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# In Age of Deglobalisation, MNCs Need Closer Ties to Thrive



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**Cultivating relationships with local communities and other stakeholders will help multinationals counterbalance increasingly powerful governments.**

Since the 2008 global financial crisis, when banks and corporations had to be bailed out by governments with taxpayers' money, world trade growth has faltered. China and the United States have decoupled. The pandemic disrupted the global movement of goods and people while Russia's war in Ukraine triggered sanctions and countersanctions. As a result, multinational companies (MNCs), for so long at the forefront of globalisation, are on the back foot.

With overseas markets no longer as accessible as before, and governments more likely to crack the whip than bend over backwards, MNCs often lack the sophisticated political nous to navigate government and public expectations.

For instance, when Alibaba founder Jack Ma openly criticised financial regulations in China in October 2020, Chinese authorities swiftly halted his fintech conglomerate's initial public offering and launched a crackdown on Big Tech companies. Similarly, India's commerce minister publicly took Tata Group to task last year after the country's largest conglomerate griped about tough new e-commerce rules.

MNCs face even greater challenges running outposts in foreign countries. Their relationships with host governments may deteriorate over time, along with the bargaining power that the MNCs initially enjoyed on entry.

To find out what makes some companies better able to deal with host hostility than others, we studied eight MNCs involved in disputes with governments in South America between 2001 and 2012: Cemex in Venezuela; Telefonica, Repsol, Vivendi, and Endesa in Argentina; Telecom Italia in Bolivia; Shell in Nicaragua; and Iberdrola in Guatemala.

Our **findings**, published in the *Journal of Management Studies*, show that reliance on local partners could result in what we call a *liability of insiderness*. Local partners tend to isolate foreign investors from local stakeholders, preventing the multinationals from developing direct, local ties and building local reputation. This in turn compromises the MNCs' capacity to react and adapt to the sudden hostility of local governments.

### **The insider's liability**

We focused on sectors such as construction, energy, and mining where high sunk costs reduce bargaining power and can make exits difficult and costly. We also zeroed in on disputes that occurred in countries with similar institutional systems. All of the companies analysed had filed expropriation claims with the World Bank's International Centre for Settlement of Investment Disputes (ICSID).

We conducted dozens of interviews with MNC executives, managers of peer companies, government officers, representatives of political associations, diplomacy and political economics experts, and labour union experts. We also examined analyst reports, newspaper articles, and corporate, legal and government documents.

### **Three phases of hostility**

We charted three phases of increasing hostility from political authorities: anticipation, escalation, and expropriation. Four of the cases we studied underestimated the trouble they were in at first, took remedial action only after the government hostility became evident, and ultimately failed to secure local and international support. Most of these companies exited their host countries and received little or no compensation for their losses.

A second group of companies caught early warning signals and mobilised quickly to propagate their own narratives and canvass for local and international support. Three of them maintained operations in the host country and/or received compensation from the host government.

### *Phase 1: Anticipation*

Disputes typically begin with symbolic, ambiguous actions that hint at the government's intention to intervene in an industry or the economy, usually in the name of protecting national interests. The actions might include setting price ceilings, increasing corporate taxes, or using trade unions to pressure MNCs through public protests or strikes.

In response to this first phase of government hostility, some of the companies such as Telecom Italia and Iberdrola relied on local partners to gather additional information and monitor the situation. They received filtered information that painted a partial and inaccurate picture that led them to delegate action to third parties.

"We were myopic," a director of Telecom Italia told us. "We delegated and we should have intervened in first person."

These companies had adopted a networking strategy that we refer to as *mediated embedding* in tandem with their narrow focus on profits. According to our interviewees, Telecom Italia saw the local investment as merely "a cash cow" while Iberdrola, a Spanish electric utility company, did not think it necessary to invest in the local communities.

Endesa, another of the MNCs that relied on a local partner to manage its relationship with the host government, built goodwill with local people by giving aid to the underprivileged and providing training and other benefits. This helps explain why the Spanish electricity company managed to mobilise local support and renegotiate tariffs with the host government in Argentina. It stayed in the country for five more years.

In contrast, other companies in our sample such as Repsol sought information from local lobbyists, trade unions or other MNCs. This helped them accurately assess government hostility and spurred them to take early action.

These MNCs pursued a networking strategy that we named *proximal embedding*. They directly owned and managed their local investments, had built relationships with a broad range of local stakeholders, and liaised with the central government through lobbyists, “high-level contacts”, or informal interactions with political authorities.

Local stakeholders helped these companies detect subtle signals of targeted hostility. Managers at the Mexican building materials company Cemex and Spanish energy company Repsol, for example, noticed that some contractors were delaying payments and some large clients had changed providers. The companies took immediate action.

A Cemex executive recalled how they collected evidence of what political authorities were saying or doing at any given time. “We would take note of it and write it down. We had it documented. We never feared that we lacked arguments.”

### *Phase 2: Escalation*

In this phase, the MNCs began to be accused by host governments of failing to fulfil investment commitments or causing pollution. They also faced demonstrations, fines, increased taxes, class action lawsuits and criticism in the media.

Yet managers of multinational corporations operating through local partners continued to dismiss the severity of the situation. At French water services multinational Vivendi, managers maintained that the hostility they faced in Argentina was due to “unfortunate events” rather than a deliberate plan to seize their assets.

Such MNCs also preferred to avoid direct confrontation, seeking instead to appease the authorities. As a Telecom Italia director lamented, “In Bolivia, my impression is now that the local partner knew [of the threat] but did not say. ...When there is no partnership, you have a better understanding of what happens.”

In contrast, managers of proximally embedded companies had already sensed danger and proactively sounded out local stakeholders to gauge whether they shared the government's hostility. Cemex's managers, for example, contacted suppliers to renegotiate the terms of their contracts. They met with clients that had stopped or delayed payments, and set up meetings with local employees to discuss rumours that senior executives were negligent. Cemex also reached out to friendly government contacts and mobilised lobbyists to gather information about the government's motives.

These proactive MNCs thus concluded that a confrontation with the government was inevitable and began to plan accordingly. All of them sought to highlight how their investments had contributed to local economic development and to convey that the actions proposed by the government would harm, not help, local communities.

For example, Telefonica insisted that the government did not have the capacity to finance the necessary investments in telecommunications. Repsol warned that the Argentinian government's actions would deter foreign investment in the country.

### *Phase 3: Expropriation*

The dispute's final phase usually sees hostile governments formally cancel or modify concessions (Iberdrola and Endesa), expropriate assets (Cemex, Repsol, Telefonica, and Telecom Italia), or seize rent sources (Shell and Vivendi) without compensation.

In our study, companies operating through local partners (Vivendi, Iberdrola, and Telecom Italia) now faced widespread hostility from local stakeholders. These MNCs' only recourse was to file complaints with ICSID even while they prepared to exit their host countries.

In contrast, proximally embedded MNCs intensified their efforts to mobilise local stakeholders and put pressure on host governments to settle disputes amicably, or at least not to cause further harm to their remaining assets.

Endesa, the only MNC in our study to pursue a hybrid strategy, lost control of its board and was forced to sell its majority stake in its Argentinean subsidiary. But, with the help of local supporters, it was able to persuade the government to renegotiate tariffs and continue its operations in the country.

In the age of deglobalisation, nurturing direct local ties and investing in social initiatives that benefit local communities has proven to be a sound business strategy for multinationals. In contrast, as our study reveals, companies that rely on joint ventures with local businesses to run their foreign operations expose themselves to a liability of insiderness. They tend to become complacent and miss early warning signs of hostile government actions – a mistake that could potentially force them to retreat from the world.

*This is an adaptation of an [article](#) published in MIT Sloan Management Review.*

### Find article at

<https://knowledge.insead.edu/strategy/age-deglobalisation-mncs-need-closer-ties-thrive>

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### About the research

["Why Do Some Multinational Firms Respond Better Than Others to the Hostility of Host Governments? Proximal Embedding and the Side Effects of Local Partnerships"](#) is published in *Journal of Management Studies*.