Module 2142: Lecture 5

Environmental Strategies

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MAN2142: Topics in International Business

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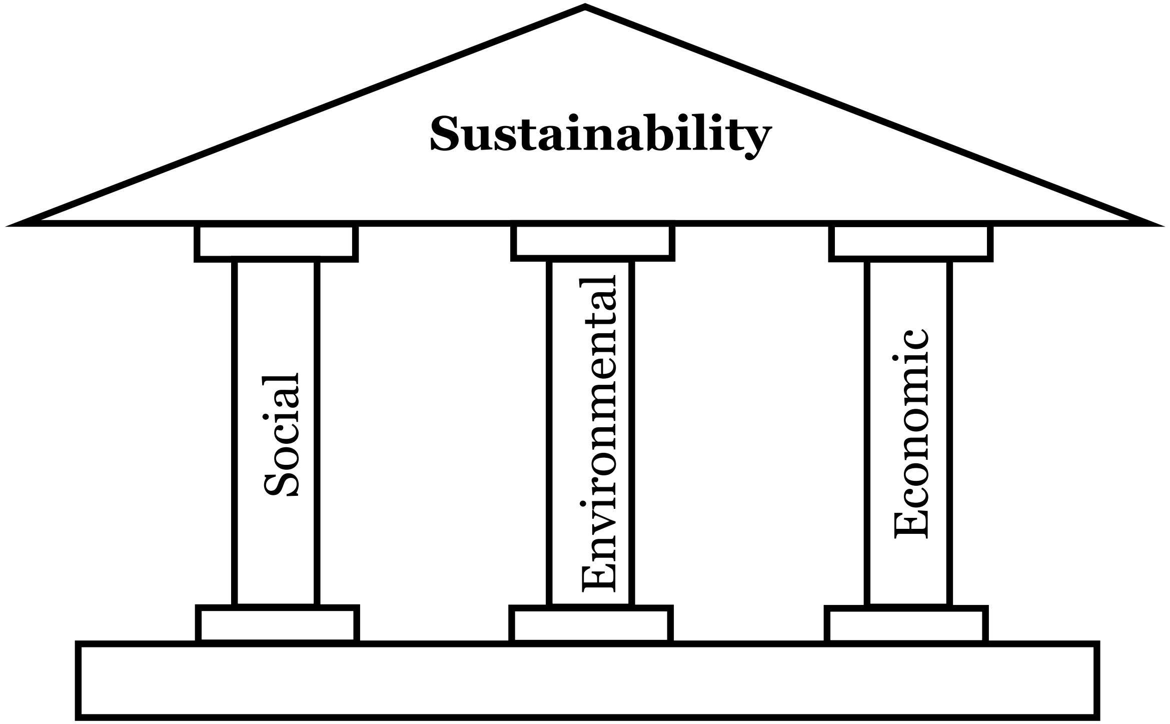
Topics for Discussion

- Traditional MNC Environmental Strategy
- Novel Environmental Strategies for MNCs
- Multiple stakeholder theory

Sustainability

Sustainability focuses on meeting the needs of the present without compromising the ability of future generations to meet their needs.



(Source: OECD, 2020 – Sustainable Agenda 2030)

Environmental Strategy

Environmental Strategy is a firm's long-term orientation on how to manage the practices that ‘fit’ with stakeholders’ expectations on how best to manage the company’s environmental impact.

Shareholder vs Stakeholders

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- **Shareholder:** A person, company or institution that owns at least one share of a company's stock, which is known as equity. See Shareholder Theory (Freidman, 1962, 1970).

- **Stakeholder:** A stakeholder is a party that has an interest in a company and can either affect or be affected by the business. See Stakeholder Theory (Freeman, 2010).

The Traditional View

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- A traditional view of MNCs' environmental strategy is based on the "Race to the Bottom" (RTB) hypothesis, which suggests that when an MNC makes a decision about where to build factories, it will choose the location with the most lenient standards.

- This hypothesis is often discussed in the context of labour standards, corporate tax rates, etc.

Duanmu, J. (2014) A race to lower standards? Labour standards and location choice of outward FDI from the BRIC countries. International Business Review.

The Traditional View - TRB

Two Players in Game:

Side 1: Countries may deliberately choose lower standards to attract investment, i.e. competitive game;

Side 2: MNCs favour those with lower standards as it lowers operating costs.

Race to the Bottom

Keller and Levinson (2002). Pollution abatement costs and foreign direct investment inflows to US states. *Review of Economics and Statistics*, 84(4), pp. 691-703.

The authors employed an 18-year panel of Relative Abatement costs and found robust evidence that abatement costs have had moderate deterrent effects on foreign investment.

RTB Theory: In Practice

1. There are many factors that contribute to an MNC’s choice for a site, which have a more profound impact on manufacturing costs than do environmental standards. This includes access to raw materials, proximity to markets, tax benefits, and other factors that typically attract investment;

2. When MNCs invest in a variety of locations, they typically implement technology that complies with the most stringent of regulations;

3. Reputation has a cost.

Two Factors Not Considered by RTB

1. It assumes that ALL MNCs have a same strategy, namely favouring countries with lower standards;

2. It does not consider that there are MNCs coming from countries with lower standards invest in countries with higher standards.

Novel Environmental Theory

- It considers that MNCs may have different strategies. It largely depends on to what extent their multiple-location activities are integrated or interconnected, and how much they care about their global reputation;

- It also accommodates the fact that there are many MNCs coming from countries with poor/low standards, which invest in countries with higher standards;

- More importantly, it does not assume that a country's standards, once set up, never change.

Uncertain Rules

		Environmental Regulatory Stringency		
		Low	Medium	High
Regulatory Uncertainty	Low	Argentina, China; Russia, Philippines	Estonia, Latvia, Mexico, Poland, Spain, Thailand	Australia, Belgium; Canada, Denmark; Finland; Germany; Japan; New Zealand; Taiwan, UK
	Medium	Bolivia; Honduras; Peru; Sri Lanka; Ukraine; Venezuela	Bulgaria; Chilli; Colombia; Costa Rica; Greece; Hong Kong; Hungary; South Korea; South Africa	Austria; Czech Republic; France; Ireland; Netherlands; US
	High	Angola; Bangladesh; Indonesia; Nigeria; Pakistan; Vietnam	Brazil; Egypt; India; Israel; Italy; Malaysia; Turkey	Iceland; Ireland

Novel Environmental Theories

1. Countries differ significantly with respect to Environmental Regulations as well as Regulatory Uncertainty;

2. This means MNCs have to take a forward-looking view, and consider the possibility that these countries will change standards in the future.

MNC Market Interdependence

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- Geographic specialisation and corporate reputation entail high market interdependence;
- Need to consider multi-country operations of MNCs
- Market interdependence and global reputation.
- Access to future funding of polluting projects might be limited

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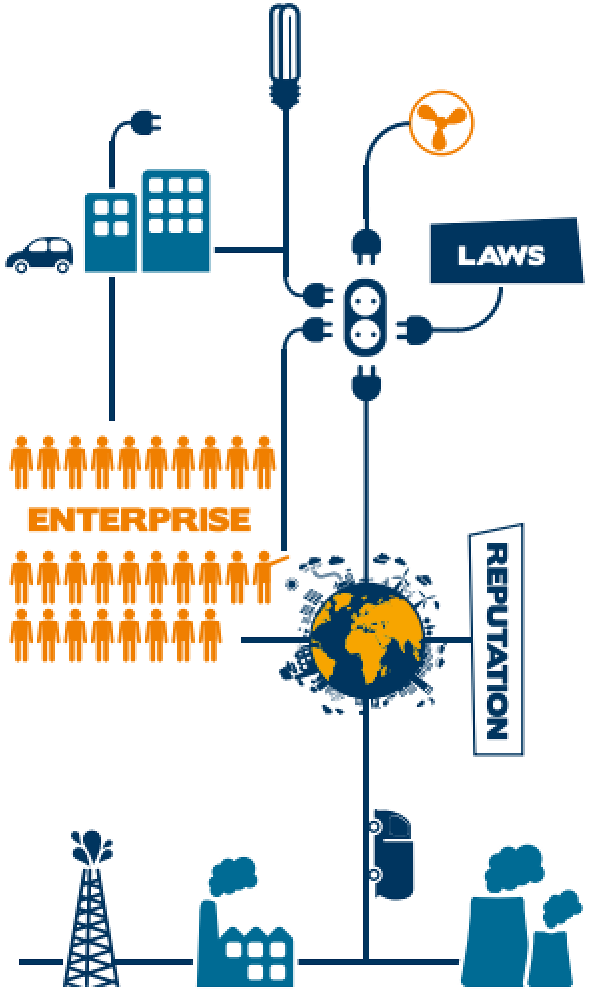
‘Billionaire Chris Hohn threatens to sue coal-financing banks’ (Hook and Flood, 2020)

Less Traditional Theory

Taking the two factors together, we may see four environmental strategies of MNCs :

1. Whether host country's standards are lower or higher than MNCs' home country standards because lower standards indicate possible rise in the future;

2. Whether the MNC has high level of market interdependence/global reputation.



International Regulatory Turbulence

"If changes to environmental regulations cannot be forecast, it is better for MNCs to err on the side of the caution…Smart multinationals look beyond the issues of the day and embed environmental strategy into their international competitive strategy." (Wijen and Tulder, 2011, p.6)

Four Environmental Strategies

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		Regulatory regimes: Degree of Host-country stringency	
Market Interdependence: Degree of Transnationality		Low (host lower than home country)	High (host higher than home country)
	Low	**(I) Fictitious Forcing Strategy**	**(II) Local Compliance Strategy**
	High	**(III) Standard Extension Strategy**	**(IV) Standard Upgrading Strategy**

(Wijen and Tulder, 2011)

Stratagy Data Source

- The study (Wijen and Tulder, 2011) is based on eight MNCs in the period of 2001-2008. Each has operations in five key host countries.

Developed Countries	Industry	Developing countries	Industry
Shell (UK-Netherlands)	Oil and gas	CNPC (China)	Oil and gas
Philips (Netherlands)	Electronics	Petrobras (Brazil)	Oil and gas
		Sinochem (China)	Chemicals
		Acer (Taiwan)	Electronics
		CEMEX (Mexico)	Construction
		Tata Steel (India)	Steel (conglomerate)

Fictitious Forcing Strategy

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Low standards in host countries and low market interdependence

What is it? Acting as if they were forced by a stringent regulatory regime

1. Why use this strategy?
2. The least stringent regulatory regimes also tend to be the most unpredictable
3. Abundant natural resource use and pollution can be considered forms of economic inefficiency

Examples:

- Tata entered emerging markets with lenient regimes, but Tata has a strong track record of corporate social responsibility. Nano car follows European Union norms for vehicle emissions standard.
- Petrobras adopted a beyond-compliance strategy by implementing a rigorous spill-prevention programme, driving its suppliers to be greener, and entering into renewable energy.

Local Compliance

High standards in host countries and low market interdependence

What is it? Comply with local regulation in the host country

Why uses this strategy?

1. No choice
2. A level playing field. Its competitors are subject to the same regulation

For whom?

MNCs who entre countries with more stringent regulations than their home countries, for example, MNCs from China invest in Europe and/or the US.

Standard Extension

High standard in home country and low standard in the host country plus high market interdependence

What is it? High level of interconnection of activities in different countries; high home country standard should be extended into host country. The most stringent regulatory regime is the determinant of the overall strategy

Why uses this strategy?

1. Economies of scale

Examples:

- Airplanes that cannot exceed certain noise or emission levels to entre North American airports will also be produced for African customers since aircraft are highly standardised products

Standard Upgrading

Low standard in home country and high standards in host countries plus high market interdependence

What is it? Upgrading standards across all locations when host standard is usually higher than home one.

Why uses this strategy?

1. Most foreign countries that the MNCs enters have higher standard, and the activities in different locations are closely related to each other.

Strategy Dynamics

		Regulatory Regimes: Degree of Host-country Stringency	
Market Interdependence: Degree of Transnationality		Low (host lower than home country)	High (host higher than home country)
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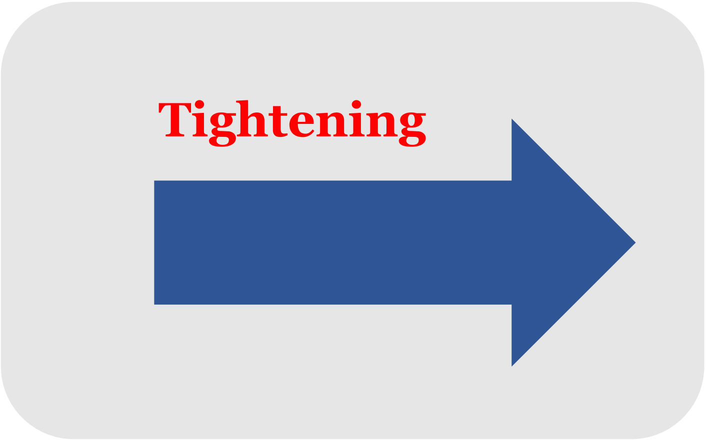
Tightening

Coupling

Loosening

De-coupling

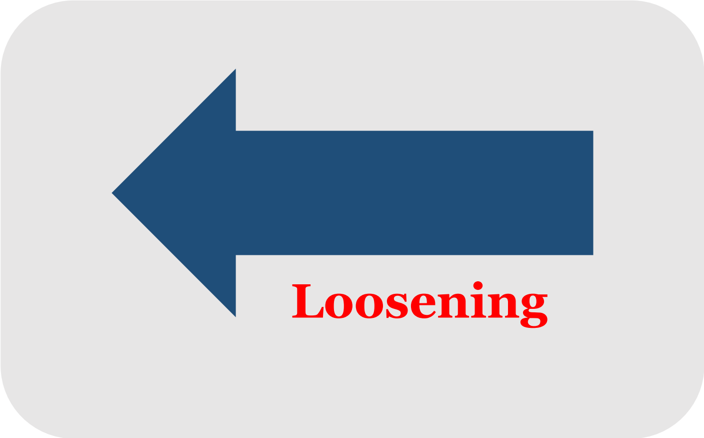
Tightening-Up



- When (a host) country's income level gets higher, more attention will be paid to environmental protection (China, India and some other developing countries)

- It may force MNCs' operating in this country to adopt higher standards

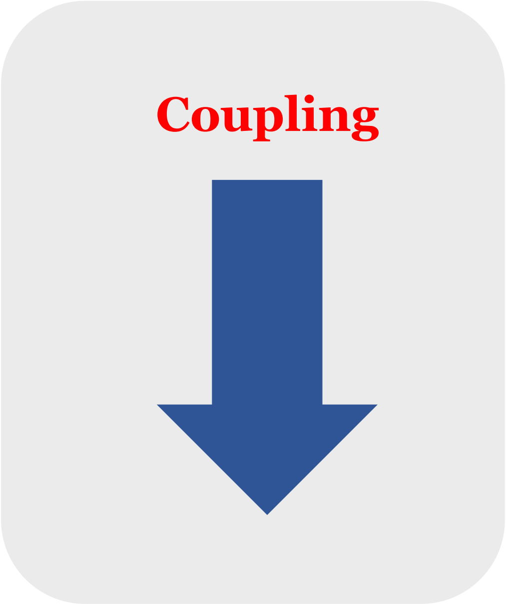
Loosening-Up



- When new governments across some countries attach less importance to environmental preservation - may induce firms to reduce the standards across their global operation (although maintains a global standard).

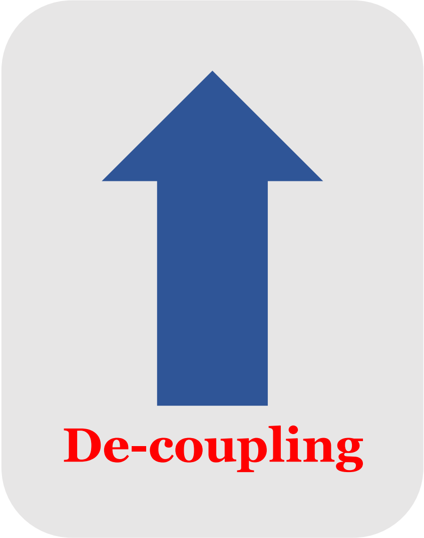
- For instance, with the current president in the US, who views environmental protection much less an issue, US environmental standards may become lower. MNCs operating in the US therefore only need to adopt the new lower standards in the US.

Coupling



- Turn local strategies into more global ones when market interdependence becomes higher, for example, when the MNC's reputation gets more spread over the globe, when its overseas' productions are more integrated.

De-Coupling



- Separate operation in different countries – comply with local standards in each operation, but no longer adopts a global standard because market interdependence becomes smaller.

- It arises when different countries have different and high standards, a universal standard may be either difficult to achieve or too expensive to attain.

Summary

1. We need to acknowledge that as profit-driven organisations, there are both socially desirable (i.e. their products) and socially undesirable (i.e. pollution) outputs from MNCs' operations.

2. When considering the trade-off between the desirable and undesirable outputs, it is important to ask from which/whose perspective that we have this discussion, as we will see, depending on the perspective taken, the answer to our discussion may differ.

A Question

How can this relate to the service Sector and Finance in particular?

Thank you

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