a). Corporatist states, as ideal types, have a significant, direct role in economic development. In contrast to both arm's length and dominant-developmental states, corporatist states recognize that independent organizations, such as unions and business associations, can at times play important roles in helping to shape economic policy and implementation (Whitley, 2005a).

The different roles that states can play in guiding (or not guiding) economic development are likely to have important implications for any HCMs that they adopt, particularly regarding their directness. Arm's length states, by definition, are less likely than any of the other ideal types reviewed here to offer direct HCMs to specific firms or sectors to invest overseas in either specific companies or countries. In such states, senior managers in firms should be the ones to decide where to invest and how to do it. However, that does not mean that such states will not have any HCMs, as they do have them (Sauvant et al., 2014).

At the other end of the spectrum, dominant-developmental states are the most likely to devise direct HCMs with clearly defined eligibility and conditionality criteria to guide OFDI in terms of, say, firm type, investment objectives, volume and technology acquisition (Pradhan, 2016; Sauvart & Chen, 2014; Sauvart et al., 2014). They are, therefore, most likely to establish direct HCMs to encourage specific firms or firms more generally in chosen sectors to invest abroad to gain knowledge and access to key resources. For instance, the Chinese government did not allow private Chinese firms to invest abroad before 2003, so all OFDI came from state-owned enterprises (Buckley et al., 2007). The Chinese state promoted investment abroad by these companies in specific sectors between 1999 and 2001 (Buckley et al., 2007).

The influence of the Chinese state on OFDI has continued in more recent times (Rogers, 2019). For example, the China Development Bank, which is a state-owned “policy” bank in China that has a remit to provide medium- to long-term funding to support the country’s strategic economic objectives, has provided crucial funding to some domestic solar photovoltaic companies to enable their development, including investments abroad in 2011 (Allen & Allen, 2015). By contrast, the United States, in general, has adopted a broader policy to promote investment abroad that is consistent across countries (Jackson, 2017); such policies typically focus on the provision of information about exporting or investing abroad rather than financial support to promote OFDI. However, some United States policies and government agencies do favour investments in emerging markets (Overseas Private Investment Corporation, 2018). Hence, the role of the state differs between countries, leading to variation in HCMs and OFDI. We therefore put forward the following proposition:

P3: The role of the state in the economy will influence HCM variation and thereby influence broad OFDI patterns (firm types, volume, location, technology area, mode of entry).

One hypothesis that builds on this proposition is that developmental states’ HCMs will be both more extensive and more targeted than those in arm’s length states. The rationale for this hypothesis is that arm’s length states are likely to provide fewer HCMs than developmental states and, with some exceptions we discuss below, HCMs in arm’s length states are likely to apply to all companies and all host countries evenly. By contrast, HCMs in developmental states are likely to be numerous and focus on particular firms and sectors as well as specific host countries. As a consequence of this variation, the potential moderating effects of HCMs are likely to be greater for developmental states than they are for arm’s length states.

### *3.3.4 Sectoral heterogeneity*

The fourth and final insight from the CC literature is its emphasis on the importance of heterogeneity not just between, but also within different types of national

economy (Lane & Wood, 2009; Wood & Lane, 2012). This diversity reflects, in part, both the sectoral specificity of state support (Lane & Wood, 2014) and differences between firms and their capabilities within any national economy and sector (Allen, 2013; Whitley, 2007). It also builds on the emphasis within the CC literature that institutional configurations are important: to assess the influence of a range of institutions – which can vary across companies and sectors – on firm behaviour, researchers need to know which specific institutions are applicable to particular firms (Allen, 2013).

This may seem like an obvious point; however, if research applies national ideal types to all companies within an economy, important variation can be missed and results may be biased. By neglecting such variation, research can inadvertently turn abstract ideal types into concrete entities that all companies within an economy are assumed to resemble closely. In reality, of course, there is variation among firms within any economy in terms of their ownership, control and direction, employee representation, types of relationships with suppliers and customers, and competition model (Kirchner, 2016).

Even within states, such as the United States, that typically do not intervene with companies and how they are run, some specific sectors receive strong government support (Block & Keller, 2009; Keller & Block, 2015). For instance, the United States Government has given relatively large amounts of funding to companies in the defence and biotechnology sectors but very little to companies in other economic sectors (Allen, 2013). Thus, the role of the United States Government in the economy varies from sector to sector and reflects the economic priorities of the federal government.

Applied to HCMs, sectoral heterogeneity suggests that HCMs within a national economy are likely to vary substantially across sectors, reflecting the economic preferences of the central government (Sauvant et al., 2014). In other words, political processes will shape which economic sectors will have HCMs and which will not, as well as the characteristics of any HCMs in different sectors. This suggests that in order to explain the likely impact of HCM variation we need, first, to understand whether national institutions are directed towards the support of particular sectors of the economy (Sauvant et al., 2014).

Moreover, national institutions are likely to influence the form of HCMs in particular sectors. For instance, depending on the sector, HCMs may be more direct or indirect. Similarly, institutional variation may result in the eligibility and conditionality criteria that are attached to HCMs being designed to promote the OFDI strategies of firms in specific sectors. In the latter case, an HCM may apply generally to all firms in a country but may be relevant only for some of them, perhaps those with limited financial resources or no experience of investing overseas. Similarly, firms that apply for and receive such support may vary systematically from those that



do not (Torres et al., 2016). Furthermore, if firms must meet certain criteria to be eligible for HCMs, this may reinforce dominant firm types within an economy, so that firms in strategically important sectors benefit the most from HCMs (Sauvant & Chen, 2014).

Even though the United States Government tends to operate at arm's length from individual firms and sectors, as noted above, some sectors receive federal funding to promote their growth. In addition, although the federal government does not have high-profile policies to promote domestic firms' OFDI, the Overseas Private Investment Corporation (OPIC), a self-sustaining federal government agency, has a remit to help United States businesses invest in emerging markets. By doing so, it seeks to promote, *inter alia*, United States foreign policy and national security priorities. In 2017, OPIC lent \$630 million to foreign energy projects that involved United States companies, Approximately 90 per cent of this money went to renewable-energy initiatives (Groom, 2018). Hence, even in the United States, which is typically viewed as an arm's length state, some funds are available to promote investment abroad and those funds can benefit certain economic sectors more than others. Building on this empirical evidence as well as on the theoretical arguments outlined above that indicate that firms' institutional specificities are important and that actors and institutions co-constitute each other, we put forward the following proposition:

P4: Countries' HCMs are more relevant to some economic sectors than others.

As noted above, the role of the state will influence how extensive and targeted HCMs are. However, this does not mean that arm's length states will not have any HCMs. It is therefore important to conduct analyses of particular sectors to determine how HCMs influence OFDI. Such policies may not play a major role in influencing OFDI in general for a country, but could be significant in some sectors and for some host countries. A specific hypothesis that follows from this is that, in arm's length states, HCMs are likely to moderate the relationship between firms and their OFDI in those sectors that the HCMs apply to, but not other sectors that do not have any HCMs.

#### **4. Conclusion and policy implications**

Compared with how state ownership influences OFDI, HCMs have received limited attention in the international business literature. Although international business research has started to theorize how home-country institutions enable and constrain EMNCs' OFDI, relatively little work has attempted to provide a systematic account of HCMs and their effects on OFDI.

We have sought to fill that gap by putting forward a series of general propositions and more focused potential hypotheses on the links between HCMs and patterns

of OFDI. By doing so, this paper makes three theoretical contributions. First, it suggests that research should consider HCMs holistically, as individual measures are likely to interact with other HCMs; these interactions could increase or impede or, by cancelling each other out, not affect OFDI. Second, our research indicates that HCMs may have a direct influence on OFDI, and, as HCMs vary between different state types, this effect is likely to be greater in developmental states than it is in arm's length ones. We have, therefore, identified an important source of HCM variation, which in turn is likely to affect OFDI. At present, much of the existing literature downplays how HCMs vary across countries, focusing instead on variation in general. As a result, we seek to provide a theoretical grounding for HCM variation. Finally, our work provides some boundary conditions about when HCMs are likely to influence OFDI. In particular, targeted HCMs in countries in which the state typically plays an arm's length role in the economy, such as the United States and the United Kingdom, are likely to apply to firms in a small number of sectors and their investments in a few host countries, potentially only emerging-market economies. Hence HCMs in some countries are only relevant for particular sectors and some host countries; they do not apply to all sectors and all host countries.

In addition, the theoretical implications of our work have consequences for policymakers and for future research to assess the impact of HCMs on OFDI. First, our research suggests that policymakers and researchers should consider the effects of HCMs holistically and sectorally. In other words, HCMs are likely to target specific sectors, so assessments of their effects must focus on those sectors (Fiedler & Karlsson, 2016). In addition, such assessments must examine HCMs collectively – as configurations or “packages” – rather than as individual measures to support OFDI, meaning that the interactions between specific HCMs will influence their effects on firms. This will complicate those assessments. Creating models to examine how the effect of one HCM varies according to the presence (or absence) of other HCMs is likely to require (1) information at the firm level to know which HCMs they use and how they use them, and (2) analytical techniques that can assess how configurations of (or the interactions between) various HCMs influence OFDI.

Second, our work suggests that HCMs may alter the strategic priorities of companies, influencing where they do and do not invest abroad. Indeed, in many instances, this is the *raison d'être* of HCMs. Assessing their net benefits is, therefore, important. For instance, HCMs may boost domestic firms' OFDI in specific countries, but they may reduce it in others. The effects of that shift in OFDI location may have long-term implications for the international competitiveness of domestic companies that policymakers must consider. This has implications for future research, as it suggests that some OFDI may be diverted away from some countries and into others. It also indicates a need to better understand the motives to invest abroad as a means, in part, to meet political objectives and conform to expectations.

Third, HCMs may merely, in some instances, subsidize domestic firms' OFDI that they would have undertaken in the absence of HCMs. Such assessments of the effects of HCMs may be particularly important when examining the link between HCMs, OFDI and socioeconomic development in emerging economies. As we discussed above, a United States government agency, OPIC, seeks to combine OFDI promotion with United States foreign policy objectives and socioeconomic development in emerging economies; yet, analyses of OPIC, its HCMs and its effects on socioeconomic development in emerging economies are rare.

Finally, if HCMs seek to promote OFDI, as well as potentially inward FDI (Buzdugan & Tüselmann, 2018), as a means to enhance domestic companies' competitiveness by enabling them to tap into resources abroad that are not available at home (Ibeh, 2018), policymakers and managers need to be aware of the challenges that operating across multiple sites will create within one organization (Whitley, 2010b). Integrating and coordinating activities that are geographically dispersed, to create and sustain competencies within a single organization, an MNE, is likely to pose significant organizational and managerial challenges (Gilmore, Andersson & Memar, 2018; Narula, 2014; Rugman & Verbeke, 1993; Whitley, 2005b). Companies will need to be able to develop organizational capabilities to surmount these, potentially affecting how employees in different locations are managed and how extensive organizational careers for different types of employees can be (Whitley, 2005b). For instance, domestic firms that acquire leading technical or scientific capabilities abroad need to ensure that those highly skilled employees who help to constitute key capabilities stay with the firm. To do so, domestic firms may need to open up senior managerial positions to employees from abroad; this may not always be easy (Allen et al., 2018; Whitley, 2012). Consequently, policymakers, if they implement HCMs to improve domestic firms' competitiveness, will have to assess how well HCMs actually enable those firms to create new capabilities or extend existing ones rather than simply whether or not firms use HCMs (Knoerich, 2015). In short, encouraging domestic firms to invest abroad may be one thing; ensuring that they use that investment to boost their competitiveness another. Policymakers will, therefore, need to ensure that they have the means to assess firms' capabilities if they wish to use HCMs to boost domestic firms' competitiveness. Future research can help to provide the basis of that assessment.

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