

**The Role of a Firm's Political Connections in  
Foreign Direct Investments and Firm Performance:  
Evidence from Listed Thai Firms**

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The candidate confirms that the work submitted is her own and that appropriate credit has been given where reference has been made to the work of others.

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## **Abstract**

This thesis aims to extend previous research that discussed the role of business-government relationship on outward foreign direct investment (OFDI) by focusing on its performance consequences. Three research objectives are pursued to answer the primary research question on how connections the firms make with political actors at home country can influence the effect of the firm's OFDI on its performance. Based on resource dependence theory (RDT) and institutional theory, two research frameworks are proposed to test the contingent value of the type of political actors and the host countries.

The research findings show that the effect of the home-country political connections and OFDI on firm performance varies depending on the type of political actors and the investment location. Political connections in aggregate influence the effect of OFDI on firm performance negatively, but, with the specific type of political actors and investment location, the political connections can facilitate OFDI to increase firm performance. Top-level political actors are not always beneficial to the firm's OFDI in enhancing firm performance, but executive and legislative ties are useful. OFDI in developing countries, in general, benefits from home-country political connections, particularly with foreign-investment regulating and supporting agencies. OFDI in developed countries, in contrast, is hindered by high degree of political connections, especially with foreign-investment regulating and supporting agencies.

Based on the findings, this research extend existing research in international business by providing the evidence that home-country political connections can influence the firm's OFDI to affect its performance. This study also extends the discussion on corporate political strategy by providing the contingent value of the type of political actors and the investment location that uniquely influence the role of political connections on OFDI and firm performance.

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## **List of Abbreviations**

BOI	Board of Investment
BOT	Bank of Thailand
BRICs	Brazil, Russia, India, and China
CPA	Corporate Political Activities
CPS	Corporate Political Strategies
EMNE	Emerging-Market Multinational Enterprise
FDI	Foreign Direct Investment
FSA	Firm Specific Advantage
FSTS	Foreign Sales to Total Sales
IB	International Business
IFDI	Inward Foreign Direct Investment
IMF	International Monetary Fund
ISIC	International Standard Industrial Classification
MNE	Multinational Enterprise
MPs	Members of Parliament
OECD	Organisation for Economic Co-operation and Development
OFDI	Outward Foreign Direct Investment
OLI	Ownership-Location-Internalisation
OLS	Ordinary Least Squares
RBV	Resource Based View
RDT	Resource Dependence Theory
ROA	Return on Assets
ROS	Return on Sales
SEC	Securities and Exchange Commission Thailand

SET	Stock Exchange of Thailand
SETSMART	SET Market Analysis and Reporting Tool
SOE	State Owned Enterprise
SWF	Sovereign Wealth Fund
UNCTAD	United Nations Conference on Trade and Development
WEF	World Economic Forum

# Chapter 1

## Introduction

*“In economics, there is one tool: money....In political science, on the other hand, the armoury of weapons is infinitely complex, with reason, argument, persuasion, diplomacy at one end and force at the other.”*

*Kindleberger (1970, p.14)*

### 1.1 Research Rationale

The increasing amount of outward foreign direct investment (OFDI) by emerging-market multinational enterprises (EMNEs) has raised the important questions for international business scholars to investigate factors that influence this rapid growth. With less market-based competitive resources available to EMNEs compared to established multinational enterprises (MNEs) (Bartlett and Ghoshal, 2000; Madhok and Keyhani, 2012), non-market factors such as government support (Luo et al., 2010; Wang et al., 2012) or business networks (Peng et al., 2001; Filatotchev et al., 2007) have been considered as important factors that can explain the rapid growth of OFDI by EMNEs. One of the non-market factors considered as a driving factor for the increasing expansion of the OFDI from emerging markets is political connections possessed by firms.

Political connections, including both organizational and personal linkages between business and government, while considered as an important factor to explain EMNEs, are used around the world (Faccio, 2006) because political behaviour of firms can occur anywhere when the market is imperfect (Boddewyn and Brewer, 1994). The widespread use of a firm's political strategies, political connections in particular, therefore increases interest of business scholars to investigate this growing research topic, particularly on how such connections can influence the firm's strategies and increase the firm's value.

Studies in international business also try to explain how a firm's connections with the government can influence the firm's internationalisations (e.g. Wang et al., 2012). The connections with the home-country government can facilitate the firm's internationalisation, especially OFDI, through various mechanisms. The government can help the firm through supporting policies by reducing home-country regulations related to overseas investment (Luo et al., 2010), or negotiating with the host-country government for a particular investment project (Li et al., 2013; Ramamurti, 2001). The connected firms can also get favourable treatments from the government which ultimately increase the competitive advantage of the connected firms (Frynas et al., 2006).

On the other hand, connections with the home-country government can also put more pressure on the connected firm due to government preferences and the host-country perspectives towards government-related firms, in particular, state-owned enterprises (SOEs). The pressure on the firms from both home and host government can influence the selection of foreign investment strategies of the government-related firms. For example, SOEs have to choose less-preferred mode of market entry or reduce equity stakes to gain organisational legitimacy when they invest in particular host countries (Meyer et al., 2014; Cui and Jiang, 2012; Pan et al., 2014). Firms engaged with government affiliates and SOEs also have different institutional pressures to choose investment location for its subsidiaries and affiliates (Wang et al., 2012). Hence, a firm's political connections, while are supportive in certain circumstances, may have different impacts on the firm's international operations and the firm's value.

The facilitating role of the government for the firm's overseas investment, yet limiting its foreign-investment strategic choices, raises the question of how the firm's connections with the government can influence its overseas investment to add value. The advantages of the political connections that enable the firm to invest overseas do not always assist the firm to compete in a foreign country. Typically, MNEs, facing higher costs and competition in the host country due to the liabilities of foreignness, transfer home-grown resources and capabilities, such as technology, financial assets, knowledge and brands, to their subsidiaries (Zaheer, 1995; Zaheer and Mosakowski, 1997). However, due to the fact that political connections are embedded in the home

country, can the firm use its political resources to overcome disadvantages associated with the liability of foreignness, to compete in the host countries, and to increase returns to its OFDI?

Previous research in IB has established that the firm's political connections created in the home country can help EMNEs to internationalise and engage in OFDI (Wang et al., 2012) by providing firms with information, government support, and beneficial policies (Luo et al., 2010; Voss et al., 2010). However, we have not had a clear understanding of whether the connections the firms have with political actors in the home country are useful when the firms invest their affiliates overseas. The firm's affiliations with the home-country government, although helpful for the firm's internationalisation, can negatively influence the perception towards the firms in the host countries that eventually limits the choices of foreign investment strategies of the connected firms (Meyer et al., 2014; Cui and Jiang, 2012). With this limited understanding on the value of the home-country political connections and OFDI in the IB research, this thesis addresses this research gap by examining how home-country political connections influence the relationship between OFDI and firm performance, and by developing a theory about the conditions that the home-country political connections may be leveraged abroad.

Among various tactics of political strategies, appointing current or former government officials to the board of director can be used to create the linkages between the firms and their important external organisations purposefully to decrease uncertainty derived from the external organisations (Pfeffer and Salancik, 1978). By appointing government officials to the board, the firm may gain unique information about public policy processes; a channel of communication or access to existing politicians, bureaucrats and other political decision makers with whom the board member is aligned; and potential access to political decision makers that may result in influencing political decisions and legitimacy (Pfeffer and Salancik, 1978; Hillman, 2005). Aiming to influence the political environment to reduce external uncertainty and gain preferential treatments, the political connections provide the firm the access to government-controlled resources, information, supports, and legitimacy (Boubakri et al., 2012b; Pfeffer and Salancik, 1978; Faccio, 2006) that can ultimately help the

firm to survive (Zheng et al., 2015; Faccio et al., 2006) and increase its performance (Hillman, 2005).

However, the value created through the relationship between firms and political actors is based on the relational rent (Dyer and Singh, 1998) that may lead to rent bargaining and appropriation in the subsequent stage (Sun et al., 2012). Political connections therefore can be the firms' burden leading to negative firm value when political actors seek for political objectives (Shleifer and Vishny, 1994), or extract rents from the connected firms (Sun et al., 2012). Political linkages through the board of directors can give opportunities for political actors to directly navigate the firm's strategies favourable for the benefits of themselves or their owned organisations (Sun et al., 2016). Moreover, political connections with a particular government regime can also turn the positive benefits to liabilities when the ruling government changes (Siegel, 2007).

The inconclusive consequences of the firm's political connections require studies in this area to focus on the contingent value of a firm's political connections conditioned by both environmental and organisational factors (Sun et al., 2012). Sun et al., (2012) argue that market and non-market environmental factors, such as institutional arrangement in the political system and inter- and intra-organisational factors, such as types of organisational ownership or types and composition of ties, can moderate the relationship between political connections and firm value. Based on the proposition of the contingent value of political connections, we develop our research framework focusing on two types of conditional factors that may influence the impact of political connections on the firm's value differently.

These two types of conditions are types of political actors to whom the firms connect and environmental factors of the host-country location. Fine-grained types of political actors based on their position in the government are focused because different types of political actors can lead to unique resources that may differently influence the firm's performance. To understand the possible resources that the firm may gain from the different types of political connections, two sets of political actors are explored in this thesis. The first focuses on the political positions based on the hierarchical levels and the government functions (i.e. executive and legislative) of political actors. Different levels of political actors offer different degrees of access to

government resources (Zheng et al., 2015; Ma et al., 2016), prestige (Johnson et al., 2011), and legitimacy (D'Aveni, 1990) to the firms. Political actors from different government functions also get access to and control over unique government resources that may be beneficial to the firms in dissimilar ways (Zheng et al., 2017).

Given our research focus on the value of political connections regarding OFDI, we target the second type of political actors from government organisations that can facilitate the firm's overseas investment. These organisations include government banks, foreign-investment supporting and regulating agencies, and the Ministry of Foreign Affairs. Although these political actors are not typically considered in prior research in political connections, they are directly related to foreign investment activities and can provide firms with different kinds of support that can ultimately influence the firm's performance. By focusing on these two sets of political actors, we can extend the studies in the area of corporate political strategy (CPS) and international business (IB) by theorising the specific types of political actors that facilitate the firm's OFDI in increasing its performance.

Environmental context of the host countries is another conditional factor that we consider to influence the relationship of political connections and OFDI on firm performance. Given our focus of political value concerned with OFDI, we cannot ignore the impact of investment location and its institutional settings in the host countries. With the linkages to the home government, the connected firms may confront with institutional pressures uniquely in different host countries. The different degree of institutional development in the host country can influence the firm's ability to exploit its political connections. In developed countries where markets are well functioning, the use of non-market strategies such as political connections are less important (Wan, 2005; Luo, 2001) compared to less-developed markets. Hence, it is important to highlight the conditions based on the host-country location that may influence the firm's ability to get advantages from its political connections. This thesis, therefore, compares the different impacts of the firm's political connections on its OFDI in host-developed countries and host-developing countries.

By considering these two conditions that may vary the effects of the firm's political connections on the firm's performance in the OFDI context, this thesis



attempts to pursue the specific research objectives and related research questions explained in the next section.

## **1.2 Research Objectives and Research Questions**

Based on the above research rationale, this thesis attempts to pursue three research objectives and to answer five research questions. The first objective is to explain the role of the home-country political connections in influencing the firm's OFDI to affect its performance. The firm's political connections can be seen as the firm's competitive resources used by the firms to substitute the lack of typical market resources and capabilities, especially in emerging markets where institutions are less developed (Peng and Luo, 2000). As discussed earlier, the relationship of the firm with the home-country government can facilitate the firm's OFDI and can limit the strategic choices of the firm. This leads to two related research questions. First, can the home-country political connections influence OFDI to ultimately increase the firm's performance? (RQ1). Second, in case political connections are influential, what is the impact of the firm's political connections and OFDI on the firm performance? (RQ2). This first objective and two research questions are the primary focus of this research that will be pursued by testing the moderating effects of the firm's political connections on the relationship of OFDI and the firm's performance.

The second objective of this research is to identify the types of political actors that influence the firm's OFDI. As prior studies focusing on the relationship of the firm's political connections and its performance have provided inconclusive results (e.g. Hillman, 2005; Faccio, 2006; Faccio et al., 2006; Siegel, 2007), we develop fine-grained types of the connected political actors, rather than test the general firm's political connections as done in typical research. By aiming to identify the impact of different types of political actors, the third research question asks which type of the political actors can enhance the relationship of OFDI and the firm's performance (RQ3). This objective and research question are explained by separating the types of political actors into two subsets which are the types based on the hierarchical level and the government functions, and the types based on political positions related to the firm's OFDI. Both sets of the political positions are explained by testing the

moderating effects of each type of political actors on the relationship between OFDI and firm performance.

The third objective of the thesis is to compare the effects of the firm's political connections in different host-countries. The institutional settings of the investment location can influence the firm's investment strategies and competitive capabilities (Oliver, 1997). The difference between the institutions in developed countries and in developing countries are therefore considered as the environmental conditions that may affect how the firm's political connections influence its performance. In a host country where the capital market is imperfect, the firm's business and social networks are more helpful to the firm to decrease transaction costs and increase financial capital (Voss et al., 2010). Also, the experience the EMNE has gained to deal with the weak institutions at home can be beneficial to the EMNE when it invests in developing countries (Cuervo-Cazurra and Genc, 2008; Holburn and Zelner, 2010). This leads to the last two research questions on whether home-country political connections assist firms to perform better when they invest its foreign affiliates in developing countries compared to developed countries (RQ4), and which type of political resources are more beneficial to the firm's performance in host-developing countries and host-developed countries (RQ5).

To answer these research questions, we focus in particular on EMNEs because the economic and political context in these emerging economies provides the policy environment that allows us to explore the role of the home-country government in influencing OFDI. As the government in emerging economies provides government support to promote the overseas investment by its domestic firms (Buckley et al., 2007; Luo et al., 2010), establishing connections with the home-country government becomes more important especially for the firms that seek to invest its affiliations in foreign markets because the firms can leverage its political connections to gain the most out of the government supporting and promoting policies. Specifically, we employ data from Thailand to test our research framework with the consideration that we can leverage the political context in Thailand to explain the research phenomenon. The Thai government recently encouraged Thai firms to expand their businesses overseas by launching supportive investment policies to promote and support OFDI by Thai firms (Bank of Thailand, 2012; Board of Investment, 2015). This political

context creates the policy environment for Thai firms to pursue the home-country political connections in helping the OFDI that matches with our research interests in both OFDI and the home-country political connections.

By pursuing these three research objectives and answering all research questions, this thesis contributes to the research areas in IB and CPS. In IB, this thesis extends the existing research on the role of the home-country political connections on the firm's internationalisation by arguing how home-country political connections can influence the firm's OFDI to increase its performance. In CPS, this thesis extends the current debate on the contingent value of the firm's political connections on its performance by providing the fine-grained political positions that differently influence the firm's political connections. It also provides a discussion of the roles of institutional settings that influence how the firm's political connections affect its performance. Hence, this thesis contributes to the studies in the areas of IB and CPS by providing the empirical findings supporting the ideas of the conditional value of the firm's political strategies. The research contributions will be explained in detail together with the consideration of the research findings in Chapter 6.

### **1.3 Definitions and Terminologies**

This section explains the definitions and terminologies applied throughout the thesis. The aim is to familiarise the reader with the terminologies that can be conceptualised or defined in several ways.

#### **1.3.1 Foreign Direct Investment**

Following the OECD's definition, foreign direct investment (FDI) refers to the investment activities of a firm in another country for the objective of the establishment a lasting interest. The lasting interest implies the existence of a long-term relationship between the direct investor and the direct investment enterprise at a significant degree of influence on the management of the company, which is determined by the direct and indirect ownership of 10 per cent or more of voting power of the firm (OECD, 2008). The threshold of the ownership control is the combined ownership of the MNE, its subsidiaries, and its associates (OECD, 2008), therefore the OFDI value includes the investment by MNE's subsidiaries and associates. The outward foreign direct

investment (OFDI) represents the outflow of the direct investment by a firm from its home country to host country. In contrast, the inward foreign direct investment (IFDI) signifies the inflow of the direct investment by a foreign firm in the home country.

### **1.3.2 Multinational Enterprises (MNEs)**

An MNE is defined as “an enterprise which owns and controls activities in different economies” (Buckley and Casson, 1976, p.1). The enterprise in a foreign country that is owned by an MNE (and its subsidiaries) by more than 50 per cent is considered a foreign subsidiary of the MNE. If the control is less than 50 per cent but is equal to or more than 10 percent of voting power, the investment company is considered as an associate (OECD, 2008). The investment value in both foreign subsidiaries and associates are included in the OFDI data collected for this thesis. This study uses the term affiliates to refer both subsidiaries and associates of a firm (or an MNE).

### **1.3.3 Political Connections**

The term ‘political connections’ and ‘political ties’ are used interchangeably in this thesis to identify the relationship between a firm and a political actor who has working experience in the government organisations. Following the definition of ‘political ties’ by Sun et al. (2012, p.68) as “boundary-spanning personal and institutional linkages between firms and the constituent parts of public authorities”, the consideration of the firm’s political connections in this thesis considers all types of political linkages that can occur through both personal relationships or the linkages at the organisational level. However, in the operationalisation of this research project, only the formal relationship between a firm and a political actor through the board of directors is included as a proxy for the firm’s political connections.

The connections with political actors can benefit firms in a myriad of mechanisms ranging from formal mechanisms such as the appointment of political actors on the board of directors or as corporate advisors, or government ownership, to informal mechanisms such as the linkages through family members, or friendships. The benefits of political connections, therefore, are broad and can cover both legal mechanism and illegal mechanisms such as bribery. While we are aware that political connections can lead to the rent seeking behaviour of political actors and firms, we limit the study only to the formal and legal areas by investigating benefits of political

connections through the role of the board of directors and discuss the benefits based on legal mechanisms.

### **1.3.4 Political Actors**

The term ‘political actor’ used in this study refers to an individual who has experience in government organisations and includes all levels of government officials and civil servants. Studies focusing on a firm’s political connections often refer to only a connection the firm makes with a politician or a top-executive government official, members of parliament (MPs) and cabinet members in particular. While it can be argued that politicians from the top-executive level can provide the connected firms with more resources and information compared to the lower level, as they are in the position that can control the policy making decision of the government, the use of politicians from only the top level assumes no benefits of the non-executive level of government officials that the firms may also make a connection with in order to seek information and support.

The use of the term political actors in this thesis, rather than politicians, therefore, considers different types of government officials including civil servants that can provide useful resources to the firm. While we use the term ‘political actors’ to represent politicians, top-level government officials and civil servants, we are aware that some government officials and civil servants are relatively “political neutral” (Drewry, 2011). Political actors in this study therefore in general refer to those who are accessible to government resources and can provide information, advice, and support to the connected firms.

### **1.3.5 Country Classification**

The country classification suggested by different supranational organisations is varied and no convention for the designation of developed countries or non-developed countries exists. The world economies are classified into two groups, namely developed and developing countries in this thesis, although we are aware that non-developed countries can be further classified as transition economies, emerging economies, or developing economies. For the methodology purpose, the developed economies/countries/markets are classified following the IMF list of advanced countries (International Monetary Fund, 2013).

## **1.4 Outline of Thesis**

This thesis consists of six chapters. Chapter 2 introduces the conceptual parts of the research project. In Chapter 2, the discussion is separated into two sections. The first section explains previous research that is relevant to this study's research focus, identifies the research gaps and forms the basis for further discussion. The second section suggests a conceptual framework of how a firm's political connections can influence OFDI to ultimately affect the firm's performance. This section is based on the resource dependence theory (RDT) and institutional theory. In Chapter 3, the methodology applied in this thesis is described. Chapters 4 and 5 provide empirical results. In Chapter 4, the RDT is applied to develop hypotheses related to research questions 1 to 3. The test focuses on number of connections, level of political actors, and government functions that often lead to greater political resources that the firm can rely on. In Chapter 5, institutional theory is incorporated to test if RDT still holds when the host-country context is considered. The test focuses on political resources that are likely to benefit the firm's internationalisation. These political positions are incorporated based on previous studies and the fact that they are more relevant to the firm's internationalisation, and they can provide relevant political resources that should be beneficial to the firm's OFDI and its performance. By testing two research frameworks which focus on the distinctive perspectives of the firm's political connections, this thesis can then extend and advance the existing studies in the area of IB and CPS. The conclusion and discussion of the research will be provided in Chapter 6, together with the research contributions and limitations.

## **Chapter 2**

### **Corporate Political Strategies in International Business Studies**

*“Competitive advantages do have an unavoidable political dimension that must be factored theoretically into strategy research, and particularly so in international business studies.”*

*Boddewyn and Brewer (1994, p.137)*

The ultimate objective of this thesis is to examine how political connections affect the relationship between OFDI and firm performance employing institutional theory and resource dependence theory (RDT). While home government is seen as a helping hand for OFDI by EMNEs, government affiliations in the form of state ownership can hinder the firm’s competitiveness (Rugman and Li, 2007) and limit its foreign strategic choices in the host country (Cui and Jiang, 2012; Meyer et al., 2014). Building on studies in CPS and IB, our research framework proposes the analysis of fine-grained types of political actors with the ultimate aim to discern political resources that are crucial in supporting the firm’s OFDI.

This chapter introduces the research background, theories, and empirical evidence that are relevant to this research. The first section provides a research background of FDI and CPS, followed by the notion of political strategies of MNEs. The second section explains the relevance of institutional theory and RDT for this research. Building on the research and conceptual background, the third section presents the research framework focusing on the moderating role of the firm’s political connections. This section, firstly, discusses the inconclusive effects of internationalisation on the firm’s performance, and then the impact of CPS on firm performance. The last section provides a summary of the chapter.

## **2.1 Research Background**

The conceptual framework of this thesis derives from studies in FDI and CPS. This section explains the brief background of these two concepts and establishes the relationship between these two research areas. The discussion starts with the concepts of FDI and EMNEs. The second part explains the concepts and objectives of CPS. A discussion of MNE's political strategies is provided in the third section.

### **2.1.1 Foreign Direct Investment and Emerging-Market MNEs**

The existence of FDI was explained by Hymer (1960) in an attempt to reason why a firm seeks to control a company in a foreign country. One of his explanations is the firm exploits its competitive advantages to make monopolistic power through the FDI activities (Hymer, 1960). The possession of technology and managerial skills is the core determinant that explains the existing of MNEs in later IB studies known either as the firm-specific advantages (FSA) (Rugman, 1981) or the firm's ownership advantages (Dunning, 2000). The essential element of FSA to yield the firm's profitability is its transferability to the MNEs' subsidiaries so that it can help them overcome the costs of doing business in foreign countries (Zaheer, 1995).

Later, the concept of competitive advantages of MNEs has been integrated with locational and internalisation advantages to form the so-called eclectic paradigm (e.g. Dunning, 1977; 1988; 2000) which has been extensively applied to explain the FDI strategy by MNEs (e.g. Cantwell and Narula, 2001; Woodcock et al., 1994). Extending the FSA explanation, the eclectic paradigm, or OLI (Ownership, Location, and Internalisation) paradigm contains macro aspects of locational advantages, derived from Ricardo's comparative advantages, that explain FDI decisions based on the attractiveness of the host country and disadvantages of the home countries (Dunning, 1977; 1988). The locational aspects of OLI related to the investment motives of MNEs explains whether firms invest for market seeking, efficiency seeking, or resources seeking (Dunning, 2000). Simultaneously, the OLI paradigm considers the transaction costs (Williamson, 1975) faced by firms to make the comparison between the cost of FDI and non-equity modes of entry. This last element of internalisation advantages explains the existence of FDI that firms will internalise



imperfect markets through FDI when the cost of using the market is higher than the firms invest in affiliates by themselves (Buckley and Casson, 1976).

These three elements of the OLI paradigm have been widely applied to explain MNEs' competitiveness and foreign activities (e.g. Cantwell and Narula, 2001; Woodcock et al., 1994) together with the extension of other relevant elements such as relational assets (R-assets) introduced for the explanation of the cooperation and network prospects of MNEs (Dunning, 2003). The extension and application is based on the core argument of monopolistic power that MNEs create through the possession of competitive advantages. This, however, has been challenged by the rise of EMNEs. The increase of OFDI by EMNEs without the possession of capabilities and technology advantages (Madhok and Keyhani, 2012) has raised new questions and debates in international business studies on whether we need new theory to explain EMNEs (Cuervo-Cazurra, 2012). While the debate is ongoing, many studies have applied institutional theory to explain FDI by EMNEs (Wang et al., 2012; Buckley et al., 2007) because the ownership advantages of the EMNEs have been argued to result from home-country institutional factors. For example, Buckley et al. (2007) explain that capital market imperfection stemmed from the inefficient banking system in emerging markets, and the provision of lower-rate capital to SOEs can be transformed to ownership advantages of EMNEs that help them expand increasingly in both advanced and developing countries.

The rising of EMNEs does not only bring the roles of home-country institutions in OFDI to light but it also leads to the new aspect of the government involvement in business activities, which can be in different forms such as SOEs, Sovereign Wealth Fund (SWF), or business-government ties. The government is often treated in IB studies as an exogenous factor that creates the rules for the firms. Studies in CPS, however, treat government not only as the external factor that only initiate, monitor, or coerce rules and regulations but as the 'player' in the political market. The rising of EMNEs that are highly involved with government leads us to take a closer look at the active role of the government as a player in the business game through the lenses of CPS. The conceptual background of CPS is discussed, and followed by the linkages between FDI and CPS, in the next section.

### **2.1.2 Corporate Political Strategy: Concepts and Terminologies**

Although political aspects are often treated as external factors and less considered in business research, studies that are interested in the relationships between firms and politics can be classified into different research concepts. Each investigation, although is interested in political behaviours of firms, emphasises particular features of those political actions and conceptualises political behaviour differently. This section discusses concepts and definitions of the main terminologies used in CPS research, following by the objectives of CPS.

The first concept that should be the starting point for further discussion is the concept of ‘political behaviour’ itself. Political behaviour is defined as “particular ways of relating to targets located in the non-market environment of firms” Boddewyn (1988, p.342), where ‘ways’ refer to the means that firms use to interact with non-market environment and ‘targets’ refer to actors belonging to non-market environment including both the government and the community (Boddewyn, 1988). These ‘actions’ and ‘actors’ (Boddewyn and Brewer, 1994) are therefore key to research concepts and research streams in this field of studies.

The ‘actions’ or ‘means’ that firms use to interact with political actors can be broadly defined as ‘activities’ or ‘strategies’ which have formed the research streams of ‘corporate political activities’ (CPA) and ‘corporate political strategies’ (CPS). Despite the difference of CPA and CPS stated by Getz (1997) that CPS is normally tied to large business and more purposefully rational than CPA, and CPA focuses more specific on behaviour taking place in the government arena, these two constructs are very closed concepts that are often used interchangeably to illustrate “proactive actions taken by a firm to affect the public policy environment in a way favourable to it” (Hillman, 2003, p.455). The political actions mentioned in the CPA research often refer to proactive actions that firms utilise to influence electoral and legislative or regulatory processes of the government which can be implemented in different forms for different objectives (Baysinger, 1984).

Firms make decisions towards political actions by considering whether they will create a short-term or long-term relationship with the government, whether they will incorporate political actions alone or in cooperation with other firms, and which

types of political strategy they will utilise (Hillman and Hitt, 1999). Hillman and Hitt (1999) suggest that there are three types of political strategies which are information strategy, financial incentive strategy, and constituency-building strategy. Firms can incorporate information strategies to influence policy makers by supplying information of their policy preferences to policy makers through the political tactics such as lobbying, or by using financial incentives such as hiring individuals who have political experience as manager, directors, or consultants. Firms can also utilise indirect strategies, known as constituency-building strategy, by influencing citizen or voters to gain political support.

Another terminology of political 'actions' employed by firms is 'political connections' or 'political ties'. Studies focusing on the firm's political connections often refer to the definition provided by Faccio (2006, p.370) that:

A company is connected with a politician if one of the company's large shareholders or top officers is: (a) a members of Parliament (MPs), (b) a minister or the head of state, or (c) closely related to a top official.

With this definition, the political aspect of 'political connections', compared to CPA and CPS, concentrates more on the relationships between the 'actors' rather than the 'actions'. In other words, political connections focus on the relationships between two organisations, being a firm and the government, based on the individual level of politicians or government officials and shareholders or top management team. The actor included in this definition is also broader than the government as it includes informal relationships through a relative or a friend of a minister or MPs (Faccio, 2006). Linking back to the CPA/CPS concepts, political connections in this definition can be seen as part of a financial strategy in which political actors are hired by firms as managers or the board of directors (Hillman and Hitt, 1999). The term 'personal service' is used to explain this financial strategy when firms hire political actors as their managers or directors, or a firm's members work as government officials (Getz, 1993; Hillman and Hitt, 1999).

The term 'political ties' is often used interchangeably with political connections but it can be defined as "boundary-spanning personal and institutional linkages between firms and the constituent parts of public authorities" (Sun et al.,

2012, p.68). With this definition, political ties can also include the organisational level of the government which can include the relationship of firms and SOEs. With the broad concept of political connections, some studies have operationalised only particular relationships that firms create through the management teams of the firms (Sun et al., 2015; Zheng et al., 2017) and investigated ‘managerial political ties’ or ‘interlocking political ties’. Furthermore, political connections can be viewed in broader perspectives that include informal ties between business actors and political actors based on personal relationships (Mahmood et al., 2017).

Another concept closely related to political connections and political ties is ‘political networks’. While political connections and political ties focus on relationships between political and business actors in the dyadic way, political networks, based on social networks, consider groups or networks of connected business and political actors (e.g. Hadjikhani et al., 2008). Political connections can be looked at through the lens of political embeddedness, which argues that economic activities are embedded in the social structure rather than an isolated unit, so when we consider the economic activity we need to consider social relationships together with the economic rationales (Okhmatovskiy, 2010; Sun et al., 2010).

It is noteworthy that CPA/CPS and political connections studies often use different contexts. The terms CPA and CPS often refer to formal political behaviour of firms from developed countries, especially the United State, where the political system allows companies to use political tactics such as lobbying, political campaigns, or political donations with more transparent information (e.g. Hillman, 2003; Hadani, 2007). Political connections and political ties studies are applied in broader political contexts (e.g. Faccio, 2006; Zheng et al., 2017), particularly in the context of developing or emerging countries where data on formal political activities such as lobbying, political campaigns or donations are unavailable. Moreover, the application of CPA/CPS typically assumes legal, political activities that are allowed under particular political systems. Political connections or political ties are not explicit in this aspect as some studies also refer/imply political connections to the conflict of interests of the political actors (e.g. Chen et al., 2010; Ionescu, 2010).

In this study, the term ‘political connections’ is applied interchangeably with ‘political ties’ as the central construct because our interest rests on the relationships

of firms and political actors rather than the political activities. Also, the interests lies in the dyadic relationships between a firm and political actors, rather than the networks of political and business actors. The term ‘political resources’, defined as “any firm attributes, assets, human resources, or any other resources that allow the firm to use the political process to improve its efficiency and profitability” (Frynas et al., 2006, p.324) is used to illustrate resources that firms can acquire based on their political connections. While we mainly use the concept of political connections/ties, the ideas discussed in CPS and political networks are also applied to understand this research phenomenon because they all explain the relationship between firms and political actors.

The ultimate objectives of the firms engaging in a long-term relationship with the government through political activities are to influence regulatory process that can benefit the firms; to defend its legitimacy when it is threatened by public policy or government regulations; and to maintain its purposes and goals by gaining supportive favour from the government (Baysinger, 1984). The firm’s political behaviour can also lead to the firm’s profitability derived from three major sources consisting of firm’s efficiency, market power, and legitimacy (Boddewyn and Brewer, 1994). The firm’s political behaviour can help decrease its production and transaction costs. Firms can generate market imperfection by gaining monopoly privilege, preferential access to resources, and involvement in policy making when they employ political behaviours. Political behaviour also help firms keep its legitimacy (Boddewyn and Brewer, 1994).

The concepts and terminologies related to political connections are discussed in this section to lay the background of the different research streams in CPS. This brief explanation can help us link the concept of political connections with the broader research area of CPS and give some brief idea on the objectives of CPS. In the next section, we explain more specifically on the topic that is directly relevant to our research interests: the political strategies of MNEs.

### **2.1.3 Political Strategies of MNEs**

In an activity related to internationalisation of a firm, especially FDI, the government role is crucial both at home and in the host countries. Studies of MNEs have not

neglected the role of government. Hymer (1960), for example, discusses the barriers created by host government in the form of prohibitions or restrictions on foreign firm's activities, as well as regulations and laws that are created by the home government. However, within the three elements of the OLI paradigm, which is widely used to explain FDI activities, the government often is in the background as policy makers or regulators whose impact on the firm's FDI is crucial but less manageable. The perspective towards government as the exogenous factors in most studies in IB hinders the ability of international business research to get the whole picture of FDI activities that are involved directly by the government and political actors. In other words, by looking at government as an external factor, we ignore the fact that political actors are also players in the business game.

Dunning (1997a, p.32) suggests that government may perform two different functions:

The first is as an initiator and overseer of the economic system, which sets the legal and institutional framework within which the resources and capabilities in its jurisdiction are created and deployed; and as an arbitrator as and when disputes arise between economic agents. The second is as an owner of assets, and as a *participator* in, or *influencer* of, the way these assets are utilized (Italics in original).

As the organisation which initiates and oversees the economic system, it is relevant directly to the foreign investments of the firms in making regulations. However, as another function of the owner of assets, scarce assets, the role of government is more than just an exogenous factor. The government is, therefore, part of the production function (Boddewyn and Brewer, 1994).

The fact that government possess valuable and rare resources makes them more attractive, and firms can also internalise some parts of this unique organisation (Boddewyn and Brewer, 1994). However, early works that considered the government roles in MNEs tend to treat government as an external factor, a given factor that MNEs need to response, rather than an organisation that proactively engages in business activities. So, IB studies need to integrate political behaviours of MNEs to understand the whole FDI phenomena as Boddewyn and Brewer (1994, p.126) state that:

The initial IB behaviour has to be a political one because, without these actors' explicit or implicit permission, no subsequent economic behavior is normally possible.

With this reason, the active roles of MNEs to internalise the government roles were discussed in a seminal work focusing on political behaviours of MNEs by Boddewyn (1988) in which he proposed the concept of a 'political market', followed by the discussion of political behaviours of MNEs in Boddewyn and Brewer (1994). In the political market, the government is the target of the firm's political activities to create FSA and governmental decision-makers can be internalised. Boddewyn (1988) suggested that MNEs need to develop and use political knowledge themselves rather than letting local firms deal with the host government as they possess higher resources and support from the home government. Besides, the advantages of multinationality of MNEs can help them deal with political issues better than its subsidiaries, although MNEs' subsidiaries are more familiar with non-market environment in the host country.

By using political activities, MNEs can create political knowledge and expertise, which can be viewed as ownership advantages of MNEs in dealing with non-market environment, in the forms of intelligence about political actors and opportunities, readier access to political opinion and decision makers, and superior influence skills through various means (Boddewyn, 1988). The ownership advantages of MNEs based on their political behaviours can ultimately generate corporate profits through three primary sources consisting of efficiency stemmed from the reduction of production and transaction cost; market power derived from monopoly privilege, preferential access to resources, and involvement in public policy-making; and legitimacy (Boddewyn and Brewer, 1994). Boddewyn and Brewer (1994) proposed thorough aspects of political strategies covering the conditions of political behaviours of MNEs in the areas of firm's characteristics, industry, and non-market environments; the management of government by MNEs ranging between compliance and avoidance; and the strategic objectives of MNEs applying political behaviours.

These two key studies in political behaviour of MNEs perceive the government as another factor of production (Kindleberger, 1970), or a set of agents (Mitnick, 1993) so that political actors can be managed by firms through the political

market, rather than using the perspective that looks at political factors as a given or exogenous factors that the firms can only adhere to its authorities. The idea of manageable government function that applied in IB research is initially derived from CPA study that perceives political actors/government as part of the production in the political market. Firm, then, can manage the relationships with political actors in order to gain access to their political products (or political resources/assets) which can be in the form of preferential treatments or privilege information. However, IB extends the aspects of political connections into the area of cross-border activities and issues. The government the firms need to deal with can be home government and host government from different sovereignty/states. The government is also related to issues involving the international trade and investment, rather than national aspects/issues. While it seems that government action can only influence firms before they invest overseas, the roles of government are continuous even after the OFDI because the government still has the control power over the FDI permission so that they can overturn its consent at any time (Boddeyn and Brewer, 1994).

Following studies focusing on government and MNEs have applied Boddeyn and Brewer's conceptual models to explain this research area in different aspects. Studies that explore the roles of home-country government in international business research can be discussed in two main themes. The first focuses on the role of home-country government on internationalisation and the second concentrates on government related firms (often in the form of SOEs) and the host-country pressures. We explain each theme in the next section.

### **2.1.3.1 Impacts of Home-Country Government on OFDI**

Typically, the value of OFDI for the home country is not much recognised from the perspectives of the home-country government because OFDI does not generate jobs and prosperity for the home country compared to the benefits of IFDI for the host country. The home-country government, especially in the emerging markets, mainly exercises its regulatory roles to prevent capital flight and protect state assets (Luo et al., 2010; Cui and Jiang, 2012; Deng, 2004). However, the ascending OFDI by SOEs from emerging markets convinces us to see another role of home-country government in supporting OFDI by domestic firms. Apart from the need to acquire resources that the country cannot produce from overseas, it is believed that OFDI is a mechanism



for the firms to transfer knowledge back to its home country. The home government, therefore, can facilitate the firm's OFDI as well as influence the decision of the firm's investment strategies in various ways, which make the linkages with the home-country government useful for the OFDI of the firms. As the regulator, the home-country government can assist the firm's OFDI through OFDI promotional policies (Luo et al., 2010) that ease investment regulations. Moreover, the home-country can support firms by negotiating and bargaining with the host country for the benefits of the firms in taking OFDI (Li et al., 2013; Ramamurti, 2001).

The home-country government not only plays the regulating roles at the macro level, but also engages directly at the firm level through its owned enterprises (SOEs) or its involvement with private firms in the form of political connections. The linkages with the home government can influence OFDI in various aspects. The government can grant firms the resource that are advantaged in overseas investment to compensate for their lack of FSA (Luo et al., 2010; Rugman and Li, 2007). Political resources that the firms created through the connections with the home-country government can help the firms to gain first mover advantages (Frynas et al., 2006) that later benefits firms to build further socio-political networks in the host country earlier than its competitors. The firm's political resources can be defined as "any firm attributes, assets, human resources, or any other resources that allow the firm to use the political process to improve its efficiency and profitability" (Frynas et al., 2006, p.324). Frynas et al. (2006) illustrates how political resources help firms gain first mover advantages based on the Shell-BP case in its first expansion to Nigeria. They discuss that privileged access to British government officials can help Shell-BP to gain favourable treatments such as extension of the exploration license and increase the size of the oil prospecting licence in Nigeria; this in turn slows down the progress of latecomers.

Political connections, however, can also limit strategic choices of connected firms in its foreign investment, especially when firms are owned by the government. At home country, SOEs are likely to conform to home-country institutions because of its dependency on the home government (Wang et al., 2012). At the same time, SOEs face the higher host-country institutional pressures because of the negative image of SOEs, which force them to conform to the isomorphic pressures in the host country (Kostova et al., 2008). SOEs have to conform to institutional pressures in the form of

FDI regulations to choose a joint ownership structure (Cui and Jiang, 2012) or some specific firm's foreign entry strategies (Meyer et al., 2014) in their foreign investment. In contrast, private firms are not subject to these pressures and inclined to increase control level in the host countries.

SOEs are not the only organisations affected by host-country pressure on their overseas investment; the firms affiliated with the government in other forms are also influenced by institutional pressures to choose a particular investment location and types of foreign investment (Wang et al., 2012). Wang et al. (2012) find that the EMNEs affiliated to high-level government officials are more influenced by the government in its OFDI than firms tied with lower level government officials. The differences between SOEs and the firm's affiliations with other government officials also influence the firm's decision to invest in its affiliates in developed or developing country, as well as, the investment motives of EMNEs in different ways.

In line with these studies, it is clear that in understanding the effect of home political connections on internationalisation there is also a need to consider the role of the host-country pressures, which will be discussed in the next section.

### **2.1.3.2 Host-Country Institutional Pressures**

In contrast to the period before the 1980s when FDI was not much welcome by host-country government (Dunning, 2005), the FDI from foreign MNEs nowadays is recognised as a useful activity for the host country's economies and societies due to its impacts on the jobs markets, economic development, and tax income. Host governments, therefore, are generally more supportive of the IFDI by MNEs. However, the regulating role of government to control inward investment and capital inflow is still crucial for the firms as the host government can grant permissions for foreign firms to invest in its country. Previous studies show that host-country governments have more difficult regulations for the inward FDI by SOEs (Meyer et al., 2014; Cui and Jiang, 2012). Meyer et al. (2014) show that host country institutional constraints on SOEs are arising in the host country with strong technology and the rule of law, especially an active protection of minority shareholders, and the pressure inhibits acquisition by SOEs and equity stake of SOEs.

Firms, therefore, need to build a relationship or negotiate with the host government before their investment. Previous studies suggest that MNEs need to bargain with the host country on two levels (Ramamurti, 2001). First, the home-country bargains with a host-country at the macro level through multilateral institutions such as the WTO, the World Bank, and the IMF. Second, MNEs bargains with the host-country at the micro level, and case by case basis. Li et al. (2013) extend this discussion by providing the modified one-tier bargaining model based on Chinese cases. They argue that home-country government will negotiate with the host-country government for both benefits of SOEs and private firms when the national firms invests in the natural resource sector in a less developed country. This idea that a home-country government can help local private firms to negotiate with the host government, however, might be difficult to apply in other context. The conditions of this model are applicable only for the bargaining by the Chinese government in natural resource sector, and into the least developed countries (Li et al., 2013). Although the negotiating role of the home-country government with the host-country government also occurs in other countries, this might happen in limited cases because the capability that the home government can provide may be restricted for governments from developing countries that have less economic power compared to China. Moreover, the conditions of the case that a host country needs to be the least developed country and the investment is in the natural resource sector also limit the applicability of this model. Hence, we argue that a more applicable model to deal with the host country might be the two-tiers bargaining model suggested by Ramamurti (2001). Even though this model is based on developed MNEs and home developed country and hosts developing countries, it should be applied in other cases. The home-country government, both in developing and developed countries, bargains with the host-country government at the macro level, as both models suggest. The negotiations that home-country government from a developing country have with the host-country government at the macro level may also include the potential benefit for OFDI by SOEs, but should not specifically include private firms. Therefore, private MNEs from an emerging country, which cannot rely on their technology or capability in the bargaining with the host-country government, need to find the connections with the home government to gain the bargaining power towards the host-country government.

While these studies (e.g. Li et al., 2013; Ramamurti, 2001; Wang et al., 2012; Frynas et al., 2006) have shown the important roles of the firm's political resources on its overseas investment, it is still unclear whether and how the political resources enhance the effect of the firm's OFDI on its performance. Previous studies (Hadjikhani et al., 2008; Sun et al., 2010) that explore the consequential aspects of the political support of MNEs tend to focus on the political resources that the subsidiaries established with the host-government and the subsidiary's performance. We yet do not understand clearly if the political connections the firms created in the home country help the OFDI of the firms enhance its performance. In the next section, the discussion of two main theories that have been widely applied to explain the internationalisations of EMNEs and CPS will be provided, and these theories will be applied to form the research framework of this study in the last section of this chapter, together with the hypothesis development that we will discuss in Chapter 4 and 5.

## **2.2 Theoretical Foundation**

To understand the role of political connections and FDI on firm performance, the conceptual framework of this thesis relies on two main theories, RDT and institutional theory. RDT has been used to understand the linkages between firms and external actors, in both business and politics, to manage external uncertainty. RDT highlights benefits and mechanisms that explain the impact of political connections on firm performance. Institution theory has been integrated as another theoretical perspective to explain OFDI, particularly by EMNEs (Buckley et al., 2007; Dunning and Lundan, 2008). With the focus of this thesis on political connections and OFDI, the application of institutional theory can help us link firm-level and institutional level factors in this research phenomena to understand the role of political connections and OFDI on firm performance. This section explains details of RDT and institutional theory regarding the OFDI and political connections.

### **2.2.1 Resource Dependence Theory**

Studies in CPS have explained the mechanisms of CPS and its consequences to firm performance based on five different theories consisting of resource based view (RBV), RDT, social capital, agency theory, and institutional theory (Rajwani and

Liedong, 2015). While both RBV and RDT focus on value of a firm's resources that help the firms gain competitive advantages, sources of resources in these two theories are different. RBV highlights more on internal resources that firms can create by themselves whereas RDT concentrates more on resources that firms create based on their relationship with external organizations. Social capital theory is implicitly utilised in many previous studies in CPS (Rajwani and Liedong, 2015) to illustrate the benefits of political actors provided to the firms. Agency theory is also applied to explain the firm's relationships with the government in the form of agent-principle where political actors act as agent for the firms to coordinate with other organisations for the firm's benefits (Mitnick, 1993). Regarding the focus of this thesis on the political resources that firms make through the connections with political actors, the application of RDT is more relevant than RBV or agency theory. Social capital, as used in previous studies in CPS (Hillman and Dalziel, 2003; Lester et al., 2008), is considered to understand social capital possession by political actors as part of benefits they can contribute to the connected firms. However, social capital theory is not the main theory applied to explain the research phenomena in this thesis as, compared to RDT, it does not highlight the element of managing external uncertainty which is an important part in the understanding of business-government relationships.

RDT, introduced by Pfeffer and Salancik (1978) has been influential in the organisation and strategic management research (Hillman et al., 2009). The main argument of RDT is that organisations deal with the external uncertainty by creating a linkage between the organisation and the critical external organisations that can provide crucial resources to help them manage existing environment or create a new preferable environment (Pfeffer and Salancik, 1978).

Originated from power dependence theory (Emerson, 1962), the dependence of resources between two organisations occurs when exchanged resources are critical and less available from alternative sources (Casciaro and Piskorski, 2005). By the exchanging of resources through the linkages, both involved organisations are interdependent, which means that each organisation "does not entirely control all of the conditions necessary for the achievement of an action or for obtaining the outcome desired from the action" (Pfeffer and Salancik, 2003, p.40). Based on Pfeffer and Salancik (1978), the interdependence between two parties is a necessary condition

that helps each organisation to manage external uncertainty without losing its autonomy, which is the critical factor that can determine the firm's performance (Drees and Heugens, 2013).

In consideration of a firm's political connections, the government or public organisations can provide both critical and rare resources to the firms, as well as that they can create uncertainty for the firms through new regulations and public policies; this explains why RDT is utilised to understand the effects of the firm's political strategies in previous research (e.g. Hillman, 2005; Dieleman and Boddeyn, 2012). Firms can engage with government or public organisations, based on RDT, through two main mechanisms. The first mechanism is proactive utilising of corporate political activities such as lobbying or political campaigns to directly influence public policies (Baysinger, 1984; Getz, 1993) and the second is co-optation with external agencies by appointing current or former political actors on the board of directors (Hillman and Hitt, 1999).

Political activity is suggested as one of the approaches that firms can utilise to create the linkages with the external organisations (Baysinger, 1984; Pfeffer and Salancik, 1978). The political mechanism is used to manipulate the environment or create the new preferable environment (Pfeffer and Salancik, 1978). Firms attempt to engage with the government, which is a crucial external organisation because, as a policy maker and regulator, a government can issue unpleasant policies that bring uncertainty to firms (Hillman and Hitt, 1999). Firms can engage with political activities in many forms. One of them is a personal service that occurs when a firm's leader is serving in government officials posts (Getz, 1993), or a firm hires a politically experienced individual as a manager or a director of the firms (Hillman and Hitt, 1999).

The appointment of political actors on a corporate board can be explained by RDT in the form of co-optation applied by the firms to cooperate with the external sources. Co-optation is described as:

A situation in which a person, or set of persons, is appointed to a board of directors, advisory committee, policy making or influencing group,

or some other organizational body that has at least the appearance of making or influencing decisions (Pfeffer and Salancik, 1978, p.162).

Co-optation has been explained in previous studies on the board of directors in the form of board interlocks and the role of outside directors (e.g. Lester et al., 2008; Agrawal and Knoeber, 2001). When firms appoint individuals on the board, they can expect that elected directors will provide not only the monitoring roles, as suggested in agency theory, but also managerial expertise, and supports for firms (Pfeffer and Salancik, 1978). By using RDT to understand the roles of the board of directors, it can explain a complete picture concerning the resource provided by the board of directors (Hillman et al., 2000). The study regarding the board of directors, therefore, should focus on resourceful types of directors (Boyd, 1990) by considering the resource providing roles of the board which can be categorised as business experts, support specialists, and community influential (Hillman et al., 2000). Political leaders are considered as part of the community influential directors based on these three categories. The benefits that firms can obtain from the political directors is explained in the next section.

### **2.2.1.1 Benefits of Linkages**

Dealing with external organizations through appointing critical individual, such as political actors, on the board of directors can create four main benefits for the firms, which are information regarding new policy or regulations, channels of communication of the firms' information to the government, government supports, and a certain level of legitimacy (Hillman, 2005; Pfeffer and Salancik, 1978). The former two benefits deal with the information in opposite directions. Both receiving and communicating information can occur on a regular basis and within the legitimate contact in the board meeting when firms appoint external individuals on the board (Hillman and Dalziel, 2003). Specifically in the case that firms appoint current or former politicians or government officials to the board, apart from insights and knowledge that experienced politicians or government officials can provide to the firms (Hillman, 2005), firms can get information related to the government's activities or government regulations that might be related to the firms (Agrawal and Knoeber, 2001). Although in many cases firms can only appoint former politicians or government officials to the board, they still can receive and communicate information

through the networks of those politically related directors. Through the networks of politically related directors, firms can access a variety of sources of information. Although a politician or an official who has a higher position can connect with many sources of information, information does not always come from those who held a higher position. Number and strength of connections are also important. While the number of connections provides a higher possibility that firms can access information, stronger ties (that are based on trust) can provide the firms with significant information.

The third type of benefits firms can receive from appointing resourceful individuals on the board is support from appointed individuals. Pfeffer and Salancik (1978) suggested that, by appointing outside directors to the board, firms expect that the appointed directors will concern themselves with the organisation's problems, favourable organisations to others, and try to aid organisations when they face difficulties. The support that firms may gain from appointed directors can be in many forms. In the case of politically related directors, firms may expect supports based on credibility derived from the reputation of those politically experienced directors. Credibility of directors can support firms especially when firms have problems, such as financial issues, and need to deal with the external organisation. Previous research on political connections shows that politically connected firms, which appointed politicians to the board or/and major shareholders are politicians, are more likely to be bailed out compared to non-politically connected firms (Faccio et al., 2006). Thus, firms with higher tendency to need more credibility require a politically experienced director who once had a higher political position, or had a well-accepted reputation.

The fourth type of benefits from linkages through co-optation is a particular value of legitimacy because the prestigious individuals who are appointed to the board can confirm the value of the firms to other people outside the organisations (Pfeffer and Salancik, 1978). Legitimacy is defined following Suchman (1995, p.574) as:

A generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions.



As a society evaluates the value and legitimacy based on organisation's activities, organisations need to maintain an association with external organisations that provide resources and support for firms to continue their business activities (Pfeffer and Salancik, 1978). Organizations can become legitimate in three ways, which are adjusting its output, goals, and methods of operation to conform to dominant definitions of legitimacy; trying to change the definition of social legitimacy, so they can adjust to organization's value; and attempting to be identified with symbols, values, or institutions that have a strong base of social legitimacy (Dowling and Pfeffer, 1975).

The organizational legitimacy is necessary not only at the domestic level but also important when firms invest overseas because businesses cannot become legitimate by conforming to varieties of institutions of host countries, so they need to use alternative legitimating mechanisms by interaction, communication, and exchange to create a perception of the firms (Kostova et al., 2008). However, the linkages between firms and home-country government may not fully legitimise the connected firms in foreign countries, as in case of SOEs that receive institutional pressures from the host country, which ultimately limit the strategic choices of the firms in foreign countries (Cui and Jiang, 2012; Meyer et al., 2014).

#### **2.2.1.2 Debates of RDT**

The expectation that appointed individuals will only benefit firms through information and supports is challenging as appointed individuals may seek for personal interests, or interests of their home organisations, or enforce some other insignificant agenda for the firms (Westphal et al., 2006). In case of politically related directors, political actors may prioritise benefits of society, their home organisations, or their personal interests higher than benefits of firms (Shleifer and Vishny, 1994; Sun et al., 2012), so they may not give information and advice to firms, or support firms as much as firms expect. While firms are likely to appoint directors who have higher political positions or well-accepted reputations to the board (Lester et al., 2008), these politically related directors may not yield positive outcomes as they also need to retain their public interests and personal reputation. Therefore, even though firms can get support from external individuals, the objectives of firms may be diverted when

appointing external individuals on the board, leading to the declining of autonomy of the firms (Dooley, 1969).

Pfeffer and Salancik (1978) address the argument of the loss of autonomy by explaining that mutual interdependence is designed to impose simultaneous constraints in order to create stable and confident environment for both organizations. The idea of interdependence is, however, criticised that it mixes two opposite concepts of power imbalance and mutual dependence (Casciaro and Piskorski, 2005). Drawing from the power-dependence theory that discussed the interplay between the concepts of 'power' and 'dependence' (Emerson, 1962), Casciaro and Piskorski (2005) identifies power imbalance as the difference of power between two organisations, whereas mutual dependence is the sum of their dependencies. The separation between these two constructs is necessary to understand how linkages between two organisations can lead to its expected outcome because the organisations may not be able to control resources and manage uncertainty as expected if one of them has much power over the other, while both parties can benefit from their linkages if they both get mutual dependencies. The key factors to determine the degree of power and dependence, based on RDT, are the criticality and availability of resources possessed by each organisation as they can define the degree of dependence between two organisations (Casciaro and Piskorski, 2005; Pfeffer and Salancik, 1978). Hence, managing the criticality and availability of resources that the firms can access through their linkages can help them gain more autonomy, which in turn helps them reduce the cost that may occur from the dependency.

This thesis aims to extend the argument made by RDT on the benefits of linkages that occur through the appointment of political actors to the board of directors, without disregarding the potential disadvantages that may occur from the loss of autonomy when the assumption of interdependency does not hold. While we develop our argument based on the benefits of linkages following RDT, the consideration of different types and positions of political actors addressed in this thesis gives room for the alternative explanation that allow us to further the RDT argument.

### **2.2.2 Institutional Theory**

Institutions are defined by North (1990, p.3) as “the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction”. Institutions can be both formal such as rules or regulations and informal such as social norms or the conventional behaviours in society (North, 1990). As the “rules of the game” (North, 1990), institutions construct political, economic, and social relationships in society (Chan et al., 2010). By taking institutional perspectives, socially constructed factors such as norms, customs, or habits are also considered to influence the decisional choices (Oliver, 1997) of the firms. The institutional environment therefore includes political institution, economic institutions, and socio-cultural factors (Mudambi and Navarra, 2002). Although it is often recognised as the rules in a society, institutions also include a player of the game in a society such as government agencies, legislatures, courts, or industrial organisations (Aoki, 2001; Nelson, 1994). So, political actors can play two parts in a society, a player of the game and a rule maker.

Institutions can be both constraints and resources for problem-solving of economic coordination through non-economic institutions (Jackson and Deeg, 2008) and can influence the strategic development of firms’ specific resources and strategies (Wan, 2005). Home country institutions affect the actions and competitiveness of firms by shaping firm strategies, operational practices and local perceptions of firms (Chacar et al., 2010; Mezias, 2002). Previous research show that strong home country institutions will generate firm capabilities that firms can leverage when investing abroad (Chacar et al., 2010) in many aspects, for example, the familiarity to deal with legal system to protect property rights (Wan and Hoskisson, 2003; Hoskisson et al., 2005), the guidance for firms to compete successfully in international markets (Chacar et al., 2010), and the access to potential executive and employee (Wan and Hillman, 2006; Brouthers et al., 2005). Therefore, home country institutions can shape firm strategies that link to firm competitiveness and may lead to firm performance. Institutions can affect firm performance through two types of production cost of the firms which are transformation costs, the cost of production and processing, and transaction costs (Yasar et al., 2011). However, the transaction costs such as the costs of establishing, monitoring, and enforcing contracts, the cost of searching business

partners, and the cost of negotiation are likely to be more influenced by institutional factors (Aron, 2000). In the society where institutions are well established, institutions will help decrease uncertainty, which will then reduce transaction cost (North, 1990).

The perspective of institutions is included in institutional economics which was firstly introduced to explain the economic activities as parts of political and social system (Hamilton, 1919). Instead of considering economic activities as independent factors, institutional economics concerns the social context that those economic activities are embedded in. The motives of human behaviours in the institutional perspective go beyond economic optimisation to social justification and social obligation (Zukin and DiMaggio, 1990). The institutional economics is the root for the later new institutional economics, firstly introduced to use transaction cost in economic analysis (Coase, 1998; Williamson, 1979). In new institutional economics, factors that can constrain choices of economic decision include both factors typically addressed in neoclassic economics, such as technology, information, or income, and socially constructed factors, such as norms, customs, or habits (Oliver, 1997). As integrating both neoclassic economics and institutional economics, new institutional economics therefore concerns both social context and the choice of decision based on the scarcity of resource and competition among economic players. We apply this new institutional economics to discuss the role of institutional factors in influencing the value of firm's political connections and OFDI in the host countries in this thesis.

Although an organisation is often perceived as a passive organisation that needs to react to the rules given by institutions (North, 1990), through the perspective of new institutional economics, organizations can react to institutional pressures through three mechanisms which are coercive, mimetic, and normative isomorphism (DiMaggio and Powell, 1983). Coercive isomorphism derives from formal and informal pressures such as political influence and the problem of legitimacy; mimetic isomorphism stems from standard response to uncertainty; and normative isomorphism is related to professionalisation. The changes that organisations have done in response to institutional pressures make organisations more homogeneous in structure, process, and behaviour (DiMaggio and Powell, 1983).

### **2.2.2.1 Institutions and Emerging-Market Firms**

In emerging economies, institutional development is relatively low, largely because institutional rules are absent, insufficient, or poorly enforced (Hoskisson et al., 2000; Khanna and Palepu, 1997; Peng and Heath, 1996; Hitt et al., 2004). A lack of reliable market information, efficient intermediary institutions, predictable government actions, and an efficient bureaucracy creates institutional voids (Khanna and Palepu, 1997), which increase transaction cost in emerging markets (Hoskisson et al., 2013). Transaction cost are raised because underdeveloped institutions come with a higher risk of unenforceable contracts and insecure property rights, which lead firms to adopt inferior technology and thus operate less efficiently and competitively (North, 1990). Weak institutions are seen as causes of problems in factor markets that can increase transaction costs of firms (Hoskisson et al., 2000; Khanna and Palepu, 1997). Weak institutions in emerging markets are also seen as factors that decrease the competitive pressure as it is argued that collusion is easier in emerging economies (Wright et al., 2005) because of less well-developed antitrust regulation and greater industry concentration (Chacar and Vissa, 2005). Moreover, weak institutions generate more imperfect market conditions that unequally affect firms. Imperfect markets in emerging markets create gaps that allow firms to exploit from institutional voids (Khanna and Palepu, 2000). To fill those institutional voids, emerging-market firms need to create their firm specific advantages that can deal with underdeveloped institutions such as business group (Khanna and Palepu, 2000).

Previous studies have explained OFDI by EMNEs in developing countries compared to developed countries from the perspectives of institutional theory (e.g. Peng et al., 2008; Wright et al., 2005). The home-country institutional environment can encourage the firms' OFDI when it is not aligned with the needs of firms (Witt and Lewin, 2007). Firms can react to misalignment of home-country institutional factors and their needs in various alternative ways. Two opposite ends of these alternatives are compliance with misalignment and escape from the misaligned institutions via OFDI (Witt and Lewin, 2007). The compromised ways to react on the misaligned institutions are by reducing or eliminating misalignment by employing political actions (Witt and Lewin, 2007). An institutional structure that is aligned with the needs of the firms provides firms with the economic advantages whereas the

misalignment between institutional environment and the firms' needs can lead to economic liabilities that force firms to invest overseas through OFDI (Witt and Lewin, 2007). It is argued that while emerging-market firms have lack of knowledge-based resources such as R&D, innovation, or technology, they can utilise institutional resources such as business groups (Khanna and Palepu, 1997), or social and political networks (Peng and Luo, 2000) when they invest in its subsidiaries overseas. Weak institutional factors in emerging markets that are recognised as the firm's disadvantages can turn to be advantages for the emerging-market firms when they invest in less developed countries (Cuervo-Cazurra and Genc, 2008) because the skills and experiences they had in emerging-country enable them to deal with weak institutions in developing countries. Besides, weak institutions can be advantages in cases where EMNEs have the ability to exploit home-country institutions such as business and social networks and capital market imperfection to decrease transaction costs and increase their financial capital (Voss et al., 2010).

The underlying assumption of institutional theory that firms are likely to conform to those institutional factors because institutional factors, in general, require a long period of time to change allow us to consider institutional context that may put more pressure on firms when they utilise political strategies with less stable perspectives. Institutional theory, in particular new institutional economics, is then incorporated with RDT to explain the role of political connections in different types of host countries, which help us advance the discussion on the potential benefits of political connections suggested by RDT.

### **2.2.3 The Combination of RDT and Institutional Theory**

Both RDT and institutional theory are concerned with the relationship between organisations and the external environment. However, a firm's strategic reactions toward the external environment based on these two theories are different. Firms are more passive, conformed and acceptance based on institutional theory, but active, resistant and manipulative based on RDT (Oliver, 1991). These differences are stemmed from diverse perspectives of the external environment in the two theories. Institutional theory considers the external environment in the form of institutional factors that shape rules and belief in society (Scott, 1987) so that they are harder to change. RDT, in contrast, perceives the external environment as external

organisations which control rare resources, so external organisations for RDT are manageable (Pfeffer and Salancik, 1978).

With the dissimilarities of these two theories towards the external environment that lead to distinctive reactions by firms, the combination of these two theories will help us to understand firms' reactions when they apply political strategies without losing the perspectives of institutional constraints that are embedded in both home and host countries, and not enable firms to manage with. By using RDT to guide our understanding on how political strategies help firms manage the external uncertainty stemmed from the government, we can understand how firms manage resource flows from the government. At the same time, with the incorporation of institutional theory, we can elaborate on when institutional constraints play a role and consider whether firms are still able to manipulate or control the external environment.

## **2.3 The Moderating Effect of a Firm's Political Connections**

This section starts with the discussion of prior research exploring how internationalisation affect MNEs' performance, following by the argument of how political strategies influence the firm's performance. From these two research areas, the research framework suggesting the role of political connections as the contingent factors to determine the effect of OFDI on firm performance will be illustrated based on theoretical perspectives of institutional theory and RDT. The framework highlights the research attempts to explain the effect of political connections on OFDI and firm performance by focusing on level and type of political actors that lead to different sets of political resources with the expectation that this thesis will extend our understanding of the firm's political connections and OFDI in IB studies.

### **2.3.1 The Effect of OFDI on Firm Performance**

Firms choose to internalise business activities in foreign countries when transaction costs of foreign direct investment are lower than other investment modes (Buckley and Casson, 1985), but OFDI does not always guarantee positive returns. The benefits of OFDI to firms may come from the flexibility to select investment location and respond the local demands in host markets (Buckley and Casson, 1985), the greater bargaining power of multinational networks (Kogut, 1984), and the difference

between product and factor markets across countries (Kim et. al., 1989). However, in overseas investment, firms encounter the cost of doing business abroad, known as liabilities of foreignness, that can create disadvantages and hinder the firms in host countries (Zaheer, 1995; Hymer, 1960). With the cost of doing business overseas, foreign firms may generate lower profit than local firms and may not survive in the host country, unless firms can transfer some FSAs to exploit overseas (Zaheer, 1995).

Many previous studies (see a meta analytic review in Kirca et al., 2011) have attempted to figure out how internationalisation or multinationality is associated with firm performance. However, empirical studies on the relationship between internationalisation and performance show mixed results including linear relationship (Qian, 1998; Tallman and Li, 1996), U-curve and inverted U-curve relationships (Lu and Beamish, 2001; Hitt et al., 1994; Sullivan, 1994), and S-shape relationship (Lu and Beamish, 2004; Contractor et al., 2003; Contractor et al., 2007). Two arguments made to reason the mixed results are the size of investment firms and period of investment (Lu and Beamish, 2001; Lu and Beamish, 2004).

Using the sample of small and medium enterprises, Lu and Beamish (2001) argue that small and medium firms have to deal with the negative returns when the cost of doing business outweigh the benefits of overseas investment due to the liability of foreignness and the lack of experience in doing business overseas in the first period of foreign investment. Along this line of explanation, studies exploring longitudinal relationship also suggest three-stage relationship between internationalisation and firm's performance (Contractor et al., 2007; Contractor et al., 2003; Lu and Beamish, 2004). These studies explain the negative relationship in the first stage of investment based on the liabilities of foreignness, then at a certain level of investments, experience of MNEs in foreign investment can help them gain positive return in the second stage, and in the third stage when the MNEs invest in many foreign subsidiaries or affiliates, they confront with transactional and governance cost from its investment (Lu and Beamish, 2004; Contractor et al., 2003). Regarding firm size and period of investment, EMNEs are comparatively smaller than advanced MNEs and have less international experience (Contractor et al., 2007). EMNEs, therefore, may encounter problems and have less ability to survive in foreign countries when



they invested aggressively overseas because they have a lower margin to deal with errors compared to larger firms from developed countries (Wright et al., 2005).

The research on the relationship between multinational and performance is, however, opposed by Hennart (2007) that there is no theoretical explanation for the profitability based on internationality. He use transaction cost perspective (Hennart, 2007; Buckley and Casson, 1976) to argue that firms diversify their investment abroad because the transaction cost of activities via the market is higher than the internalisation by the firm itself. Firms invest overseas not only to seek the lowest production costs, but there are many reasons encouraging firms to invest overseas such as access to broader markets, or closeness to resources (Dunning, 2000), therefore, OFDI may be able to either generate supreme profit for firms, or create more liabilities for firms (Hennart, 2007).

With this line of argument, rather than attempting to create solid relationships between OFDI and performance, this thesis focuses more on factors that may help firms to have monopolistic advantages in the home country that can be transferred overseas and help firms create more value. These mixed empirical results lead us to explore under which condition that OFDI can enhance firm performance. The firm's political resource is the focus of this thesis because it not only facilitates firms to invest in its subsidiaries overseas, but also creates monopolistic advantages for firms, and may ultimately help them gain higher performance.

### **2.3.2 The Effect of Political Connections on Firm Performance**

As firms implement political strategies aiming for the preferences of political actors, most empirical studies have confirmed this relationship. Studies in CPS that focus on the firm's performance have found positive effects of political connections on the firm's financial, accounting, and market performance (Hillman, 2005; Faccio, 2006; Boubakri et al., 2012a; Zheng et al., 2015). The benefits that firms can get from their political ties can be in different forms. With political connections, the firms can get preferential treatments such as low-cost bank loans (Khwaja and Mian, 2005), government bailouts (Faccio et al., 2006), exemption from the capital controls (Johnson and Mitton, 2003), facilitating market entry (Agrawal and Knoeber, 2001), or obtaining government contracts (Goldman et al., 2013).

Previous studies in the area of political connections have widely discussed the consequences of the firm's political connections not only for the firm's performance but also for other aspects of the firm's operations (see the updated review in Lawton et al., 2013; Rajwani and Liedong, 2015; Mellahi et al., 2016). Some of these studies discuss the consequential factors that political actors can give to the firms (e.g. Faccio et al., 2006; Khwaja and Mian, 2005; Goldman et al., 2013; Faccio, 2010). Those factors can be seen as the mechanisms that lead political connections to firm performance. One of the main discussions in former research is on company's loans. Many studies in finance have illustrated how political connections links to financial leverages (e.g. Boubakri et al., 2012b; Khwaja and Mian, 2005; Claessens et al., 2008). Studies that have explored the effects of political connections on the ability to access loan have been aligned with the research findings that political connections can lead to better access to financial loans, especially from the government banks compared to non-connected firms (e.g. Khwaja and Mian, 2005; Bliss and Gul, 2012; Wu et al., 2013). However, the ability to access government loans has a reverse effect on the firm performance (Bliss and Gul, 2012; Duchin and Sosyura, 2012) as many studies show that the loan which the connected firms access is unlikely to lead to the firm performance due to the higher cost that comes from the less risk efficiency of the firms (Bliss and Gul, 2012; De Jonghe et al., 2012), lower quality of portfolio (Carretta et al., 2012), and lower asset quality (Liang et al., 2013). One possible reason that might explain this is firms are likely to take a higher risk in investment when they get easier financial access (Boubakri et al., 2013).

However, the links between political connections and ability to get support from government may be conditioned by other factors as shown in previous studies that politically connected firms only get government subsidy when the firm has a high managerial reputation (Wu et al., 2013) and the government may consider to give support only to companies that show strategic strength (Frye and Iwasaki, 2011). Moreover, while firms are seeking benefits from connected political actors, political actors may also appropriate rent from the connected firms (Sun et al., 2012). The relationship between firms and political actors can be a negotiating game between two parties that possess strong bargaining power (Shleifer and Vishny, 1994); one in the form of money, another in the form of scarce and valuable resources such as

information and political power to control over regulations and policies. Political actors also have negotiating power that may ultimately result in a firm's negative outcomes. The firm's political strategies can then hinder the firms' performance because the costs stemmed from the rent extracted by politicians may offset their ability to generate private rents (Shleifer and Vishny, 1994), as well as that the government-related firms may also need to accommodate social needs and concerns (Ramamurti, 2001).

Similarly, in the case of co-optation, those political actors that are appointed as directors may seek their own interests, or interests of their home organisations, or enforce some other insignificant agenda for the firms (Westphal et al., 2006). For example, political actors can take advantages of firms by asking firms to hire their relatives (Li et al., 2009). Also, by appointing political actors on the board, the firm will have unprofessional managerial or board members compared to directors who have experiences in business (Fan et al., 2007). The political actors on the board therefore can divert the objectives of firms, especially if the firm is highly dependent on the political actors (Sun et al., 2016), leading to the declining of autonomy of the firms. The negative impacts of political connections can also occur through other mechanisms; for example, CEOs of politically connected firms may have incentives to pursue social objectives at the firm's expense (Fan et al., 2007); political connections with a certain government can turn into liabilities for the firms when a new political party is elected to power (Siegel, 2007).

With inconclusive theoretical and empirical debates, understanding the value of a firm's political connections on firm performance requires the consideration of various conditions that may create a different impact on the firm's value. Studies in this area therefore need to focus more on the contingent value of the firm's political connections (Sun et al., 2012). Early research on the effect of CPS on the firm's performance mainly focuses on the contingent effect of the industry as it is suggested that a regulated industry may have higher political connections than an unregulated industry (Holburn and Vanden Bergh, 2004). The effects of political connections on the firm's performance is also reported to have different impacts between regulated and non-regulated firms in which the regulated firms have higher positive effects than

non-regulated firms (Hillman, 2005) or only regulated firms have positive effects while non-regulated firms have negative impacts (Hadani and Schuler, 2013).

The value of the firm's political connections can depend on institutional context. Previous research finds that the firm's connections with government officials in China influence the firm's value more than ties with managers of other firms (Peng and Luo, 2000). However, when a later study (Sheng et al., 2011) integrates the institutional factors for consideration, they find that the political ties only outperform business ties when the firms operate in the institutions that provide weak government supports or within the low-technology instability environment.

Apart from the industrial and institutional factors, recent research has tried to consider other perspectives/factors that may affect the outcome of the firm's political connections. Studies in this area have recently started to compare the different outcomes that the firms gain from different kind of political organisations or political actors (Okhmatovskiy, 2010; Zheng et al., 2017; Zheng et al., 2015). The different effects based on the different types of the firm's political connections can be explained from the perspective of the different degrees of access to resources based on the levels of the government consisting of state, national, and local government (Zheng et al., 2015) or the degrees of political embeddedness based on a direct or an indirect relationship between the firms and the government (Sun et al., 2015; Okhmatovskiy, 2010).

Building on these two areas of research in IB and CPS that focus on the effect of the MNE's internationality and corporate political connections on firm performance, we develop our research framework that highlights the moderating role of political connections on the effect of OFDI on firm performance. In the next section, we discuss three research focuses incorporated to develop our research framework.

### **2.3.3 The Research Framework**

The research frameworks are built on the three focuses of the research, which are performance effect of home-country political connections, the contingent value of level and types of political actors, and the effect of investment location.

### **2.3.3.1 Performance Implications of Home-Country Political Connections**

As discussed earlier that most previous studies (e.g. Wang et al., 2012; Li et al., 2013) in MNE's political strategies have concentrated on the explanation of how political connections influence OFDI, the lack of performance implications of CPS for MNEs (Rajwani and Liedong, 2015) is, therefore, a promising research area to be investigated. That being said, it does not mean that no research has attempted to figure out the performance of MNEs' political strategies. Previous research focusing on the performance of MNEs' political behaviours tend to look at the subsidiaries' political connections and their performance (Hillman and Wan, 2005; Hadjikhani et al., 2008) rather than political connections that the parent firms established in the home country. It might be argued that host country political actors are more relevant to the MNEs because they control regulations and are able to create more uncertainties for the firms' subsidiaries in host countries. While this might be true, the connections that the subsidiaries created in the host countries and their effects on firm's subsidiaries do not explain whether home-country political connections that firms establish in the home country can be perceived as the ownership advantage that firms can transfer and leverage overseas. This research, therefore, focuses on the role of home-country political connections that EMNEs rely on in the home country in order to figure out if these political affiliates that assist them in their overseas investment can help them gain higher performance.

The first question one might ask is why home-country governments need to bother with the firm's OFDI activities when most of the benefits that MNEs have abroad may not return to its home country as much as the advantages that the government can earn from supporting home-bound investment. Despite recent arguments supporting the idea that OFDI can create knowledge from overseas investment and transfer back to the home country (Luo et al., 2010), the government may not directly support firms to invest overseas if the firms are not owned by government. In the extreme case if we assume that the home government does not have positive benefits based on OFDI by private firms and therefore opposes the OFDI by private firms through its regulations such as capital control, the home-country government will be more relevant to the firms. This makes the connections with the home-country government, or political actors more important because it controls

regulations of OFDI that may obstruct the firms from going overseas. The benefits such as information or support that firms can gain from its home-country connections are therefore more useful for the firms as firms are allowed to take monopolistic rent from the connections.

The reality, however, appears that home government in emerging markets are supportive to the firm's OFDI (Luo et al., 2010; Li et al., 2013). The home government is not only supportive for EMNEs, previous studies also discuss the role of home government in negotiating and bargaining with the host government in helping advanced MNEs (Ramamurti, 2001; Fagre and Wells, 1982). The firm's affiliation with home government is also shown in previous studies that can influence OFDI (Wang et al., 2012). The question, however, is whether the political connections that help the firms invest in its subsidiaries overseas can help the firms gain higher performance.

The home-country government is the first point that can generate conditions for firms in its overseas investment through investment policies and regulations. It can provide firms the access to socio-political networks in the host country and privileged information about the host country that is known among political actors. For this reason, rather than expecting direct support from the government itself, firms can create connections with political actors to gain direct benefits from the government. Without distinct government support for OFDI, firms then need to put more efforts into finding information or seeking help when they operate overseas. The dependency in the forms of informal connections with government is therefore important for firms to gain insight and support. Political connections can affect EMNEs' performance after their OFDI in several possibilities. We discuss these in the hypothesis development in Chapters 4 and 5 together with the research framework.

### **2.3.3.2 The Contingent Value of Political Actors: Level, Type, and Resources**

One of the focus of this thesis is the different roles of political actors based on their different political positions. While former work that explores the firm's involvement with government often refer to SOEs or the government officials at the top-executive levels, we cannot deny that other political actors such as administrative officials also have access to government information, and engage in specific tasks that may relevant to the OFDI activities more than some top officials. To deal with both formal and

informal institutions, firms do not deal with an organisation itself; rather they do it through relevant individuals. The consideration of political connections from the perspective of social capital of the political actors therefore leads to our understanding of the role of political connections as a more complete picture.

Often when mentioning political connections, most studies refer to politicians who hold high position at the executive level as we always assume that they have more power, and better access to resources. Previous studies in CPS (Faccio, 2006; Hillman, 2005) are concerned with only whether the firms are connected or focused on the size of connections that the firms possess without considering the fine-grained types of political actors. The underlying assumption of these studies that focus only on political connections the firms have with high-level government officials or politicians is that top-level government officials are close to the centre of political power and can have control over the policies and regulations as well as the government budgets. It also assumes that all politicians (that is included in the definition) equally generate resource to the firms. While it cannot be denied that top-level officers have control over policy decisions and have access to most relevant government information, the assumptions made by previous work (e.g Faccio, 2006; Hillman, 2005) are challenging because it is not only top executive levels of political actors who can provide firms with access to government information, the communication channels, or to give firms some support.

Government consists of many public organisations and agencies including regulatory or administrative agencies whose works/duties involve detailed information and involve other private sectors such as firms and communities (De Figueiredo, 2009). These bureaucrats, while they have a lower hierarchical position, they are close to valuable information. It is suggested that CPS should include other types of political actors especially regulatory agencies (Holburn and Vanden Bergh, 2004; De Figueiredo and De Figueiredo, 2002). These administrative officials in regulatory agencies are required to contact the private sectors including firms to gain practical information (De Figueiredo, 2009). By all means, information is the most important instrument that firms can use to influence policy makers because it is legal and in many cases government officials also need information from a practical perspectives (De Figueiredo, 2009). These regulators or bureaucrats typically have

relatively permanent position in government compared to the top-executive political actors whose position changes accordingly with the ruling government party.

High-level politicians, in contrast, while may have more political power, may not have opportunities to communicate or share the information with firms as well as that they may be responsible for the bigger picture with less detailed information compared to those government officials that have lower power but are involved with more rich information. Moreover, higher power of politicians comes with more hidden cost. Firms that rely more on high-level political actors may have less autonomy because those high-level politicians may have higher bargaining power than the firms.

In addition, in the particular activities such as the firm's OFDI, not all types of political actors are beneficial to the firms. A study that can highlight the different types of political resources that are valuable to the firms' OFDI and its performance will give more insight into the discussion in this area of research. This thesis, therefore, proposes a research framework that investigates the different role of political actors from different levels and types of political positions in an attempt to examine which kind of political actors benefit firm performance in the context of overseas investment.

Based on RDT perspectives, we suggest taking a closer look at the types of political actors based on their political positions. The government itself consists of many organisations and individuals who possess different kinds of resources. These resources are relevant and accessible to the firms in different level and in turn lead to different outcomes (Zheng et al., 2017). To consider the position of political actors, we integrate the lenses of human and social capital that connected political actors can provide to the firms. Human capital refers to skills, experiences, expertise, and knowledge, whereas social capital refers to prestige and connections with other firms (Withers et al., 2012). Hillman and Dalziel (2003) combined these two constructs into 'board capital', and suggested that board capital can lead to the provision of resources to the firms, which in turns leads to the firm's performance. Studies in the board selection show that the different degree of depth and breadth of social capital of an individual made them attractive to the firms to appoint on the board of directors in different degrees (Lester et al., 2008). Hence, we suggest that the different degrees of



human and social capital possessed by the connected political actors based on their political positions can lead to the different degrees of resources that they can provide to the connected firms, and ultimately lead to different levels of the firm performance.

We consider the hierarchical level and different types of political actors based on government functions in the first research framework (which will be discussed in Chapter 4) to figure out if the position and function of political actors is relevant and helpful for a firm's performance. In the second research framework (presented in Chapter 5), we then focus more on particular types of political resources that are relevant to OFDI and may be useful for firms to manage uncertainty in both the home and host country. Three types of government officials are included. First, we consider the role of political actors who have experience in government banks in our model as they may lead firms to government financial supports. Second, political actors whose positions are related to foreign investment regulating and supporting agencies are included in our model as they can both help firms to reduce uncertainty derived from home-country government/regulators as well as give some support to firms regarding the host country. Third, we consider political actors who have experiences in foreign affairs, such as diplomats or ambassadors, to influence the firm's OFDI and performance as they may give firms some support particularly related to foreign countries, such as information about host countries or social networks in the host country. We discuss details of each type of political actors in the hypothesis development together with Research Frameworks 1 and 2 in Chapters 4 and 5 respectively.

### **2.3.3.3 The Effect of Investment Location**

When considering the overseas investment of MNEs, we cannot ignore the important influences of investment location. The role of the host country is often seen as both the determinant factors guiding firms to make their investment decision and helping firms to gain higher performance. Therefore, the differences of host countries between developed countries and emerging countries should be considered in the study of institutional and resource effects on MNEs' performance. Emerging home country institutions may impact the performance of EMNEs better when they invest in emerging markets as suggested by former research that EMNEs can have a similar experience to deal with institutional voids in emerging host countries (Cuervo-

Cazurra and Genc, 2008; Holburn and Zelner, 2010). At the same time, resources of EMNEs may also influence firm performance differently when they invest in developed country compared with emerging countries.

Previous research suggests that strategies of MNEs are shaped by the nature and interactions between home and host country institutions (Moore et al., 2010; Sorge, 2005). It has also frequently been argued that the greater the institutional distance between the home and host countries, the more difficult it will be for a firm to establish operations in a host country successfully (Kostova and Zaheer, 1999; Kostova and Roth, 2002; Xu and Shenkar, 2002). However, weak institutions in emerging markets can also turn to be an advantage for emerging-market firms when they invest its subsidiaries or affiliates in other developing countries (Cuervo-Cazurra and Genc, 2008) because emerging-market firms are more familiar and more able to develop skills to deal with similar weak institutions in host developing countries, that mean emerging-market firms can expand their operations in higher policy risk countries (Cuervo-Cazurra and Genc, 2008; Holburn and Zelner, 2010). In contrast, emerging-market firms that invest its subsidiaries in developed markets may not be able to leverage these institutional-based advantages in more developed countries due to the lack of incentive compared to their former home emerging-markets and the need to deal with the unfamiliar institutional system in developed countries (Wright et al., 2005). Moreover, emerging-market firms are likely to invest in advanced countries for developing new resource and capabilities (Hoskisson et al., 2004); hence, the objectives of their investment is for long-term perspectives in the form of potential absorptive capacity (Zahra and George, 2002), rather than the firm's short-term profitability.

Based on institutional theory, the interaction between home-country political connections of firms grounded in home-country institutions are discussed against host-country institutions. The comparison of host-developed countries and host-developing countries are applied to represent the well-developed institutional environment and less-developed institutions in Research Framework 2 (presented in Chapter 5).

Building on these three areas of research focus, the main conceptual framework presented here is that home-country political connections can influence

the roles of OFDI on the firm's performance, but the effects are varied based on types and level of political actors, types of political resources provided by different types of political actors, and host-country institutions. This conceptual framework is distinguished into two research frameworks highlighting different sets of types of political actors. The first research framework develops mainly on RDT to highlights the benefits of political connections based on types and level of political actors. The second research framework integrates RDT and institutional theory to understand the specific roles of political resources related to OFDI and the effects of investment destinations.

By developing the research framework focusing on the moderating effect of the firm's political connections in influencing the role of OFDI on firm performance, we can extend our understanding of the business and government relationships in IB research, particularly, the role of the home-country government in helping the EMNEs to increase firm performance based on OFDI. Considering that previous studies in IB (Wang et al., 2012; Luo et al., 2010) only explain how the firm's relationship with the home government can help the firm's internationalisation, especially OFDI, the research framework focusing on the moderating role of the home-country political connections in influencing OFDI and firm performance will extend this research area in IB by explaining the consequence value of the home-country political connections in enhancing the OFDI value of the EMNEs. In addition, by focusing on the different types of the firm's political actors, we can provide discussion on the contingent value of the firm's political connections. The focus on the level and type of political actors in this research can provide an explanation that can extend our understanding on the inconclusive role of the firm's political connections on firm performance (Sun et al., 2012).

The details of each research framework and the development of hypotheses will be explained together with the results and discussion in Chapters 4 and 5.

## **2.4 Chapter Summary**

This chapter gives the background of research that links political connections with OFDI by highlighting the concepts, theories and relevant empirical studies to build

the conceptual research framework. Previous literature (Wang et al., 2012; Li et al., 2013) has shown that political affiliates with home-country political actors can influence the firm's internationalisation, particularly OFDI, but we have not had a clear understanding if the firm's political involvement can enhance the roles of OFDI on the firm's performance. This thesis therefore aims to find out by providing a research framework that focuses on connections the firm has established with different types of political actors. The argument is different level and types of political actors allow firms to leverage political resources that may be advantageous to firms in different ways. The research framework also highlights the role of institutions in the host country that may also influence the benefits of political connections in helping the firm's OFDI to generate the firm's value. The next chapter will provide information on the research methodology designed to test this research framework.

## **Chapter 3**

### **Research Methodology**

To test the interaction effect of political connections and OFDI on firm performance, this research is conducted by using the quantitative research method based on a set of sample and an analytical technique. This chapter describes the research design and the operationalisation of the research. The first part of the chapter discusses details of the research design covering research philosophy, research approach, research method, and the unit of analysis. The second section explains data and the sample applied to test the research framework. The third part portrays the measurement of variables. The fourth section deals with the method of estimation.

#### **3.1 Research Design**

This section briefly discusses the research design applied to test the research framework. It starts from the philosophical stance applied in conducting the research, followed by an explanation of the research method, and the unit of analysis.

##### **3.1.1 Research Philosophy and Method**

This research is conducted from a positivist perspective. Positivism epistemology values the observable experiences as sources of knowledge (Benton and Craib, 2011). Within the positivism paradigm, the research phenomenon is perceived as objective, rather than subjective, hence the research phenomenon is assumed as external to the researcher. The researcher is therefore only an observer of the research phenomenon (Cohen et al., 2007). Positivism suits this research the most because the objectives of research require the observation of a relationship pattern between dependent and independent variables. By asking how the firm's political connections influence the OFDI to affect firm performance, the pattern of the relationship between three variables can be observed based on the existing firms' data. Because the researcher neither affects nor is affected by the research subject, the application of positivism epistemology therefore creates value-free knowledge (Benton and Craib, 2011).

Regarding the underlying positivism epistemology and the research objectives, this thesis applies a deductive approach to test the hypotheses derived from existing theories. Deduction suits this research that aims to test and extend existing theory, rather than creating completely new knowledge. By applying a deductive research approach to test existing theory, this thesis uses quantitative research methods in both data collection and data analysis. This study is explanatory research as it attempts to establish causal relationships (Saunders et al., 2009) and to explain how political connections interact with OFDI to affect firm performance.

### **3.1.2 Unit of Analysis**

This section explains three aspects regarding the unit of analysis, which are social unit, space, and time (Hakim, 2000). We explain why firm-level analysis of a cross sectional data from Thailand is selected in our research design.

#### **3.1.2.1 Firm-Level Analysis**

As the research objectives of this thesis aim to test the relationship between the firm's political connections that influence OFDI to affect firm performance, firm-level analysis suits this objectives. Firm-level analysis allows us to evaluate the heterogeneous value of political connections that are created and owned by a firm in form of a firm specific advantage on the firm-level OFDI and performance. Firm level is mostly applied to research political connections in previous work (e.g. Hillman, 2005; Zheng et al., 2015), although country-level analysis can also be used (e.g. Faccio, 2006; Chen et al., 2010). Country-level analysis, while is useful for a comparison of impacts of political connections between different countries within a certain time frame, is restricted with less detailed information of political connections. Our objective to evaluate the fine-grained type of political actors is therefore not met with this limitation of country-level analysis.

#### **3.1.2.2 Thailand as a Research Context**

To investigate the role of political connections, we chose to sample from one country, rather than multiple countries, for the ease of the comparison of political positions. As the role of government toward the globalisation and IB is likely to vary between countries according to different factors, such as institutional frameworks, stages of development, and degree of openness (Dunning, 1997b), combining samples from

different countries that have different political system may lead to discrepancy in the interpretation. By selecting one country as a research context, we can control the difference of regulations and institutions, which are important factors that can determine the effect of political connections on OFDI.

Thailand is selected as a research context for three reasons. First, OFDI from small and medium countries, Thailand in particular, is under-researched (Peng et al., 2001). Previous empirical studies that focus on EMNEs mostly relied on large economies, especially Brazil, Russia, India, and China (BRICs) (e.g. Buckley et al., 2007; Luo et al., 2010; Peng et al., 2008). Although it can be argued that EMNEs from BRICs are more active and become important sources of OFDI in the world economy (Sauvant, 2005), it cannot be denied that other developing countries are also “home to new important global businesses” (Aykut and Goldstein, 2007, p. 8). Thai firms are recently more active in OFDI. It shows in the aggregate value of OFDI stock from Thailand that it has increased from US\$ 6,666.27 million in 2006 to US\$ 85,636.54 million in 2016, accounting for 11.85 percent in a last decade (UNCTAD, 2017)<sup>1</sup>. The growing of OFDI from Thailand is partially because the new encouraging OFDI’s policies, known as the Capital Account Liberalization Master Plan, announced from the year 2012 to relax some government regulations previously used to limit overseas investment (Bank of Thailand, 2012). Also, the investment supporting agency, the Board of Investment, which has focused only on encouraging inward FDI to Thailand for a long period, has just started promoting the outflow investment from Thai firms by the establishment of the overseas investment centre for assisting the overseas investment of Thai firms at the end of the year 2012 (Board of Investment, 2015). With the early stages of active OFDI, most Thai firms may need more support from non-market factors such as government support or information that is not publicly accessible compared to the firms in countries that have long been involved with OFDI. This made political connections more relevant to the firms that invest overseas, hence Thailand fits well with the research objectives.

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<sup>1</sup> The aggregate value of OFDI flow from Thailand increases from US\$310.90 Million in 2006 to US\$13,229.21 Million in 2016, accounting for 42.38 percent (UNCTAD, 2017).

Second, most prior studies related to political connections in emerging markets tend to be sampled from former centrally-planned economies, such as China (e.g. Zheng et al., 2017) or Russia (Okhmatovskiy, 2010). Whilst the government-led countries obviously provide a good example of the firm's political connections, political connections created by firms that are embedded in centrally-planned economy may influence firms in different ways from other countries that rely more on market system. Thus, evidence from other countries that have different political background from centrally-planned economies should provide alternative evidence that help us to understand the role of political connections from different perspectives.

Third, the political context of Thailand is suitable to study political connections. Thailand, while officially a free market economy, is rooted in bureaucratic polity (Riggs, 1966) making politics in Thailand fall under the shadow of bureaucracy and military (Chambers, 2013; Ockey, 2007), especially since the recent coups in 2014 have shifted the country towards authoritarianism (Baker, 2016). Moreover, the growth of business in Thailand that was built from the connections between business groups and the government create crony capitalism (Hewison, 2005). The fact that it has free market economy means that it allows firms to seek its competitive advantages more freely compared to centrally-planned economies, we therefore can assume the existing of the political market in which firms can seek to create the political connections through market mechanism, such as hiring political actors on the board. At the same time, the characteristic of bureaucratic country (Riggs, 1966) and crony capitalism (Hewison, 2005) of Thailand accentuate the role of political actors in the business arena. The political connections in Thailand are also shown in previous research that, as of the year 2001, 34 per cent of Thai business is related to political actors (Faccio, 2006). Studies investigating the internationalisation of Thai firms also show that Thai firms rely on social networks in their internationalisation (Hemrit, 2010), especially before the Asian financial crisis in 1997, but move toward technology-building strategies after the financial crisis (Pananond, 2007).

Because of three reasons above, Thailand should give us a suitable research context for the study that focuses on political connections and OFDI as it allows us to investigate the OFDI and political connections by early stage EMNEs from a country



that was set in bureaucratic and network oriented context, yet its firms are moving toward technological oriented strategies. Also, while several specific reasons are considered to select Thai firms as the sample, the importance of the randomness of the sample that can represent firms in general for the sake of generalizability is also considered. We discussed this more in details in the sample section.

### **3.1.2.3 Cross-Sectional Analysis**

This research uses a cross-sectional analysis of listed Thai firms based on one-year data. The cross-sectional data is created to suit the research design that focuses on the fine-grained data of political actors based on the political position of each board member. Cross-sectional analysis is used in previous studies focusing on the effects of the firm's political connections on the firm's performance (Hillman, 2005).

The use of cross-sectional data, however, creates at least two limitations. First, it does not allow us to capture the changes of government regime and institutional changes. The connections that the firms created with political actors from the currently ruling political parties may not be beneficial to the connected firms when the new parties are elected. The firm's political connections can then turn to be liabilities for the connected firms (Siegel, 2007). Also, the political power of former political actors appointed on the company board can deteriorate over time (Lester et al., 2008). Second, the cross-sectional data may lead to potential endogeneity. This study therefore obtains one-year lag sales to measure the firm performance to reduce this potential problem.

## **3.2 Data and Measures**

This thesis is conducted by using secondary data to test the hypotheses. This section provides information related to the data used in this thesis. The first part deals with the data sources used to collect the firm's level data for the dataset creation. The second part describes the sample and its representation. The third part explains the measures of variables by firstly reviewing the measurement applied in previous work following by justifications of the selected measures.

### 3.2.1 Data Sources

The company data used in this thesis is obtained from two databases: the SET Market Analysis and Reporting Tool (SETSMART) and Thomson One database. SETSMART is an online database of listed companies in Thailand provided by the national stock exchange of Thailand (Stock Exchange of Thailand; henceforth, SET). The investor's version database, which can be purchased through the SET's website, provides a maximum of five years historical data of the listed companies in both two stock markets in Thailand. SETSMART database was used to access a company's reports consisting of a note to financial statement of the listed companies and the annual registration statement, known as Form 56-1 (Form 56-1), which cannot be accessed through international databases such as Thomson One.

The note to financial statement and the Form 56-1 are the main sources of OFDI and a firm's political connections. In the note to financial statement, information related to a company's investment in its subsidiaries is reported in the 'Investments in subsidiaries and associates'<sup>1</sup> section. Investment data of a company's subsidiaries generally includes registered capital, paid-up capital, costs of investment, percentage of equity share, investment destination, and business activities of the subsidiaries. This information provided in this section of the note to financial statement is the main source to construct the firm's OFDI variable.

The Form 56-1, similar to the company's annual report, contains information of the important developments of the listed company in the past year. This report, while containing information similar to the company's annual report, includes more specific information than the annual report<sup>2</sup> including the profile information of the board of directors. Two sets of information collected from this report are the board of director and shareholder structure. In the 'Profile of directors and senior managers' section of the Form 56-1, a profile of each board member is provided. It includes

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1 The section's title may be varied in each company. For example, some companies use 'Investment in subsidiaries and interests in joint venture'.

2 Some companies provide the same set of information in both reports, but this study uses the Form 56-1 for the data source as a company is required to report more detail information in this form than it does in the annual report.

information such as age, relationships with other board members in the company, the percentage of the company's equity owned by each board member, the director's degree of education and trainings, and the past experiences. The information of the director's political experiences is collected from this past experience section reported in this report to construct the different sets of variables regarding the political connections (see details in the section 3.2.3). Moreover, the information of the company's shareholders provided in the Form 56-1 is also used to construct the dummy variable of the government related firms. In addition, the Form 56-1 is also used to obtain additional information on a company's investment in its subsidiaries due to incomplete information of the investment activities provided in the note to financial statement for some companies.

Thomson One database is used to obtain a company's financial information and a company's industry identification. Financial data of the listed company includes a firm's number of employees, intangible assets, financial leverages, and firm's sales are obtained from Thomson One. However, Thomson One provides incomplete data of the number of employees, so the missing data is collected from the Form 56-1 to create more completed data for number of employees. Thomson One was used to obtain the company's financial data rather than SETSMART, which also provides some basic companies' financial information, because it provides much company's information such as the ISIC code, and is more accessible than the SETSMART database<sup>1</sup>.

Details of data collection and coding of OFDI and Political connections is explained in section 3.2.3.

### **3.2.2 Sample**

This study uses 539 listed firms in Thailand as of 2013 as a sample. These firms are listed in two stock markets in Thailand, which are the Stock Exchange of Thailand (SET) and Market for Alternative Investment (MAI). SET is the first Thai stock market operating since the year 1975; whereas, MAI, started in the year 1999, is a

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<sup>1</sup> The investor's version of the SETSMART database can be used only in 3 months after the first access.

new market targeting small and medium sized firms in Thailand. Firms listed in the MAI are therefore generally small and medium sized firms compared to the firms listed in SET. Data of 628 firms listed in both markets as of the year 2013 are firstly collected, but, after deleting all those with missing data, only 539 observations are left as the sample. The selected year 2013 is the last year before Thailand was under the military regime since the military coup occurred in May 2014.

By using data of all listed firms in both markets, our sample provides mixed types of firms from different industries, different stages of experience (age) of firms, and firms with and without OFDI. Table 3.1 presents the summary of the sample firms separated by industry, OFDI, and the firm's political connections.

**Table 3.1** Number and Percentage of Firms by Sector, OFDI, and Political Connections

Sector	Sample Firms	Firms with OFDI			Firms with Political Connections		
	Number of firms	Number of firms with OFDI	Number of firms with OFDI in developed countries	Number of firms with OFDI in developing countries	Number of political connected firms	Number of firms with high-level political actors	Number of government owned firms
Agriculture, Forestry and Fishing	0	0	0	0	0	0	0
Mining	7 (1.30%)	5 (3.18%)	4 (4.30%)	5 (3.85%)	7 (1.84%)	3 (3.09%)	2 (8%)
Construction	45 (8.35%)	11 (7.01%)	5 (5.38%)	9 (6.92%)	29 (7.63%)	10 (10.31%)	0
Manufacturing	229 (42.49%)	70 (44.59%)	44 (47.31%)	55 (42.31%)	147 (38.68%)	29 (29.90%)	6 (24%)
Transportation, Communications, Electric, Gas and Sanitary service	48 (8.91%)	16 (10.19%)	13 (13.98%)	14 (10.77%)	41 (10.79%)	14 (14.43%)	9 (36%)
Wholesale Trade	34 (6.31%)	8 (5.10%)	3 (3.23%)	6 (4.62%)	18 (4.74%)	5 (5.15%)	1 (4%)
Retail Trade	23 (4.27%)	10 (6.37%)	4 (4.30%)	8 (6.15%)	16 (4.21%)	4 (4.12%)	0
Finance, Insurance and Real Estate	79 (14.66%)	16 (10.19%)	7 (7.53%)	15 (11.54%)	69 (18.16%)	18 (18.56%)	5 (20%)
Services	72 (13.36%)	21 (13.38%)	13 (13.98%)	18 (13.85%)	51 (13.42%)	14 (14.43%)	2 (8%)
Public Administration	2 (0.37%)	0	0	0	2 (0.53%)	0	0
Total	539 (100%)	157 (100%)	93 (100%)	130 (100%)	380 (100%)	97 (100%)	25 (100%)

Note: The percentage of firms in each sector to total firms in parentheses

### **3.2.3 Variables**

This section discusses the measure of each variable by providing the justification of the selected measure and the construct of some variables.

#### **3.2.3.1 Dependent Variable: Firm Performance**

Sales is chosen to measure firm performance in this study. Previous studies focusing on the effect of political connections on performance use market-based (e.g. market value) and accounting-based measures (e.g. ROA or ROS) to measure firm performance (e.g. Hillman, 2005; Brockman et al., 2013). Studies in IB that focus on the relationships between multinationality and firm performance, however, typically use accounting-based measures to capture how the firm's internationalisation can impact the firm's profitability (e.g. Lu and Beamish, 2004; Contractor et al., 2007). We follow the IB research using accounting based measures.

Accounting based measure can measure based on a firm's revenue or a firm's profitability (Kirca et al., 2012). Revenue based measure (i.e. sales, sales growth) does not take into account the cost of operation, whereas profitability based (i.e. ROA, ROS) does. It is suggested that to select the measure for firm performance in the study related to internationalisation, the purpose of MNEs should be taken into account (Verbeke et al., 2009) because MNEs have different motives in their overseas expansion (Dunning, 2000).

We choose sales to measure firm performance, rather than profitability index in this study because OFDI by EMNEs may not yet return the firms in the form of profit, especially in the short period of the investment by early-stage EMNEs. Given the investment in overseas subsidiaries requires a large amount of fix-investment cost, firms that are in the early stage of OFDI as in case of EMNEs may still not be able to manage to profit from its OFDI. The profitability of the firms in this stage of investment is therefore volatile (Kafouros et al., 2008) and may lead to misinterpretation of how much firms can benefit from its OFDI and political connections. Sales, in contrast, capture the firm's outputs (Kafouros et al., 2008) without concerning the cost compared to profit based measure.

Moreover, considering the ultimate objective of EMNEs in OFDI that may be in various forms, EMNEs' affiliates are not always established based on profit driven.

For example, an MNE's affiliate may be established because it has resource sought by MNEs. EMNEs may establish its affiliates overseas for the purpose of developing resources and capability that can be useful for their activities in the home country. In line with this reason, we measure the performance at the EMNE's level, rather than using the subsidiary performance.

### **3.2.3.2 Independent Variable: OFDI**

As the OFDI-performance can be seen as a part of the widely researched topic on the effect of internationalisation on the firm's performance, we discuss some drawbacks of the measurement normally used in this area of research.

Previous studies focusing on the effect of internationalisation or multinationality on the firm's performance have widely discussed the measure of the degree of internationalisation or multinationality (Lu and Beamish, 2004; Lu and Beamish, 2001). Foreign sales to total sales (FSTS) is a common measure used to capture the degree of internationalisation in previous works (Capar and Kotabe, 2003; Contractor et al., 2007), but FSTS does not well represent OFDI as it also includes sales from exports. FSTS is also criticised as part of a unidimensional measure that it does not reflect the breadth and depth of internationalisation simultaneously (Hitt et al., 1997).

To address the critique of a unidimensional measure of FSTS, some studies (Lu and Beamish, 2004; Hitt et al., 2006) choose to measure multinationality using a multidimensional measure which is measured by average ratio of count number of overseas subsidiaries and number of countries in which the firms invested its subsidiaries (Lu and Beamish, 2001; Lu and Beamish, 2004). While this measure is claimed to capture breadth and depth of OFDI, the count number of subsidiaries does not represent the actual magnitude of investment value. By using this measure, a firm that invests less amount of investment value in more number of subsidiaries is considered as having more depth than another firm that invests a higher amount of investment in a fewer number of subsidiaries. This measure therefore cannot capture how much a firm is involved in its overseas investment.

Therefore, this research choose the actual OFDI value to measure OFDI following previous studies related to foreign investment (Buckley et al., 2007; Wang

et al., 2012). By using OFDI value, while it may not capture the breadth of investment based on number of countries in which firms invest, it can represent how much the firms commit to and engage with the OFDI activities. In this thesis, stock value of OFDI is used to capture the OFDI (cf. Buckley et al., 2007; Wang et al., 2012). Although the use of the stock OFDI value cannot capture the trend of investment value as OFDI flow, it suits the research design of cross sectional data.

Following prior studies on Thai OFDI (Pananond, 2013; Stock Exchange of Thailand, 2016), the OFDI value is manually collected from the company reports and constructed based on the firm's investment in affiliates since the firm-level data of OFDI value is not publicly available in Thailand. The firm is considered as having the OFDI if it reports at least 10 percent investment in a foreign firm, unless it is identified as a portfolio investment, following the OECD's definition (OECD, 2008). While FDI, by its definition, includes investment in the form of equity capital, the reinvestment of earnings and intra-company loans (OECD, 2008), we capture OFDI value only in the form of equity capital in this thesis due to the lack of data on reinvestment of earnings and intra-company loans in the firms' annual reports. According to the OECD's definition that regards FDI of the firm either directly or indirectly through its subsidiary or associate, all foreign firms that the focal firm ultimately owns at least 10 percent, unless it is identified as a portfolio investment, are included in this study no matter if it is invested by a parent company or its affiliates.

To collect the firm's OFDI data, we used two types of a company's reports, the Form 56-1 and the note to financial statement. The Form 56-1 of each company in the initial lists of all 628 publicly listed companies reported in the SETSMART database were read in order to identify if a company has OFDI investment<sup>1</sup>. From these 628 firms, 175 firms reported investment information in its foreign affiliate(s). The note to financial statement of these 175 companies was then accessed to collect the OFDI data. Two reports were used for the purpose of getting complete OFDI data

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<sup>1</sup> In 2016, SET published the report on OFDI that contains the lists of firms that have foreign revenue. While the firms included in this list can have foreign income from both OFDI and export, it can also reduce time taken to identify the OFDI activities for future research.



as each report has some limitations. The note to financial statement, while providing more details of investment value in subsidiaries and associates, does not always provide detailed information of the investment accounting for less than 20 per cent as it is not considered as the company's associates. This creates an issue concerning the 10 per cent threshold of FDI. Form 56-1, on the contrary, does not always provide value of investment in the firm's subsidiaries, or provide only the value of registered capital in some cases, so it cannot be the main source for the firm's investment value in FDI. However, the Form 56-1 often gives all the information of the firm's foreign investment even though it is less than 20 per cent investment. This explains why the Form 56-1 of all listed companies were consulted before the note to financial statement of particular companies were read.

To construct the OFDI variable, the investment value of each of the firm's subsidiaries or associates is collected and converted into US dollars, before being summed up to generate the OFDI value of the parent firm. The investment value in each foreign affiliate is collected from the 'Investment in Subsidiaries and Associates' section of the note to financial statement. In general, three types of investment were reported: the registered capital, the paid up capital, and the cost of investment. This study used either the paid-up capital or the cost of investment value, depending on the availability of data. In case that the paid-up capital is collected, the value of paid-up capital is multiplied with the percentage of equity owned by the parent company, to generate the investment value, that is equivalent to the cost of investment reported in the same section. The investment value, either the calculated paid-up capital or the cost of investment, is then converted into US dollars using the foreign exchange rate at the end of the year 2013. The foreign exchange rate used to calculate this data is based on the World Bank data (World Bank, 2016) for every currency except the Taiwanese dollar that is based on the Central Bank of the Republic of China (Taiwan) (2016) (See Appendix A). It is notable that the countries in the Appendix A are not all investment destinations as most value of the paid-up capital is already reported in US dollars and the cost of investment is normally reported in Thai baht. The investment value in US dollars of each affiliate is then summed up to create the total OFDI value of the focal firm (i.e. OFDI variable). This OFDI value is the independent variable for the research model in Chapter 4.

As this thesis is also interested in the comparison of the host-country effects, the OFDI value is therefore needed to calculate separately into different sets of the host countries. The investment destination of each affiliate is collected either from the investment section in the note to financial report or the Form 56-1 together with the OFDI value discussed earlier. The investment value of the firm in each subsidiary or associate is divided into two groups based on its host country. Following previous studies (Wang et al., 2012), this study separates host countries into two categories: developed countries and developing countries. While institutional development can be assessed from economic, political, and social dimensions (Chan et al., 2008) using different indicators to measure the quality of institutions provided in Global Competitiveness Reports by the World Economic Forum (WEF), we simply use developing and developed countries to capture less-developed and developed institutional context. The separation of developed countries and developing countries are based on the lists of advanced economies classified by the International Monetary Fund (2013) (see Appendix B). The two separated sets of OFDI value are the independent variables that are used to test the hypotheses in Chapter 5.

### **3.2.3.3 Moderating Variables: Political Connections**

Two main questions arising in the consideration of the measurement of the firm's political connections are how to identify the politically connected firm and who should be included as the political actors. As discussed earlier in Chapter 2 that the linkages of the firm and political actors can be classified broadly as political activities or political connections, the measurement of political linkages also depends on these two main distinct concepts. Studies grounded in CPA often apply specific political expenditure in formal political activities such as a campaign contribution to a political action committee (PAC)<sup>1</sup> or money the firm spent to hire the lobbyists (Hadani and Schuler, 2013; Schuler et al., 2002; Hadani et al., 2015) to measure political activities. In contrast, studies on the firm's political connections identify the firm's connections in more various ways. The connections of the firm can be identified ranging from formal relationship between firms and politicians, such as political actors as

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<sup>1</sup> In the US, firms can contribute to a political action committee (PAC) which is an organisation that pools campaign contributions from its members.

company's shareholders or board of directors (Faccio, 2006), to the informal relationships such as political ties through family members or close friends of political actors (Zhu and Chung, 2014).

Many studies on the firm's political connections follow Faccio (2006) to identify a politically connected firm when a company's shareholder or top officers is: "(a) a member of Parliament (MP), (b) a minister or the head of state, or (c) closely related to a top official" (Faccio, 2006, p.370). While these criteria capture the connections made through both shareholders and top management officers, it only includes top executive level government officials and politicians. Moreover, in terms of measurement, following an approach suggested by Faccio (2006), most studies can identify only whether a firm has political connections using a dummy variable to capture the firm's political connections. By using a dummy variable, these studies can only separate connected firms from non-connected firms, but they cannot provide more details on with whom the firm connected with. This means that a firm that is connected to the prime minister is treated equally with the firm that has connections with other politicians who may not have access to government resources. Given our objectives to explain the effect of political connections based on the resource dependence perspectives where resources can come from various types and levels of government officials, the identification of the firm's political connections based only on top executive politicians is not enough as it does not include all types of political resources that the firms can depend on the external organisations or individuals.

Considering the limitations of this widely used method of measurement and the aim of this research in identifying the effects of different types of political resources, we measure political connections based on the board of directors following Hillman (2005) and Sun et al. (2015). The use of the board of directors is also following the main argument of RDT that explains the resource dependence of the firms through co-optation of the board members. Several political activities such as lobbying, advocacy advertising, and political contribution will typically result in more collective benefits (Schuler, 1996; Hillman et al., 1999). Personal service (e.g. former government officials on the board) is therefore a better indication of firm-specific benefit from its strategy (Hillman et al., 1999). RDT scholars suggest that political

actors on the board of directors increase the tendency that firms can gain access to policy makers (Pfeffer, 1972).

MNEs need to fully internalise some political resources by ‘the recruitment of former government officials’ (Boddeyn, 1988, p.353) because only the firm’s top managers can approach non-market decision makers, negotiate for government permissions, as well as commit the organization’s resources in return. Measure of political connection based on the profile of the board of directors can also be justified from empirical studies that show that the firm has abnormal stock return following the announcement of the nomination of politically connected individuals on the board (Goldman et al., 2009). Hence, a firm’s political connection is identified based on previous experiences of board members.

To identify whether a board member has ever hold a political or government position, the profile data of each board director, provided in the ‘Profile of Directors and Senior Managers’ section in the Form 56-1, of all 628 listed firms were read. Information of each director consists of the director’s name, the position in the focal company and its subsidiaries, age, education and training, relationship with other directors, percentage share in the company, and previous experiences is collected. The individual dataset of the board director is created and later aggregated to the firm level data. Two research assistants were hired to help collect all data of the directors for 200 firms each with the guide of the collection to organise the information in the same format. All data is later revised and rechecked by the lead researcher.

After the raw individual dataset is collected, the different types of political experience of each director is identified based on the provided working experiences. In case that the information provided in the annual report is not clear, the name of each director is searched from other sources such as the websites of government organizations related to that person as well as using Google search because it links to more sources than the official government website, such as newspaper. However, it is necessary to note that this search is only meant to confirm data for some cases, but not use as the main data source. The Google search can be used because Thai names are very specific to a particular person, and it is very rare that two people will have the same first name and surname in Thailand. This individual director data is then

coded by the lead researcher based on different types of political positions, and then aggregated in to the firm-level data.

In contrast to previous work (Faccio, 2006; Hillman, 2005; Brockman et al., 2013) that focuses solely on the top-level government officials, this study opts for a different approach to identify political actors. Apart from the top executive levels as former studies, we also include civil servants (government officials), the government advisors and the government committee as political actors. While it can be argued that the civil servants are at the lower rank and the committee and advisors are not government officials, it cannot be denied that these people have access to particular resources that can also be beneficial to the firms. Civil servants while having lower ranks compared to cabinet ministers or parliament members and although they may not make final policy decision, they have less temporary work experiences in particular positions. The executive and management level of civil servants deal with all sources of information and regulations before it is delivered to the Minister or PM, or the parliament. The different types of political actors are hypothesised as different moderators in these studies, in order to identify which one is helpful for the firm's performance. After all qualitative data of the board members were collected, the data is coded according to each hypothesis identified in the research frameworks. Six variables regarding political connections are used in this study. Each variable is explained as following:

***Political Connections:*** Political connection is measure by a ratio of politically related directors to board size. To create the ratio, we count number of directors who previously or currently have political positions in a government organisation, and then divide by total number of directors. By using the ratio of the politically connected directors to board size, instead of absolute number of politically connected directors, we control the effect of different board size across the sample. The political positions in this variable include all types and level of political actors as discussed earlier.

Most studies that used profiles of the directors or executive members to capture the firm's political connections identify a firm's political connections only when a firm ties with a top government official or a politician (Faccio, 2006; Hillman, 2005). This method creates two limitations. First, identifying whether firms have political connections using a dummy variable cannot capture fine-grained details of

the firm's political connections. Second, using only top politicians or government officials limits types of political connections only to the top level. Considering these limitations, the measurement of the firm's political connections in this study is a more fine-grained method by including political actors not only from the top level, but also including lower government positions. We then include other variables related to political connections to measure different level and type of political actors.

***Level of Political Actors:*** We used the average level of political actors for each firm to measure the level of political actors. To calculate the average level of each firm, we first assigned a level of political position for each director. The rank of political position is classified into five levels illustrated in Table 3.2. The lowest level of political actor is represented by 1, and the highest level is indicated as 5. To assign the rank for each director, the position of government officials and civil servants are compared with the official ranks of government officials and civil servants in Thailand together with the salary rate of the government officials based on the *Civil Service Act, B.E. 2551 (2008)* of Thailand. By using salary rate, we can compare the ranks of political actors across different types of government officials and organisations as well as the ranks of political actors before and after the change of the ranking system of civil servant positions in Thailand in 2008. According to the *Civil Service Act, B.E.2551 (2008)*, the positions of civil servants in Thailand are classified into four categories consisting of executive positions, managerial positions, knowledge worker positions, and general positions. We assigned the political positions of the cabinet ministers as the highest level (Level 5) and other political positions in parliament (Senate of Thailand and House of Representatives of Thailand) as Level 4. Political positions of government officials are not typically considered as civil servants but their positions are generally comparable with the high level of the executive positions in the current ranking of civil servant positions. However, considering that these political actors have a higher level of access to government resources and policy decisions together with the comparison of salary rate and the higher rank in the older system of civil servant positions, we assigned them to a higher level than other civil servants in this thesis. The executive positions, which are heads of government agencies and deputy heads of government agencies at ministerial and departmental levels (*Civil Service Act, B.E. 2551 (2008)*, Ch.2, s.45), are assigned as level 3. The

managerial positions, which are heads of government agencies at level lower than departments (*Civil Service Act, B.E. 2551 (2008), Ch.2, s.45*), are assigned as level 2. The knowledge worker positions and general positions are included in the assigned level 1 together with the government committees and advisors. We included the government committees and advisors in our assigned ranks of political actors, despite that they are neither government officials nor civil servants, because they are a part of policy making and able to provide political information to the connected firms. We, however, considered them in the lowest level, as their level of resources access is more limited compared to the government officials or civil servants in management or executive levels.

After we assigned each director with the political level, we multiply the number of directors in each level with the assigned number in each level (i.e. 1 to 5), then divide by the number of politically related directors. So, each politically connected firm has a level ranging from 1 to 5, and 0 represents firms with no political actors.

**Table 3.2** Hierarchical Level of Political Positions

<b>Level</b>	<b>Position</b>
5	Prime minister, deputy prime minister, minister, deputy minister
4	Senators, members of parliament, advisors to the president of the national assembly senate, the speaker of the house of representatives
3	Government officials (Executive level), principle private secretary to the Prime minister and ministers, advisors to Prime minister and ministers
2	Government officials (Management level)
1	Government officials (General public officers), government committee, advisors to government organizations

Source: The author creates this level based mainly on the official positions of government officials and civil servants in Thailand

**Types of government functions:** Two types of government functions, executive and legislative, are considered as each variable. We counted the number of directors who have experience in each function, and divided by total number of directors, to create ratio of executive ties and legislative ties. The complicated part however is the fact that some political actors have experience in more than one

government function. For example, some senators are former minister. In this case, we coded every political actor that once had experience in executive function such as PM or minister as executive ties. Only senator and MPs who have not had any executive positions were assigned in legislative ties. Only top-level of political actors is used in this variable to address the high multicollinearity with political connections shown in our preliminary test of correlations.

***Government-Bank Related Directors:*** We use ratio of government-bank related directors to measure directors' experiences in government banks. We counted the number of directors who have working experience in government banks, and then divided by the total number of directors, to create the ratio of government-bank related directors.

***Foreign-Investment Related Directors:*** The ratio of directors with experience in foreign-investment related agencies to total number of directors are used as the measure. To create the ratio, we first counted the number of directors who have working experiences in three government organisations that are related to foreign investment in Thailand, and then divided by the total number of board members. These three government institutions are the Ministry of Finance, the central bank (Bank of Thailand), and the board of investment (BOI). Ministry of Finance and Bank of Thailand are two government organisations that regulate capital flow in Thailand. Policies and regulations related to the capital outflow from Thailand are made by these two organisations, so they represent the regulating agencies. BOI is an investment-promoting agency in Thailand. BOI used to focus on promoting IFDI to Thailand, but BOI shifted its role to encourage OFDI from Thai firms more after the government policy to promote OFDI in 2012 (Board of Investment, 2015).

***Foreign-Affairs Related Director:*** Ratio of directors whose work is related to foreign affairs to total number of directors is used to measure foreign-affairs related directors. To calculate the ratio, we first counted the number of directors whose positions are/were a diplomat, an ambassador, or a government official from the Ministry of Foreign Affairs, then divided by the total number of board members.

***Limitations of The Selected Measures:*** While our method can provide details of connected political actors that may link to different kinds of resources, measuring political connections based on the board of directors is far from perfect. First,



compared to the typical measure of political connections suggested by Faccio (2006), the method used in this research does not include the connections that firms have via shareholders and other executive or management members of firms. However, as politicians in Thailand are required to disclose their assets when they join the government, many politicians therefore try to avoid having their name as a shareholder. So, the use of large shareholders to represent political connections may not give any significant information. For the information of CEO and management teams, CEO and most management teams normally work full-time for firms, so they are unlikely to have a position in both government and the firms. Moreover, other top officers such as CEO in most cases, at least in our sample, also sit on the board of directors. So, in case those political actors are invited to work as a firm's CEO or executives, they are likely to sit on the board of directors. In addition, family-controlled firms are likely to appoint their family members to the board. Hence, using profile data of the board members to identify political connections, although unable to get completed data of political ties, can capture the firm's political connections in a certain degree.

Also, by using the formal source of the board of directors to measure political connections, we can compare profiles of political actors sitting on the board across the firms. This fits with our research's objective to compare different types of political actors. Also, the political connections based on formal information of the board of directors can be identified by the involved parties in the host countries, such as business partners or investors, so it suits the research context focusing on the cross-border effects of political connections. The use of the board of directors to identify political connections is also supported by previous studies (Goldman et al., 2009; Hillman et al., 1999) that show the relationships between board ties and firm performance.

#### **3.2.3.4 Control Variables**

Since the firm's performance can be influenced by industry and firm characteristics, variables that can affect the firm's performance are included as control variables.

**Firm size:** As firm size is an important determinant of profitability (Rugman 1983), we include firm size as a control variable. Firm size can be measure in several ways such as total sales, number of employee, and total assets. This study uses number

of employees, log transformed, following previous studies (Hadani and Schuler, 2013; Hillman, 2005). Thomson One is our main source for number of employee data, however there is missing employee data of Thai firms in Thomson One database, we therefore manually collected the employee data from the Form 56-1. Still, many firms do not provide this information in their company's reports. The missing data of number of employees in our sample reduces our sample size to 539 observations in our final analysis.

**Board size:** As data of political connections are based on the profile of board of directors and studies in corporate governance suggest that board size can increase the firm's performance (Dalton et al., 1999), board size is therefore included as a control variable. Following previous studies (Hadani and Schuler, 2013; Hillman, 2005), board size is included using number of directors.

**Firm experience:** The effect of a firm's experience is included in the models as a control variable using firm age as its proxy. As the period of existence of firms can impact on the amount of resources that firms can possess (Baum et al., 2000) and may influence firm performance since firms with long period of overseas investment can have more experience on foreign markets and can be able to adapt their strategy and operation better in foreign markets. Moreover, studies in corporate political strategies often use firm age as a proxy of reputation, credibility or experience, and visibility of the firms (Hillman et al., 2004) which links to the success of firms and choices of political strategies. Firms with older age can also build a relationship between the top management team and government official which turns to firm credibility and links to political strategies (Luo, 2001). Firm age is measured by the number of years since the firm was established.

**Intangible assets:** Studies in RBV suggested that the firm's intangible resources can sustain the firm's competitive advantages (Hall, 1993) and are an important factor that can influence the firm's performance (Delios and Beamish, 2001). Intangible assets, which represents non-physical assets such as goodwill, patents and trademarks of firms, is controlled using the book value of intangible assets (Kafouros and Aliyev, 2016).

**Financial leverage:** Financial leverage shows a firm's capital structure. It is argued to affect firm performance because it influences how managers choose the

firms' operating activities (Jensen and Meckling, 1976). Studies in political connections also argue that political connections can lead to a higher level of financial leverage because of financial access to lower interest rate loans, but this loan may lead to poor performance (Duchin and Sosyura, 2012; Bliss and Gul, 2012; Boubakri et al., 2012b). So, we control financial leverage by using debt to equity ratio following Lu and Beamish (2004).

**Internationalisation:** Studies in IB that focus on the MNEs performance have been widely focus on the internationalisation or multinationality of firms as influential factors to affect firm performance. The internationalisation reflects the bread and depth of the firm's foreign investment activities and can lead to the firm performance. Therefore, we include internationalisation as a control variable to capture the multinationality aspect of the firms. Internationalisation is measured following Lu and Beamish (2004) using the calculated ratio based on the average of count number of foreign subsidiaries/associates and countries. To get this ratio, a count number of foreign subsidiaries/associates and a count number of countries in which a firm operates its subsidiaries/associates are divided by the maximum number of subsidiaries/associates and the maximum number of countries respectively; then these two ratios are calculated to get the average ratio ranging from 0 to 1 for the measure of internationalisation.

**Government ownership:** Ownership types can both affect the appointment of political actors to the board and affect to the firm's value (Peng and Luo, 2000; Wang, 2015). The government ownership is particularly controlled for in this present study following previous works (Sun et al., 2015). Data of the top ten lists of shareholders and percentage share as of end of the year 2013 were collected from the Form 56-1 using the same approach with political connections as the data of ownership coded in different ways at a later stage. Then, following Okhmatovskiy (2010), the government ownership is identified when a firm is owned by government or SOEs in at least a 5 per cent share. A dummy variable is used to represent whether the firms have government ownership following previous studies (Sun et al., 2015; Peng and Luo, 2000).

**Industry effects:** The effects of the firm's internationalisation and political connections on its performance varies across industries (Lu and Beamish, 2004; Peng

and Luo, 2000; Hillman, 2005). Following previous studies (Gomes and Ramaswamy, 1999; Capar and Kotabe, 2003), industry effects were controlled by using dummy variables representing each firm's primary two-digit SIC code (see Appendix C).

The summary of all variables used in this thesis is provided in Table 3.3. This table briefly describe the definition of each variable together with the data sources we used to obtain the data.

### **3.3 Method of Estimation**

This research applies the Ordinary Least Squares (OLS) regression as the method of estimation. OLS has been commonly used in studies similarly to this research, especially those with cross-sectional data. Although some instrumental methods can be used to analyse the data such as 2SLS (Wooldridge, 2010), it is suggested in former works that other instrumental methods do not give much better results compared to OLS (Kafouros, 2008). Therefore, this study uses OLS as the estimation technique. However, by using OLS, some issues arise based on the OLS's assumptions. First, it is assumed in the linear regression model that the explanatory variables must not be collinear. If not, the regression creates multicollinearity, and the OLS assumption is violated (Wooldridge, 2010). Second, OLS assumes that the variance of the disturbances must be equal (homoscedastic) and the presence of unequal variance (heteroscedasticity) can violate the OLS assumption (Hair et al., 1998). Third, the endogeneity issue can arise when there are reverse effects in which dependent variables also determine independent variables. This then creates the reverse estimation. Fourth, OLS assumes no autocorrelation, which occurs when there is a pattern of the correlation of the disturbances. The presence of autocorrelation creates unbiased estimators (Wooldridge, 2010).

In this chapter, the research design and operationalisation are explained covering the research method, data, measures, and estimation method applied in this thesis. Using the OLS technique to analyse the sample of Thai listed firms to test the interaction effect between political connections and OFDI on firm sales, we present the discussion of the specific research framework and the research findings in the next chapter.

**Table 3.3** Definition of Variables and Data Sources

<b>Variables</b>	<b>Definition</b>	<b>Data source</b>	<b>Chapter</b>
<b>Dependent variables</b>			
Sales	Value of total sales (Million US\$)	Thomson One	4&5
<b>Control variables</b>			
Firm size	Log number of employees	Thomson One+Form56-1	4&5
Intangible assets	Value of intangible assets (Million US\$)	Thomson One	4&5
Financial leverage	Debt to equity ratio	Thomson One	4&5
Internationalisation	Average number of foreign subsidiaries/affiliates and countries a firm operates	Form56-1+FS*	4&5
Board size	Total number of directors	Form56-1	4&5
Firm age	Number of years since firm established	SETSMART	4&5
Government ownership	Equal to 1 for government owned firms, and 0 otherwise	Form56-1	4&5
Industry	A firm's industry based on two-digits ISIC codes (dummy)	Thomson One	4&5
<b>Independent variables</b>			
OFDI	Direct investment value in foreign countries (Million US\$)	Form56-1+FS*	4
OFDI in developing countries (NDC)	Direct investment value in developing countries (Million US\$)	Form56-1+FS*	5
OFDI in developed countries (DC)	Direct investment value in developed countries (Million US\$)	Form56-1+FS*	5
Political connections	Ratio of politically connected directors to total number of directors	Form56-1*	4&5
Level of political actors (PC Level)	Average level of director's political positions ranked from 1-5 and 0 is no political connection	Form56-1*	4
Executive ties	Ratio of directors with experience in executive branch to total number of directors	Form56-1*	4
Legislative ties	Ratio of directors with experience in legislative to total number of directors	Form56-1*	4
Government bank related directors (GBD)	Ratio of directors with experience in government banks to total number of directors	Form56-1*	5
Foreign-investment related directors (FID)	Ratio of directors with experience in foreign investment related agencies to total number of directors	Form56-1*	5
Foreign-affairs related directors (FAD)	Ratio of directors with experience in foreign affairs to total number of directors	Form56-1*	5

Note: FS denotes note to financial statement

\*New constructed data.

## **Chapter 4**

### **The Role of Home-Country Political Connections in Enhancing the Effect of a Firm's OFDI on Its Performance**

#### **4.1 Introduction**

Creating connections with political actors such as government officials, agents and politicians is a corporate strategy that may reduce regulatory uncertainty and provide the firm with various benefits (Pfeffer and Salancik, 1978; Faccio, 2006; Boubakri et al., 2012a). Such connections may provide access to government-controlled resources, information, and insights that can help the firm survive (Zheng et al., 2015; Faccio et al., 2006), increase its performance (Hillman, 2005; Fisman, 2001) and internationalise (Wang et al., 2012). Extant international business research has predominantly focused on how political connections influence foreign investment strategies (Frynas et al., 2006). However, although prior research has shown that connections with home country political actors help firms to internationalise and engage in outward foreign direct investment (OFDI) (Lu et al., 2014; Wang et al., 2012), very little research (e.g. Brockman et al., 2013) has examined whether political connections in the home country can be leveraged abroad to help the firm compete in the foreign countries in which it invests. Having the ability to go abroad does not mean that a firm also has the ability to compete abroad. As such, we have a limited understanding of whether political connections can help the firm benefit from its OFDI.

When firms establish their subsidiaries in foreign countries, they face higher costs and competition due to the liability of foreignness in the host country and they also have to deal with host country institutions. To deal with the liability of foreignness and other disadvantages, MNEs transfer home-grown resources and capabilities to their subsidiaries (Zaheer, 1995), including technology, financial assets, knowledge and brands (Zaheer and Mosakowski, 1997). However, can the firm use political connections, which by definition are embedded in home-country institutions, to overcome disadvantages associated with liability of foreignness,

compete in host-countries and therefore increase the returns to its OFDI? This chapter addresses this question by examining how home-country political connections influence the relationship between OFDI and firm performance. It also provides the investigation and the development of theoretical explanation about what types of political connections are more beneficial and about the mechanisms through which home-country political connections can be leveraged abroad.

Political connections may positively affect firm performance (Hillman, 2005) by giving advice to the firm as to how to navigate the political landscape in foreign countries and by helping the firm to be more aware of foreign policies and negotiate deals with host-country governments. However, it can also be insignificant or even be a liability for firms, especially when the government changes (Siegel, 2007) or the firm does not have a political ally in the host country. To understand how political connections affect firm performance, we identify the different types of political actors that firms choose to connect with. The underlying assumption of previous work on political connections is every type of political positions is equal and can generate equal benefits to the firms. This work typically considers only top-level politicians and operationalises political connections either as a dummy variable (Faccio, 2006) or number of connections (Hillman, 2005). However, a firm that has a connection with a prime minister may access different resources compared with other firms that have connections with non-executive government officials. Equating the prime minister with a low-ranked government official negates the value of the prime minister. This chapter is therefore not only considering the existence of a connection but also the positionality of each connection.

Although it can be argued that having many connections with any type of political actors may benefit firms through the broad networks of political actors, the criticality and availability of resources provided by different types of political actors are not the same and may not benefit all firms equally. We argue that the lack of detailed consideration of resources based on connected political actors leads to incomplete understanding of this phenomenon and inconsistency of empirical studies in this area of research. Few studies have recently started to compare the effects of different types of political connections such as the difference between local and central ties (Zheng et al., 2015), formal and informal ties (Mahmood et al., 2017),

personal and organizational ties (Sun et al., 2015), and ties with executive and legislative officials (Zheng et al., 2017). However, the explanations of performance effects of different types of political actors are still limited theoretically and empirically. We extend prior studies on political connections by providing empirical evidence based on the exploration of the hierarchical authority of political positions and different government functions.

By considering both the number of corporate political connections as well as the fine-grained details of the connected political actors, this research enables us to examine whether positionality of political actors has different effects on the relationship between OFDI and performance. This in turn allows us to contribute to two research areas. First, we extend international business research by providing the discussion on the value of firms' resources derived from the home-country political connections on its OFDI and performance in addition to the existing research which has concentrated more on the determining the effects of political connections on the internationalisation. Second, we extend research in corporate political strategies by exploring the various effects of the firm's political connections based on resources provided by different political positions of connected political actors.

## **4.2 Theoretical background and Literature Review**

### **4.2.1 Resource Dependence Theory and the Firm's Political Connections**

RDT has been used to explain the benefits of the firm's political connections, in particular the connections created through the board of directors, in reducing uncertainty stemming from external organisations (Pfeffer and Salancik, 1978; Hillman, 2005). To gain benefits of the linkages between the firm and external organisations or individuals, RDT considers that the interdependence between the firm and the external parties is an important condition that help the firm maintain its autonomy which in turn increases firm performance (Drees and Heugens, 2013). The idea of interdependence is, however, criticised that it mixes two opposite concepts of power imbalance and mutual dependence (Casciaro and Piskorski, 2005). Drawing from power-dependence theory which discusses the interplay between the concepts of 'power' and 'dependency' (Emerson, 1962), Casciaro and Piskorski (2005) identify



power imbalance as the difference of power between two organizations, whereas mutual dependence is the sum of their dependencies. The separation between these two constructs is important to understand how linkages between two organizations can lead to an expected outcome. An organisation may not be able to control resources and manage its uncertainty as expected if another organisation has much more power, on average, over the other, while both organisations can benefit from their linkages if they both get mutual dependences. The key factors to determine the degree of power and dependence, based on RDT, are the criticality and availability of resources possessed by each organisation as they can define the degree of dependence between the two organisations (Pfeffer and Salancik, 1978; Casciaro and Piskorski, 2005). Hence, managing the criticality and availability of resources that the firms can access through their linkages can help them gain more autonomy, which in turn helps them increase performance.

Considering a firm's political connections, the government or public organisations can provide both critical and rare resources to the firm but also create uncertainty for the firm by launching new regulations and public policies. This explains why RDT has been utilised to understand the effects of a firm's political strategies in previous research (e.g., Hillman, 2005; Dieleman and Boddewyn, 2012). According to RDT, firms can engage with the government or public organisations by utilising corporate political activities that directly affect public policies such as lobbying or political campaigns (Baysinger, 1984; Keim and Zeithaml, 1986; Getz, 1993) or by appointing current or former political actors to the board of directors (Hillman, 2005; Lester et al., 2008; Agrawal and Knoeber, 2001).

Creating a long-term relationship with the government through political activities follows the firm's ultimate objective which is to influence the regulatory process. The firm can defend its legitimacy when it is threatened by public policy or government regulations or sustain its purpose and goals by gaining supportive favour from the government (Baysinger, 1984). Utilising co-optation strategy to deal with external organisations by appointing critical individuals to the board of directors, political actors in this case, can create four benefits, based on RDT, for the firms (Pfeffer and Salancik, 1978). These benefits are information regarding new policy or regulations, channels of communication the firms' information to the government,

supports from the government, and a certain level of legitimacy (Pfeffer and Salancik, 1978; Hillman, 2005). These benefits are further developed in our hypotheses.

#### **4.2.2 Types of Political Connections and Firm Performance**

Prior studies have attempted to illustrate how the connections between firms and government, or politicians, can improve the firm's value (e.g., Hillman, 2005; Faccio, 2006; Zheng et al., 2015; Boubakri et al., 2012a). The benefits that a firm can obtain from its political ties are discussed in different forms. With political connections, the firms can secure preferential treatments such as low-cost bank loans (Khwaja and Mian, 2005), government bailouts (Faccio et al., 2006), exemption from the capital controls (Johnson and Mitton, 2003), easier market entry (Agrawal and Knoeber, 2001), or government contracts (Goldman et al., 2013).

Despite the benefits suggested by previous work (Hillman, 2005; Goldman et al., 2013; Johnson and Mitton, 2003), the firm's political strategies can theoretically hinder the firms' performance because the costs stemmed from the rent extracted by politicians may offset their ability to generate private benefits (Shleifer and Vishny, 1994), and government related firms may need to accommodate social needs and concerns (Ramamurti, 2001). In case of co-optation, those political actors who are appointed as directors may seek to satisfy their personal interests, interests of their home organisations, or enforce another agenda which is insignificant to the firm (Westphal et al., 2006). The political actors sitting on the board, in turn, can divert the objectives of firms, leading to the declining autonomy of the firm. The negative effects of political connections are also supported by the empirical studies. For example, CEOs of politically connected firms have incentives to pursue social objectives at the firm's expense (Fan et al., 2007); the higher information asymmetry between investors and managers lead to less accuracy of earning forecasts (Chen et al., 2010). Moreover, political connections with a certain government can turn to be liabilities for the firm when a new political party grabs power (Siegel, 2007).

With an inconclusive theoretical and empirical debate, understanding the value of political connections on firm performance requires the consideration of various conditions that may create different impact to the firm's value. Previous studies (Sheng et al., 2011; Hillman, 2005) have integrated macro environment to

understand the impacts of political connections. For example, Sheng et al. (2011) find that political ties only outperform business ties in the context that has low government support or low technology instability. This study extends Peng and Luo (2000) who previously suggest that ties with government officials are more important than ties with managers of other firms. Environmental factors that influence the role of political connections on firm performance also include the industrial effects as shown in Hillman (2005) that the effects of political connections on the firm's performance are higher when the connected firms are in highly regulated industries.

However, based on the RDT perspective, we suggest to look closer at the different types of political connections and in particular on political positions of the connected political actors as different positions can provide dissimilar resources or benefits to the connected firms. The government itself consists of many organizations and individuals who possess different kinds of resources. These resources are relevant and accessible to the firms at different levels and in turn lead to different performance outcomes (Zheng et al., 2017). Previous work in this area has been only concerned with whether or not a firm is connected (Faccio, 2006), or has focused on the number of connections that a firm possess (Hillman, 2005). Such work only considers top-level political actors in their studies, so it does not reflect the criticality and availability of resources provided to the firm through various types of connected political actors. Studies in this area have recently started to compare the different outcomes that the firm gains from different kind of political organizations or political actors (Zheng et al., 2015; Okhmatovskiy, 2010). The explanations of the heterogeneous role of political connections on the firm's value can be viewed from the perspective of the resource access stemmed from the different levels of the government consisting of state, national, and local government (Zheng et al., 2017) or the levels of political embeddedness concerning with direct or indirect relationship with government through the ownerships (Sun et al., 2015; Okhmatovskiy, 2010).

To consider the heterogeneous value of political actors based on their government position, the lenses of human and social capital are integrated into this research. Human capital refers to skills, experiences, expertise, and knowledge, whereas social capital refers to prestige and connections with other firms (Withers et al., 2012). Hillman and Dalziel (2003) combined these two constructs into 'board

capital’, and suggested that board capital can lead to the provision of resources to the firms, which in turns lead to the firm’s performance. The depth and breadth of social capital possessed by an individual are attractive to firms in different ways and lead to the different degree of appointment on the board of directors (Lester et al., 2008). Hence, we suggest that the different degree of human and social capital possessed by the connected political actors, based on their political positions, can lead to the different degree of resources that they can provide to the connected firms, and ultimately lead to the different impact on OFDI and firm performance. While previous studies (Hillman, 2005; Sun et al., 2015; Okhmatovskiy, 2010) in corporate political strategies comprehensively discussed the mechanisms and impacts of the firm’s political connections, they mostly concentrate on the outcomes that occurred within the country where the connections are created, and rarely explain the mechanisms and the effects of the home-country’s political connections on the firm’s performance in foreign countries. To understand the role of the firm’s political connections overseas, which is the main objective of this present study, we propose the research framework shown in Figure 4.1.

**Figure 4.1** Research Framework 1: Connections, Level, and Government Functions

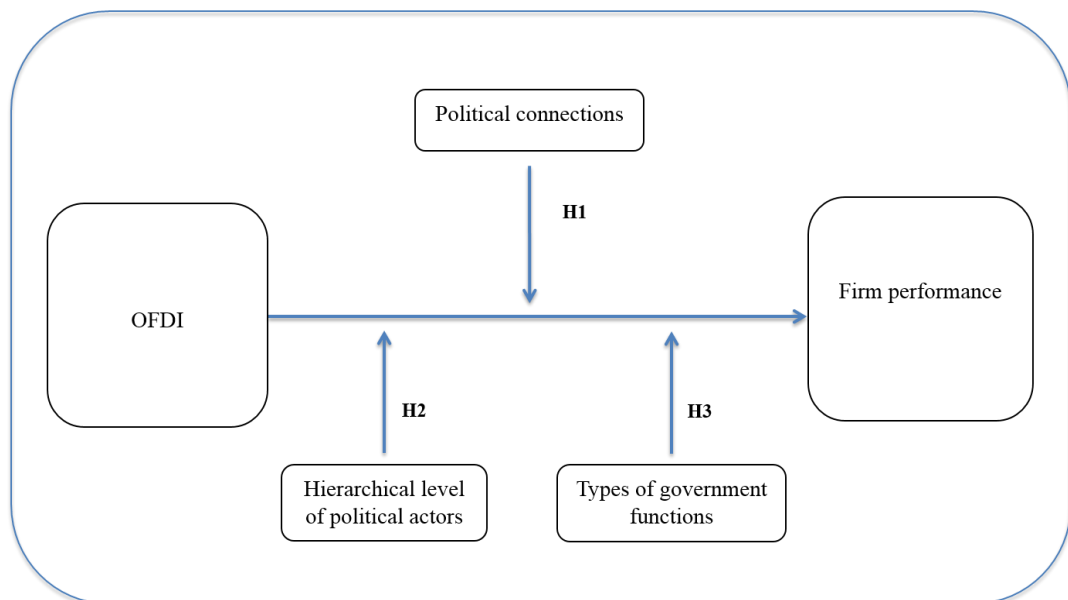


Figure 4.1 illustrates our research framework focusing on number, level, and types of political connections. In this framework, the direct effect of OFDI on firm

performance is established as the baseline relationship. We, however, have not developed the hypothesis on the direct effect of OFDI on firm performance because it has been shown in previous studies (Lu and Beamish, 2004; Contractor et al., 2007) that OFDI can either increase or decrease the firm performance. Rather, we focus only on the moderating effect of the firm's political connections as it highlights the conditional factors that influence the role of OFDI on firm performance. Three moderating variables, namely political connections, hierarchical level of political actors, and types of government functions, are added to illustrate our Hypothesis 1 to 3 respectively. We explain the hypothesis development on how the firm's political connections can influence the effect of the firm's OFDI on its performance in the next section.

### **4.3 Hypothesis Development**

#### **4.3.1 Home-Country Political Connections and Their Value in Foreign Countries**

Four main benefits that firms can obtain from their linkages with other organizations, based on RDT, are information, channels of communication, supports, and a certain level of legitimacy (Pfeffer and Salancik, 1978). These four benefits are adopted to explain why politically connected directors positively influence firm performance in previous work (Hillman, 2005). We apply these benefits to elaborate how connections the firms make with political actors can influence OFDI to enhance firm performance.

First, firms can obtain crucial information related to overseas investment from its politically connected directors. RDT suggests that appointing external individuals to the board of directors brought firms the information related to the activities of external organisations (Pfeffer and Salancik, 1978). By appointing government officials to the board, firms can get information related to the government's policies or regulations that may benefit the firm's overseas operations. As OFDI is involved with various kinds of foreign investment regulations from both home and host governments such as capital control or foreign ownership restrictions, home-country political connections can provide firms with the information that help firms deal with both regulations at home or abroad. The earlier the firms can get information about

both roles of the government, the quicker the firms can manage uncertainty stemming from the government and able to have new strategies that suit the new policy environment. With the information they get through its connections, the firms can lower the cost of being an outsider, especially in foreign countries. Moreover, when the government has a new project that may require a business partnership, the connected firms can get this information earlier than their competitors, so they can utilise this information to adjust themselves to suit the government's requests quicker and have a higher opportunity to become the government's business partners. It is reported in previous research that the politically connected board can help firms gain government contracts (Goldman et al., 2013).

Political connections do not only provide firms with government related information, but they can also provide firms with relevant information regarding the overseas investment in the host country, such as the information about potential business partners and business competitors, or insights about the local communities. The social networks that the firms established in the home country through the connected political actors can lead the firms to both political actors and business partners in the host country. As illustrated in the previous work by Frynas et al. (2006), the first mover advantages the firm gain from its political connections includes the link to socio-political networks of the connected firm in the host country prior to the latecomers. The more number of political actors the firms have connections with, the higher the possibility that they can get information related to the host-country government or business partners. With information the firms obtain from their connections, they can reduce unpredictable circumstances and deal with the host country's unwritten rules (North, 1990) that might be difficult for foreign firms to identify without any help from local contacts. The socio-political networks of political actors in the home country therefore provides firms information and insights related to government policy, bureaucratic procedures, and local practices that help the firm reduce transaction costs when doing business in host countries. The higher the number of connections, the stronger these benefits will be.

Second, firms can communicate their preferable information to the government agencies or regulators (De Figueiredo and De Figueiredo, 2002). RDT suggests that the linkages with external organisations can give firms the channels of

communication to and from the connected organisations (Hillman, 2005). By having political actors on the board of directors, the firms can then use the politically connected directors to pass on their favourable information to government agencies or relevant regulators (Pfeffer and Salancik, 1978). The government agency itself also needs to gather practical information from interest groups, including business organizations (De Figueiredo and De Figueiredo, 2002). The firms that have connections with political actors can use these opportunities to give the government agencies the information that can favour the firm's operations (De Figueiredo, 2002). The information the firms provide the government regulators through its politically connected directors may then lead to the firm's favourable government policies and regulations.

Third, firms can take advantages of political resources, experiences, skills and insights of political actors connected to the firms to help them deal with government bureaucracy in both home and host countries. By sitting on the company board, the external directors are committed to give some support to the firms (Pfeffer and Salancik, 1978). Political actors sitting on the company board can predict government actions using skills from their previous participation, knowledge and friendship with decision makers (Agrawal and Knoeber, 2001) and utilise their skills to navigate home-country government bureaucracy (Goldman et al., 2009) especially those actions that are related to the OFDI. In the same manner that the political actors can support the firms in the home country, they can utilise their networks, experiences, and skills to help firms deal with the bureaucracy and informal rules in the host countries.

It is illustrated in a previous study (Rasiah et al., 2010) using the case of the government of Singapore and Malaysia that the home government of emerging countries give support by setting up the special economic zones overseas for its national firms to ensure that the firms have the maximum benefits in the host countries. The firms with home-country political connections can then have support when they invest overseas, so that they can reduce the cost that may occur when firms invest in overseas (Zaheer, 1995).

Fourth, firms with political linkages can benefit from a certain extent of the legitimacy. The prestigious or legitimate persons and organizations, especially

through the board of directors, can confirm the value and the worth of the firm to international outsiders (Pfeffer and Salancik, 1978). Home government can negotiate or bargain with the host-country government to support the firm's OFDI (Li et al., 2013; Ramamurti, 2001). With the connections to the home government, the firms may have organizational legitimacy and autonomy to operate its subsidiaries without much intervention from the host-country government.

The involvement with home government, however, can be a double-edged sword as it may send a negative signal to foreign markets based on its dependency on the government. The negative perceptions of the host government and community are likely to occur with SOEs as they are more embedded with home-country politics compared to private firms (Okhmatovskiy, 2010; Sun et al., 2015). Previous studies have shown that SOEs are under pressure to please host-country institutions (Meyer et al., 2014) and its government owner to invest in the government preferable projects (Wang et al., 2012). In contrast, firms that only link with high officials are pressured to be more competitive as the firm's success reflects the reputation of the connected political actors (Wang et al., 2012).

Although there are possibilities that the connected firms can gain or lose its legitimacy in the perspectives of the host country, with the connections they have with home-country political actors that may link them to the host government, we expect that firms are able to use the channels of communications they have with political actors to give information to the host government and local community that ultimately help them gain more autonomy. This can then help them reduce the possibilities of negative perspective or intervention in the host country.

Considering all possible benefits the firms may have from their political connected directors, we expect that the firms that possess more connections with political actors in the home country can positively influence OFDI to enhance firm performance. Hence, the first hypothesis is introduced as following:

***Hypothesis 1:** The higher the number of political ties a firm has (irrespective of the level and type of such ties), the stronger positive the effects of OFDI on firm performance will be.*



### **4.3.2 Level of Political Positions and Its Effect on Firm Performance**

One of the main underlying assumptions of resource dependency is power imbalance. Those who control more resources are more powerful than the other (Casciaro & Piskorski, 2005; Emerson, 1962). The important consideration is therefore who controls more resources. The firm's dependency of resources on external organisations occurs when those organisations possess critical and rare resources (Casciaro and Piskorski, 2005). The political actors, as parts of government, are able to give the firms such valuable resources. However, the benefits the firms obtain from the connected political actors are not equal due to their different levels in the government (Wang et al., 2012; Ma et al., 2016). The levels of government officials lead to the different degree they access to government information and the controls over policies and regulations. Previous studies have considered the level of government based on the closeness to central government as a source of political resources (Wang et al., 2012; Zheng et al., 2015). We argue that the access to political resources depends on the political power that comes with the hierarchical level of the political position.

Top-level government officials are normally considered as important individuals who can make more important decision on policies and regulations that can influence the firms, and they are normally included as the targeted political actors in previous studies on political connections (Faccio, 2006). Apart from the ability to influence policies and regulations, top-level government officials, such as the Prime-Minister or cabinet members, are often seen as having prestige and high political status that can increase the social capital of the board (Johnson et al., 2011). These high-status directors can also influence the positive perception of the external individuals or organisations, and in turn contribute to the firm's legitimacy (D'Aveni, 1990). Therefore the high-level political position, such as members of parliament or cabinet ministers, can send a signal of legitimacy to the external organisations and individuals. The legitimacy the firms gain from its top-level political position can help the firms gain autonomy in operating its subsidiaries overseas, with less intervention from the host community.

Moreover, the high-level political actors are less accessible compared to lower level political positions, therefore only a certain amount of firms that can create

linkages with these top-level political actors, which generate the firm's specific advantages over other firms. It might be argued that lower-level government officials, such as those in administrative agencies or civil servants, may engage in the process of making regulations and policies more than the top-level officials and they are, to a certain level, politically-neutral (Drewry, 2011). However, from the perspective of availability, these lower level officials are more accessible compared to the top-level officials. The ties with fewer organisations, or weak ties, is strength (Granovetter, 1973) because it leads the connected firms to more competitive resources that are not accessed by other competitors. The firms tied with political actors who have high political positions therefore have a competitive advantage stemmed from the rareness of information and resources they can access to those higher-level political actors. The benefits of the low-level political actors therefore may not offset the rareness of resources and information that the top-level political actors can provide to the firms and make firms gain the competitive advantage over their competitors.

Hence, the difficulties of the access to the high-level political actors compared to lower level political actors lead firms tied with higher positions to more competitive advantages because the resources they possess are less available to other firms. In contrast, the low-level political actors are easier to access and may engage with many firms, which make political resources provided by the low-level political actors less-competitive compared to the resources offered by the top-level political actors. It is suggested in social-network studies that structure holes from less-connected networks have a positive effect on the firm performance (Batjargal et al., 2013). Therefore, political resources that the firms have from low-level political actors are not competitive compared to the resources that are provided by higher-level political position.

In consideration of the role of home-country political connections in the host country, political actors that have high status and authority, such as the cabinet members, because of their positions, have more opportunities to interact with politicians, business leaders, and social elites in foreign countries. Although the power based on hierarchical level of political positions can be inconsistent between the ranking system in a local hierarchy and global hierarchy (Magee and Galinsky, 2008), firms connected with political leaders are able to access to international networks and

gain socio-political information, get insights into the political and business systems in host countries more than firms connected to lower level political actors. Moreover, political leaders are better known in the international level than lower level political actors. Hence, they can signal a certain level of legitimacy of the firms they are sitting on the board of directors to the firm's potential business partners in the host countries. Furthermore, the firms tied with high-level political actors also have pressure to invest in a more competitive market in their OFDI as the success of the firms in the competitive markets can reflect the success and reputation of the high-level government officials (Wang et al., 2012). Therefore, we expect that the higher level of political actors will strengthen the effects of OFDI on firm performance.

*Hypothesis 2: The higher the political position of a firm's connected political actors is, the stronger positive the association of OFDI and its performance will be.*

### **4.3.3 The Roles of Government Functions in Enhancing the Firm OFDI's Performance**

Types of political actors to whom a firm chooses to connect with can affect the firm's performance due to different resources they can access via the political actors (Zheng et al., 2017). One way to consider the different roles of the political actors is by categorising based on the government functions, namely executive, legislative, and judiciary (Getz, 1993)<sup>1</sup>. Although it can be argued that the government operates based on the interactions between these three institutions and the separation of power may not be clear cut (Drewry, 2011), resources that political actors from each branch can provide to the firm are dissimilar (Zheng et al., 2017) due to their distinguishing roles and responsibilities (De Figueiredo, 2009) and different levels of social capital stemming from their unique experiences (Lester et al., 2008).

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<sup>1</sup> These three functions are based on the concept of the separation of powers. In the parliament states where the cabinet is also a part of the legislatives, the separation of powers are impossible (Harris, 1976). The consideration of these three government functions, however, based on the argument of the main duty and responsibility of each branch. The operation of the government functions is also based on the assumption of the separation of their core functions.

Previous research suggests that the executive and legislative branches are more targeted by firms for their corporate political activities (CPA) than the judiciary branch (Getz, 1993). Although the court has the ability to overturn the government rules made by the government agencies when firms are not satisfied with them (De Figueiredo, 2009), the role of the judiciary is mainly to affirm the decision of administrative agencies and has less impact on regulations (Getz, 1993). We therefore consider only the executive and legislative ties in this study.

Political actors from the executive branch, especially those in the cabinet that are responsible for the execution of regulations and making public policies, are the main political target for the firm when it is considering to use political strategies because of their roles on policy implementation (Zheng et al., 2017) and their networks of regulatory agencies that can influence business operations (Getz, 1993). Not only do the political actors from the executive function, especially those who are part of the cabinet, get access to and control resources, but they also have regulatory ability to issue government licenses and permission (Zheng et al., 2017). Moreover, the social capital derived from broader experiences of the cabinet ministers can make them more attractive to the firms than the senators and the house representatives to the firms that consider to appoint political actors on the board of directors (Lester et al., 2008). The firm connected with political actors from the executive branch therefore can benefit from their political connections more than the firms without connections with political actors from the executive branch.

Regarding the OFDI, the government officials from the executive branch, both from the cabinet and the administrative agencies, are directly involved in the government supporting policies and regulations. Studies reporting the role of the Chinese government in promoting OFDI show that the government agencies in the executive branch, such as the State Council, Ministry of Commerce, the central bank (People's Bank of China) and State Administration of Foreign Exchange (SAFE), have active roles in the increasing OFDI by Chinese MNEs (Luo et al., 2010; Voss et al., 2008). As well as the case of China, the government agencies from the executive branch of India, such as the Export-Import Bank of India, is also reported to provide funding schemes for helping the investment of Indian companies in its overseas affiliates (Kumar and Chadha, 2009). This home-government support, while may be

seen as the driving factors for the firm's OFDI, can generate advantages for the firms even after its OFDI. The firms that get government support such as cheap government loans can invest in their overseas affiliates with lower cost compared to the firms that invest in their affiliates with higher interest rates.

In addition to the direct benefits based on the OFDI promoting roles of executive officials, political actors from the executive branch also have a scope of responsibility that is more related to international affairs than compared to the other two branches. Due to the variety of social capital of the executives (Lester et al., 2008), the connections with home-country executive function of the government can also help firms access to the socio-political networks of the political actors to create connections with the host country government. The political actors from the executive branch whose positions allow them to have experiences and socio-political networks on an international level, such as those government officials from the Ministry of Foreign Affairs or cabinet ministers, are able to convey the information or insights and give suggestions about the host-country institutions to the connected firms better than legislatures whose responsibilities are mainly concerned with domestic affairs. The connections with the host-country government can facilitate the internationalisation of the firms by helping firms gain access to the government clients in the host countries as well as help the connected firms deal with the host country institutional pressures (Hitt et al., 2006) especially those that derive from regulatory agencies.

Apart from the executive government officials, political actors from the legislative branch are also one of the main target of the firm's political strategies (Getz, 1993; De Figueiredo, 2009). The legislative branch of the government has important roles in making the law and regulations that govern economic activities (De Figueiredo, 2009). The connections created with the political actors from legislative functions therefore can give the firm a channel of communication of its information to the regulators (De Figueiredo and De Figueiredo, 2002). However, due to the wide scope of law engaged by the legislators, they allocate the rule-making ability to the administrative or bureaucratic agencies, which makes the government agencies the most influential player for the daily operation of businesses (De Figueiredo, 2009). Therefore, despite the influential roles related to creating law and regulations of the

legislative branch, the broad areas of the law under the responsibility of political actors from the legislative branch make them engage with less specific details concerning the implementation of public policies and the monitoring of regulations compared to administrative or bureaucratic agencies (Bonardi et al., 2006; De Figueiredo, 2009), which is a part of the executive branch (Drewry, 2011).

Hence, the connections the firms created with the legislative function, while may influence the firm's performance, have less impact on the firm's performance compared to the executive functions. The study based on 47 countries by Faccio (2006) also shows that the firms connected to government officials in the cabinet (i.e. prime minister and minister) can influence its stock price premium more than the firms tied with members of parliament, by which the coefficient of the executive ties accounts for 12.31% compared to 1.28% of the legislative connections. Despite the tendency of the positive influences of the executive ties compared to legislative ties, the role of the political connections from these two functions may also vary on the host-country institutional development. Recent studies (Mahmood et al., 2017; Zheng et al., 2017) suggest that the legislative branch is more valuable than the executive branch in the opened or developed markets than in the less developed economies. Our study only focuses on home-country government of the EMNEs, and so we then expect the positive role of the executive functions, rather than the legislatures.

Considering that firms connected with political actors in the executive function can access more political resources in the form of advices and support regarding the host-country government and institutions as well as communicate with organisations, social elites, and business partners in foreign countries through their wider international networks compared to legislative branches, it is expected that the relationship between OFDI and a firm's performance will be enhanced when the firm has connections with political actors from the executive branch of the government, but not do so in case of the firms connected with the legislative functions. Hence, the hypothesis is developed as following:

***Hypothesis 3:** The more the firm has executive ties, the stronger positive the effect of OFDI on its performance, relative to the firm with legislative ties.*

## 4.4 Empirical Results

To test the hypotheses, we use data and research method as described in Chapter 3 to test our research framework. Table 4.1 reports means, standard deviations, and Pearson correlations for all variables used in this chapter. Overall, the correlation coefficients among the independent variables are fairly low. There are only three cases that are slightly higher than 0.5. The correlation between the political connections and the level of political actors has coefficient at 0.54, the correlation between OFDI and intangible assets has coefficient at 0.53, and the correlation between OFDI and internationalisation also has coefficient at 0.53. The maximum correlation coefficient at 0.54 suggests no threat of multicollinearity in this data. However, to avoid problems of multicollinearity, variables are mean-centred in the interaction terms (Aiken and West, 1991).

Table 4.2 presents the regression results. Model 1 includes only control variables. OFDI and all variables related to the firm's political connections are introduced in Model 2 showing the direct effects of all independent variables. Models 3-6 introduce the interaction effects between OFDI and political connections, OFDI and level of political actors, and OFDI and types of political actors, respectively. Model 7 incorporates all three interactions together.

The direct effect of OFDI is negative and statistically significant at 0.1 per cent level throughout Models 2 to 6, but loses its significance in the combined model (Model7). The negative coefficient of OFDI indicates that, on average based on this sample, OFDI hinders firms' sales. The direct effects of all variables related to political connections are, however, statistically insignificant.

The interaction effect between OFDI and political connections is negative and statistically significant in Models 3 and 7, indicating that political connections do not help firms gain higher sales from their outward direct investment. This finding hence does not support Hypothesis 1, which expects the positive effect of the firm's political connections on OFDI and firm performance. The interaction effect between OFDI and the level of political actors shows the positive and statistically significant coefficient at 1 per cent level in Model 4, but lose its significance in Model 7 when other variables related to political connections are integrated. The finding in Model 4 indicates that,

on average, the firm's OFDI can enhance its sales when firms have connections with the higher level of political actors, rather than the lower level. However, considering the inconsistent effect of the level of political actors in Models 4 and 7, Hypothesis 2, which expects that the higher level of political actors will increase the relationship between OFDI and its performance, is therefore inconclusive.

The interaction effects between OFDI and executive ties, and OFDI and legislative ties are presented in Models 5 and 6, respectively. The findings show the positive and statistically significant of the interaction effect between OFDI and both ties, indicating that both political actors from executive and legislative branches can help the role of OFDI in enhancing sales. The interaction effects of both ties are also positive and significant in the combined model (Model 7). This finding, therefore, supports Hypothesis 3, suggesting the positive relationship of OFDI and executive ties on firm performance.



**Table 4.1** Descriptive Statistics and Correlations<sup>1</sup>: Research Framework 1

	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12	13
1 Sales	628.89	3,944.26	1												
2 Firm size	6.37	1.57	0.26	1											
3 Intangible assets	59.76	394.14	0.70	0.25	1										
4 Financial leverage	0.30	0.13	0.08	0.13	0.09	1									
5 Internationalisation	0.03	0.08	0.47	0.33	0.50	0.05	1								
6 Board size	10.24	2.63	0.20	0.36	0.20	0.08	0.16	1							
7 Firm age	31.38	16.04	0.01	0.22	-0.02	0.00	0.06	0.26	1						
8 Government ownership <sup>2</sup>	0.04	0.21	0.30	0.12	0.21	0.01	0.10	0.25	0.00	1					
9 OFDI	43.16	346.03	0.15	0.17	0.53	0.05	0.53	0.13	0.03	0.16	1				
10 Political connections	0.17	0.18	0.24	0.10	0.20	0.14	0.14	0.18	0.04	0.49	0.17	1			
11 Level of political actors	1.61	1.29	0.09	0.08	0.10	0.12	0.05	0.15	0.01	0.13	0.06	0.54	1		
12 Executive ties	0.01	0.03	0.10	0.14	0.09	0.02	0.19	0.12	0.19	0.01	0.16	0.31	0.33	1	
13 Legislative ties	0.01	0.04	0.07	0.07	0.01	0.01	0.06	0.13	0.06	0.09	0.00	0.28	0.39	0.07	1

Note: <sup>1</sup> Pearson correlation coefficients are reported. Industry dummy variable is excluded.

<sup>2</sup> Dummy variable

**Table 4.2** Regression Results: Political Connections, Level, and Government Functions

VARIABLES	Sales Model1		Sales Model2		Sales Model3		Sales Model4		Sales Model5		Sales Model6		Sales Model7	
	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE
Constant	-7620***	(1206)	-2722*	(1174)	-2614*	(1166)	-2537*	(1168)	-2436*	(1135)	-2141	(1179)	-1778	(1146)
<i>Control variables</i>														
Firm size	116.4	(88.25)	81.22	(79.29)	65.90	(78.86)	96.47	(78.94)	77.00	(76.57)	98.21	(78.81)	76.79	(76.28)
Intangible assets	6.174***	(0.349)	7.290***	(0.329)	7.439***	(0.330)	7.254***	(0.327)	7.586***	(0.321)	7.468***	(0.331)	7.887***	(0.334)
Financial leverage	743.1	(910.8)	543.3	(825.6)	479.8	(819.6)	486.8	(820.2)	286.4	(798.3)	456.9	(819.1)	191.3	(792.4)
Internationalisation	7932***	(1707)	14253***	(1665)	13704***	(1662)	15005***	(1675)	13731***	(1610)	13420***	(1672)	12164***	(1718)
Board size	12.00	(49.40)	11.60	(44.59)	8.907	(44.26)	18.21	(44.35)	33.65	(43.21)	15.13	(44.23)	28.32	(42.90)
Firm age	-2.437	(7.631)	-2.755	(6.933)	-1.878	(6.887)	-3.819	(6.896)	-6.278	(6.719)	-3.982	(6.886)	-5.674	(6.680)
Government ownership	3617***	(584.6)	3378***	(601.1)	3589***	(600.7)	3377***	(597.0)	3665***	(582.3)	3221***	(598.1)	3657***	(582.3)
Industry Dummies	Included		Included		Included		Included		Included		Included		Included	
<i>Independent variables</i>														
OFDI			-4.570***	(0.405)	-3.101***	(0.635)	-10.66***	(2.182)	-6.051***	(0.458)	-4.952***	(0.420)	-3.220	(2.753)
Political connections			1294	(826.8)	1553	(825.1)	1111	(823.8)	1143	(798.8)	1109	(822.0)	1293	(797.6)
Level of political actors (PC Level)			-133.4	(103.8)	-161.7	(103.5)	-123.8	(103.2)	-48.50	(101.2)	-101.5	(103.5)	-64.76	(102.1)
Executive ties			4803	(3641)	6005	(3635)	862.6	(3873)	-7888	(4068)	1423	(3767)	-6657	(4124)
Legislative ties			3647	(2820)	3954	(2800)	2983	(2810)	2237	(2732)	2443	(2822)	1694	(2729)
<i>Interactions</i>														
H1: OFDI*Political connections					-3.208**	(1.074)							-3.477**	(1.317)
H2: OFDI*PC Level							2.551**	(0.898)					-0.559	(1.302)
H3: OFDI*Executive ties									26.29***	(4.240)			20.49***	(5.735)
OFDI*Legislative ties											43.71**	(13.94)	48.36**	(17.41)
Observations	539		539		539		539		539		539		539	
R-squared	0.584		0.669		0.675		0.675		0.692		0.676		0.699	
Adjusted R-squared	0.572		0.657		0.662		0.661		0.680		0.662		0.685	
F test	48.97***		52.47***		51.16***		51.03***		55.41***		51.29***		49.76***	

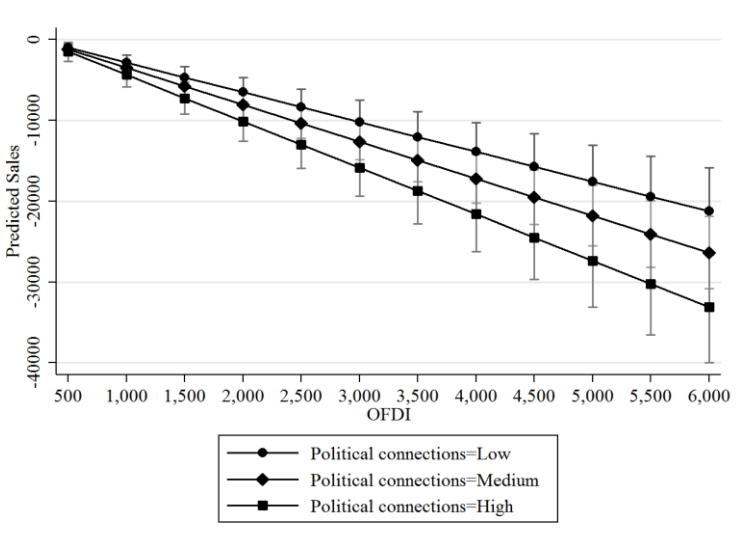
Standard errors in parentheses

\*\*\* p<0.001, \*\* p<0.01, \* p<0.05

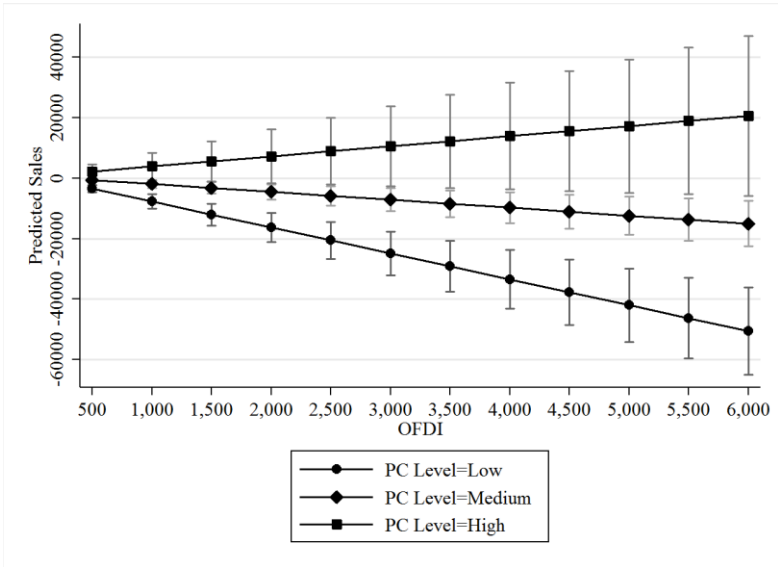
To examine these interaction effects further, in Figures 4.2 to 4.5, we graphed the results showing the marginal effects of OFDI on firm sales at different levels of each moderating variables. We classified each moderator related to political connections into three levels: low, medium, and high for the illustration. Figure 4.2 presents the marginal effects of OFDI on firm sales at different levels of political connections. This figure confirms the results that political connection negatively moderates the effect of OFDI on firm sales. Figure 4.3 shows the marginal effects of OFDI on firm sales at different levels of political actors' position. This figure clearly illustrates that the relationship between OFDI and firm sales changes from negative to positive when the level of political actors increases. Figure 4.4 provides the marginal effects of OFDI on firm sales at different degrees of executive ties. The figure confirms the results that the executive ties moderate the role of OFDI on firm sales changing negative relationship to positive relationship when the degree of executive ties increases. Figure 4.5 demonstrates the marginal effects of OFDI on firm sales at different degrees of legislative ties, therefore confirming the results that the legislative ties positively moderate the role of OFDI on firm sales.

Overall, the results confirm the role of political connections in moderating the OFDI and firm sales. However, the effect of political connections and OFDI on sales vary depending on different dimensions of political connections. The number of political connections regardless of levels and types shows a negative effect but the levels and types of government functions indicate the positive role of political connections and OFDI on sales. The results are discussed further from the perspectives of RDT in the next section.

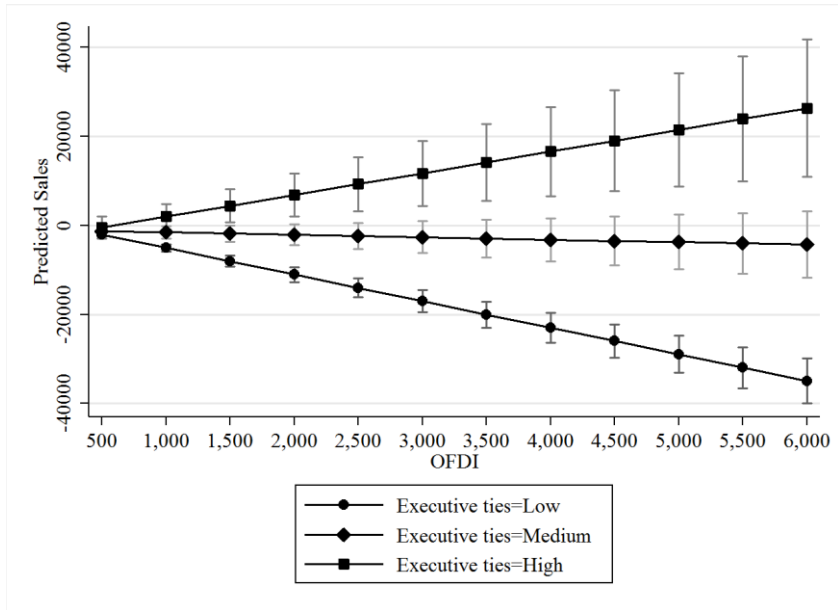
**Figure 4.2** Marginal Effect of OFDI on Firm Sales at Different Levels of Political Connections



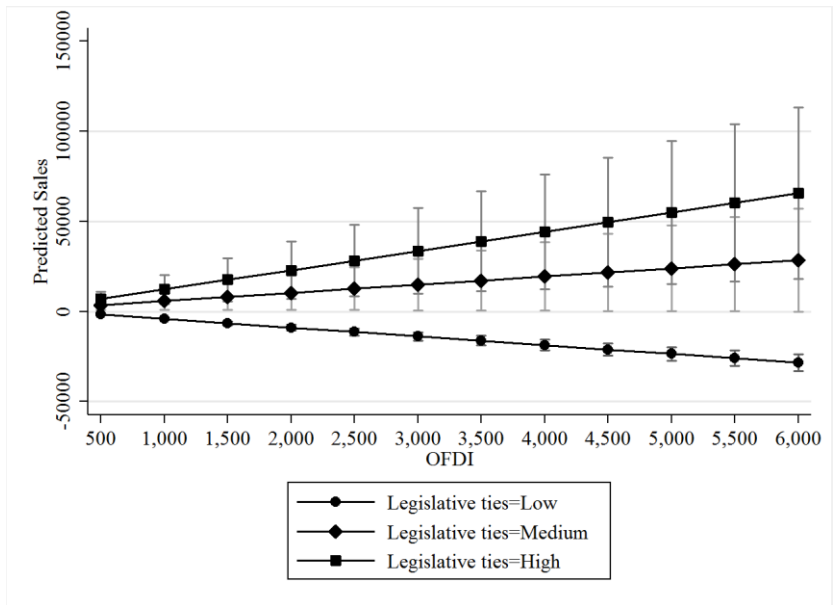
**Figure 4.3** Marginal Effect of OFDI on Firm Sales at Different Levels of Political Actors' Positions



**Figure 4.4** Marginal Effect of OFDI on Firm Sales at Different Levels of Executive Ties



**Figure 4.5** Marginal Effect of OFDI on Firm Sales at Different Levels of Legislative Ties



## 4.5 Discussion and Conclusion

Corporate political connections have been widely seen as one of the firm's resources (Frynas et al., 2006) that can help the firm increase its value (Hillman, 2005; Faccio, 2006) through various mechanisms. The political connections that the firms established in the home country are also seen as the non-market strategy that influences the firm's internationalisation, especially FDI (Wang et al., 2012). Yet, it is not clear whether the home-country political connections can transfer abroad to help the firms perform better in foreign countries that they invest in. This study investigates this value of the firm's political connections in the interaction with OFDI to influence firm performance by considering the value of the number of political connections, the hierarchical level of political positions, and the type of political actors based on the government functions.

Our results suggest that the firm's political connections have positive value on the relationship between OFDI and firm performance only with particular level and types of political actors. Connections with a high number of political actors, instead of helping firms enhance its performance from OFDI, exacerbate the negative effects of OFDI on the firm's performance. The negative effect of the interaction between OFDI and political connections on firm performance contradicts the argument of benefits of political linkages suggested by RDT. However, this can be explained from the perspectives of rent appropriation of political actors (Sun et al., 2012). As the relationship between firms and political actors lie on the relational rent (Dyer and Singh, 1998), it allows political actors to take actions that are favourable for their home organisations (Sun et al., 2012), social needs and concerns (Ramamurti, 2001), or even their personal interests (Shleifer and Vishny, 1994). The higher number of political connections, therefore, leads to the higher cost for firms rather than the benefits as suggested in RDT.

To extend and elaborate the perspectives of RDT suggesting the benefits of linkages with external organizations and the formerly inconclusive work in political connections, we argue that the effect of the firm's political connections are not homogeneous but it depends on the political positions of the connected political actors. Specifically, the political actors who have higher political positions and those

who have experiences in the executive function can benefit the firm's OFDI performance. Our results on the level of political connections show the inconclusive effect of the level of political positions. In the separated model (Model 4), the connections the firms established with the higher hierarchical level of political actors is positive as indicated in our Hypothesis 2. This positive effect of the level in the separated model supports the argument made by Wang et al. (2012) that the higher level of political actors tends to pressure firms to invest in high competitive markets to gain better outcomes and signal the success and ability of the connected political actors.

However, based on our findings, the effect of the level of political positions loses its significance in the full model (Model 7) indicating that the positive effect of higher levels of political positions is still inconclusive. There are two possible reasons that may explain why the higher level political actors may not generate more value to the firms. First, the low-level political actors engage more with the process of making regulations. De Figueiredo (2009) argues that legislators allocate rule-making ability to administrative and bureaucratic agencies because of a wide scope of law in their responsibility. These political actors, therefore, involve and engage more with government information at the same time that they are more accessible by firms. Second, the argument of power imbalance that critiques the interdependency assumption of RDT (Casciaro and Piskorski, 2005) can be applied to explain why top-political actors are not always beneficial to the firms. Political actors who have a higher political position may have higher power over the connected firms and are able to put pressure for firms to operate in the way that favours their interests. This can also support the argument about rent appropriation by the political actors to whom the firms engage with (Shleifer and Vishny, 1994; Sun et al., 2016).

The second type of political actor we focus on in this chapter is the government functions. Our finding shows that both executive and legislative ties can facilitate OFDI to enhance firm performance. Although this finding opposes our expectation that only executive ties may be useful for the firms to gain benefit from its OFDI due to the limited role of legislators in overseas activities, it supports former studies that found positive impacts of legislative ties (Zheng et al., 2017; Mahmood et al., 2017). Although government officials from the executive function mainly involve

permissions and regulations related to OFDI, legislators also engage with law and regulation making at the macro level, so they can still be able to give advice to the connected firms as well as lead firms to their socio-political networks.

The results in this chapter can offer two contributions. First, it extends IB study that previously suggested the role of political connections in facilitating the firm's OFDI (Wang et al., 2012) by providing empirical evidence to support our argument that the home-country connections can influence OFDI to affect its performance. However, the findings in this chapter illustrate that home-country political connections can facilitate OFDI to increase firm performance only when firms are connected to particular types of political actors. High-level political actors may advance the role of OFDI on firm performance, but it is still inconclusive. The executive and legislative ties that firms create with both MPs and cabinet ministers are beneficial for firms to gain positive return from its OFDI. Based on our results, this chapter can extend our understanding on the role of political connections on the internationalisation strategy in IB research by proposing that home-country political connections may worsen the firm's ability to gain return from its OFDI.

Second, this chapter extends the discussion in CPS by investigating the unique role of different types of political actors. Research in the area of CPS has recently started to compare the effect of the different types of political connections (Zheng et al., 2017; Mahmood et al., 2017; Sun et al., 2015; Okhmatovskiy, 2010) and particularly call more research on the contingent factors that can further explain the role of political connections on firm performance (Zheng et al., 2015; Sun et al., 2012). Our results in this chapter provide empirical support for the argument that political connections, in general, can be negative to the firm value when considering foreign investment strategy such as OFDI. It also shows that top-level political actors may not always generate a positive return to the firms, but top-executive and legislative ties can positively influence the firm's OFDI to generate positive return to the firms.

To extend our discussion on the contingent factors that may influence the role of political connections in facilitating OFDI to increase firm performance, we investigate the role of different types of political actors further in the next chapter by focusing specifically on political actors who are relevant to OFDI. Together with the



types of political actors, we also introduce the roles of investment location that may influence how political connections affect OFDI and firm performance in the next chapter.

## **Chapter 5**

### **Home-Country Political Resources and their Usefulness in Host Countries**

*“A firm’s ability to generate rents from resources and capabilities will depend primarily on the firm’s effectiveness in managing the social context of these resources and capabilities”*

*Oliver (1997, p.711)*

#### **5.1 Introduction**

Prior research suggests that a firm’s political resources created through government ownership and/or linkages with political actors can influence its internationalisation. The linkages with the home-country government can influence the firm’s foreign investment strategies such as mode of market entry (Meyer et al., 2014; Frynas et al., 2006), degree of subsidiary’s ownership (Cui and Jiang, 2012; Pan et al., 2014), and location choice (Lu et al., 2014; Wang et al., 2012). While these studies have considered the role of political resources on the firm’s overseas investment, it is still unclear whether and how such political resources can be used abroad and therefore influence the firm’s OFDI in enhancing its performance.

Home government can be supportive for the firm’s OFDI by providing the investment promotional policies that can help the connected firms to take investment risks and deal with uncertainties in its foreign investment (Luo et al., 2010) specifically in a particular location (Lu et al., 2014). The firm, influenced by its connected political actors, however, may not select the investment location because of economic reasons but rather for political agendas of the involved organisations or individuals (Li et al., 2013). The hidden purposes of the government affiliates in influencing the firm to choose the investment location raise the questions on how such connections help the firm’s OFDI to generate its return when the firm invests in different locations. Moreover, types of the government relations also differently influence the firm’s location choice regarding the dissimilarity of institutional

pressures and interests of the involved institutions or individuals (Wang et al., 2012). Hence, the types of affiliated political actors involving the firm's foreign investment can explain which type of political actors are more beneficial to the firm's OFDI in enhancing its performance. This chapter provides the empirical results of these two contingent factors that influence the role of the firm's political connections and OFDI on its performance.

How a firm utilises its political connections when it invests in developing and developed countries might differ. Engaging with political actors, while is widely done by firms in both developed and developing countries (Faccio, 2006; Frynas et al., 2006; Hillman, 2005), is more prominent in countries with weak institutions and particularly those that have a higher level of corruptions and imposing restrictions on foreign investments by their residents (Faccio, 2006). The imperfect markets in emerging countries (Khanna and Palepu, 1997) often pressure firms to utilise non-market strategies more than countries with strong institutions (Peng and Luo, 2000; Wright et al., 2005). The transition to opened market state of developing countries forces its domestic firms to depend more on managerial networks based on personal ties, including the political connections, as they are unable to rely on government subsidies as in the past and are unable to develop its market-based competitive resources and capabilities (Luo, 2003).

The EMNEs operating their subsidiaries in developing markets may also need to gain political support from both home- and host-country government. The connections with home government can facilitate the firm's overseas investment by providing financial access, easing the investment regulations (Luo et al., 2010), and negotiating with the host-country government (Li et al., 2013). The political advantages based on the relationship with the home government can also help the connected firm establish political linkages with the host government (Frynas et al., 2006) that can then reduce investment pressures regarding host-country regulations and increase the firm's legitimacy (Kostova et al., 2008) to operate in the host countries. With the less-developed institutional context of the developing countries that allows and requires the firms to use political connections, it is typical to expect that the firm's political connections can influence its OFDI to enhance its performance more when the firm invests its subsidiaries in the developing countries. However,

considering the different kinds of institutional pressures faced by the firm when it involves itself with the different types of government affiliates that can influence the location choice of the connected firms (Wang et al., 2012), the types of political actors are considered as important factors that can influence the firm's ability to generate return from its OFDI.

The business and government relationships can take different forms of connections ranging from the direct links of the government ownership (SOEs) to the informal connections that the firm's executive members or shareholders create through their friendship or kinship. The role of the firm's political connections based on different type of linkages on its performance is therefore distinguished. Scholars in the area of CPS have recently started to compare the effect of the different types of political linkages such as connections with central or local government, formal and informal ties, organisational or personal ties, and ties with executive or legislative officials (Zheng et al., 2017; Zheng et al., 2015; Mahmood et al., 2017; Sun et al., 2015).

One of the main arguments discussing the types of connections in previous research is the political embeddedness of the firms engaged with government through ownership in the form of SOEs and the firm connected with executive level of the government affiliates (Sun et al., 2015; Okhmatovskiy, 2010; Sun et al., 2010). These studies argue that the effects of the government involvement based on these two types are different because the linkages through ownership are more embedded in the political institutions. Hence, this type of connections puts more pressure on the firms to follow the government's agendas, violate the firm's autonomy to utilise the optimal strategies, and in turn hinder the firm's value. The connections with high level affiliates, in contrast, make firms concentrate more on developing the firm's competitive advantages because the firm's success represents the reputation of the involved political actors (Wang et al., 2012). The connections with high-level government affiliates, therefore, influence EMNEs to invest more in developed countries, compared to the SOEs that are likely to invest more in developing countries (Wang et al., 2012).

This chapter follows this stream of research by proposing and providing the empirical findings to compare the performance impact of the firm's political

connections based on political actors who can give government support for the firms related to foreign investment. The political actors included in this chapter are those who are involved with three government institutions that may provide the government supports for the firm's foreign investment, namely the government banks, the investment supporting and regulating agencies, and the ministry of foreign affairs.

The attempts to identify under which type of political actors and host-country location that makes political connections affect the firm's OFDI to advance its performance in this chapter will extend the discussion of recent research in the area of IB and CPS. Research in IB encourages us to find out which resource of the EMNEs are transferable to other countries and how much those advantages can offset the liability of foreignness that firms face in the host countries (Ramamurti, 2012). This thesis participates in this discussion by providing empirical evidence to support our argument that the firm's political resources can help firms reduce the liabilities of OFDI when EMNEs invest its affiliates in a specific investment location.

This chapter also extends RDT by considering the cross-country effects of political dependency based on the comparison of different sets of host countries that may influence the benefits of the political resources. RDT, while it explains how companies deal with external uncertainty by utilising the dependency of the firms on external organisations (Pfeffer and Salancik, 1978) expecting the benefits of the firm's interdependence, does not discuss in which circumstances that resources dependence does not yield this expected positive outcome.

## **5.2 Theoretical Background**

To understand how firm political connections influence the relationship between OFDI and firm performance, a conceptual framework is developed based on the combination of institutional theory and RDT. While institutional theory focuses on the impact of institutional factors that are difficult to change over short period (North, 1990) and firms need to conform with the institutional context (DiMaggio and Powell, 1983), RDT suggests that firms can cope with external uncertainty that may also stem from those institutional factors by managing the external environment through the linkages (Pfeffer and Salancik, 1978). In other words, firms do not only need to adapt

themselves following institutional pressures that threaten firm's operations but can change the external environment for their preferences. While there may be some environmental factors where firms might be able to manage their preferences, firms can only conform to some institutional factors, especially in the host countries. The combination of institution theory and RDT perspectives, therefore, helps us understand the interplay between the firm's political strategies and institutional context. In particular, it helps us understand the role of political resources that help firms interact with external uncertainty and the role of institutional factors that may foster or hinder the impact of external resources that the firms rely on.

### **5.2.1 Resource Dependence Theory and Political Connections**

RDT suggests that firms engage with external organisations or individuals to manage external uncertainty that may affect firms' ability to operate (Pfefer and Salancik, 1978). The external organisations or individuals to whom the firms connect can provide resources that help firms cope with issues arriving from the environment. Political actors are one of the external actors that firms can engage with to gain resources related to the government. The benefits of linkages with political actors by appointing them to the board may come in the form of information, support, a channel of communications and legitimacy (Hillman, 2005).

Firms can gain support from the government or political actors when they invest its affiliates overseas in various forms. Information that firms can get from linkages with political actors that may benefit the firm's OFDI may come in the form of information related to investment regulations in both the home and host country; information that is related to the host country that may not be publicly available. Firms can also have a channel of communication (Hillman, 2005) to the host government by linking them with the political actors, so firms can give political actors information that may favour firms (De Figueiredo, 2009) in their overseas investment. Support can be in the form of permission to invest abroad due to the government role in regulating overseas investment (Voss et al., 2010), to provide a lower-rate loan from government financial institutions (Buckley et al., 2007). To a certain extent, the firms can also get a certain level of legitimacy from their political connections (Hillman, 2005). The firm's legitimacy can help the firms gain more autonomy to operate in the host country and reduce the intervention by the host government or host communities.

All these benefits can ease the internalisation process of firms, but how these benefits will help firms perform in the different institutional setting is needed to be understood through the institutional perspectives.

While RDT discusses the interactive actions of organisations upon the external factors, it does not focus on whether resources can be leveraged in the same manner under the different institutional context. We integrate institutional perspectives and discuss in the next section to understand the role of political resources in different institutional host countries.

### **5.2.2 Institutional Based View and Internalisation of EMNEs**

Institutions are defined by North (1990:3) as “the humanly devised constraints that shape human interaction”, and it is more commonly known as formal and informal rules in society that can be classified into regulative, normative, and cognitive structures and activities (Scott, 1995). Institutions construct political, economic, and social relationships in society (Chan et al., 2010). By taking institutional perspectives, socially constructed factors such as norms, custom, or habit are also considered as being able to influence the decisional choices (Oliver, 1997) of the firms. Non-economic institutions can also be resources for problem-solving of economic coordination (Jackson and Deeg, 2008) and can influence the development of firm’s resources and strategies (Wan, 2005). Institutions can affect economic performance through the exchange and production costs of firms (North, 1990). From two types of the production cost of the firms which are transformation costs and transaction costs (Yasar et al., 2011), the transaction costs tend to be more influenced by institutional factors (Aron, 2000). In the society that institutions are well established, institutions will help to decrease uncertainty, which will then reduce transaction cost (North, 2005).

Considering home country institutions, they affect the actions and competitiveness of firms by shaping firm strategies, operational practices and local perception of firms (Chacar et al. 2010; Mezias 2002). Previous research has shown that strong home country institutions will generate firm capabilities that firms can leverage when investing abroad (Chacar et al., 2010) such as the familiarity to deal with the legal system to protect property rights (Hoskisson et al., 2005; Wan and

Hoskisson, 2003), the guidance for firms to compete successfully in international markets (Chacar et al., 2010) and the access to potential executives and employees (Brouthers et al 2005; Wan and Hillman 2006). Therefore, home country institutions can shape firm strategies that link to firm competitiveness.

In emerging economies, institutional development is relatively weak because institutional rules are absent, insufficient, or poorly enforced (Hitt et al., 2004; Hoskisson et al., 2000; Khanna and Palepu, 1997). A lack of reliable market information, efficient intermediary institutions, predictable government actions, and an efficient bureaucracy creates institutional voids (Khanna and Palepu, 1997, 2000), which increase transaction cost in emerging markets. Transaction cost is high in weak institutions because underdeveloped institutions create a higher risk of unenforceable contracts and insecure property rights leading firms to adopt poor technology and thus operate less efficiently and competitively (North, 1990). It can also reduce competitive pressures among firms because of less well-developed antitrust regulations and greater industry concentration (Chacar and Vissa, 2005). To fill those institutional voids, emerging-market firms need to create their firm-specific advantages that can deal with underdeveloped institutions such as business group (Khanna and Palepu, 1997) or social networks (Peng and Luo, 2000). Weak institutional factors in emerging markets that are typically recognised as a disadvantage can turn into advantages for the emerging-market firms when they invest in countries with similar institutions (Cuervo-Cazurra and Genc, 2008).

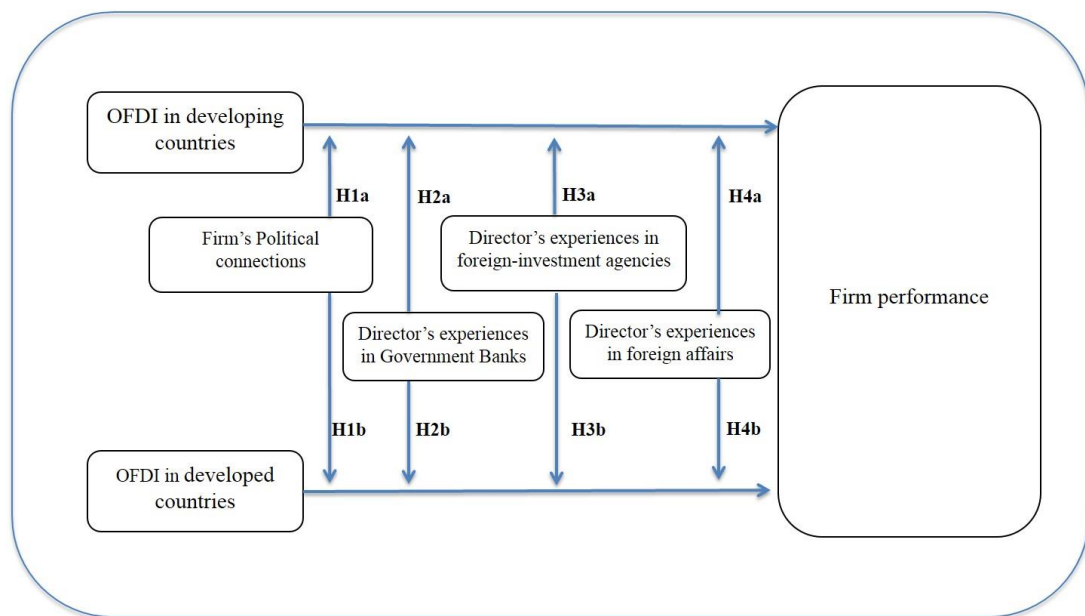
### **5.2.3 The Combination of RDT and IT**

Both IT and RDT are concerned with the relationship between organisations and the external environment. However, a firm's strategic reaction toward the external environment based on these two theories are different as firms are more passive, conformed, and accepting based on IT, but active, resistant, and manipulative based on RDT (Oliver, 1991). These differences stem from opposing perspectives on the external environment in the two theories. IT considers the external environment in the form of institutional factors that shape rules and belief in society (Scott, 1987) so that they are more difficult to change. RDT, in contrast, perceives the external environment as external organisations which control rare resources, so external organisations for RDT are manageable (Pfeffer and Salancik, 1978).



With these dissimilarities in the perceptions of these two theories towards external environment that lead to distinctive reactions by involved parties including firms, the combination of these two theories will help us to understand the reactions of firms when they apply political strategies without losing the perspectives of institutional constraints that are embedded in both home and host countries and not enable firms to manage with. By using RDT to guide our understanding on how firms' political strategies help them manage their external uncertainty stemming from the government that may lead to higher firm performance, we can understand how firms manage resource flows from the government. At the same time, with the incorporation of IT, we can elaborate on when institutional constraints play a role and firms no longer manipulate or control the external environment. Based on these two theoretical perspectives, we propose the second research framework illustrated in Figure 5.1.

**Figure 5.1** Research Framework 2: Political Resources and Investment Location



In Figure 5.1, we separate OFDI value into two independent variables based on the types of the host countries. These two independent variables are OFDI in developing countries and OFDI in developed countries. We then establish direct effect between each independent variable and firm performance as our baseline relationship. Four moderating factors are then added to the model to test four main hypotheses focusing on the firm's political connections, director's experiences in government

banks, director's experiences in foreign-investment agencies, and director's experiences in foreign affairs. The influence of each moderating factor is then tested against two baseline relationships which are OFDI in developing countries and firm performance and OFDI in developed countries and firm performance. The moderating factors influencing OFDI in developing countries and firm performance are represented by H1a, H2a, H3a, and H4a respectively and the moderating factors influencing OFDI in developed countries and firm performance are represented by H1b, H2b, H3b, and H4b respectively. The development of hypotheses is discussed in the next section.

## **5.3 Hypothesis Development**

### **5.3.1 The Effect of Political Connections by Host Countries**

In contrast to RDT that disregards locational impacts, institutional theory value the dissimilarity of the social context that may influence the firm's ability to generate rent in different ways (Oliver, 1997). Considering that the firm's political behaviours occur when the market is imperfect (Boddeyn and Brewer, 1994), the firm's ability to leverage its political resources should be diverse in host countries that have different levels of institutional development. Weak institutions in developing countries are likely to create failures in the capital, labour, and product markets as well as to increase the level of government regulations and interventions (Khanna and Palepu, 1997). This institutional context encourages firms to incorporate non-market strategies as a response to the weak institutions (Peng and Heath, 1996). The firm's political connections, therefore, are more important in less-developed institutional contexts (Luo, 2001) as shown in the empirical study based on the sample across 47 countries by Faccio (2006) that political connections are more common in countries with higher level of corruptions.

Within the promising environment for the firm's political strategies, a firm can leverage its home-country political connections through various mechanisms. First, the politically connected firm can develop communication channels (Hillman, 2005) based on its political networks to obtain information regarding the foreign investment in both the home and host-country. Not only do weak institutions in developing

countries enlarge the uncertainty of government regulations and business transactions, but it also creates information asymmetry. So, the connections with the home-country political actors will keep the firms informed when any change occurs even in the subsequent stage of OFDI. Moreover, the connected firm can use channels of communication with political actors to deliver its information to relevant organisations (De Figueiredo, 2009) such as home- and host-country regulators or potential business partners in the host country. The connections with political actors allow firms to pass information to connected political actors, which may later benefit firms in forms of favourable regulations or potential business partnership with the host-country government organisations.

Second, the connections with the home-country government allow firms to gain government supports in their overseas investment. RDT suggests that the linkages that the firm establishes with external actors create the commitment for supports from the connected organisations (Pfeffer and Salancik, 1978). The home-country government's supports for the OFDI can be in the form of investment incentives such as lower-interest rate loan, or tax reduction (Luo et al., 2010). The home-country government can also play a significant role in bargaining with the host-country government for the potential FDI projects (Li et al., 2013; Ramamurti, 2001). Furthermore, the home-country political connections can also lead the firm to socio-political networks in the host country. Networking with government officials in the host country will help the firm reduce bureaucratic processes by bypassing rules and reducing market uncertainty especially in the weak institutional context (Luo, 2001). The connections with home-country political actors, therefore, guide the firm to government support regarding foreign investments in both home and host country.

Third, a firm associated with a home-country government may signal credibility in developing countries where institutional settings approve the government connections. RDT suggests that the firm's political strategy is beneficial for the organisational legitimacy (Pfeffer and Salancik, 1978), but this is debatable. The involvement with home-country government may be perceived in diverse ways depending on specific cases and context. In some cases, the relationship with the government can reduce political risks in a foreign location because the host government will reduce pressure on connected firms to preserve diplomatic

relationships (Contractor, 2013; Alden and Davies, 2006). In contrast, SOEs have been documented in several studies (Cui and Jiang, 2012; Meyer et al., 2014) of facing limitations in foreign investment strategies due to the perceptions of the host country on SOEs. However, considering the institutional context in developing countries that require domestic firms to rely on political networks (Peng and Luo, 2000), the firm's political connections may be more acceptable. This, therefore, gives the connected firms the organisation legitimacy to operate in the developing countries with less intervention from host-country communities.

Moreover, considering the EMNEs, in particular, the benefits of political connections may also derive from the similarity of home and host institutional settings. The experience of less-developed institutions in the home country may enable the EMNEs to deal with institutional voids and manage its operations better in less-developed countries (Holburn and Zelner, 2010; Cuervo-Cazurra and Genc, 2008). So, the political networks of the EMNEs can facilitate them to develop knowledge and increase the richness of information that helps them in emerging markets (Wright et al., 2005; Koka and Prescott, 2002).

With all the benefits that firms can leverage from their home-country political connections to deal with market imperfections in the host-developing country, the politically connected firm can reduce its transaction cost stemming from poor institutions such as a cost of information or a cost of enforcement of a contract. As it is shown in previous empirical research (Li et al., 2008), the connections with politicians in China influence the firm's performance more significantly in the less liberal market in contrast to the less value of the connections in the developed markets. Hence, the firm's political connections should benefit the connected firm when investing in host-developing markets as in the following hypothesis:

***Hypothesis 1a:** The relationship between OFDI in developing countries and firm performance is more positive for a firm with a higher ratio of politically connected directors.*

In contrast, in developed countries where the institutional system, financial, capital and labour markets are more developed (Khanna and Palepu, 1997), firms are required to rely more on the market system. The legal and institutional system in

developed countries that protects intellectual property rights or limits the collusion between firms may also curtail the advantages of social networks (Wright et al., 2005) in developed countries. Within a context that highly relies on market competition, the firms that are used to leveraging non-market strategies such as political connections may not be fully aligned with the institutional context in the host-developed countries. Moreover, social capital can have a negative influence on knowledge development when firms are restricted to only social capital without learning new ideas and knowledge (Wright et al., 2005; Nahapiet and Ghoshal, 1998). Firms that are used to exploiting political connections may not be able to quickly adapt their competitive strategies that help them explore new knowledge, resources and capabilities for their long-term advantage.

Although previous studies suggest that firms with a higher level of government affiliation are likely to invest in developed countries (Wang et al., 2012) due to the normative pressures that drive the firm to increase its competitiveness and capabilities in large developed markets (Ramamurti, 2012) and the coercive pressures of the firm's political affiliations to develop innovation because investment in developed countries can signal success and creditability to the home government (Yamakawa et al., 2008), this may not apply to the firm's performance, particularly in the short period of time of OFDI.

Considering the benefits of information and advice that firms may gain from their connected directors (Hillman, 2005), even though information asymmetry also exists in developed markets, information is relatively readily available through the market system and more predictable, so the benefits of information that firms can gain from their political connections may be less compared to developing host countries. Further, the organisational legitimacy that may enhance the performance of connected firms in the developing country may impact reversely in developed countries because sources of legitimacy in developed countries might be different from developing countries. In developed countries, the firm with political connections may be treated as a government-related organisation that may be harmful to the host country especially if the firms involved with the government through its ownership as shown in the study on SOEs. The firm's political connections, therefore, cannot help firms reduce their liability of foreignness and may worsen the firm's performance in

developed countries. Hence, we expect the firm's political connections will worsen the effect of OFDI on the firm's performance as suggested in the next hypothesis.

***Hypothesis 1b:** The relationship between OFDI in developed countries and firm performance is more negative for a firm with a higher ratio of politically connected directors.*

### **5.3.2 Political Actors Related to Government Banks**

The linkages that a firm establishes with external organizations through the board of directors can provide the firm with a commitment of supports from the connected organisations (Pfeffer and Salancik, 1978). A financial institution is one of the crucial targets for a firm's co-optation that leads the firm to financial supports (Pfeffer, 1972). Financial benefits have been documented as the consequences of the firm's political connections in previous studies in the form of access to bank loans (e.g. Su and Fung, 2013; Boubakri et al., 2012a; Claessens et al., 2008) with lower interest rate (Khawaja and Mian, 2005) or less collateral required (Charumilind et al., 2006).

In the internationalisation process, financial supports by the government can also encourage the firm's overseas expansion, as illustrated by previous studies that the funding and cheap loan given by the Chinese government influence the OFDI decision of Chinese firms (Voss et al., 2008; Luo et al., 2010). The association with financial institutions through political actors who have experiences in the government institutions could therefore lead the connected firm to financial access that is beneficial to its OFDI. The financial support that the connected firm gains through the linkages may also carry on to the stage after the firm's OFDI, especially when the firm needs to increase its capital or raise funds for its further expansion. However, by applying institutional perspectives, the significance of financial support may vary between developing and developed countries due to the development of institutional factors. In a country that has a less-developed financial market, the alternative source of funds such as government loans may be seen as a substitution for firms (Buckley et al., 2007). The impact of political actors related to government banks on the firm's performance should also be different.

In developing countries where capital market is less developed (Khanna and Palepu, 1997), the alternative source of fund such as funding within the business group

or government banks are more essential to the firm than in developed countries. When the firm invest in developing countries, the linkages that the firm established with financial institutions in the home country can then become beneficial to the connected firm. The connections with political actors who have experiences in government banks are likely to help firm's access to capital more than firms without connections. In contrast, developed countries have more developed financial markets (Khanna and Palepu, 1997) which allow firms operating in these countries to have less dependency on the alternative sources of capital.

The dependency of the firm on the alternative source of funding in its OFDI's location plays an important role to the different level of the firm's performance. While political connections may lead the firm to financial access in less developed countries, the greater access to higher level of bank loans does not guarantee that the firm will have higher profits. Previous empirical studies show that politically connected firms that gain access to higher bank loan have poorer performance compared to non-connected firms (Duchin and Sosyura, 2012). The firm's higher leverage can lead to lower financial performance because the firm with easier access to financial fund tend to invest in more risky investment projects or in lower-quality assets (Boubakri et al., 2013) and have lower risk efficiency or lower asset quality (Liang et al., 2013). Moreover, the higher leverage of the connected firm may also have higher default rate (Khwaja and Mian, 2005) and higher cost of debt due to the higher risk of assets (Bliss and Gul, 2012). In line with this reason, it can be expected that the firm's connections established with political actors who have experiences in government banks will hinder firm's capabilities, especially in the global competition. Hence, in a developing-host country where the financial market is underdeveloped, the linkages with the government banks that help the firm in its OFDI may affect its performance negatively. On the other hand, the investment expansion of the firm in developed countries may pressure the firm to gain more competitiveness and capabilities in order to gain financial access in a developed capital market, and lead the firm to have fewer lower-quality assets, less financial cost, and perform better.

We then hypothesise that the firm engaging with political actors who have experiences in government banks are more likely to have lower performance when they invest its subsidiaries in developing countries. In contrast, the firm with political

actors who have experiences in government banks are likely to have more positive performance when they invest its subsidiaries in developed countries.

***Hypothesis 2a:** The relationship between OFDI in developing countries and firm performance is more negative for a firm with a higher ratio of directors who have experience in government financial institutions.*

***Hypothesis 2b:** The relationship between OFDI in developed countries and firm performance is more positive for a firm with a higher ratio of directors who have experience in government financial institutions.*

### **5.3.3 Political Resources Related to Foreign Investment**

Linkages with external organisations create interdependency between firms and the external organisations that will reduce external uncertainty arising from the linked organisations (Pfeffer and Salancik, 1978). Scholars in RDT suggest that firms can obtain preferable regulations by appointing outside directors who have socio-political power that can influence regulatory body membership (Pfeffer, 1972), which makes firms in the regulated industry have more politically connected directors (Hillman, 2005). In the process of OFDI, firms need to deal with both home and host-country regulations involving the overseas subsidiaries arrangement (Buckley et al., 2007; Cui and Jiang, 2012). In the home country, firms need to deal with government agencies that regulate overseas transactions by a local firm to restrict the capital outflow (Voss et al., 2010). Apart from regulatory roles, government agencies in the home country can also act as the OFDI promoting agencies (Luo et al., 2010). Research focusing on emerging countries, China in particular, found that the home-country government can act as an investment promoter who gives support to firms to invest overseas because OFDI can be a mechanism for knowledge spillovers that help emerging-market firms gain more capabilities and a competitive advantage (Luo et al., 2010). The regulatory and supporting agencies that are related to foreign investment are therefore crucial external organisations that firms may consider to engage with for favourable regulations, government permissions, and support.

By appointing political actors on the board, firms will have a channel of communication that they can communicate their information to and get information



from those politically connected directors (Hillman, 2005). Government agencies, administrative agencies in particular, do not only deal directly with regulations and promotions for OFDI, but they are also required to contact stakeholders to whom the new regulations have an impact (De Figueiredo, 2009). Hence, political actors in administrative agencies or regulators themselves are good means that firms can leverage to communicate their information for their preferable policy or regulations (De Figueiredo, 2009). Firms that can manage their relationships with government agencies engaging in foreign investment, therefore, can leverage their relationships to reduce processes in dealing with government regulations and facilitate the internalisation process of firms.

With the benefits that facilitate the firms' OFDI, it is expected that firms will leverage these benefits after its investment and gain more competitive advantages than non-connected firms. However, with different levels of institutional development in host countries, the effects of connections might be varied among developing and developed countries. The benefits that connected firms can get by having a channel to communicate their information to regulators as well as receiving information from investment promotions are not limited only to the pre-investment stage. As government agencies do not engage directly in the real situation, especially in the host countries, they also need insights from the firms to improve their existing regulations. This allows firms to communicate their problems or limitations regarding government regulations. Firms can use this channel of communication to influence regulators for their favourable policy or regulations (De Figueiredo, 2009).

Likewise, supports that firms can get from investment promotional agencies regarding the host country are also beneficial to firms after they invest their subsidiaries. In general, information about host countries is not privileged to some firms, so the benefits that these promoting agencies can provide to the connected firms may not override non-connected firms. However, if we take into account the institutional factors in the host countries, the benefits of host countries that connected firms can obtain from these promotional agencies should be more important in the country that information is not equally accessible. In host developing countries where markets are not well operated, asymmetric information is more critical than in host developed countries, so firms are required to get information from other sources such

as home-country investment supporting agencies. Hence, it is hypothesised that firms with connections to government officials from foreign-investment regulating and supporting agencies can gain more benefits from its investment in developing countries than non-connected firms. In contrast, in host developed countries where institutions are more developed and information is more equally accessible without the assistance of non-market factors, the connections with those foreign-investment related directors may not help the firms improve its performance.

***Hypothesis 3a:** The relationship between OFDI in developing countries and firm performance is more positive for a firm with a higher ratio of directors who have experienced in government agencies relating to foreign investment.*

***Hypothesis 3b:** The relationship between OFDI in developed countries and firm performance is more negative for a firm with a higher ratio of directors who have experience in government agencies relating to foreign investment.*

#### **5.3.4 Benefits of Diplomatic Experience**

The government positions involved directly with both business and political activities in foreign countries are diplomatic positions. Unlike other government officials that mostly deal with internal affairs in the home country, diplomatic representatives such as diplomats or ambassadors are home-government officials who engage with foreign affairs and are posted overseas. Their duties and working experiences in foreign countries therefore equip them with specific kinds of resources and knowledge that ultimately becomes the exceptional social capital. While the main concerns of diplomatic representations previously were international politics, their roles nowadays concentrate more on business interests such as trade and investment promotions in the form of commercial diplomacy (Lee and Hudson, 2004). The term commercial diplomacy can be defined as the use of diplomat means to promote business activities between the home and host country (Kostecki and Naray, 2007). The main objective of the commercial diplomacy is to develop business opportunities such as international trade and inward investment, but it can also support outward

investment by firms from the home country of the diplomats of the local firms (Rana and Chatterjee, 2011). With the promoting role of the commercial diplomacy that requires them to establish networks and credibility (Rana and Chatterjee, 2011) engaging with socio-political elites in the host country, they are therefore a principal source of information, networks, and legitimacy that can be beneficial to the firm connecting to these diplomats.

By appointing a former diplomatic representative to the board of directors, a firm can get access to information and insights about particular foreign countries that the appointed director was once posted as a diplomat or an ambassador. While typically general information about the host country is publicly available for any firm that is interested in investing its subsidiaries in that country, some relevant information and insights are accessible and shared only among privileged groups of people. Moreover, political actors experienced in foreign affairs are also familiar with host-country informal institutions that are hard to realise for foreigners or outsiders without direct experience through living in the country or working with the locals. Hence, political actors who have experiences in foreign affairs such as diplomats, foreign ministers, and consuls are of benefit for the firms when they invest their subsidiaries overseas. The important role of government officials in foreign affairs is documented by a former study using case studies of Daewoo group to illustrate that two former American foreign ministers are appointed as business advisors for socio-political activities in Europe (Hadjikhani et al., 2008).

Moreover, political actors who are experienced in foreign affairs can give some supports for the connected firms based on their socio-political networks they built when they were posted in foreign countries. The socio-political networks of diplomacy representatives can be introduced to the connected companies; the networks may include political elites in the host country and business partners such as suppliers or customers for connected firms. Besides, in the process of OFDI, companies may need to negotiate or bargain with the host-country government (Ramamurti, 2001), the connections that businesses have with diplomats can be helpful as it puts the connected firms in a better position than non-connected firms based on the networks and credibility that the ambassador can provide to the connected firms. Besides, with their socio-political networks, they can provide firms

a channel of communication with the host-country public agencies and business partners. When firms encounter any issues or problems with the other organisations in the host countries, this support that firms can get from the connected directors can help firms to reduce some operational costs, and in turns, gain higher performance. In comparison to the government officials whose duties and responsibilities are mainly focused on internal affairs, such as the national military, these political actors may not have an impact on the firms in foreign countries. The legitimacy of some political positions that can positively affect the firm's performance of politically connected firms in the countries of origin (Pfeffer and Salancik, 1978) may not transfer across the border even if they hold the executive level. The responsibility in the internal affairs of those political actors can also threaten the firms tied to them in foreign countries because the political actors with a lack of international preferences may concern themselves with benefits of the home country more than the interest of the firms in foreign countries.

Taking the institutional context of the host country into account, the benefits of the linkages with political actors who have experiences in foreign affairs might be more valuable in developing countries than in developed countries. Owing to the institutional voids and underdeveloped markets leading to 'a severe dearth of information' (Khanna and Palepu, 1997, pp.41-42) in developing countries, the benefits of the connections with political actors who have direct experiences in the host-developing can be leveraged by the connected firm better than in developed countries. The lack of public information in developing countries in the product market and capital market in developing countries (Khanna and Palepu, 1997) lead to both operational and transactional cost that the firm need to deal when investing its subsidiaries in the developing countries. The connections with political actors who are familiar with the formal and informal institutions of the host country can bypass costs that may occur from the lack of information. The lack of information in developing countries is not presented only in product or capital market, but it also lead to the lack of information in general that create the information asymmetry for everybody who cannot access the inner circle of society. The connections with diplomats or ambassadors who have more opportunities to access the socio-political elites in the host country can therefore give access to the information of the inner

circle. The focal firm operating its subsidiaries in the host developing countries therefore encounters the liabilities of foreignness and liabilities of outsiders (Johanson and Vahlne, 2009). With the connections the firm have with political actors from home country who have direct experiences and networks in the host country, the firms therefore can benefit from its inner circle of the connected political actors. Moreover, regulations in the host-developing countries that are hard to predict also lead to the benefits that the connected firms may gain over non-connected firms.

***Hypothesis 4a:** The relationship between OFDI in developing countries and firm performance is more positive for a firm with a higher ratio of directors who have experience in foreign affairs.*

In the host-developed countries, while the institutional context is not as weak as in developing countries, access to privileged networks of diplomats and ambassadors of the connected firms should still be beneficial. Unlike other types of home-country political actors that are based in the home country, the presence of political actors with experiences in foreign affairs in the host country can link them to business and political actors in the host countries. The political resources that diplomatic representatives can give to the connected firms are not only information that helps the firm deal with the external uncertainty, but also the networks of socio-political elites that the connected firms can inherit from this particular type of political actors. Within a developed institutional context, the benefits of the connections with political actors in foreign affairs can still present because the firms can use their connections with diplomats or ambassadors as the channels of communication to the host-country government. The firms can use their connections to relay their information to the regulators or government officials. The networks that diplomats have within the host country therefore help the connected firms to reduce liabilities of foreignness and being an outsider in the host country.

In addition, the firm connected to diplomats or ambassadors can also be realised with the informal institutions in the host country that allow firms to be able to conform to the institutional context of the host country. In this case, even the institutional context is not underdeveloped, or in developed countries, the informal institutions that are difficult for foreigners to recognise may also present. So, the

connections with the political actors who have direct experiences in the host country should help the firms to align with the host-country institutions. Hence, we hypothesise that connections that the firms established with government officials whose positions relate to foreign activities affect firm's performance positively when the firm's invest its subsidiaries in both developing and developed countries.

***Hypothesis 4b:** The relationship between OFDI in developed countries and firm performance is more positive for a firm with a higher ratio of directors who have experience in foreign affairs.*

## **5.4 Empirical Results**

To test the hypotheses, we use data and research method as described in Chapter 3 to test our research framework. Table 5.1 provides descriptive statistics and correlation of all variables used in this chapter. Overall, the correlations among the independent variables are fairly low. This indicates that multicollinearity is not a serious problem in this data. However, variables are mean-centred in the interaction terms to avoid problems of multicollinearity (Aiken and West, 1991).

Table 5.2 presents the regression results of the analysis. Model 1 includes all control variables. OFDI in both developing countries and developed countries, and all variables related to the firm's political connections are presented in Model 2 giving the direct effects of all independent variables. Models 3 to 6 introduce the interaction effects between OFDI in different host-country locations and different types of political connections. Model 7 integrates all interactions together.

The direct effect of OFDI in both developing and developed countries are negative and statistically significant at 5 and 0.1 per cent level, respectively. However, only the direct effect of OFDI in developing countries that is negative and statistically significant throughout the estimated models (Models 2 to 7). The direct effect of OFDI in developed countries loses its significance in some of the models (Models 3 and 7) after the introduction of the interaction terms, implying that the direct effect is not always strong. The negative coefficient of OFDI indicates that, on average based on this sample, OFDI in both developing and developed countries constrain firm sales.

The direct effects of all variables related to political connections are, however, statistically insignificant.

Model 3 presents Hypotheses 1a and 1b concerning the interaction effects between OFDI in both host-country location and political connections (PC). The interaction effect between OFDI in developing countries and PC is positive and statistically significant ( $b=18.74$ ,  $p<0.001$ ), but the interaction effect between OFDI in developed countries and PC is negative and statistically significant ( $b=-8.753$ ,  $p<0.001$ ). This indicates that political connections help firms to enhance its sales in developing countries, but deteriorate its sales when firms invest in developed countries. This finding hence supports both Hypotheses 1a and 1b, suggesting that the firm's political connections will enhance the firm's performance when firms establish their subsidiaries and affiliates in developing countries and will decrease the firm's performance when the firm's OFDI is in developed countries. These relationships are consistent in the combined model (Model 7).

**Table 5.1** Descriptive Statistics and Correlations<sup>1</sup>: Research Framework 2

	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1 Sales	628.89	3944.26	1													
2 Firm size	6.37	1.57	0.26	1												
3 Intangible assets	59.76	394.14	0.70	0.25	1											
4 Financial Leverage	0.30	0.13	0.08	0.13	0.09	1										
5 Internationalisation	0.03	0.08	0.47	0.33	0.50	0.05	1									
6 Board size	10.24	2.63	0.20	0.36	0.20	0.08	0.16	1								
7 Firm age	31.38	16.04	0.01	0.22	-0.02	0.00	0.06	0.26	1							
8 Government ownership <sup>2</sup>	0.04	0.21	0.30	0.12	0.21	0.01	0.10	0.25	0.00	1						
9 OFDI in developing countries (NDC)	16.67	109.27	0.24	0.26	0.29	0.07	0.74	0.17	0.12	0.06	1					
10 OFDI in developed countries (DC)	26.50	299.92	0.09	0.10	0.50	0.03	0.34	0.09	-0.01	0.17	0.27	1				
11 Political connections (PC)	0.17	0.18	0.24	0.10	0.20	0.14	0.14	0.18	0.04	0.49	0.15	0.15	1			
12 Government-bank related directors (GBD)	0.02	0.07	-0.01	-0.02	-0.02	-0.08	-0.02	-0.05	-0.02	-0.01	-0.03	-0.02	-0.03	1		
13 Foreign-investment related directors (FID)	0.02	0.06	0.04	-0.03	0.03	0.04	-0.02	-0.06	-0.08	-0.01	-0.05	-0.03	0.03	0.24	1	
14 Foreign-affairs related directors (FAD)	0.01	0.02	0.18	0.03	0.11	0.01	0.08	0.11	0.03	0.16	0.05	0.00	0.33	0.00	0.01	1

Note: <sup>1</sup> Pearson correlation coefficients are reported. Industry dummy variable is excluded.

<sup>2</sup> Dummy variable



**Table 5.2** Regression Results: Types of Political Actors and Host-Country Location

VARIABLES	Sales Model1		Sales Model2		Sales Model3		Sales Model4		Sales Model5		Sales Model6		Sales Model7	
	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE	Coef.	SE
Constant	-7622***	(1205)	-2844*	(1212)	-2375*	(1135)	-2409*	(1202)	-2767*	(1145)	-2344*	(1180)	-1812	(1030)
<i>Control variables</i>														
Firm size	116.4	(88.25)	91.68	(79.24)	56.65	(74.35)	84.88	(78.29)	76.40	(74.88)	82.60	(76.82)	37.41	(67.14)
Intangible assets	6.174***	(0.349)	7.242***	(0.341)	7.628***	(0.323)	7.304***	(0.338)	6.588***	(0.334)	7.321***	(0.331)	6.719***	(0.308)
Financial leverage	743.1	(910.8)	374.0	(828.9)	454.7	(776.5)	280.3	(819.0)	332.2	(783.4)	365.4	(804.0)	309.9	(701.2)
Internationalisation	7932***	(1707)	13545***	(2163)	18573***	(2120)	13019***	(2157)	12800***	(2074)	13421***	(2100)	17321***	(2067)
Board size	12.00	(49.40)	9.212	(44.58)	36.65	(41.88)	1.575	(44.13)	18.84	(42.15)	20.13	(43.47)	30.76	(37.94)
Firm age	-2.437	(7.631)	-0.964	(6.880)	-5.201	(6.489)	1.444	(6.823)	1.103	(6.507)	-3.161	(6.783)	0.641	(5.920)
Government ownership	3617***	(584.6)	3374***	(583.5)	3786***	(550.2)	2986***	(584.8)	3242***	(551.4)	3186***	(575.3)	3102***	(509.9)
Industry Dummies	Included		Included		Included		Included		Included		Included		Included	
<i>Independent variables</i>														
OFDI in developing countries (NDC)			-3.521*	(1.408)	-15.08***	(2.055)	-3.107*	(1.395)	-3.413*	(1.336)	-5.685***	(1.477)	-13.70***	(2.196)
OFDI in developed countries (DC)			-4.577***	(0.444)	-0.639	(0.707)	-4.741***	(0.440)	-4.085***	(0.425)	-4.591***	(0.434)	-0.663	(0.643)
Political connections (PC)			910.6	(712.9)	540.7	(676.5)	1079	(706.0)	851.3	(675.5)	606.7	(699.5)	593.1	(613.8)
Government-bank related directors (GBD)			-223.1	(1527)	-276.8	(1429)	-831.3	(1602)	-887.1	(1445)	-681.1	(1485)	219.9	(1381)
Foreign-investment related directors (FID)			1098	(1775)	751.3	(1661)	1503	(1758)	226.1	(1687)	1299	(1721)	-200.6	(1519)
Foreign-affairs related directors (FAD)			7146	(4451)	2763	(4197)	3544	(4493)	6651	(4206)	837.5	(4454)	-1325	(3892)
<i>Interactions</i>														
H1a: OFDI in NDC*PC					18.74***	(2.816)							17.62***	(4.483)
H1b: OFDI in DC*PC					-8.753***	(1.240)							-7.658***	(1.139)
H2a: OFDI in NDC*GBD							-114.6	(59.33)					-499.0***	(106.3)
H2b: OFDI in DC*GBD							123.8***	(31.91)					285.2**	(97.25)
H3a: OFDI in NDC*FID									764.4***	(95.50)			1017***	(99.35)
H3b: OFDI in DC*FID									-236.6**	(79.00)			-253.6***	(70.71)
H4a: OFDI in NDC*FAD											90.09***	(26.55)	30.13	(45.10)
H4b: OFDI in DC*FAD											127.3***	(32.49)	-151.9	(100.3)
Observations	539		539		539		539		539		539		539	
R-squared	0.584		0.669		0.712		0.679		0.706		0.691		0.768	
Adjusted R-squared	0.572		0.656		0.699		0.664		0.693		0.677		0.755	
F test	48.97***		49.84***		55.23***		47.32***		53.80***		49.97***		58.10***	

Standard errors in parentheses

\*\*\* p<0.001, \*\* p<0.01, \* p<0.05

Model 4 denotes Hypotheses 2a and 2b regarding the roles of directors with experience in government banks (GBD). The results show a positive and statistically significant coefficient of the interaction between OFDI in developed countries and GBD, but the statistically insignificant coefficient of the interaction between OFDI in developing countries and GBD. This finding indicates that, on average, the firm's connections with political actors who have experience in government banks can enhance firm's sales only when the firm invests its subsidiaries in developed countries, but the government-bank connections do not influence the effect on firm performance when the firm's OFDI is in developing countries. Therefore, only Hypothesis 2b is supported.

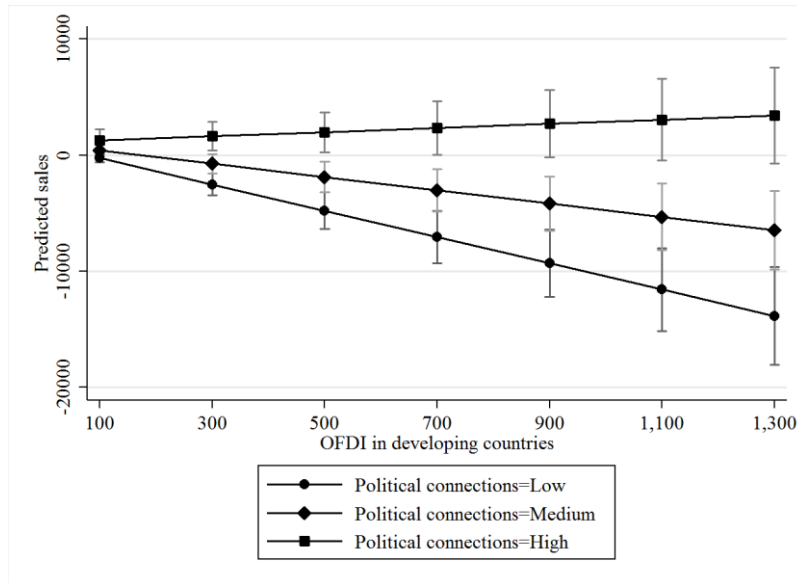
Model 5 provides the analytical results of Hypotheses 3a and 3b concerning the interaction effects between OFDI in both types of host countries and the firm's connections with government officials in foreign investment agencies (FID). The interaction effect between OFDI in developing countries and FID is positive and statistically significant ( $b=764.4$ ,  $p<0.001$ ), but the interaction effect between OFDI in developed countries and FID is negative and statistically significant ( $b=-236.6$ ,  $p<0.01$ ). This indicates that government officials whose work is related to foreign investment help firms to enhance its sales in developing countries, but worsen its sales when firms invest in developed countries. This finding, therefore, supports both Hypotheses 3a and 3b. These relationships are consistent in the combined model (Model 7).

Model 6 exhibits the findings of Hypotheses 4a and 4b stating positive interaction effects between OFDI in both types of host countries and the directors who have experiences in foreign affairs (FAD). Both interaction effects between OFDI in developing countries and FAD and OFDI in developed countries and FAD illustrate positive and statistically significant at 0.1 per cent level. This shows that the firm's connections with government officials who have experience in foreign affairs will help firm's OFDI in enhancing its performance, regarding the investment location. However, the findings in the combined model (Model 7) illustrates statistically insignificant coefficient of the interaction between OFDI and FAD, implying that the role of directors' experience in foreign affairs is not stable, especially when the firm

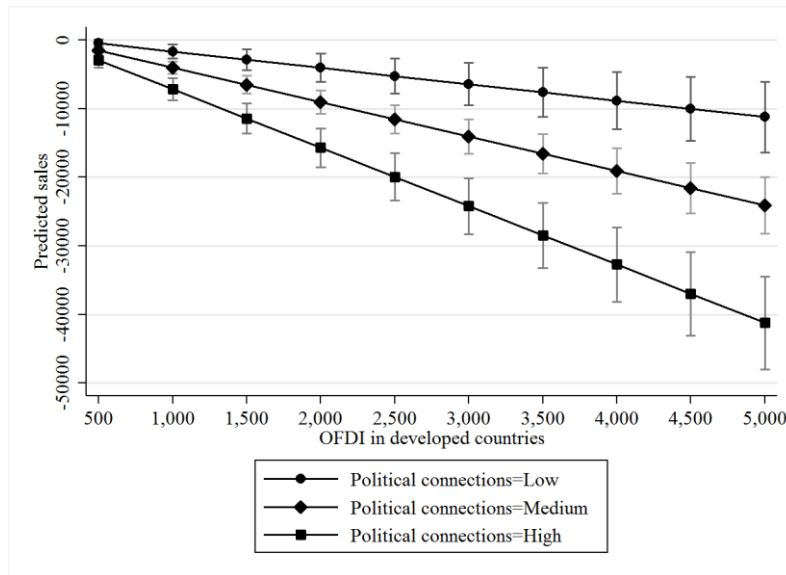
incorporates other types of political connections. Hence, Hypotheses 4a and 4b are not supported.

To examine these interaction effects further, Figures 5.2 to 5.9 illustrate the marginal effects of OFDI on firm sales at different levels of each political actors. We classified each moderator related to political connections into three levels, low-medium-high, for ease of illustration. All figures confirm the results of the interaction effects. Figures 5.2 and 5.3 present the marginal effects of OFDI in developing countries and OFDI in developed countries on firm sales at different levels of political connections respectively. Both figures confirm Hypotheses 1a and 1b showing that the higher level of political connections positively moderates the role of OFDI on firm performance when firms invest in developing countries but negatively moderates the effect of OFDI on firm performance when firms invest in developed countries. Figure 5.4 and 5.5 provide the marginal effects of OFDI in developing and developed countries on firm sales at different degrees of political actors who have experience in government banks. The figure illustrates that the higher ratio of government-bank related directors has a higher positive relationship between OFDI and firm sales. Figures 5.6 and 5.7 illustrate the marginal effects of OFDI in developing countries and OFDI in developed countries on firm sales at different levels of foreign-investment related directors respectively. Both figures confirm Hypotheses 3a and 3b showing that the higher level of political actors who have experience in foreign-investment regulating and supporting agencies positively moderates the role of OFDI on firm performance when firms invest in developing countries but negatively moderates the effect of OFDI on firm performance when firms invest in developed countries. Figures 5.8 and 5.9 show marginal effects of OFDI in developing and developed countries on firm sales at different degrees of political actors who have experience in foreign affairs. The figures indicate the positive slope when firms have a higher ratio of those directors, compared to the slightly negative slope of the relationship in the lower level of those directors.

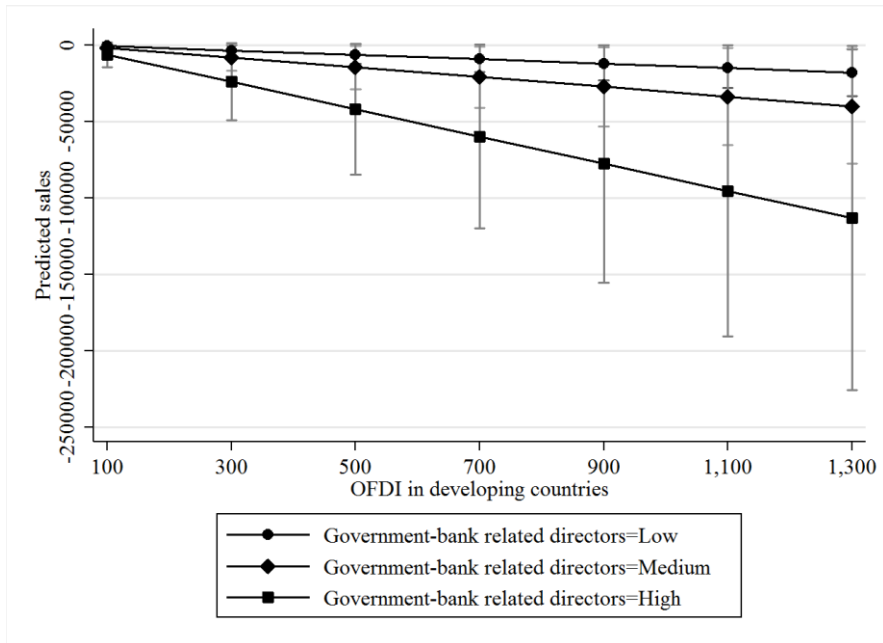
**Figure 5.2** Marginal Effect of OFDI in Developing Countries on Firm Sales at Different Levels of Political Connections



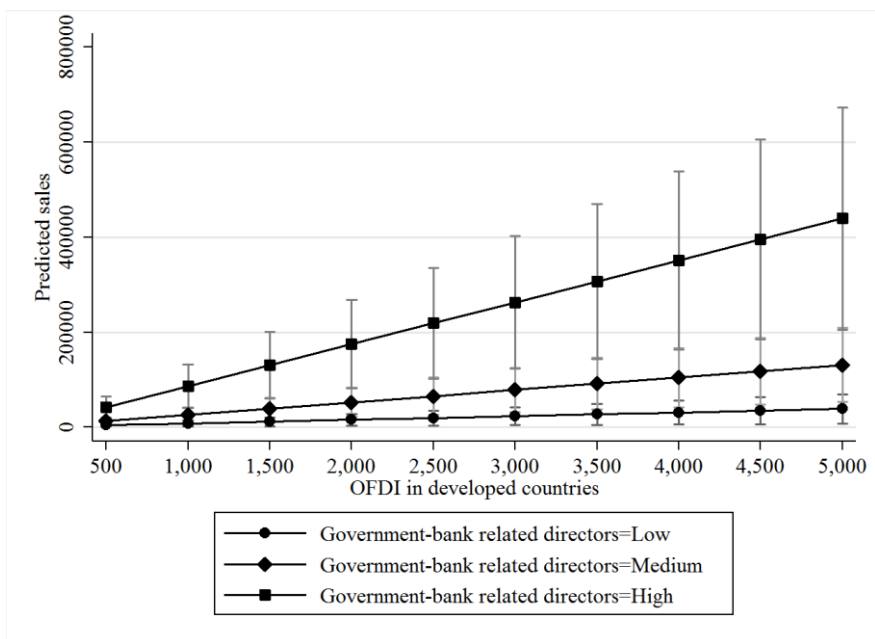
**Figure 5.3** Marginal Effect of OFDI in Developed Countries on Firm Sales at Different Levels of Political Connections



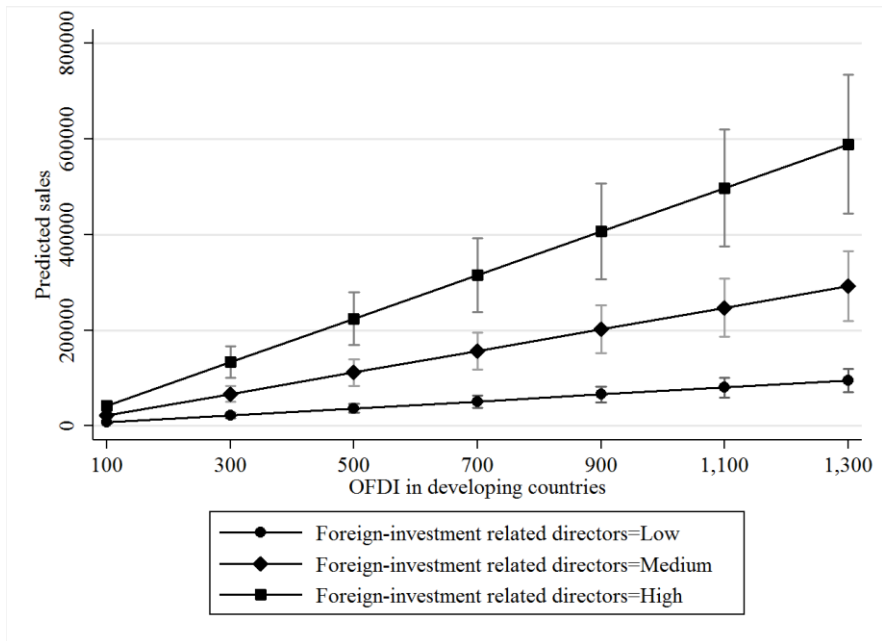
**Figure 5.4** Marginal Effect of OFDI in Developing Countries on Firm Sales at Different Levels of Government-Bank Related Directors



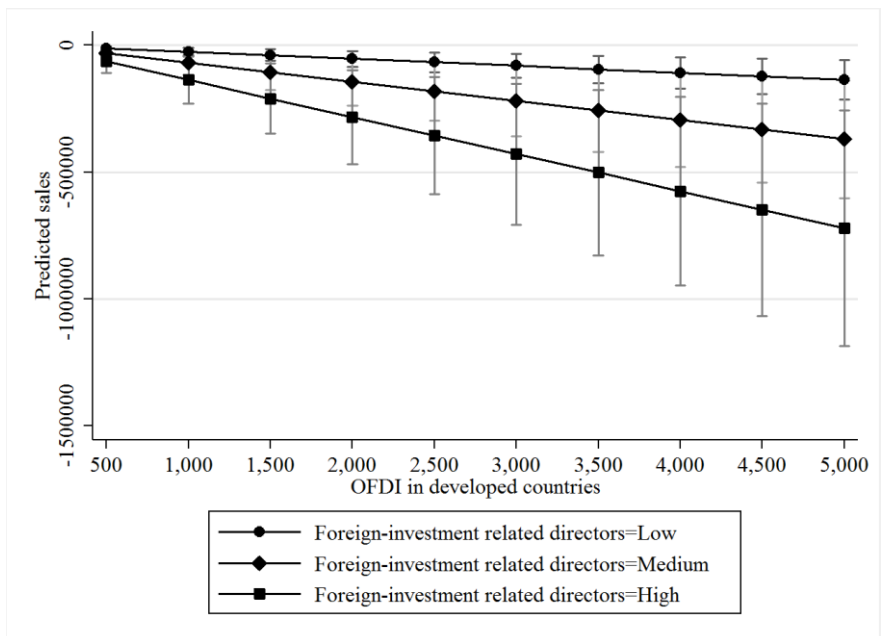
**Figure 5.5** Marginal Effect of OFDI in Developed Countries on Firm Sales at Different Levels of Government-Bank Related Directors



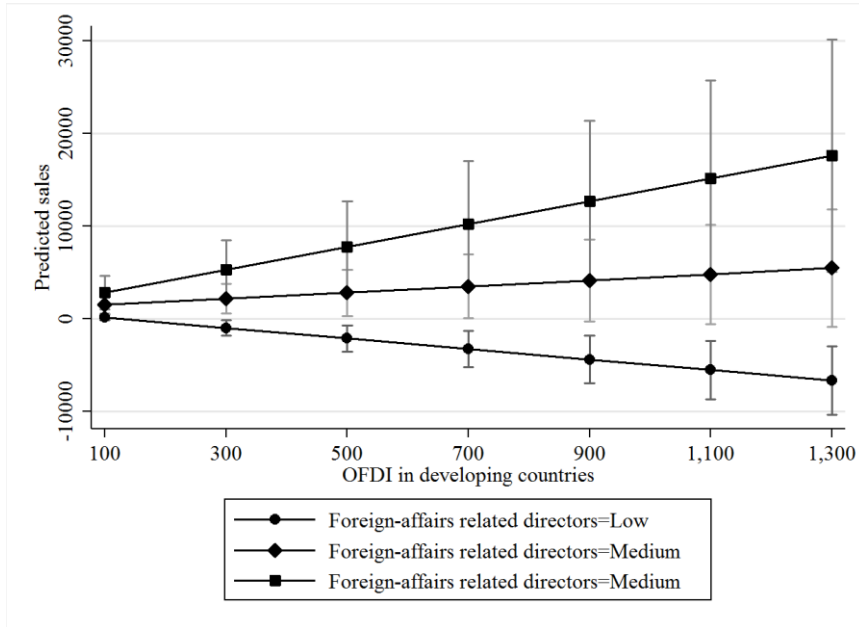
**Figure 5.6** Marginal Effect of OFDI in Developing Countries on Firm Sales at Different Levels of Foreign-Investment Related Directors



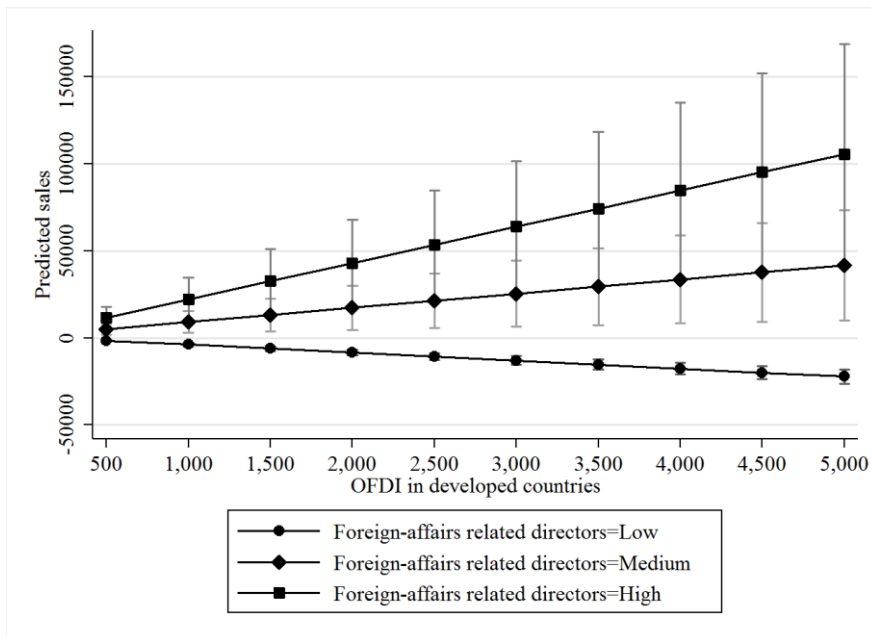
**Figure 5.7** Marginal Effect of OFDI in Developed Countries on Firm Sales at Different Levels of Foreign-Investment Related Directors



**Figure 5.8** Marginal Effect of OFDI in Developing Countries on Firm Sales at Different Levels of Foreign-Affairs Related Directors



**Figure 5.9** Marginal Effect of OFDI in Developed Countries on Firm Sales at Different Levels of Foreign-Affairs Related Directors



Overall, the results confirm the role of political connections in moderating the OFDI and firm sales. However, the effect of political connections and OFDI on sales varies depending on different types of political actors and host-country location. Based on the combined model (Model 7), the firm's political connections and directors related to foreign-investment supporting and regulating agencies improve firm sales when the firms invest their affiliates in developing countries, but reduce firm sales when their affiliates are in developed countries. The government-bank related directors, in contrast, only increase firm sales in developed countries. The results are discussed further from the perspectives of RDT and institutional theory in the next section.

## **5.5 Discussion and Conclusion**

This chapter investigates how home-country political connections influence OFDI to affect firm performance, focusing on the different sets of a host country and the type of political actors. The findings show that the impact of political connections in helping the firm's OFDI to gain higher performance is contingent upon the type of political actors and investment location. In general, political connections facilitate OFDI in developing countries to enhance the effect of firm performance, but it hinders the effect when firms invest its affiliates in developed countries. This finding offers some insights to explain the inconclusive effect of political connections on firm performance in previous studies (Hillman, 2005; Siegel, 2007; Faccio et al., 2006). It partially supports the argument suggested by RDT that political linkages can generate some benefits to the connected firms (Hillman, 2005; Pfeffer and Salancik, 1978). However, the negative performance effect of political connections and OFDI in developed countries indicates that the benefits stemmed from the dependency of home-country political resources are restricted only in a particular context. Previous work has shown that political ties are more useful in transition countries (Peng and Luo, 2000; Peng, 2003), but many studies also found positive impact of political connections in developed countries (e.g. Hillman, 2005; Goldman et al., 2013). This finding, therefore, extends our understanding of political connections in the OFDI context by showing that political connections in general can negatively influence the



effect of OFDI on firm performance, but it also depends on the type of political actors and investment locations.

This chapter does not investigate the role of political connections only at the aggregate level. We incorporate recent discussion in CPS study arguing that different types of political connections can lead to different effects on performance (Zheng et al., 2017; Sun et al., 2015; Okhmatovskiy, 2010) to participate in the call for more study on contingent factors that explain the effect of political connections on firm performance (Zheng et al., 2015; Sun et al., 2012). We address this call by investigating the role of three different types of political actors who are relevant to OFDI in this chapter. By considering both the type of political actors and different sets of investment location, we found that government-bank related directors can influence OFDI in developed countries to enhance firm performance. This finding gives empirical support for the argument made in previous IB research suggesting that EMNEs can benefit from its social capital building through business and political networks when they invest its affiliates in developed countries for the purpose of seeking for innovation and technology (Wright et al., 2005; Nahapiet and Ghoshal, 1998).

Previous studies in CPS suggest that politically connected firms can get financial access more easily than non-connected firms, but the cheaper loan may make firms invest in high-risk projects, and in turn can either increase or decrease its performance (Boubakri et al., 2013; Bliss and Gul, 2012). The negative effect of government-bank related directors when firms invest its affiliates in developing countries shown in Model 7 in the findings, therefore, supports this argument, indicating that firms with government-bank connections may invest in less-conservative investment projects in developing countries that ultimately give them the negative returns. In contrast, the positive return the connected firms have when they invest its affiliates in developed countries leads us to conclude that firms are more conservative when they invest its affiliates in developed countries, so the easier financial access they may have through their connections help them invest in more thoughtful and competitive projects that in turn increase its outcome.

Moreover, our findings show the positive effect of the interaction between OFDI in developing countries and political actors from foreign-investment promoting

and regulating agencies on firm performance, but the effect turns negative when OFDI is in developed countries. This finding partially supports previous studies suggesting the positive roles of regulating agencies (De Figueiredo and De Figueiredo, 2002). This might be able to be explained from institutional perspectives. It is suggested that developing countries have weak institutional contexts containing information asymmetry and less-property right protective institutions (Khanna and Palepu, 1997), therefore the connections with political actors from regulating and supporting government agencies, who can provide advice and support for firms investing in developing countries, can help firms get advantages from its OFDI. In contrast, the institutional context in developed countries is more functioning and requires less assistance from non-market strategies such as political connections. Firms that invest in developed countries are expected to invest in new technology and innovation that help them gain more competitive advantages (Wright et al., 2005). Politically connected firms that rely much more on political networks rather than concentrating on developing new competitive advantages may not be able to yield benefits from its connections as it is suggested that firms relying on social capital with exploitation behaviour may not have any progress (Nahapiet and Ghoshal, 1998).

The third type of political actors we highlight in this chapter is foreign-affairs related directors. The finding (in Model 6) shows that firms can get benefits from these political actors in both developing and developed countries based on their direct experience in foreign countries that allow them to give useful information regarding the host country as well as the socio-political networks they may have in foreign countries. However, in the consideration of this type of political actors together with other types in the full model (Model 7), the statistical significance is lost and relationship changes suggesting the inconclusive role of this type of political actors in influencing OFDI to affect firm performance.

Apart from the general discussion for the firm's political strategy, considering that our findings are based on the emerging-market firms, we can also take a closer look at political connections from the perspective of EMNEs and its ownership advantages. As EMNEs possess fewer competitive resources and capabilities compared to advanced MNEs (Madhok and Keyhani, 2012), some EMNEs choose to create the firm specific advantages based on non-market factors, especially political

and business networks (Luo and Rui, 2009). EMNEs, therefore rely on ‘relational capabilities’ (Luo and Rui, 2009) more than advanced MNEs. The findings in this chapter show that the firm specific advantages based on relational capabilities such as political connections may not help EMNEs to gain competitive advantage and increase their value, especially when the EMNEs expand their affiliates in developed countries. In other words, the firm’s specific advantages based on political connections are not transferable to some investment location. The use of relational capabilities, especially political connections, to substitute the lack of competitive resources and capabilities such as R&D, therefore, may not help EMNEs to compete with other MNEs. To gain better performance from OFDI, especially when OFDI is in developed countries, EMNEs need to develop and increase competitive resources and capabilities that are transferable to both developed and developing host countries such as R&D investment or brand development.

This chapter makes three contributions. First, it advances IB study by extending the existing research on the role of home-country government on the internationalisation of EMNEs. Previous studies in IB discussed the role of political connections in facilitating the firm’s internationalisation, especially OFDI (Wang et al., 2012) but it is still unclear whether and how such political resources can help firms enhance the effect of OFDI on firm performance. The findings in this chapter illustrate that home-country political connections can enable OFDI to increase firm performance when firms invest its affiliates in developing countries, and when firms have ties with a particular type of political actor. A previous study focusing on EMNEs encourages us to find out which type of resources are transferable to other countries and how much those advantages can offset the liability of foreignness that firms face in the host countries (Ramamurti, 2012). This study participates in this discussion by providing empirical support for the specific types of the firm’s political resources that can help firms gain positive return from its OFDI. In addition, this study extends IB literature focusing on the institutional context in emerging markets. The empirical evidence that shows how political connections can help firms gain advantages by comparing the impact in host-developing and host-developed countries extends the discussion of the usefulness of the firm’s political resources in different institutional contexts (Peng, 2003) of the host countries.

Second, this chapter extends the discussion in CPS literature. The distinguished role of the firm's political connections based on different types of political actors on its performance extends the discussion in CPS research, especially those that rely on RDT. Recent scholars in the area of CPS have started to compare the effect of the different types of political linkages (Zheng et al., 2017; Zheng et al., 2015; Mahmood et al., 2017; Sun et al., 2015) and particularly called more research on the contingent factors that can further explain the role of political connections on firm performance (Zheng et al., 2015; Sun et al., 2012). Our study proposed the contingent value of different types of political actors that are relevant to the firm's international strategies as well as the contingent value of the different investment location.

Third, by integrating RDT and institutional theory, the consideration of institutional context of the host country in this chapter can advance the use of RDT to explain the relationship of the firm's political connections on the firm's performance. RDT, while explaining how firms utilise the external dependency and expect benefits of the firm's interdependence (Pfeffer and Salancik, 1978), does not discuss under which circumstance that resources dependency may not yield this expected positive outcome. Engaging with political actors, while is widely done by firms in both developed and developing countries (Faccio, 2006; Frynas et al., 2006; Hillman, 2005), is more noticeable in countries with weak institutions (Faccio, 2006). Our comparative findings of the performance effect of political connections based on OFDI in developing and developed countries show that institutional context plays important role in enhancing or reducing the benefits of political connections suggested by RDT.

While our results contribute to the understanding of the role of political connections in OFDI and performance, the sample of Thai firms that are grounded in the political system in Thailand may lead the political connections in a specific direction. This may limit the generalisability of the results. However, we believe that our findings can also apply to other emerging countries, which may need to rely on non-market strategies such as political connections as Thailand. In the next chapter, we discuss more on the limitations of this research, together with the overall conclusion and discussion.

## **Chapter 6**

### **Conclusion**

The criticality and rareness are two elements of resources that create the interdependency between two organisations. The firms will be able to benefit from its interdependency when the external organisations they are linked with can provide them the useful resources that are crucial and difficult to obtain elsewhere. Government officials, who gain access and control important resources through the policies, regulations, or government supports, are those who have been considered as an important external organisation who will be able to create the firm's ownership advantages that help them not only survive the external uncertainty but also able to compete with its competitors. However, does the ability to provide crucial and rare resources of the home-country political actors still exist when the firms operate overseas? Which type of political actors is beneficial to the firm's performance in its OFDI? How can the political connections created within the institutional context in the home country influence the firm's performance in different institutional settings in the host countries? These are the primary questions this thesis attempts to address and develop the explanation throughout this thesis.

The answers to these main research questions are summarised and discussed in this Conclusion Chapter. The first part of the chapter summarises the overview of the main research finding by revisiting three main research objectives pursued in this research and explaining the research findings. The second part of the chapter discusses the research contributions and practical implications. Then, the limitations and future research are discussed in the third part.

#### **6.1 Overview of the Research Findings**

In this section, three main research objectives are revisited to discuss the main research findings under each objective and its related research questions.

### **6.1.1 The Effect of the Home-Country Political Connections on OFDI-Performance**

The first objective of this research is to explain the effect of the home-country political connections in helping the firm's OFDI to increase its performance. Two related research questions are addressed to pursue this research objective. First, can the home-country political connections influence the OFDI to ultimately increase the firm performance? Second, what is the impact of the firm's political connections and OFDI on the firm performance?

The empirical findings of the interaction effect between OFDI and political connections on firm performance show, in both Chapters 4 and 5, that political connections can influence OFDI to ultimately affect firm performance. The effect, however, depends on types of political actors to whom the firms connect and the investment location. In Chapter 4, we show that political connections in general negatively influence OFDI to decrease firm sales, but the effect becomes positive when particular types of political actors are considered. The further investigation focusing on level of political actors and types of political connections based on the government functions, executive and legislative ties, highlights the positive effects of executive and legislative ties. In addition, in Chapter 5, we further explore the role of different types of political actors by testing four specific types of political actors that are relevant to the firm's OFDI. We found that political actors related to government banks and foreign-investment policies can influence the OFDI and firm performance, but its effect depends on the investment location.

The results in both Chapters 4 and 5 reveal that the political connections established in the home country do not only facilitate firms to establish its overseas affiliates, but it also has an impact on firm performance. Studies in IB have theorised that the connections the firms made with home government can facilitate its OFDI (Wang et al., 2012), but we do not yet know whether such connections can also help the firms gain better performance. Our findings in this thesis therefore illustrate that having connections with a high number of political actors may not help a firm increase its value and the political connections can help firms perform better when firms establish the connections with only top-level political actors from executive and legislative functions.

Previous studies in IB also theorise that different types of association the firms have with the home government influence the firm's foreign investment strategies in different ways (Wang et al., 2012). The relationship with the home government in the form of SOEs puts more pressure from both the home and host government on firms and restricts their choices of investment strategies (Meyer et al., 2014). The involvement with the home government through the political linkages also put some pressures on firms to choose an investment project that sends a positive signal to increase the reputation of political actors (Wang et al., 2012). The different types of pressure the firms get from its government associations lead us to explore further how the impact of home-government connections and OFDI on firm performance is. The findings in this thesis support the mixed role of the government affiliations by showing the mixed impacts of the connections based on the different types of political actors and investment location. The results in this thesis therefore extend the study in IB that previously discussed the role of home-government linkages on the internationalisation by illustrating its influential role on firm performance.

### **6.1.2 The Comparison of the Types of the Connected Political Actors**

The second objective of this research is to identify the types of political actors that can influence the firm's OFDI to enhance its performance. This objective lead to the third specific research question to discover which type of political actors based on their positions can enhance the relationship of OFDI and firm performance (RQ3). These research objective and question are explained by separating the type of political actors to assess its individual effect on OFDI and firm performance.

To compare the different types of political actors, we separate our consideration into two categories. The first category concerns the position of political actors in the form of level and the type of government functions; and the second category focuses more on political resources, provided by different types of political actors, that are useful for the firm's overseas investment; each group is investigated separately in Chapters 4 and 5 respectively. In Chapter 4, we classify the type of political actors based on two criteria: level and government functions. The level of political actors does not show the stable statistical significance throughout the models, therefore we conclude that higher level of political actors do not always lead to positive performance. Two possible reasons that may explain this finding are the

relevance and permanence of lower-level political actors, and power imbalance between higher political actors and firms. Former studies that focus on different levels of political actors and performance found mixed results and have different arguments to support the benefits of each level (Wang et al., 2012; Ma et al., 2016; Zheng et al., 2015). The high level of government officials can control more important resources and have power to make decision on important policies, but the lower level political actors are more accessible to the firms, so firms are able to pass on the favourable information to these political actors.

The findings in Chapter 5 show that the connections with political actors from government banks and foreign investment supporting and regulating agencies are influential to OFDI and firm performance. The effect of each type of political actors is unique when the firms invest its overseas affiliates in the different investment location. Our results show that political actors from government banks are helpful for firms to increase their performance when the firm's OFDI is in developed countries, but it is harmful for firm performance when the firms invest their affiliates in developing countries. Previous studies have shown that the connected firms tend to get access to cheaper loan easier than non-connected firms and may invest in riskier projects compared to non-connected firms (Boubakri et al., 2013; Khwaja and Mian, 2005). The easier financial access and risk-taking can either reduce (Bliss and Gul, 2012) or increase (Boubakri et al., 2012a) the firm performance. Our results lead us to conclude that, in spite of the easier financial access, the connected firms are more conservative when they invest its affiliates in developed countries, so the easier financial access they may have through their connections help them invest in more thoughtful and competitive projects that in turn increase its outcome. In contrast, when they invest its affiliates in developing countries, getting financial access make firms invest in less conservative projects that in turn leads to negative return.

In contrast to the government-bank related connections, political actors related to foreign investment are useful when firms invest its subsidiaries in OFDI in developing countries. The positive findings suggest to us to conclude that, in the establishment of the firm's subsidiaries and affiliates in developing countries, firms can get advice and support regarding foreign investment in less-developed institutional context from these agencies. Due to the lack of well-function institutional



context in developing countries, firms need to rely more on non-market factors to enhance the role of OFDI on firm performance.

By considering different types of political actors, we can conclude that the role of political connection in helping firms gain higher performance is contingent upon the types of political actors. As in the case of OFDI, the executive and legislative ties, the connection with government banks, and ties with foreign-investment related agencies could be helpful for firms to gain higher performance. However, the effect of political connection also depends on the host country that the firm operates its subsidiaries and affiliates.

### **6.1.3 The Effect of the Host-Country Institutional Settings**

The third objective of the thesis is to compare the effects of the firm's political connections in the different institutional settings of the host-countries. This leads to the last two specific research questions on whether the moderating roles of the home-country political connections on the relationship of OFDI and firm performance are different when the firm invest its affiliates in the developed country compared to when their OFDI is in the developing country (RQ4), and if they are different, which type of political resources that are more beneficial to the firm's performance in the particular host countries (RQ5).

The comparison of the performance effects of political connections and OFDI in different host countries in Chapter 5 clearly demonstrates the important role of the host countries in dissimulation of the political connection impacts. The findings in Chapter 5 suggest that the resource provided by the same type of political actors can be beneficial or a liability for firms in the different types of host countries. The political connections that have negative roles on OFDI and performance shown in Chapter 4 are actually beneficial to the firm's when they invest in developing countries, and are harmful for firms when they invest in developed countries, as shown in Chapter 5. This finding suggests that the benefits of political connections on firm performance depend mainly on the institutional context in which the firms operate its subsidiaries and affiliates.

The further investigation of the different types of political actors in different host countries in Chapter 5 also reflects how the institutional context in the host

countries affect the roles of political connections and OFDI on firm performance. The positive effect of the firm's connections with government banks in host-developed countries in contrast to the negative impacts of overall political connections and foreign-investment related directors can imply that the institutional pressure in developed countries forces firms to invest in more competitive activities, so the connections the firms have with government banks that lead to the access to cheaper loans can be used in more high-return projects in developed countries. In contrast, the positive impacts of the connections with foreign-investment related directors in developing countries indicates the roles of non-market factors such as political connections in helping firms gain more information and support that help them operate better in the weak institutional context.

This study's three main objectives disentangle the complexity of the performance effects based on two main factors: OFDI and political connection. The complicated prediction of the relationship between internationalisation and firm performance found widely in former studies does not lead us to make further attempt to find another prediction and explanation to describe this relationship, but it does guide us to explore the conditional aspect of the firm's political connection that may relevant to explain the different performance based on the firm's OFDI. Although, there are many possible factors that may influence the relationship between internationality and performance, yet these have not been theorised, in this study, we focus on the firm's political connections based on the fact and past academic findings that government plays an important role in helping OFDI by EMNEs. The findings in this study lead us to the conclusion of the important role of home-country political connections in helping the firm's OFDI and performance.

The firm's political connections have also been considered as the black box in which we are not sure how it can benefit or be harmful to the firms. The inconclusive results in former works focusing on the roles of political connections and performance give us the opportunity to investigate more of this research area that may lead us to both theoretical conclusion and practical implication. The complexity of the political connections is still too complicated to make a generalised conclusion about its role on performance by one single prediction. As in the fact of social science, the context always plays a role. The attempt we made in this study contributes to both academic

and managerial areas. We discuss the theoretical contributions and practical implication in the next section.

## **6.2 Contributions and Implications**

By pursuing three research objectives discussed earlier, this research has both academic and practical contributions. This section provides the discussion on the research contributions academically and practically.

### **6.2.1 Research Contributions**

The research findings make four contributions to the research in IB and CPS. First, it advances IB study by filling the gap of existing research in EMNE's political behaviour which still have insufficient explanation on whether it helps the EMNEs to increase firm performance. Although extant research in international business has primarily concentrated on how the political connections increase the firm's ability to invest overseas (Wang et al., 2012; Frynas et al., 2006), very limited research (e.g. Brockman et al., 2013 on post M&A performance) examines whether the advantages that the firms gain from its connections with the home country can be leveraged after its foreign investment. It is therefore unclear whether and how the firm's political connections can influence the firm's OFDI to increase its performance. This thesis furthers this area of research by providing the evidence to support our argument that the performance impact of political connections in facilitating OFDI is varied depending on the type of political actors and the investment location. The findings in both Chapters 4 and 5 indicate that the political connections that the firms establish in the home country, in general, influence the firm's OFDI to reduce its performance. However, the firm's political connections can be helpful for firms to increase the role of OFDI on firm performance depending on the type of political actors and the host location.

Second, this thesis participates in the discussion in IB strategy that attempts to explain the performance of internationalisation. The extant studies in IB strategy attempting to figure out how internationalisation affects the firm performance previously found inconclusive-mixed results (Kirca et al., 2011; Tallman and Li, 1996), but the relationship is moderated by FSA (Kirca et al., 2011). This thesis

provides the discussion of the firm's political resource, which can be viewed as a non-market FSA, in moderating the relationship between OFDI and firm performance. Although, our ultimate attempt is not to focus particularly on internationalisation (or multinationalisation) on performance, the focus of this thesis, specifically on the role of political connections that can change the relationship of OFDI and performance can contribute to this research area in IB. The findings in both Chapters 4 and 5 provide the evidence to support our argument that the type of political resources can moderate the role of OFDI on firm performance. Therefore, this thesis furthers the discussion in this research area by opening the debates that political resources can influence the internationalisation by EMNEs to affect firm performance.

Studies in IB have extensively attempted to establish the explanation on how institutional factors influence the OFDI by EMNEs (Meyer et al., 2014; Buckley et al., 2007; Lu et al., 2014), and discuss how institutional factors affect EMNE's performance (Chacar et al., 2010; Kafouros and Aliyev, 2016). This thesis, by concentrating on the firm's political connections, discusses whether the firms can internalise the institutional factors to generate the heterogeneity benefit from it. Political connections are embedded in the home-country institutional context and internalised by firms through mechanisms such as appointing the political actors on the board of directors. By focusing on the role of home-country political connections on the performance effect of OFDI in different host-country setting, we can then extend the discussion on the interplay between home and host institutions.

Third, it extends the study in CPS by comparatively discussing the different types of political actors as well as the investment location that can make political connections become a helping hand or a grabbing hand. By providing the fine-grained type of political actors, this thesis helps us understand which type of political actors that benefit the firm's performance, rather than focus only on the top-level government officials who may provide unnecessary resources to the firms.

Fourth, it contributes to IB research that focuses on EMNEs and the role of home government in influencing internationalisation (Wang et al., 2012; Cui and Jiang, 2012; Meyer et al., 2014; Lu et al., 2014) by extending the discussion on the government involvement in the form of political connections, rather than SOEs as many prior studies. The employment of political connections from both private firms and government-owned firms in this thesis can show that both types of firms can take

advantages of political strategies through linkages with political actors. The focus on the political connections made by private firms are more applicable compared to the study focusing on SOEs. The findings lead to the discussion of the role of government or the political strategies of EMNEs that can be applied for firms in the transition economy or other emerging countries especially from high bureaucrat countries. We discuss more on the practical implication in the next section.

### **6.2.2 Practical Implications**

This thesis potentially has practical implications when a firm considers applying political strategies. Private companies, especially the ones which have invested their affiliates overseas, may consider appointing some particular types of political actors to the board of directors as part of their political strategies. In this thesis, we empirically show that the connections the firms made with the home-country government not only facilitate the firm's overseas expansion but also help the firms to perform better in OFDI. However, we also show in this thesis that more connections the firms made with political actors are not always beneficial to the connected firms. To gain benefits from appointing political actors to the board of directors, the firms need to consider types of political actors and types of the host countries.

As shown in Chapter 4, the higher level of political positions, while it seems to give more benefits to the connected firms, does not always enhance the firm performance from its OFDI. The connections made with the high level political actors can decrease the benefits from interdependency between the connected firms and the political actors as the firms may lose autonomy when needing to rely on high level political actors. Besides, the firms can access lower level political actors as well as communicate their information to political actors at this level more easily than to the high level political actors.

Firms can also consider, based on the result in this thesis, that not all types of political actors are helpful for the connected firms in enhancing performance when they expand the firms' affiliates overseas. Some types of political actors can help the firms perform better in overseas expansion, especially the political actors who have direct experiences in foreign affairs such as ambassadors or diplomats. From the findings in this thesis, the firms can also consider the negative impacts of some types

of political actors that we would have thought that they would be beneficial to the firms. As shown in Chapter 5, the connections with political actors who have experiences in the government banks may lead to negative firm value when the firms invest their affiliates in developing countries. The firms therefore need to take into account the types of the host countries, especially the host-country institutions, in which they invest their affiliates when the firms consider applying political strategies. The firm can adjust their political strategies to fit more with the host country's institutional context by appointing political actors who are more beneficial in their specific investment location.

In Chapter 5, we show from our findings that the host-country institutions are important factors that the firms need to consider because the host-country institutions can affect the firm's ability to leverage benefits from the connections with political actors. In host-developing countries, more connections with political actors and the connections with political actors who have experiences in foreign investment supporting agencies and foreign affairs can help the firms enhance performance when they invest in affiliates in these countries. In contrast, in developed countries, the connections with higher number of political actors as well as the connections with political actors whose work relates to foreign-investment promotion do not help the firm increase performance from its OFDI.

From the findings in this thesis, we can provide the evidence and explanation to show that firms need to be more cautious and selective when they apply political strategies, especially, when the firms invest the firm's affiliates in developed countries. Moreover, this thesis also shows that relational capability such as political connections is not always transferable to the host countries. To compete in global markets, the firms, EMNEs in particular, need to create the competitive resources and capabilities that can be transferred to different types of host countries such as R&D investment, brand development, or managerial improvement, rather than relying heavily on the firm's political strategies.

### **6.3 Limitations and Future Research**

This section discusses some limitations of this research together with the suggestions for potential future research.

First, the use of the cross-sectional research design, while allows us to collect fine-grained data of the political position of each board member, creates limitations in twofold. First, it does not allow us to capture the changes of government regime and institutional changes. Political power is not static. The connections that the firms created with political actors from the currently ruling political parties may not be beneficial to the connected firms when the new parties are elected. The firm's political connections can then turn to be liabilities for the connected firms (Siegel, 2007) when the government changes. Also, the political power of former political actors appointed to the company board can deteriorate over time (Lester et al., 2008). Furthermore, institutional context changes over time. During the period that emerging countries have been transitioning to the more developed states, political system, particularly political power, has evolved over time. The role of political power is more crucial in the authoritarian regime than in a more democratic government and the effect of the firm's political connections on the firm's performance should also change over time. Second, although this thesis has lagged all independent variables for one year, the cross-sectional data may lead to potential endogeneity. To address this issue, the future research should apply longitudinal data that can capture the changes of both political regime and/or institutional changes. One possible way to do this is by tracking the appointment time of each politically related director and matching with the ruling political regimes and the OFDI value at the time of appointment. This longitudinal data can help us find out if the role of political connections in OFDI and performance has changed when the government changes (or when the institutional context changes if the data can be collected over an extended period of time that allows the institutional factors to change). However, the data collected in this way may include only the top-executive level of political actors, such as Prime Minister, ministers, or members of parliament, as the historical data of lower levels of government officials is less possible to obtain. It also requires the outflow value of OFDI data at the firm level. The event-study approach is also suggested to study the effect of the firm's political connections on the firm's performance, as it can reduce

the potential endogeneity problem better than the cross-sectional approach (Boubakri et al., 2012a).

Second, this study is restricted only to the context of firms from Thailand. Relying on the context of one country, while it allows us to compare the different types of political positions without a concern of a discrepancy between different political systems, may limit the generalisability of the research findings as the institutional context varies across countries. Future research can obtain data from other countries and compare the results between countries. This, however, needs to carefully design the comparable measures of the level and types of political position across countries.

Third, the firm's performance captured in this study is the parent firm's performance rather than the subsidiary's performance. This thesis purposefully chose the performance of the parent firms as it indicates the ultimate return of the MNEs because MNE's affiliates are not always established for profit purpose. For example, the subsidiaries may be established because it can provide cheaper supply, or it has resource sought by MNEs. Moreover, EMNEs may establish its affiliates overseas for the purpose of developing resources and capability that can be useful for their activities in the home country. However, it can also be argued that the test of the subsidiary' performance may capture the OFDI performance in a more direct way. Hence, the future research better compares the test of the parent firm's performance against OFDI and political connections of the firms to the test of the subsidiary performance against OFDI and political connections, to provide more robust findings.

Fourth, this study focuses on the influential role of firm's political connections on the OFDI of the firm without considering the details of the entry mode and the investment motives. Some OFDI motives, such as the national resource seeking required more supports from the home-country government than other motives. The connections to the home government can lead to the government negotiation with the host countries that can facilitate the OFDI (Li et al., 2013). Also, different types of political involvement can influence the different OFDI motives, as it is argued by Wang et al. (2012) that SOEs can influence the resource seeking OFDI, whereas the connections with high-level of government affiliates can affect market seeking OFDI. Future studies can separate the OFDI motives and compare whether the firm's



political connections can influence the effects of each type of OFDI motives on the firm's performance differently. This, however, requires OFDI data that has more detail on investment projects in order to identify the motives. Also, the future study can compare the investment modes, i.e. green-field FDI, mergers and acquisitions (M&A), or joint venture, as each investment mode may be influenced by the firm's political connections differently. While the green-field OFDI may require the home-government supports such as negotiations or bargaining with the host government, the M&A or joint venture may require the link to the partnership with the host-country government, or the networks to the private partners in the host country. Each type requires a different degree of the firm's political connections; hence, the effects of the firm's political connections and OFDI on the firm's performance will be varied by different investment modes. Moreover, as suggested in RDT that the firm is less dependent on a particular external organisation when it invests in a joint venture because it can diversify the sources of resource dependency (Pfeffer and Salancik, 1978), the roles of the firm's political connections may have less impact on OFDI and performance when the firm invests in a joint venture than in a wholly owned subsidiary.

Fifth, this thesis only focuses on the role of the firm's political resources without simultaneously considering the role of market-resources and capabilities of the firms. While the firm's political resource is argued to have important roles for the firm's OFDI, especially the firms from emerging markets, possessing only political resources is not enough for the firm to compete in the international arena (Frynas et al., 2006). The study of both market resources, such as R&D and innovation, and political resources by simultaneously considering both types of resources should lead to more understanding of how the firm's political connections can interact with other kinds of the firm's competitive resources to help the firm's increase its OFDI and performance. The control of the intangible assets as done by this thesis is not enough to understand the interaction between the firm's market-resources and political resources.

Sixth, organisation study suggests that intra-organisational power consists of hierarchical authority, resource control, and network centrality (Astley and Sachdeva, 1984). This study takes into account only the hierarchical authority and resource

control of the political actors but does not include the network centrality of the political actors. The study of political networks, while it is closely related to the study of political connections and political ties, has another specific focus on the centrality of the networks. In the context of this thesis, while it differentiates the political connections into three aspects, which are the number of political connections, the hierarchical level of political position, and the types of political resources, it does not provide discussion on the centrality of political ties. Future study can focus on this aspect by using social-network analysis to investigate the role of political actors who are appointed to the board of directors of many companies to find out whether their strong ties are beneficial for the firm's OFDI and performance.

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## Appendix A

### Foreign Exchange Rate for the Calculation of OFDI Value

Currency	Country/ Region	FX Rate (2013=1US\$)	Currency	Country/ Region	FX Rate (2013=1US\$)
Ariary	Madagascar	2206.9142	Kyat	Myanmar	933.5705
AUD	Australia	1.0358	MNT	Mongolia	1523.9275
BDT/Taka	Bangladesh	78.1032	MOP	Macao	7.9893
BRL	Brazil	2.1561	MR	Malaysia	3.1509
BZD	Belize	2.0000	Naira	Nigeria	24.7228
CHF	Switzerland	0.9269	NZD	New Zealand	1.2194
CZK	Czech	19.5706	Omani Rial	Oman	0.3845
AED	UAE	3.6725	PHP	Philippines	42.4462
DKK	Denmark	5.6163	PLN	Poland	3.1606
EUR	Europe	0.7532	RMB	China	6.1958
HUF	Hungary	223.6950	RON	Romania	3.3279
GBP	UK	0.6397	RUR	Russia	31.8371
LAK/Kip	Laos	7860.1375	S Peru	Peru	2.7019
GHS	Ghana	1.9541	SEK	Sweden	6.5140
HKD	Hong Kong	7.7560	SGD	Singapore	1.2513
IDR	Indonesia	10461.2400	THB	Thailand	30.7260
INR	India	58.5978	TRY	Turkey	1.9038
JPY	Japan	97.5957	TWD/NTD	Taiwan*	29.7700
KHR	Cambodia	4027.2500	VND	Vietnam	20933.4167
KRW	Korea	1094.8529			

Note: \* Taiwan is not separated from China in the lists of World Development Indicators, therefore, FX rate of Taiwan is collected from the Central Bank of the Republic of China.

Source: The World Bank (2016) and the Central Bank of the Republic of China (2016)

## Appendix B

### Lists of Advanced Economies

Australia	Hong Kong	Portugal
Austria	Iceland	San Marino
Belgium	Ireland	Singapore
Canada	Israel	Slovak Republic
Cyprus	Italy	Slovenia
Czech Republic	Japan	Spain
Denmark	Korea	Sweden
Estonia	Luxembourg	Switzerland
Finland	Malta	Taiwan Province of China
France	Netherlands	United Kingdom
Germany	New Zealand	United State of America
Greece	Norway	

Source: International Monetary Fund (2013)

**Appendix C**  
**Coding System of Industry Based on SIC Code**

<b>SIC code</b>	<b>Sector</b>	<b>This study's Code</b>
0100-0999	Agriculture, Forestry and Fishing	1
1000-1499	Mining	2
1500-1799	Construction	3
2000-3999	Manufacturing	4
4000-4999	Transportation, Communications, Electric, Gas and Sanitary service	5
5000-5199	Wholesale Trade	6
5200-5999	Retail Trade	7
6000-6799	Finance, Insurance and Real Estate	8
7000-8999	Services	9
9100-9729	Public Administration	10