

**Re-conceptualising economic upgrading from global value chain
participation: A dynamic firm-level perspective**

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Submitted in accordance with the requirements for the degree of
Doctor of Philosophy

The University of Leeds
Leeds University Business School

December 2017

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

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To my parents

Vincent Francis Dindial – my best friend, life mentor and father

1954-2017

Though you walk this earth no more, you will forever be in my heart

Acknowledgements

This doctoral journey has been both a scholarly endeavour and an emotional experience. I would like to thank both my supervisors for their support and patience as I embarked on and travelled through this academic expedition. Professor L. Jeremy Clegg, I am grateful for your mentorship, one that started as your MSc student back in 2010. Your unique perspective ignited a curiosity within me that still burns today. Dr Hinrich Voss, I thank you for always pushing me to do better. Your creativity, critical mindset and eye for detail are second to none.

To my parents, none of this would have been possible without you. Although opportunities were scarce throughout both your lives, you somehow ensured that I was always cared for. While I may never fully comprehend your sacrifices, I will always be grateful. To my sister Melissa, you are an inspiration and I thank you for keeping me grounded throughout this PhD. To Molly, I consider you more as my second mother than an aunt. You have been there for me since my first memory of life itself – thank you. Kyrece, you are my life partner and everything I do is for our future. I thank you for believing in me, even when I misplaced belief in myself. This PhD has been a journey for both of us, one that would not have been possible without your love and emotional support.

The insights offered in this document would not have been possible without the interviewees who selflessly offered me their time and experiences – for this, I will always be thankful. To everyone at CIBUL, thank you for the support, academic advice and encouragement. Heartfelt appreciation to Naunghathai, Ayaz, Liang, Yi and Janja - my PhD colleagues that became friends. To my friends Colette and Nadine, thank you for the support and laughs as I worked through this challenging experience. Last but not least, I would like to extend my gratitude to the Government of the Republic of Trinidad and Tobago acting on behalf of its people. This research would not have been possible without the financial support of my fellow citizens.

Abstract

The last two decades have seen unprecedented increases in the global fragmentation and dispersion of production and trade. This phenomenon is commonly referred to as global value chains (GVCs) and is largely driven by the actions of multinational enterprises (MNEs). It is widely accepted, both within academic and policy spheres, that rising GVCs accelerate the advancement of domestic firms in developing countries through new market access and knowledge transfer from MNEs. This research critically investigates the common assumption that this transfer of knowledge enables domestic firms to “upgrade” to generate higher value-added. To date, we have not measured or theorised upgrading in a meaningful way. As such, existing work has only emphasised superficial indicators of the effects of GVC participation.

Employing transaction cost economics (TCE) and power-dependence theory as a foundation, I refine our understanding regarding the impact of GVC participation on developing economy firms. I show that while GVC participation may lead to various upgrading trajectories, it can also produce mechanisms that enable asymmetric value-added appropriation by MNEs.

Using empirical insights from an in-depth embedded case study, I demonstrate that TCE’s core efficiency seeking assumption is overly static and only one of the motives driving an MNE’s choice of governance structure. In this sense, the contractual relationship that allows for transaction cost minimisation may not be the one that is pursued by the MNE. While prior research has investigated this assumption, the arguments put forward are justified from a constrained perspective. Such theorization positions suboptimal contractual relationships as an organisational decision of “last resort”. This thesis proposes a novel theoretical argument, one where MNEs may intentionally engage in relationships that conform to the notion of suboptimality. The analysis suggests that MNEs can strategically engage in suboptimal contracts in

order to create the conditions needed to maintain a favourable long-term bargaining position.

Beyond this 1st tier theorization, I provide much needed insight into the implications of GVC participation on the lower tiers of the value chain. GVCs rarely comprise of value-adding processes that involve only the MNE and a single tier of producing firms. Instead, it is common for value-adding tiers to exist beyond MNE-1st tier relationships. Even so, GVC and linkage studies have focused on understanding the effects of interactions between the MNE and its immediate suppliers. The empirical analysis suggests that in the presence of 1st tier supplier lock-in, the MNE can extend its control beyond its direct contractual relationships.

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Chapter 1

Introduction

1.1 Background of the research topic

The multinational enterprise (MNE) has for a long time been the focal point of international business research. In its infancy stages, the research agenda focused on understanding the MNE's existence (Hymer, 1976; Buckley and Casson, 1976). As the global economy evolved, researchers became interested in the MNE's response to new global challenges and opportunities (Buckley, 2002). While this mainstream agenda progressed, the developmental implications of MNE activity quietly advanced on the periphery. This thesis is concerned with and makes a contribution to the latter.

This peripheral position did not nullify research interest in the international business developmental agenda. In fact, research on the host country implications of international business has advanced greatly since the pioneering work of Caves (1974). This initial phase of research looked predominantly at host country impact driven by foreign direct investment (FDI). On the surface, foreign direct investment (FDI) offered developing countries much needed financial capital and domestic employment. More importantly, the literature assumed these inward investments embodied knowledge, expertise and technology. It was argued that this tacit element can over time spillover to domestic firms operating within similar spheres. The effects were however not uniformly positive. Just as superior capabilities can form the basis for domestic learning, it can also crowd out domestic activity. The question at that time was simple – is the externality effect of foreign capital inflows negative or positive?

During these earlier periods, most MNEs operated as vertically integrated organisations where a great deal of its value-adding activities were internalised. As such, earlier studies looked at the horizontal host effect of MNE activity – the effect of FDI on competing host country domestic firms. The early 1990's saw an increased

interest in what was by then becoming a “leaner” MNE. Outsourcing became prominent and the MNE’s value chain became more fragmented and globally dispersed. This increased propensity towards outsourcing was not limited to auxiliary activities. Instead, it was common for MNEs to outsource activities that were once considered core primary functions (Denicolai et al., 2015). In the early 2000s, this trend intensified and gave rise to the empirical lens of global value chain (GVC) analysis (UNCTAD, 2013). This is the focus of this thesis, one that looks outside of the MNE’s horizontal host country impact. Instead, I will investigate the relational and non-equity engagements of the MNE.

In the case of the vertically integrated MNE, preventing knowledge leakage to host country competitors is paramount. This assumption has been relaxed for the fragmented MNE seeking to externalise key activities (Javorcik, 2004). In this context, the MNE and the domestic firm are perceived less as rivals and more as co-creators of value (Scott-Kennel and Enderwick, 2004; Ernst and Kim, 2002). This perspective has given prominence to the concept of economic upgrading and the positive role that the MNE can play in the development of its contractual partners.

Economic upgrading is not reserved for only activities that were once internalised by the MNE. It is true that many MNEs have increased the proclivity towards the externalisation of primary production. Even so, and as this thesis’s case study will illustrate, economic upgrading is compatible with activities that the MNE might have never conducted internally. In this thesis, I look specifically at this concept of economic upgrading and the conditions on which it occurs. Particular attention is placed on how it is defined, the manner in which it has been operationalised and its implications for the distribution of value-added.

1.2 The research problem

In this dissertation, I contend that economic upgrading from GVC participation is an adequately researched but under-theorised phenomenon. Eakin and Mykhalovskiy

(2003) defined under-theorisation as “the failure to conceptualise the data beyond everyday ‘common sense’” (pp.190). Elaborating on this, I refer to under-theorisation as instances where the abstraction of empirical insight is limited to explication superficial relationships - where a clear understanding of the contingent factors is absent. In other cases, the argumentation that underpins these relationships can be marred by strong underlying assumptions that are inconsistent with the empirical world (Alvesson and Sandberg, 2011). These assumptions may not always be explicit or even known to the researcher.

Such a research landscape provides opportunities to advance our understanding of both the phenomenon as well as general bodies of theory. On one hand, grounding empirical insight within a stronger theoretical framework can enhance our understanding of key aspects of the phenomenon. Likewise, empirical contexts that have previously eluded theoretical scrutiny provide fertile ground to extend, elaborate or refine substantive bodies of theory (Buckley et al., 2007a).

This dichotomous predicament fits well with this dissertation. The last two decades have seen a significant amount of studies on economic upgrading from GVC participation. Even so, economic upgrading itself has received little conceptual scrutiny. A great deal of the literature has focused on the process by which knowledge, resources and technology are transferred from the MNE to other actors in the value chain. This has given rise to various typologies for interfirm governances coupled with numerous classifications outlining how economic upgrading may manifest itself (Gereffi et al., 2005).

Despite this mass of empirical insight, little theorization has been conducted regarding the terms on which upgrading occurs. While economic upgrading may assist in the creation of value-added, the literature falls surprising short on how this value-added may be distributed amongst the various actors. This shortfall transcends silence. Instead, strong assumptions are made regarding the effect that economic

upgrading “trajectories” have on interfirm bargaining power. I use this standoff as a starting point to investigate the phenomenon of economic upgrading from GVC participation.

1.3 Research questions

Three research questions guide this investigation. Each research question is driven by the problematization mentioned in Section 1.2.

RQ1 – How is the concept of economic upgrading utilised in the GVC literature?

This initial research question seeks to gain insight into the current conceptualisation and operationalisation of economic upgrading. As I have alluded to in Section 1.2, the concept itself has received little critical consideration in the literature. This research question sets the foundation for a systematic review of the GVC literature on economic upgrading. The core assumptions are brought to the forefront and its potential implications discussed.

RQ2 – How does economic upgrading affect value-added distribution within the interfirm relationship?

As Chapter 4 will discuss, one of the core shortcomings of the GVC work on economic upgrading is related to its assumptions around value-added creation and its distribution. It is typical for studies to evaluate upgrading solely on its potential to create value-added. As a result, the implications of value-added distribution and interfirm bargaining power are assumed to be either negligible or in the domestic firm’s favour. This research question tackles this aspect of the phenomenon.

RQ3 – Do the effects of economic upgrading permeate to the lower tiers of the value chain?

It is common for the MNE to only have direct interactions with the 1st tier of the GVC. As such, studies investigating economic upgrading have remained fixated on explicit MNE engagement and direct coordination. Beyond this, research has remained somewhat silent on the role and influence of the MNE on the upstream actors of the

GVC. This research question address this void in the literature. It does so by mapping the effects that 1st tier economic upgrading can have on the lower tiers of the GVC. The lack of formal or explicit engagement should not imply that the MNE has relinquished its influence over these lower tiers.

1.4 Thesis structure

This thesis is separated into eight chapters. An overview of these chapters is as follows:

Chapter 2 describes two alternative perspectives that are frequently employed to investigate the effects of MNE activity on domestic firms in the host country. I first introduce the work on knowledge spillovers, with particular emphasis on vertical linkages. In the process, I highlight some of the agenda's shortcomings. A similar review is performed on the work of economic upgrading from GVC participation. I consider this chapter as the background chapter. This was deliberate in order to highlight the a-theoretical nature of both perspectives. I argue that neither the work on knowledge spillovers nor economic upgrading has a strong theoretical underpinning. Instead, they implicitly leverage on a set of assumptions where relationships are typically posited based on logic and intuition. After presenting both perspectives, I suggest that a GVC framing is the most appropriate contextual lens - given the thesis's focus.

Chapter 3 presents the first part of the thesis's research methodology. It is somewhat unconventional for a monographic thesis to dissect its methodological insights into two distinct parts. However, this was necessary to present details when most appropriate. In this first part, I present methodological insights related to the thesis's abductive research approach with particular emphasis on the manner in which theory will be utilised.

Chapter 4 begins with a problematization of the research around economic upgrading. Here, the purpose is to provide a more complete review of this conceptual

shortcoming and the implications that may arise from such oversight. Specifically, I highlight the tendency for GVC studies on economic upgrading to implicitly assume a symbiotic relationship between the creation and appropriation of value-added. Building on this problematization, I present the a priori theoretical framework that will form the foundation for the abductive approach to theory building. This framework is constructed by leveraging on theoretical insights from TCE and power dependence theory. This framework, while robust, remains sufficiently flexible to allow for successive modifications based on empirical insight.

Chapter 5 provides details about the data collection methods employed in this study. This thesis adopts a single embedded qualitative case study where data is collected across three tiers of a global value chain. The research approach is an abductive one where Chapter 4's a priori framework guides the data collection process. Beyond this, the abductive approach facilitates theoretical modification to the a priori theoretical framework - through an iterative process. This chapter justifies this pragmatic methodological approach by elaborating on the (1) sampling strategy (2) chosen case (3) data sources (4) data analysis process.

Chapter 6 and **7** present the findings of the 1st and 2nd tiers of the value chain respectively. Data related to the MNE-domestic processor and domestic processor-domestic farmers are reported and analysed. In both value chain tiers, elements of the theoretical framework are supported by empirical data from the case study. Even so, other aspects are not readily reconcilable with the Chapter 4's arguments. This theoretical disconnect facilitated the abductive approach outlined in Chapter 3, an approach that transcends deductive theory testing. Unexplained empirical findings were referred back to the substantive bodies of theory to determine if suitable explanations were omitted from the theoretical framework. The thesis's main theoretical contribution was developed through this iterative process. The empirical data allowed for a dynamic and processual view of economic upgrading that could

not be well explained by the largely static view of transaction cost and power-dependence theories.

Chapter 8 summaries the thesis's findings with a clear articulation of its theoretical contribution. A portion of the chapter is dedicated to addressing the managerial and policy implications. The limitations of the study and areas for further research are also discussed.

Chapter 2

Framing the research: Linkage effects versus economic upgrading

2.1 Chapter overview

This chapter outlines the empirical framing that will be used to position this thesis. When I refer to empirical framing, I am concerned with the research agenda or perspective that the phenomenon is grounded within. As such, this chapter does not engage in any discussion of the theoretical arguments that will underpin this thesis. Theory will be discussed in Chapter 4.

This chapter is necessary given the propensity for many international business phenomena to be disaggregated and looked at from varying perspectives. These varying perspectives give rise to different streams of academic research – which are sometimes developed in isolation of each other. This diverse research landscape is evident in works that look at the developmental implications (host country) of international business. When parallel research streams exist, it is important to give consideration to this diversity and align the thesis to the one deemed most appropriate.

Section 2.2 provides what I refer to as a primer on the MNE. I argue that while theories on the MNE may differ, they all position firm-specific advantage as the catalyst for internationalisation. In Section 2.3 I look specifically at the developmental agenda with international business research. I contend that this developmental agenda is largely driven by a reversal of this assumption of MNE firm-specific advantage. I take this opportunity to review the work on spillover and linkages effects – the dominant developmental perspective within international business. In Section 2.4, I discuss the increase in global trade fragmentation and the pressure it places on the relationships that have been deduced from the spillovers literature.

In Section 2.5, I introduce the concept of economic upgrading and its relationship with GVC participation. Via Table 2.3, I use this section to contrast both the spillovers and economic upgrading literature streams to highlight the (1) underlying assumptions (2) empirical focus (3) key determinates (4) conceptual shortcomings. Following this comparative assessment, I conclude with Section 2.6 where I position the GVC and economic upgrading literature stream as most appropriate - given the thesis's focus.

2.2 A primer on the multinational enterprise

This thesis investigates the developmental implications for domestic firms that engage with MNEs. I place theoretical emphasis on what was once broadly considered the externality effect of MNE operations (Caves, 1974). In the international business literature, this relationship between the MNE and domestic firms in host countries has been a controversial one. On one hand, the MNE's presence in the domestic economy and its interaction with indigenous firms is seen as having predominantly positive implications (Hamida and Gugler, 2009). Conversely, studies have also found negative relationships between MNE activity and domestic firm development (Görg and Strobl, 2001).

Concurrent with this debate, the focus has shifted away from understanding the impact of direct forms of MNE host country involvement such as FDI (Crespo and Fontoura, 2007; Meyer and Sinani, 2009). Instead, more recent streams of research focus on investigating the implications of non-equity modes (NEMs) of engagement (UNCTAD, 2011; Buckley, 2009). This pivot in MNE production strategies is seen as a positive shift for firms in developing countries (Giroud and Scott-Kennel, 2009; Ivarsson and Alvstam, 2009). Proponents of this view argue that NEMs facilitate linkages with MNEs that are more pronounced thereby forging a stronger conduit for resource and knowledge transfer (Ivarsson and Alvstam, 2011). This thesis places emphasis on the latter types of engagements where it looks specifically at the

phenomenon of firm-level economic upgrading from GVC participation. To understand the underlying premise of both developmental perspectives, we must first understand the theoretical justification for the MNE's existence.

The question of what makes the MNE the ideal structure to organise economic activity is tied to the domestic development logic that this thesis will investigate. To illustrate this, I will focus briefly on three widely used theoretical perspectives on the MNE, namely those associated with Hymer (1976) – rent-seeking view of the MNE, Buckley and Casson (1976) – internalised view of the MNE and Kogut and Zander (1992) – knowledge-based view of the MNE. These theories represent unique perspectives where each other's underlying assumptions are not always in harmony (Forsgren, 2013). The differences are strongest in their arguments on why the MNE exists. When I refer to disagreement on "why the MNE exists", I emphasize the long standing debate on why firms choose ownership over other forms of international operation (Yamin and Forsgren, 2006).

The body of theory around Hymer (1976) positions the MNE as a mechanism for hierarchical control. Direct ownership allows the MNE to better close markets, control competition and achieve above-average profitability in the foreign market (Hymer, 1970). Conversely, Buckley and Casson (1976) based their logic of the MNE's existence on insights from transaction cost economics (TCE) (Coase, 1937). Here the MNE exists as it is the most efficient coordinating mechanism for many aspects of cross-border activity. Problems arising from uncertainty, information asymmetry and opportunism make contracting with the agents in the foreign market an inefficient and costly organising mechanism (Forsgren, 2013). These problems become more acute for knowledge-driven MNEs (Buckley and Casson, 2009). Proponents of Kogut and Zander (1992) position the MNE as a repository for knowledge. This knowledge is multi-faceted and is embedded in organisational routines, experiences and the competences of individuals. Transferring this knowledge within a single multinational

entity may not necessarily be constrained by cost and efficiency considerations as dictated by Buckley and Casson (1976). Instead, the firm may not be able to package and transfer certain knowledge outside its hierarchical confines, regardless of the cost – hence the MNE is born (Kogut and Zander, 1993).

The above theoretical outline is intentionally simplistic as it is not my aim at this point to provide a detailed review of international business theories. Instead, it was meant to illustrate that the discussions around the MNE are unsettled. In the midst of the disagreement, there is still a common thread that runs through all of these theoretical perspectives. They all position firm-specific advantage as the catalyst underlying internationalisation.

For instance, Hymer (1976) is largely credited with conceptualizing the liability of foreignness (Petersen and Pedersen, 2002). This liability is manifested in the costs that a firm operating in a foreign market is likely to experience that a local firm will not incur (Zaheer, 1995). Hymer argued that the firm must, in turn, possess some firm “special” or monopolistic advantage that allows it to not only neutralize the liability of foreignness, but also permit superior earnings (Forsgren, 2013). Buckley and Casson (1976) and Kogut & Zander (1992; 1993) adopt a similar underlying assumption of superior capabilities. They both emphasise the importance of knowledge as a superior asset driving cross-border activity. Buckley and Casson (1976) argue that the firm is more likely to internalize its foreign operations when the core activities are knowledge or intangible based. Information asymmetry and the possibility of opportunistic behaviour makes coordinating via interfirm arrangements difficult and costly to monitor. Kogut & Zander (1992; 1993) explicitly position firm-specific knowledge-based advantages as the pivotal factor promoting cross-border activity by firms.

The above are only three of the dominant theoretical perspectives in international business research. Even so, the underlying logic of resource, asset or capability

superiority is also consistent with the strategy-oriented theories that have made its way into the study of international business phenomena. These strategy oriented theories include, but are not limited to, the resource-based (Wernerfelt, 1984; Barney, 2001) and the dynamic capabilities (Teece and Pisano, 1994; Teece et al., 1997) views of the firm.

2.3 MNE activity: the developmental agenda

I have highlighted that a core assumption justifying cross-border activity is the possession of firm-specific advantages (Dunning, 2000). The international business literature on host country firm development has, in principle, repositioned this assumption. Here the logic is simple, MNE activity represented in the flow of foreign direct investment (FDI) involves more than capital transfer. The knowledge, experience and managerial skills mentioned in Section 2.2 will also be embodied in the MNE's host country activities (Blomström and Kokko, 1998). As such, firms in the domestic economy can benefit from what the literature refers to as FDI or knowledge spillovers (Branstetter, 2006). These implications can be both horizontal and vertical and may not be uniformly positive for the domestic firms (Crespo and Fontoura, 2007). Horizontal spillovers are those affecting domestic firms that perform operations in areas similar to the MNE. From this perspective, spillovers are attributed to one of the following (1) competition, (2) demonstration effects or (3) labour mobility (Liu et al., 2009). Horizontal spillovers imply that there is little direct link between the MNE and the domestic firm¹. Instead, the spillover benefit happens as a consequence of the MNE's operations. In fact, MNEs actively try to prevent these spillover effects but are usually unable to achieve full appropriation due to the public good nature of knowledge (Kneller and Pisu, 2007). For instance, demonstration effects occur through observation, where domestic firms are able to study and replicate superior MNE practices (Chang and Xu, 2008). Labour mobility effects manifest when skilled

¹ The term domestic firm is used throughout this thesis to represent the indigenous firms in the host or overseas country

employees leave the MNE and subsequently take up jobs at domestic firms. The assumption is that the employee will bring with them valuable knowledge and experience from their time at the MNE. Likewise, competition effects can push domestic firms to make more efficient use of resources in light of competitive pressure from MNEs (Crespo and Fontoura, 2007).

Studies have urged caution in assuming only positive horizontal effects. MNEs equipped with superior firm-specific assets can also force domestic firms to operate on a less effect scale, bid up the price of skilled domestic labour, and crowd-out them altogether (Aitken and Harrison, 1999). As such, it is reasonable to expect that the empirical evidence on horizontal spillovers has been inconclusive. Meyer and Sinani (2009) conducted a meta-analysis of 66 studies that investigate FDI based spillovers. Of these 66 studies, almost half had results that reported either a negative or partially insignificant relationship between domestic productivity and FDI presence (Meyer and Sinani, 2009). An earlier review by Görg and Greenaway (2004) made similar conclusions where 18 of the 40 studies in the sample reported ambiguously positive or insignificant relationships (Görg and Greenaway, 2004).

Even so, the research agenda on horizontal spillovers appears to have subsided owing to a general consensus on the role of moderating factors. For instance, Meyer and Sinani (2009) argued that the quality of host country institutions explains much of the disagreement in the empirical evidence. Appropriate technological gap between the MNE and domestic firms are also seen as a key moderator of FDI related spillovers (Buckley et al., 2007b). Too small a technological gap then the domestic firms has minimal scope for spillover benefit (Kokko, 1994). If the gap is too large, domestic firms are unable to internalise elements of the MNEs advantages, more so in instances where domestic absorptive capacity is low (Crespo and Fontoura, 2007).

Vertical linkages are typically more explicit forms of benefits and possess the greatest level of empirical overlap with studies on economic upgrading from GVC participation.

They occur via formal relationships with domestic firms where the effects are more intentional (Giroud and Scott-Kennel, 2009; Hansen et al., 2009). In order to carry out activities domestically, the MNE may opt to source intermediary inputs locally (backward linkages). In other instances, the MNE may create new supply markets from which domestic firms can source from (forward linkages). Unfortunately, work on backward and forward linkages have not received as much attention as horizontal spillovers (Liu et al., 2009). In the limited empirical studies conducted, the results are less conflicting relative to horizontal spillovers (Havranek and Irsova, 2011). Javorcik (2004) argued that this may be because MNEs have the incentive to prevent leakages to their immediate competitors (horizontal spillovers) but may be more inclined to work with intermediate suppliers and buyers to enhance their operations. It is common for the vertical linkage literature to start with the implicit assumption that relationships with the MNE will make available knowledge and resources that can lead to improved domestic firm performance. This is consistent with Javorcik (2004), where MNEs are incentivised to help enhance the capabilities of its domestic links. Many studies are thus constructed to examine the role of various contingent factors in promoting or nullifying positive linkages effects. In line with the work on horizontal spillovers, technological gaps and absorptive capacity are seen as important determinants of linkage effects (Crespo and Fontoura, 2007). Liu et al. (2009) echoed the importance of domestic technological prowess when they found that domestic state-owned enterprises (SOEs) gained from vertical linkages, while non-SOE firms did not. The authors argued that this may be due to higher capabilities within SOEs (Liu et al., 2009). Other studies such as Belderbos et al. (2001) argued that the quality of host country infrastructure and local content regulations promote MNE vertical linkages with domestic firms.

The majority of linkage studies assume homogeneity in the linkages. However, the nature of MNE-domestic firm relationships are not uniform and little is known of (1)

the linkage characteristics that make some more beneficial or (2) exactly how linkage benefits manifest themselves. Giroud and Scott-Kennel (2009) argue that there has been insufficient conceptualisation of the linkage phenomenon where researchers have not been able to identify or develop the underlying constructs that determine the efficacy of linkages (Giroud and Scott-Kennel, 2009, pp. 555). Studying the role of institutional and firm-level characteristics on linkage effects is useful. However, we also need to consider that MNE-domestic firm relationships and the nature of the linkage are idiosyncratic. The authors argue that not all linkages have the same intensity and do not offer up homogeneous benefits to the domestic firm. For example, any given MNE relationship will have varying levels of linkage scope, quantity and quality (Giroud and Scott-Kennel, 2009). The agenda's focus on firm-specific (e.g. absorptive capacity) and location specific (e.g. institutional quality) influences tend to overshadow the importance of these relationship specific factors.

2.4 The rise of vertical fragmentation: new opportunities for development

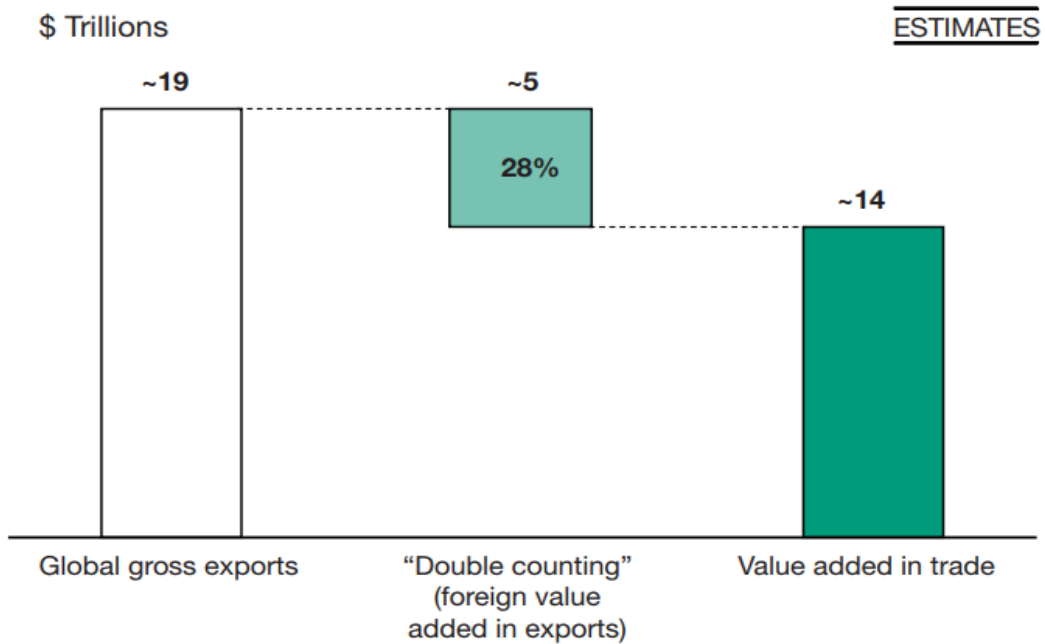
I have thus far acknowledged that the FDI spillovers literature overlaps with studies focusing on economic upgrading from GVC participation. As such, it is important to consider its contribution towards understanding the developmental implications of MNE activity. In the process, I have highlighted some of its shortcomings. Specifically, that little emphasis has been placed on understanding issues internal to the relationship or specific to the linkage (Driffield et al., 2002). Recent work has begun to address this (Giroud and Scott-Kennel, 2009; Giroud et al., 2012).

Even so, deeper theoretical understanding of the role of endogenous relationship factors is needed. Recent MNE led-trade developments have placed increased pressure on the spillovers literature to explain domestic development from MNE activity. These global production trends can be captured in the (1) intensity of value chain fragmentation and dispersion and (2) increase non-equity MNE orchestrated relationships.

In 2013, the United Nations Conference on Trade and Development (UNCTAD) provided insight on what it called rising global value chains (GVCs) (UNCTAD, 2013). In 2014, the Organisation for Economic Co-operation and Development (OECD) followed with a report on “Global Value Chains: Challenges, Opportunities, and Implications for Policy” (OECD, 2014a). The general consensus was that MNE-led value chains have become increasingly fragmented. Fragmentation in this sense is akin to what Buckley (2009) referred to as “activity fine slicing”. The functional view of value creation has morphed into a disintegrated approach where MNEs are now more inclined to break up functional areas into activities and individual tasks (Buckley and Ghauri, 2004). This is reflected in macroeconomic trade statistics. The UNCTAD (2013) estimated that around 60% of global trade consists of trade in intermediate goods and services.

This disintegration of value-added functions is considered in combination with location optimality. Together they are central to the MNE’s strategy of creating and maintaining a competitive advantage by capitalizing on location bound comparative advantage (Dunning, 1977; Mudambi and Venzin, 2010). This global fragmentation is so pronounced that UNCTAD estimates (2010 figures) that approximately 28% of global export trade are double counted (UNCTAD, 2013). Figure 2.1 illustrates the extent of double counting in traditional trade statistics. This double counting can be attributed to globally dispersed and fragmented trade strategies. It captures instances where intermediate goods and services move across borders multiple times before it is ready for final consumption. Each time the intermediate leaves a country, its total value-added up until that point is captured in gross exports. This is inclusive of the value-added that is attributable to a separate fine-sliced activity that occurred in another country.

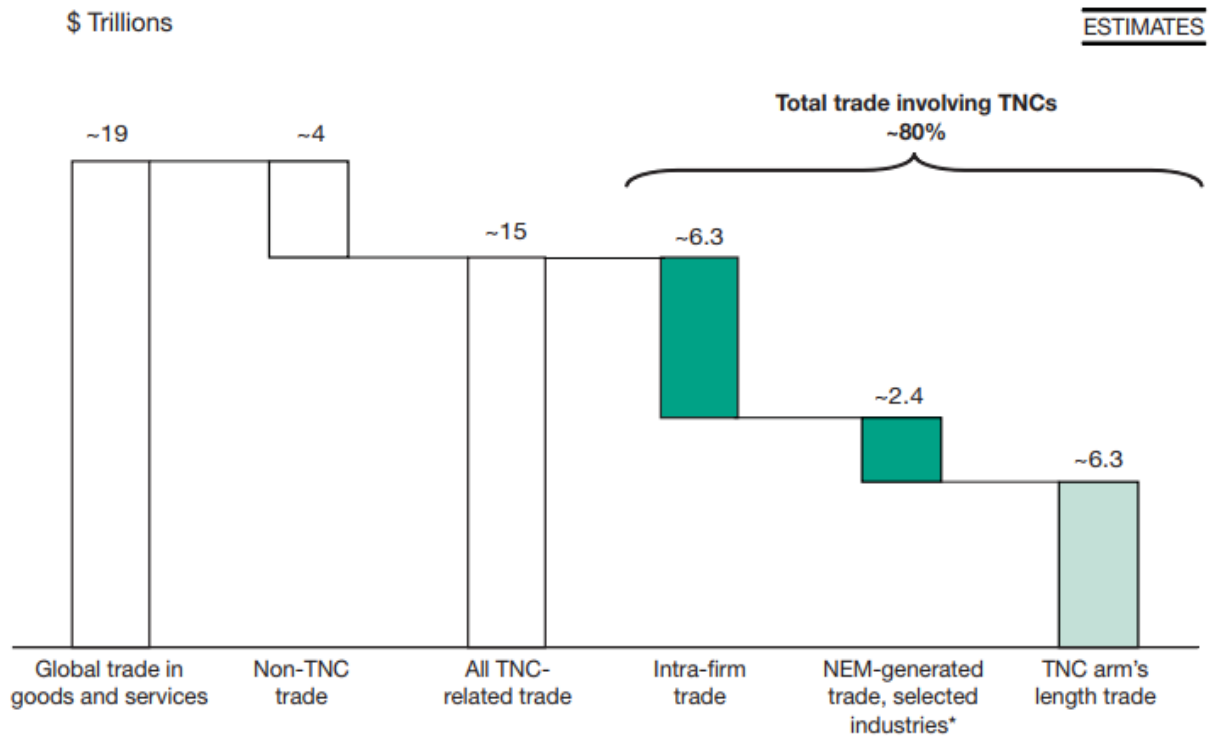
Figure 2.1 Value added in global trade, 2010 (US\$)



Source: UNCTAD (2013)

The fragmentation and dispersion of value chain functions represent only part of the rising GVCs narrative. It is a manifestation of the MNE's optimal level of activity fine-slicing and the most optimal location in which to undertake it (Buckley, 2009). It does not include decisions on orchestration, that is, how the fine-sliced activity will be organised and controlled. The traditional MNE was highly integrated both vertically and horizontally, where FDI was the primary internationalisation mechanism (Hymer, 1976). Within this hierarchical structure, each unit was embedded into linkages with other divisions (Buckley and Ghauri, 2004; Strange and Newton, 2006). MNEs are now increasingly willing to engage in various forms of non-equity production strategies and UNCTAD (2013) estimates that almost 60% of this MNE-related trade is contractually based. Figure 2.2 provides an aggregate breakdown of MNE related trade and the extent to which such trade is internalised or externalised.

Figure 2.2 Global gross trade by type of MNE involvement, 2010 (US\$)



Source: UNCTAD (2013)

I will discuss the dominant arguments that have been advanced to explain the sharp increase in both global fragmentation and NEMs of engagement in Chapter 4. I will also use that opportunity to highlight some of the internal conflicts within these lines of reasoning and why more theoretical refinement is needed. Thus far, I have positioned the work on spillovers (horizontal and vertical) as the dominant IB perspective on domestic firm development. However, its tendency to focus on empirically driven, aggregate analyses makes it difficult for the agenda to account for the implications of rising GVCs. I will illustrate this by applying the spillover-based logic to both of these GVC trends: 1) intensity of value chain fragmentation and dispersion and (2) increase non-equity MNE orchestrated relationships.

Although horizontal spillovers are not the focus of this thesis, it is necessary to illustrate the pressure that rising GVCs place on the ability of the entire spillovers literature to explain domestic development. As I have previously highlighted, the

literature starts with the assumption that there is useful and valuable knowledge embedded in capital flows. The increased propensity for MNEs to “fine-slice” its value chain places pressure on this fundamental assumption. As the propensity for activity disintegration increases, it is likely that the knowledge embedded within each individual capital flow (subsidiary activity) also diminishes. In the case of horizontal spillovers, increased value chain disintegration can present situations where offshored subsidiary activities are only useful in combination with other MNE units, but not independently. This possibility is overlooked in spillover studies. Focusing on aggregate flows implicitly assume that FDI investment in the form of foreign operations represents a monolithic element of the MNE’s value chain operation.

However, diminished activity scope can render traditional horizontal spillover mechanisms ineffective. Labour mobility effects may be questionable if the employee was only exposed to an isolated aspect of the MNE’s operation. In a fragmented and dispersed value network, it is likely that the former MNE employee was unable to gain an accurate understanding of how isolated tasks integrate with other value chain activities. Demonstration effects can also be misinterpreted by domestic firms that seek to observe the subsidiary’s operations. The benefits can become marginal if domestic firms are unable to understand and apply the narrow elements of the subsidiary’s operations. It can also contribute negatively if local firms wrongly copy what they believe to be the MNE’s organisational practices.

Even in light of this, the MNE may still be able to reconstruct fragmented pools of subsidiary knowledge into a competitive advantage (Kogut and Zander, 1992). This argument can also be applied to MNEs that engage in what might be considered competence exploiting activities (Cantwell and Mudambi, 2005). Take manufacturing, for instance, each fragmented subsidiary may only be responsible for the production of a narrow range of components. These components together with those from other fragmented and globally dispersed subsidiaries can then be combined at a central

location. In GVC situations like this, positive horizontal spillover becomes questionable. Aggregate figures discount the heterogeneity of FDI inflows and the possibility that GVC fine-slicing may negate the potential for any domestic spillover. In this sense, it is possible that a host country can experience an increase in inward FDI flows without producing a result that the horizontal spillover literature would hypothesize.

This argument is illustrated in a recent study by Gooris and Peeters (2016). The authors show that the degree of activity fine slicing is not solely influenced by the prospect of tapping into location advantages (Dunning, 2000). With empirical support, they argued that MNEs also engage in value chain fragmentation to reduce horizontal spillover effects, especially when host countries offer weak legal protection (Gooris and Peeters, 2016). Relevant to this thesis is the chain of causality which can be deduced from the paper's findings. More specifically, that the absence of positive externalities is not merely a by-product of increased GVC fragmentation. Fragmenting processes across multiple foreign production units, as opposed to a concentrated FDI strategy, may be a strategic MNE appropriation mechanism (Gooris and Peeters, 2016).

More relevant to this thesis is the theoretical pressure rising GVCs places on the spillovers literature dedicated to linkages effects. This pressure is related to increases in non-equity MNE relationships (UNCTAD, 2011; 2013). Backward linkages have traditionally focused on the sourcing of secondary inputs, where the linkages are auxiliary to the MNE's main line of activity (Lin and Saggi, 2007; Spencer, 2008). In most cases, these studies make no distinction regarding domestic supplier tiers. MNEs are now increasingly relinquishing ownership of main aspects of the value chain (Buckley and Strange, 2015; Strange and Newton, 2006). These activities are not restricted to the supply of auxiliary inputs but can represent an MNE's decision to outsource all its production activities. There are many prominent

examples, including American electronics giant Apple (Dedrick et al., 2010), Swedish furniture retailer IKEA (Ivarsson and Alvstam, 2010) and German designer clothing company Hugo Boss (Tokatli, 2007a). The externalisation of what might be considered core functions has not been limited to production activities (Grimpe and Kaiser, 2010). Firms in the biopharmaceutical industry, for example, have been engaging in significant levels of R&D outsourcing (Sen, 2009).

It is debatable whether these externalised activities conform to what might be considered the MNE's competitive advantage (Barney, 2001) - I will pick up this debate in Chapter 4 when I introduce the thesis's conceptual framework. Less debatable is the role of these externalised activities in bringing the MNE's product to market. These relationships transcend arm's length exchange (Veugelers and Cassiman, 2004; Hansen et al., 2009). They are likely to be processual – in that they frequently repeated and develop incrementally over time (Ivarsson and Alvstam, 2011; Duanmu and Fai, 2007). This form of externalisation brings the forefront issues of governance, bargaining power and value-added distribution (Strange and Newton, 2006).

It is reasonable to posit that a stronger positive correlation between rising core activity subcontracting and MNE-led learning in domestic firms will exist (Javorcik, 2004; UNCTAD, 2013). Giroud and Scott-Kennel (2009) argued that the linkage literature was unable to identify the underlying constructs that determine the efficacy of linkages. Even so, the definition of efficacy is fairly consistent, where learning and knowledge transfer are means to produce increases in valued-added (Saliola and Zanfei, 2009). The use of total factor productivity (TFP) in many aggregate studies supports this efficacy measure (Liu et al., 2009; Driffield et al., 2002; Havranek and Irsova, 2011). While the ownership separation in subcontracting relationships are unambiguous, rising GVCs blur the control boundary between the MNE and the domestic firm (Buckley and Strange, 2015; Buckley, 2009). Ownership and control

are not always synonymous and the ownership of assets is not necessary for a firm to possess control over its use (Strange and Newton, 2006). Control not only influences how production is orchestrated, it is also instrumental in determining how value-added is distributed. The vertical linkages literature has not fully addressed issues related to control despite its influence on the efficacy of linkage effects.

The inability of the vertical linkage literature to provide insight into these important dimensions is illustrated in a study by Driffield et al. (2002). Regarding intra-sectoral backward linkages, the results suggest a negative relationship between MNE involvement and gross domestic value-added output. More specifically, intra-industry sales by domestic firms supplying inputs to MNEs in the same industry resulted in poorer performance for the domestic sector (Driffield et al., 2002). This result is counterintuitive to what is postulated by the linkage literature (Javorcik, 2004). This is more so the case for intra-sectoral linkages where the MNE is more likely to possess appropriate knowledge to the domestic firm's benefit (Buckley et al., 2007b; Los and Timmer, 2005). The authors were not able to leverage on the prior linkage literature to explain this result. Instead, they suggested that the inverse relationship may be driven by circumstances where the MNE is able to appropriate away the linkage benefits that originated in the domestic firm (Driffield et al., 2002). Assuming that this is an accurate rationalisation, our understanding of how these adverse effects materialise still remains unresolved within the vertical linkage research agenda.

The vertical spillovers literature tends to cluster domestic linkages into abstract learning categories (Giroud et al., 2012; Hansen et al., 2009). A considerable amount of detail is lost in the process and little is known about the nature of the technology transfer, or the conditions under which it occurs. A domestic firm may adopt new technology that allows them to increase their production output significantly. However, this level of insight is not adequate to determine the amount of value-added that the

firm may be able to appropriate from this investment – a key research question of this dissertation. For instance, this investment may only be sustainable if the domestic firm can maintain a certain level of demand. If the MNE is the only entity capable of filling this demand then this alters the relationship's control and bargaining dynamics and is likely to have an effect on the distribution of value-added (Ivarsson and Alvstam, 2011). Testing how efficiently and intensely the domestic firm inputs are utilised (TFP) also does not provide transactional details of various linkage benefits (Perri and Peruffo, 2016). Naturally, these macro-level analyses are conducted by sacrificing a deeper theoretical understanding of the role of micro foundational factors.

2.5 Economic upgrading from GVC participation

The global value chain research agenda has taken us closer towards understanding the multi-dimensions nature of linkage effects via the concept of economic upgrading. Economic upgrading represents the positive impact that is accrued to various economic actors from their involvement in GVCs (Gereffi, 2005). Earlier work by Gereffi (1994; 1999) established the empirical foundation for studies on economic upgrading. Upgrading was described as the process where firms move into more profitable and/or technologically sophisticated capital and skill-intensive niches (Gereffi, 1999b). Humphrey and Schmitz (2002) later referred to it as increases in the skill content embedded within products or shifts in firm activities that allow for movement into market niches. These earlier definitions advanced the notion that domestic firms can become “better” through GVC induced strategies. For example, a firm may improve its current production processes to make them more efficient (Ivarsson and Alvstam, 2011). Others may broaden their activity scope to encompass new activities or functions e.g. research and development (R&D) or own brand marketing (Rossi, 2013). Table 2.1 outlines the categorizations that are frequently used to describe economic upgrading.

Table 2.1 Conventional view of upgrading trajectories

Upgrading Trajectory	Key Elements
Product	<ul style="list-style-type: none"> • The movement into sophisticated product lines (Gereffi, 1999b; UNCTAD, 2013) • Introducing new products or improving old products faster than rivals (Kaplinsky and Morris, 2002)
Process	<ul style="list-style-type: none"> • The ability to transform inputs into outputs more efficiently through superior technology or reorganised production systems (UNCTAD, 2013; Humphrey and Schmitz, 2002; Schmitz, 1999) • Increasing the efficiency of internal processes such that these are significantly better than those of rivals, both within individual links in the chain and between the links in the chain (Kaplinsky and Morris, 2002; Ponte and Ewert, 2009)
Functional	<ul style="list-style-type: none"> • Acquiring new functions within the chain. For example, Moving from production to design or marketing in order to increase the overall skill content of activities (Bair and Gereffi, 2001; UNCTAD, 2013) • Increasing value-added by changing the mix of activities conducted within the firm (for example, taking responsibility for, or outsourcing accounting, logistics and quality functions) or moving the locus of activities to different links in the value chain (for example from manufacturing to design) (Kaplinsky and Morris, 2002)
Chain	<ul style="list-style-type: none"> • The application of competencies acquired in a particular function of a chain to an entirely new industry (Guerrieri and Pietrobelli, 2004; UNCTAD, 2013) • Moving to a new value chain (Kaplinsky and Morris, 2002)

Source: Author


More recent upgrading definitions have begun to explicitly emphasize the value-added component of value chain participation (Giuliani et al., 2005; UNCTAD, 2013; Gereffi, 2005; Gibbon and Ponte, 2005; Milberg and Winkler, 2011). Here the notion of value-added is captured as an accounting measure (Mudambi, 2008). It represents the margins that a firm can achieve from its value chain activities. It is important to separate the concept of value from that of value-added. Value can be broadly defined as the price that a party is willing to pay for a good or service, usually based on the party's utility function for the good or service in question (Grewal et al., 1998). Value-added on the other hand represents the accounting different in the price that is paid for the good and the cost to produce or acquire the good (Haller and Stolowy, 1998). From this perspective, a rise in the value of a good is one of two ways in which value-added can increase. The other being any mechanism that can lower the cost of producing the good in question, while holding the selling price constant.

Frequently, the MNE is the orchestrator of the value chain where it controls the flow of knowledge and leads the organisation of activities throughout the entire chain (Gereffi, 1994; Saliola and Zanfei, 2009; Ponte et al., 2014). Similar to the research

on FDI spillovers, MNE firm-specific advantages act as the impetus for economic upgrading (Caves, 1974; Crespo and Fontoura, 2007). Interfirm relationships brought on by fragmented GVCs act as the conduit for knowledge and resource transfer. Many of these upgrading trajectories are frequently supported or initiated by the MNE (Ivarsson and Alvstam, 2011; Humphrey, 2004). MNEs are presumed to assist domestic firms in learning and upgrading their capabilities to maximise competitiveness and create value-added that can be of mutual benefit (Humphrey and Schmitz, 2002; Liu and Zhang, 2014). Ernst and Kim (2002) referred to these MNEs as “network flagships”. According to the authors, these “knowledge transfer mechanisms” can be mediated through market or non-market arrangements with varying levels of passivity. Actively, knowledge can be transferred to local firms through foreign licencing and technical consultations. On the passive side, flagships may also encourage local firms to accept sophisticated equipment as a means of improving their production capabilities (Ernst and Kim, 2002).

Unlike the vertical spillovers literature, the GVC agenda looks closer at the governance relationship between the MNE-domestic firms as an important element of economic upgrading. Gereffi et al. (2005) provided the GVC governance framework that is most often utilised to analyse economic upgrading. The framework defines three factors that determine which governance structure will be induced by the lead firm: (1) the complexity of the information, (2) the extent to which the information can be codified (3) the capabilities of the actual and potential suppliers (Gereffi et al., 2005) (see Table 2.2).

Table 2.2 Key determinants of global value chain governance

Governance type	Complexity of transactions	Ability to codify transactions	Capabilities in the supply base	Degree of coordination and power asymmetry
Market	Low	High	High	Low  High
Modular	High	High	High	
Relational	High	Low	High	
Captive	High	High	Low	
Hierarchy (internalization)	High	Low	Low	

Source: Gereffi et al. (2005)

Much of the literature on economic upgrading utilises this typology to explain the conditions under which upgrading is most likely to occur. They argue that relational and to a lesser extent, modular governance modes provide domestic firms with the greatest opportunity for substantial upgrading (Ponte et al., 2014; Jean, 2014; Pietrobelli and Rabellotti, 2011). According to this typology, a domestic firm that was once in a captive governance type may move into a modular or relational governance structure as its capabilities increase (upgrading). As these capabilities continue to increase, the degree of power asymmetry within the relationship becomes lower and the domestic firm is able to capture greater value-added (Gereffi et al., 2005).

Table 2.3 provides an overview of both the spillovers and GVC literature streams where their key attributes and conceptual shortcomings are highlighted. Here it is evident that the work on economic upgrading is not without its conceptual shortcomings. These shortcomings are evident in the assumptions around bargaining and the distribution of value-added. I will discuss these shortcomings in details in the problematization section of Chapter 4. Even so, it represents the most appropriate body of literature in which to ground this thesis. The empirical focus of studies on economic upgrading provides a good frame for investigating the transactional elements of MNE induced learning and knowledge transfer.

Table 2.3 Literature streams on domestic firm development

	FDI Spillovers		Global Value Chains (GVCs)
	Horizontal Spillovers	Vertical spillovers	Economic upgrading
Underlying Assumption	<ul style="list-style-type: none"> The FDI spillover and GVCs share a common underlying assumption: MNEs possess firm-specific advantages (FSAs) which sustains its cross-border activity. These FSAs may manifest itself in technological know-how as well as management skills and experience. When the MNE engages in FDI, elements of its FSAs are embedded in the inward capital flows. <ul style="list-style-type: none"> Horizontal spillovers - Blomström and Kokko (1998); Dunning (1977) Vertical spillovers - Rodríguez-Clare (1996); Hansen et al. (2009) Economic upgrading - Ivarsson and Alvstam (2011); Ernst and Kim (2002) 		
	<ul style="list-style-type: none"> Spillovers are positioned as an externality - Caves (1974). Effects on domestic firms are largely unintentional where the MNE endeavours to prevent knowledge leakage - Hallin and Lind (2012); Fosfuri et al. (2001) 	<ul style="list-style-type: none"> Spillover effects to domestic firms are largely intentional where the MNE endeavours to increase the capabilities of its backward links (suppliers) and forward links (buyers) - Javorcik (2004); Gentile-Lüdecke and Giroud (2012) 	<ul style="list-style-type: none"> Domestic firm upgrading is largely intentional where the MNE endeavours to increase the capabilities of its suppliers - Ivarsson and Alvstam (2011); Gereffi (1999b); Navas-Alemán (2011) MNEs dissuade or prevent domestic firms from encroaching on activities that are of competitive advantage - Pavlínek (2012); Choksy (2015);
Empirical focus	<ul style="list-style-type: none"> Studies based on the effect that MNE activity has on domestic firms in the same line of activity (competitors) – Crespo and Fontoura (2007) Empirical studies at aggregated levels of analysis. Domestic firm productivity regressed against foreign presence in the same sector - Caves (1974); Kokko (1994) 	<ul style="list-style-type: none"> The intentional assumption of vertical spillovers positions studies as investigations into factors hindering positive linkage effects - Javorcik (2004) Studies frequently at the sectoral or industry level focused on aggregate relationships - Havranek and Irsova (2011); Liu et al. (2009) 	<ul style="list-style-type: none"> Externalisation is not restricted to non-core or auxiliary inputs. MNE's frequently engage in the outsourcing of activities that important to bringing product to market - Gereffi (1999b) Emphasis on key manifestations of upgrading with rich description on the manner in which upgrading occurs in the domestic firm - Ivarsson and Alvstam (2011); Humphrey and Schmitz (2002)
Key determinants	<ul style="list-style-type: none"> Understanding the role of spillover channels on domestic firm development. These channels include: <ul style="list-style-type: none"> Competition - Spencer (2008); Mansfield and Romeo (1980) Labour mobility - Crespo and Fontoura (2007); Balsvik (2011) Demonstration - Wang and Blomstrom (1992); Das (1987); 	<ul style="list-style-type: none"> Understanding the influence of factors both exogenous to the linkage relationship itself. Factors are usually related to firm characteristics or institutional context. These factors include: <ul style="list-style-type: none"> Technological gap - Liu et al. (2009); Absorptive capacity - Marcin (2008) Host country context – Javorcik and Spatareanu (2009) Foreign ownership structure - Javorcik and Spatareanu (2008) 	<ul style="list-style-type: none"> Interfirm governance structure between the MNE and domestic firm as the key determinant of economic upgrading - Gereffi et al. (2005); Gereffi and Lee (2012); Humphrey and Schmitz (2004) Institutional voids and government intervention as dampeners on the MNE dominated inter-firm relationships and facilitators of financial resources and technological access - Tokatli (2007a)

	<ul style="list-style-type: none"> • Moderating consideration given to the role of country and firm-specific factors. These factors include: <ul style="list-style-type: none"> ○ Technological gap - Buckley et al. (2002); Zhang et al. (2010) ○ Absorptive capacity - Zhang et al. (2010); Mancusi (2008) ○ Entry mode and ownership structure - Javorcik and Spatareanu (2008); Blomström and Sjöholm (1999); Dimelis and Louri (2002) ○ Host country context - Meyer and Sinani (2009); 	<ul style="list-style-type: none"> • Recent studies argue for more consideration of relationship-specific factors. Including: <ul style="list-style-type: none"> ○ Linkage intensity captured in; (1) scope (2) quantity (3) quality - Giroud et al. (2012); Giroud and Scott-Kennel (2009) 	
<p style="text-align: center;">Conceptual Shortcomings</p>	<ul style="list-style-type: none"> • Domestic activities performed in offshored subsidiaries may not be “monolithic” or have value in isolation of other MNE units. This conceptual oversight places pressure on the spillovers literature to understand the implications of rising GVCs on domestic firm benefit - Gooris and Peeters (2016) 	<ul style="list-style-type: none"> • Rising GVCs deepen linkages with domestic firms. Relationships transcend arms-length arrangements and encroach on core activities. However: <ul style="list-style-type: none"> ○ Little known about the manner linkage benefits manifest in domestic firm - Giroud and Scott-Kennel (2009) ○ Positive aggregate relationship between MNE presence and domestic productivity can coexist with asymmetry in value-added capture. Even so, little consideration is given to interfirm governance - Driffield et al. (2002) 	<ul style="list-style-type: none"> • Inter-firm governance contributes to knowledge diffusion and capital deepening. However, physical upgrading of the production process of a supplier and the appropriation of the new value-added created may not be coterminous: <ul style="list-style-type: none"> ○ considerations around interfirm bargaining and the distribution of value-added are underdeveloped and underpinned by strong and potentially flawed assumptions - Bair (2005); Tokatli (2013)

Source: Author

2.6 GVCs – an empirical framing

Both the vertical linkages and GVC streams of research explore the development implications for domestic firms that engage with MNEs. In this chapter, I have outlined the reasons why the GVC perspective is best aligned with the objectives of this thesis. The decision to use a GVC approach over a vertical linkage perspective was not a decision based on theoretical grounding. In fact, it can be argued that studies based on either of these approaches are not explicitly grounded within a substantive theoretical paradigm. For instance, Perri and Peruffo (2016) argued that many studies on spillover effects lack proper theoretical development when positing relationships. Instead, they rely on intuitive logic to reason why certain variables should behave in a particular manner (Perri and Peruffo, 2016). A similar critique can be levied to work on economic upgrading from GVC participation. Peters (2008) argued that GVC analysis is primarily useful as a methodological tool for examining patterns of production, and the manner in which value-adding nodes are organised. My decision to frame the thesis from a GVC participation and economic upgrading perspective is made based on empirical grounds. This perspective provides a contextual framing that offers insights which can help develop a stronger theoretical understanding of the distributional effects of value-added creation. GVC analysis describes the structure and operations of global trade in a manner that moves beyond traditional country or industry-specific units of analyses (Brewer, 2015). A micro-level investigation into the value chain allows for a deeper understanding of how the pertinent activities are linked together. Beyond this, it allows me to probe the actors themselves to understand how their roles evolve over time and the effect that it has on their bargaining position within the value chain. This level of analysis is absent from the work on spillover effects.

As I conclude this chapter, I acknowledge that a well-articulated theoretical foundation is missing from this review of the literature streams. Chapter 4 addresses

this and will meld two theoretical perspectives to develop an a priori theoretical framework. This framework will be used as part of an abductive research approach that will (1) provide guidance through the data collection process (2) provide a foundation to embark on theoretical refinement.

Chapter 3

Research Methodology: Part 1

3.1 Chapter overview

It is common for monographic theses to present the research methodology in a specific manner. This conventional style of presentation bears two features. First, details of the research methodology are laid out in a single chapter. This single chapter approach provides insight on both (1) the research approach, and (2) the data and data analysis process. Second, this consolidated chapter is usually introduced *after* the author has presented any theoretical arguments or frameworks.

Given what could be considered the norm, this thesis adopts an unorthodox presentation of the research methodology. I have separated the research methodology content into two distinct parts (Chapter 3 and Chapter 5 respectively). Each part is introduced at specific stages of the thesis. I determine these junctures based on content appropriateness. Methodological insight presented prematurely can become disconnected from the overall thesis. Likewise, insight provided late fails to provide the reader with a timely explanation for the decisions made throughout the thesis.

In this first part, I focus specifically on articulating the research approach that underpins this investigation. I present this aspect of the methodology prior to Chapter 4's theoretical discussion. This is done to provide a comprehensive understanding of how theory will be used for the purpose of this thesis. This is necessary to properly introduce the abductive research approach that will underpin the thesis. The theoretical framework, and the manner in which theory is used, differs from the frameworks employed in deductive theory testing research. As such, it is necessary to articulate this approach prior to engaging in any theoretical discussion. Chapter 5 continues with the rest of the research methodology. In that segment (part 2), I focus specifically on methodological insights related to the sampling strategy, data

collection methods and the data analysis process. These details are presented prior to the empirical chapters of the thesis to maintain a smooth flow throughout the thesis.

The rest of this chapter is as follows. I first discuss the philosophical assumptions that will guide the thesis. I discuss the manner in which the phenomenon and the data will be construed. Section 3.3 delves into the thesis's research approach and focuses on two specific elements; problematization and abduction. Both these elements are central towards understanding the manner in which theory will be used in this study. In Section 3.4, I justify the research strategy and why a case study strategy is most appropriate to conduct the dissertation's theory elaboration objective.

3.2 Philosophical underpinning

Research projects usually adopt one of two philosophical underpinnings. On one hand, a researcher can conduct their investigation with a philosophical assumption that conforms to, or associated with a subjectivist ontology. Here, the researcher is guided by an ontological assumption where reality is seen as a projection of the human imagination (Cunliffe, 2011). Reality in this sense is socially constructed and objectivity or independent fact is not a core tenet. Instead, there may be many individual truths based on idiosyncratic perceptions and interpretations. Human beings create their own social realities as a mechanism to make their world understandable and intelligible. Within this assumption, individuals may not always possess isolated realities, but may collaborate with others to create a shared reality. Even so, this notion of reality is still a subjective construction, one which can dissipate once its members no longer sustain belief (Morgan and Smircich, 1980).

This thesis, and the methodology utilised within it, is however grounded within an objectivist ontology. This philosophical stance assumes that the phenomenon under investigation exists independently of the research's interactions or his/her individual perceptions. The phenomenon under investigation is seen as an objective occurrence, one that can be observed across individuals, regardless of their

individual perceptions. In doing so, I position the truth as having an independent external reality that is accessible through the registration of facts (Khin et al., 2011). This philosophical position permits me to record observations objectively, in which the truth underlying the phenomenon can be determined in an unbiased manner (Cunliffe, 2011).

As it relates to this thesis, the phenomenon under investigation focuses on firm-level economic upgrading and the process by which it occurs in underdeveloped firms that participate in GVCs. Economic upgrading is defined as firm-level structural changes which enable the organisation to increasingly create and appropriate value-added from its GVC activities. Beyond identifying the existence of firm changes, the thesis investigates the role of governance relationships between the MNE and the various tiers of domestic firms in this upgrading process. In both cases, it positions these changes and its role in value-added appropriation as observable and independent of the perceptions of the respondents and those connected with the phenomenon. Elements of subjectivity may be introduced if the research was interested in understanding a respondent's individual perceptions on what might be considered a fair distribution of value-added. However, while the thesis is qualitative in nature, value-added is treated as an accounting notion, one that is reflected in the margins that the firm is able to achieve from its GVC operations. Focus is placed on understanding the process by which asymmetry in the distribution of value-added may arise over time and the role that upgrading plays in this process. This research focus negates the introduction of subjectivist views, thereby making it consistent with an objectivist ontology.

3.3 Research approach

The thesis extends existing theory by developing novel insights regarding the process of GVC participation by domestic firms in developing countries. Particular focus is placed on understanding how the ability to create and capture value-added

is affected by the firm's interaction with the MNE. That being said, studies on the rise of GVCs and the implications of GVC participation on domestic firms in developing countries are not uncommon. The Global Value Chain Initiative and its database of published studies on the topic is a testimony to the significant body of work on the phenomenon (Global Value Chains Initiative, 2017). It would be overly harsh to assert that these prior works are devoid of empirical and policy contribution. Fresh studies seeking to advance knowledge in the field should take the opportunity to leverage on these studies, albeit with criticality. In the context of this thesis, they represent a collection of seminal and impactful studies on inter-entity bargaining, contractual inter-firm relationships and GVC participation. In combination, they provide a foundation for deepening our understanding of economic upgrading and the capture of value-added by underdeveloped firms, for example, Emerson (1962); Williamson (1996); Gereffi et al. (2005).

When undertaking a study around a phenomenon that has received significant attention, the researcher is usually faced with an important decision regarding the initial research approach. This decision is captured in the ongoing discussion around gap spotting versus problematization (Alvesson and Sandberg, 2011). In both cases, the researcher acknowledges that a substantial body of theoretical and empirical work on the phenomenon already exists. Tenants of the gap spotting approach consciously choose to contribute to the theory by simultaneously building on and manoeuvring around these studies by focusing on specific areas that can help close knowledge gaps. Knowledge gaps may manifest itself as research questions that shed light on areas or perspectives of a phenomenon that have received little attention. Gaps can also be constructed in situations where competing explanations or conflicting empirical findings exist leading to, for example, the need for greater contextual considerations. While this can be a complex and creative process, it is usually done within a framework that leaves the underlying assumptions of prior studies unchallenged (Alvesson and Sandberg, 2011).

Conversely, the research approach of this thesis is in line with a problematization methodology (Alvesson and Sandberg, 2011; Abbott, 2004). Rather than scanning for overlooked areas or attempting to compare alternative causal explanations, problematization looks more closely at the assumptions that underpin a concept or theory. Research questions are devised by challenging underlying assumptions with the aim of uncovering fundamental shortcomings of the dominant perspectives within the field (Alvesson and Sandberg, 2011; Deacon, 2000). In order to make theory generalizable, theoretical parsimony is usually required. Such parsimony is achieved, in part, by making specific assumptions regarding the relationship or phenomenon under investigation. While many of these assumptions are not always explicit, its implication on how we explain relationships and predict outcomes is profound. In certain cases, these assumptions are open to varying degrees of problematization.

The problematization strategy outlined in Alvesson and Sandberg (2011) provides the foundation for developing the initial focus of this thesis. Without a guiding structure, problematization as a research question development tool can become messy and confusing. Alvesson and Sandberg (2011) provide a useful typology of assumptions that are likely to underpin a particular research area. More importantly, they outline useful principles to help navigate the problematization process. An overview of Alvesson and Sandberg (2011) problematization approach is summarised in Figure 3.1.

Table 3.1 The problematization methodology and its key elements

Aim of the problematization methodology					
Generating novel research questions through a dialectical interrogation of one's own familiar position, other stances, and the literature domain targeted for assumption challenging					
A typology of assumptions open for problematization					
In-house: Assumptions that exist within a specific school of thought	Root metaphor: Broader images of a particular subject matter underlying existing literature	Paradigm: Ontological, epistemological, and methodological assumptions underlying existing literature	Ideology: Political-, moral-, and gender-related assumptions underlying existing literature	Field: Assumptions about a specific subject matter that are shared across different theoretical schools	
Principles for identifying and challenging assumptions					
1. Identify a domain of literature: What main bodies of literature and key texts make up the domain?	2. Identify and articulate assumptions: What major assumptions underlie the literature within the identified domain?	3. Evaluate articulated assumptions: Are the identified assumptions worthy to be challenged?	4. Develop alternative assumptions: What alternative assumptions can be developed?	5. Relate assumptions to the audience: What major audiences hold the challenged assumptions?	6. Evaluate alternative assumptions: Are the alternative assumptions likely to generate a theory that will be regarded as interesting by the audiences targeted?

Reproduced from Alvesson and Sandberg (2011)

Chapter 2's background review provided the reader with an overview of the dominant perspectives employed to study the domestic firm effects of MNE activity. Two mainstream perspectives exist, namely the research agendas on linkage effects and economic upgrading. An argument was then presented to justify the decision to adopt a GVC and economic upgrading framing for this thesis. Part of Chapter 4 employs this problematization methodology and will highlight the core in-house assumptions embedded in both the conceptualization and operationalisation of firm-level economic upgrading. This is an application of Principles 1 and 2 in Figure 3.1. An argument is then mounted to justify why this implicit assumption brought about by weak conceptualizations of economic upgrading has led to frequent inconsistencies between theoretical predictions and real-world outcomes (Tokatli, 2013; Brewer,

2015). This aspect of the argumentation is guided by Principles 3 to 6 in Alvesson and Sandberg (2011).

3.4 Theory elaboration through abductive reasoning

The problematization methodology outlined in Section 3.3 is restricted to crafting the initial research problem. It facilitates this by focusing on underlying assumptions in the literature that contribute to underdeveloped theoretical relationships. In other words, its value as a methodological tool is limited to informing the earlier phase of the research process. While challenging core assumptions can be viewed as a destructive process, it should not always be viewed as an attempt to discard entire streams of theory. Instead, I position it as part of a broader abductive approach aimed at theoretical elaboration (Fisher and Aguinis, 2017).

To pursue this theory elaboration objective, I depart from the conventional and dichotomous choice between deductive and inductive research approaches. Traditionally, a deductive approach is guided by a desire to test an extant theory. Novel hypotheses are constructed from extant theory and tested against empirical data to establish the degree of support, if any at all (Bitektine, 2008). On the other hand, an inductive approach infers patterns from the empirical data that has been collected. No conceptual framework or logic is imposed a priori. Instead, emerging patterns and relationships from the data form the basis for theory generation (Parkhe, 1993).

This thesis starts with problematization approach, driven by an extensive review of the literature on GVC participation, with emphasis on critically evaluating its underlying assumptions. This nullifies a-theoretical data collection and moves the research away from a pure inductionist approach of generating theory. Building on this problematization approach, the thesis addresses the assumption based shortcomings in existing theorization by introducing a more appropriate theoretical logic regarding the implications of economic upgrading. Even so, it is not intended to

be an attempt at explicit theory testing, or an investigation aimed at statistical confirmation. The theoretical framework although robust and detailed, is intended to be sufficiently flexible. This allows for theoretical modification, informed by the analysis of empirical data. The framework's role is rather to provide a foundation to commence the process of theoretical refinement/elaboration (Dubois and Gadde, 2002).

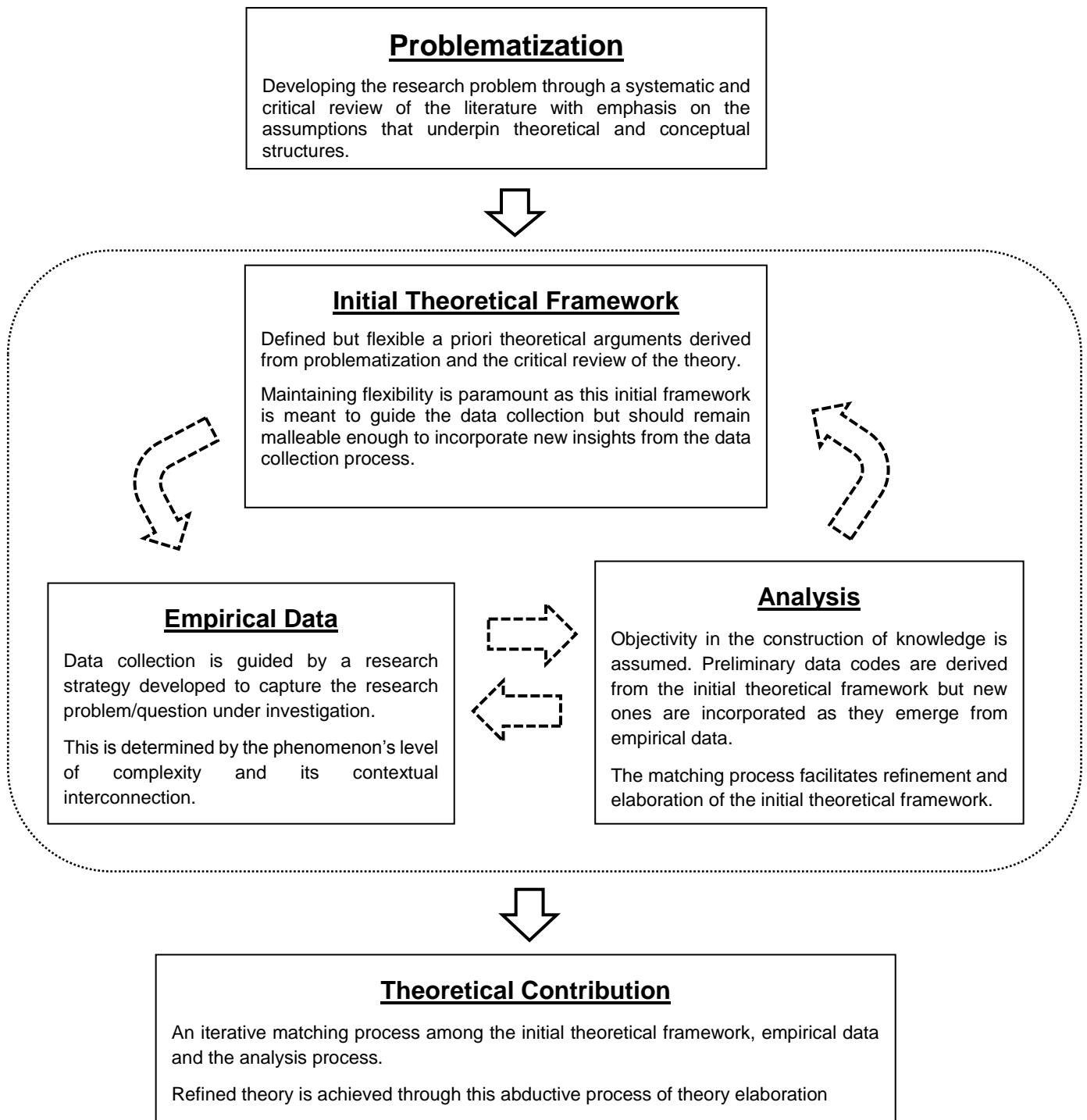
It is important to note that existing theory is not discarded in this process. In fact, extant theories are well positioned to explain much of the micro-level activity around GVC participation and economic upgrading. Even so, Chapter 4 will illustrate that there is still a degree of theoretical inadequacy when it comes to fully understanding the phenomenon. This inadequacy is not merely theory's lack of focus or its inability to explain certain relationships (traditional theory gaps) but also includes instances where theoretical predictions are counterintuitive to observation. A priori problematization is meant to highlight and address some of these shortcomings through logic. However, elements of pre-existing conceptual and theoretical ideas are still embedded within this robust but flexible theoretical framework. They are meant to provide a starting point for data collection (Lee et al., 1999). The ultimate objective is to build a better theory, one that is better able to account for, explain and predict the effects of GVC participation on firm-level economic upgrading (Fisher and Aguinis, 2017).

As with many research questions, the host country implications of value chain participation is a complex phenomenon. Among other things, it involves an investigation of (1) various tiers of supplier firms (2) variation in firm competence and development and (3) evolving dimensions that may alter the governance relationship. Such contextual complexity makes the likelihood of a complete and robust ex-ante theory unlikely. This iterative process of theoretical refinement is influenced by the work of Peirce (1974) and articulated by Dubois & Gadde (2002;2014) and Fisher

and Aguinis (2017). Commonly referred to as the abductive approach, it stresses on the interplay among theory, data and analysis (Dubois and Gadde, 2014). It permits the initial theoretical framework to be successively modified over time due to unanticipated empirical findings and fresh theoretical insights gained during the process (Dubois and Gadde, 2002). Starting with a robust and detailed theoretical framework provides the degree of structure and insight needed to navigate the mass of empirical data typically encountered from confronting reality. However, maintaining theoretical flexibility reduces the possibility of being blinded from important empirical insights that may not have conformed to initial the initial theoretical framework. These unanticipated insights contribute to advancing the thesis's framework by triggering the search for complementary theoretical explanations or the development of novel ones (Dubois and Gadde, 2002).

The process of matching (Dubois and Gibbert, 2010) is a cornerstone of abductive reasoning and important to achieving the objective of theory elaboration (Fisher and Aguinis, 2017). In the early stages of the research process, the matching process allows me to juxtapose the initial theoretical framework to the empirical data that has been gathered. This is undertaken in the absence of the naïve assumption of a perfect fit, but with the understanding that the initial framework is merely the first step of the theory refining process (van Hoek et al., 2005). Elements of misfit are assumed to occur at this stage. Aspects of the overall misfit would have been captured by problematization, but it is likely that empirical analysis may present insights that are not consistent with the initial theoretical framework or its arguments. This mismatch provides the grounds for theoretical refinement. Successive iterations between the theoretical framework and the empirical data, through analysis, allows for elaboration of the theory. This learning loop (theory matching) is referred to as systematic combining (Dubois and Gadde, 2014), and is aimed at developing a more complete theoretical explanation of the phenomenon. Figure 3.2 provides a simplified illustration of this process.

Figure 3.2 The research process



Source: Author

Before delving into the intricacies of the research strategy, it is worthwhile to mention that adopting this abductive research approach is not an attempt to achieve *statistical* generalizability. This abductive approach is pursued to support the thesis's attempt

at developing theory that has *analytical* generalizability. In other words, it does not endeavour to make a statement of the general relationship between GVC participation and domestic firm upgrading, that is, one that is likely to exist across the population of all developing country firms. Instead, it aims to make a theoretical contribution by refining general theory, with clear contextual conditions, that if exists, would possess both explanatory and predictive power (Firestone, 1993). While the reader may identify contextual conditions that can hold across a wider subset of the population of firms, theoretical testing or attempting to extrapolate from sample to population is outside the scope of this thesis. The focus is therefore on a deep understanding of the process of economic upgrading from GVC participation, so as to build a more elaborate and complete theory.

3.5 Research strategy

I position the research strategy as the technique used to confront the reality of the issue or phenomenon under investigation (Yin, 1981a). From this perspective, the research strategy becomes distinguishable from considerations around specific data collection methods. It is considered an umbrella terminology as a single research strategy can include a range of data collection techniques (Marschan-Piekkari and Welch, 2011). How one chooses the research strategy is an important methodological decision that is influenced by the dimensions of the phenomenon under investigation as well as the thesis's research approach - as determined by the project's research question (Benbasat et al., 1987).

First, it is crucial to understand the extent to which the phenomenon can or should be divorced from the context in which it occurs. The extent of this separation is usually guided by the research problem or question that is being investigated (Yin, 1984). Some studies may require an explicit separation of the phenomenon and context, so as to ascertain the relationship between a small number of distinct variables (McCutcheon and Meredith, 1993). For example, research strategies based on

experiments explicitly attempt to control the context by keeping all the empirical conditions constant, with the exception of few variables. Conversely, the phenomenon and context may be heavily interdependent, where it becomes difficult to study one without giving consideration to the other. In other words, the phenomenon may be conditioned by the environmental context (Dubois and Gadde, 2002). Baxter and Jack (2008) use the example of a study aimed at understanding the type of decisions made by nursing students and the factors influencing this decision-making process. The scope of this study made it difficult to understand this decision making process without involving the context in which the skills and decisions were being developed and made, that is, the clinical and classroom setting.

The complexity induced by the project's research focus and its underlying research approach is central to deciding on an appropriate research strategy (Benbasat et al., 1987). For instance, a study designed to explicitly test a theoretical relationship is typically aimed at determining statistical significance. Theoretical uncertainty and complexity are mitigated by the ability to leverage on extant theory to construct the hypotheses needed to conduct the empirical investigation. Such a deductive approach may require a research strategy that is able to capture breadth in the empirical data (large n samples) to operationalize the underlying replication logic (Dubois and Gadde, 2014). Conversely, a researcher may be faced with a situation where less is known about the phenomenon, or where received theory provides counterintuitive predictions and explanations when compared to the empirical world. Such research problems may call for a theory building approach as relationships around the phenomenon remain conflicted or unexplained (Alvesson and Sandberg, 2011). These circumstances warrant an investigation that offers deep insight in order to facilitate the theorization process.

Taking into consideration the above discussion, this thesis will implement a case study research strategy. Within social sciences, and management fields in particular,

case studies have been traditionally equated to the conducting of interviews or ethnographies (McCutcheon and Meredith, 1993; Yin, 1981b). Positioning case studies as a research strategy avoids this misconception and allows me to maximise its methodological utility. Data can be collected from both primary and secondary sources to develop a clear and detailed understanding of the phenomenon and its context (McCutcheon and Meredith, 1993). This rich backdrop of insight not only allows me to confront the empirical world, but to discover and refine logical causal relationships that have been neglected or mis-specified in extant theory.

The abductive theory refining approach of this thesis is best suited for a case study approach for a number of reasons. Chapter 2 outlined the inadequacies of the mainstream perspectives used to understand GVC participation and economic upgrading. These inadequacies have given rise to a degree of “unknown”. In Chapter 4 I will argue that these unknowns are manifested in the incomplete explanations offered by theory regarding the relationship between economic upgrading and GVC participation. These voids in our understanding include questions such as: (1) why are instances of economic upgrading from GVC participation able to co-exist with asymmetry in the distribution of value for the domestic firms (2) Why do the domestic firms engage in MNE induced economic upgrading in the presence of averse bargaining and value-added appropriation conditions. While extant theory is not incapable of explaining aspects of these research questions, this thesis argues that a comprehensive understanding of these “why” questions requires an elaboration of our existing theoretical toolbox. This places demands on the research strategy to provide empirical insight that not only supports or rejects the initial framework, but provides insight that can also facilitate theoretical modification or elaboration (Piekkari et al., 2009). The rich insight and depth of understanding offered by a case study research strategy complement this abductive approach to developing theory.

As previously stated, the thesis seeks to understand the complex phenomenon of how GVC participation affects the economic upgrading of domestic firms located in developing countries. In Chapter 4, I will position economic upgrading as the ability for a firm to create and appropriate greater value-added from its operations. Economic upgrading can in principle occur in any firm. That being said, developing country firms are faced with certain resource and institutional constraints that may have a unique influence on its GVC participation and the resulting upgrading process. It is frequently argued that their lack of capital, technological know-how and international experience provides fertile conditions for economic upgrading from MNE interaction (Saliola and Zanfei, 2009). However, this context can also have mitigating effects on the terms on which MNE-led upgrading are made. For instance, the lack of factor resources and international experience can lead to significant information asymmetry between the MNE and the domestic firm. This can then allow for ex-ante contractual arrangements that would, in another context, be considered un-strategic or irrational.

The complexity in how GVC relationships are organised and how they evolve further supports a decision to leverage on the depth and richness of empirical insight offered by a case study research strategy (Ghauri and Grønhaug, 2005). Understanding the parameters of these GVC relationships is crucial towards understanding its implications for economic upgrading. These parameters may include the scope of the value chain activity that is being performed by the domestic firm. For instance, the MNE may on the surface appear to have an intensely fine-sliced value chain. Qualitatively, the scope of the activity may be negligible across the finely sliced activities and it is important that the research design is able to capture and assess the implications of these variances. Likewise, it is useful to understand the extent of GVC spread across the various tiers of suppliers. A particular activity or task can be outsourced by the MNE to one supplier who then further subcontracts it to other firms. Conversely, the MNE may choose to retain a larger set of suppliers, thereby splitting

demand across a wider set of firms. It is also likely that these parameters will evolve as the GVC relationship matures or develops. Governance-related issues are dynamic in nature and this has implications on how domestic firms upgrade. Understanding this dynamism is embedded within, and is a crucial element of the thesis. A case study strategy is well suited to gather longitudinal data while maintaining the rich detail needed to uncover and describe the underlying relationships.

3.6 Chapter conclusion

This chapter has engaged with foundational elements of the thesis's research design. The philosophical underpinning is important to understand the manner in which the phenomenon and the empirical data will be perceived and interpreted throughout the study. Beyond this, I have provided detail on the two main elements driving the thesis's research approach. The thesis's research problem was not developed through the conventional approach of gap spotting. Instead, I have chosen to focus on a critical assessment of the underlying assumptions attached to many of the empirical studies on economic upgrading. This exercise in problematization will be undertaken in Section 4.2 of Chapter 4. This problematization methodology is nested within the broader methodological approach of abduction. It was important to introduce the abductive approach prior to engaging in any theoretical discussion. As I have explained in Section 3.4, this is in part due to the manner in which the theoretical framework will be used for the purpose of this thesis. This notion of a theoretical framework is not utilised in a manner that is consistent with deductive theory testing. It is important that this is properly articulated at an early stage.

Details on the data collection methods and the analysis of the data have been reserved for Chapter 5 – the second part of the research methodology. This allows for a seamless transition into the empirical chapters of the thesis. This is in line with my attempt to provide detail at the most appropriate juncture. Even so, it was

necessary to outline and provide justification for the research strategy (case study) as it is intrinsically tied to the theoretical objectives of the research project. Utilizing the problematization methodology and an abductive research approach, I have positioned this thesis as an exercise in theory elaboration. This has implications for the research strategy that will be employed to confront the phenomenon of economic upgrading (Yin, 1981a).

Chapter 4

Theoretical framework

4.1 Chapter overview

Chapter 2 provided insight into the two dominant empirical framings for studies on the host country firm-level implications for MNE activity. Despite a large number of studies on linkage effects, I argued that this body of work lacks insight into the role of interfirm governance between the MNE and the domestic firm. This made the empirical lens an inadequate fit for this thesis given its lack of insight into issues related to interfirm bargaining and the distribution of value-added. A GVC framing was best aligned with my particular empirical focus as it provides an abundance of descriptive insight into the manner in which value chain relationships develop. It allows for rich detail that can help understand the effect of upgrading on domestic value-added capture. Even so, the GVC framing is not without its conceptual shortcomings. It underutilises theory when positing relationships among GVC participation, economic upgrading and the ability for domestic firms to capture value-added. This approach to explaining relationships lends itself to underspecification where the core dimensions are not adequately considered. This introduces implicit assumptions that can undermine propositions and even contradict fundamental evidence from the phenomenon being investigated.

The problematization section of this chapter will provide a more complete review of this conceptual shortcoming and the implications that may arise from such oversight. Afterwards, I will present the a priori theoretical framework that will form the foundation for the abductive approach to theory building. It will be constructed by leveraging on theoretical insights from TCE and power dependence theory. This will be outlined in Section 4.3 and will serve to ground the GVC framing on a robust theoretical footing. This framework is not fixed. Consistent with abduction, it is expected that the empirical insight arising from the thesis's data will inform the

theoretical framework. This need for theoretical refinement is justified in Section 4.4. Here I highlight aspects of economic upgrading phenomenon that are not completely consistent with the predictions of either base theory - thus provoking the need for greater theoretical development.

4.2 Problematization

Gereffi et al. (2001) proposed three metrics that can be used to assess the extent of economic upgrading. Two of these metrics are related to firm-level economic upgrading and will be incorporated into this thesis. They are captured in the domestic firm's ability to gain increases in overall profitability or profit margins (Gereffi et al., 2001). Both metrics capture aspects of value-added. Here value-added is considered as an accounting term, where it captures the variation between a product's selling price and the cost incurred in production (Haller and Stolowy, 1998). Overall profitability captures what could be considered absolute value-added where the overall sales are subtracted from total intermediate input purchases (Girma et al., 2004). It reflects *absolute* value-added as it is affected by the total product output sold by the domestic firm. Conversely, profit margins capture what could be considered *relative* value-added. This income proxy is based on the activity itself and accounts for the relative gains attributed to any particular upgrading trajectory.

It is important to contrast these upgrading metrics with the upgrading trajectories that were presented in Table 2.1 of Chapter 2 (table reproduced below). Trajectories are paths towards achieving upgrading, but in themselves do not constitute instances of economic upgrading. This is an important distinction as many of the earlier studies failed to explicitly acknowledge the strategic intent of upgrading (Ponte and Ewert, 2009). Upgrading is a transformational process that is partially aimed at *creating* additional value-added. Equally important, it is meant to also accompany conditions that allow the firm to *appropriate* greater value-added (Ponte and Ewert, 2009; Brewer, 2015).

Table 2.1 Conventional view of upgrading trajectories

Upgrading Trajectory	Key Elements
Product	<ul style="list-style-type: none"> • The movement into sophisticated product lines (Gereffi, 1999b; UNCTAD, 2013) • Introducing new products or improving old products faster than rivals (Kaplinsky and Morris, 2002)
Process	<ul style="list-style-type: none"> • The ability to transform inputs into outputs more efficiently through superior technology or reorganised production systems (UNCTAD, 2013; Humphrey and Schmitz, 2002; Schmitz, 1999) • Increasing the efficiency of internal processes such that these are significantly better than those of rivals, both within individual links in the chain and between the links in the chain (Kaplinsky and Morris, 2002; Ponte and Ewert, 2009)
Functional	<ul style="list-style-type: none"> • Acquiring new functions within the chain. For example, Moving from production to design or marketing in order to increase the overall skill content of activities (Bair and Gereffi, 2001; UNCTAD, 2013) • Increasing value-added by changing the mix of activities conducted within the firm (for example, taking responsibility for, or outsourcing accounting, logistics and quality functions) or moving the locus of activities to different links in the value chain (for example from manufacturing to design) (Kaplinsky and Morris, 2002)
Chain	<ul style="list-style-type: none"> • The application of competencies acquired in a particular function of a chain to an entirely new industry (Guerrieri and Pietrobelli, 2004; UNCTAD, 2013) • Moving to a new value chain (Kaplinsky and Morris, 2002)

Source: Author

A large number of GVC studies on economic upgrading have been fixated on describing the way in which upgrading trajectories occur within the underdeveloped firm². However, evidence based on the *observation* of trajectory shifts cannot be taken as instances of upgrading without considering its implications on *both* value-added creation and appropriation. This separation between upgrading trajectories and economic upgrading is rarely pursued in the extant GVC literature (Tokatli, 2013). Gereffi et al. (2001) acknowledged that it is often difficult to get accounting records for many firms that participate in GVCs. These firms are either not publically traded or fail to keep proper accounting records. It is also not uncommon for suppliers in GVCs to be unwilling to comment on issues of value-added appropriation, especially with regards to its arrangements with the MNE (Ivarsson and Alvstam, 2011).

² The term underdeveloped firm is used to describe the domestic firm from within the developing country. These firms are usually resource and capability deficiency and lack prior experience in GVC participation (Blomström and Persson, 1983).

Regardless of the underlying reasons, studies tend to implicitly assume that case descriptions consistent with Table 2.1 equate to instances of economic upgrading. For instance, Milberg and Winkler (2011) classified upgrading as hard to quantify, but one of those things that “you know when you see it” (pp. 343). Given the simplicity of the assumption, one may be motivated to believe that only a minimal number of studies fall into this category. However, an extensive review of the concept of economic upgrading has revealed it to be a widespread assumption. Appendix A provides a summary of studies done on economic upgrading over an 18 year period. The table (Appendix A) highlights the manner in which upgrading has been defined and proxied in prior studies. The pool of studies was collated by utilizing on Google Scholar as well as the comprehensive publication database available on the Global Value Chains Initiative (Global Value Chains Initiative, 2017). These searches were limited to specific keywords, namely, global value chains, GVC, economic upgrading, industrial upgrading and value-added. The studies were restricted to those published in peer-reviewed journals. In total, 58 studies fit the initial criteria. The pool of studies was then individually reviewed to determine which studies were indeed focused on economic upgrading from GVC participation. The final number of studies was 45.

Two issue become apparent from this review (Appendix A). First and most evident is the tendency for studies to be conducted in an a-theoretical manner. Emphasis is placed on description, where relationships are grounded on intuition and basic logic. This in itself is not something that should be considered negative. In a broad sense, theory is an explanation of how and why relationships are logically tied (Wacker, 1998). Description and intuition are thus at the core of any theoretical perspective. However, a robust theoretical foundation is accompanied by (1) definitions of essential constructs (2) core assumptions (3) relationships of variables (Wacker, 2004). This lack of a strong theoretical foundation exposes work on economic upgrading to a key shortcoming.

This shortcoming is linked to the second issue emanating from Appendix A. Emphasising descriptive insight has led GVC researchers to focus on outlining the manner in which an upgrading trajectory occurs within the domestic firm. As such, these studies have the tendency to align evidence of an upgrading trajectory to instances of upgrading. This assumption is problematic for two main reasons. First, undertaking a functional upgrading trajectory by, for example, extending operations into R&D activities cannot be considered upgrading without understanding its underlying influence on value-added. While investments in functional areas such as R&D or marketing can positively impact value-added, they are also costly, inherently risky and prone to failure (Fernandes and Paunov, 2014; Fu et al., 2011).

A similar line of argument can be made against recent attempts to link upgrading to product and process changes motivated by quality standards compliance (Kaplinsky, 2010). Adhering to international or MNE standards require domestic firms to make significant changes to its operations. Adopting stricter quality standards may result in higher end prices, lower costs and larger volume sales, however, it is also costly to acquire and maintain accreditation (Kaplinsky, 2010). Prior research has also shown that standards frequently do not provide any significant competitive advantage but are simply a minimum qualification for market entry (Ponte and Ewert, 2009).

While some upgrading trajectories are inherently risky and may fail to create value-added, it is reasonable to assume that many do succeed in creating value-added. This presents an even greater danger in aligning trajectories with upgrading. More specifically, these studies do not address the factors that determine how this newly established value-added will be distributed among the GVC actors. Remaining silent on these distributional effects underlines the tendency for existing studies to implicitly assume that increases in value-added will be allocated to the domestic firm in which the trajectory has materialised. However, a domestic firm may undertake a process upgrading trajectory to increase production efficiency by reducing input wastage and

increasing production speed. At a given price point, value-added creation is facilitated through a cost reduction mechanism. This value-added can only be appropriated by the domestic firm if the selling price with the MNE remains, at worst, constant. If the MNE is able to dictate pricing conditions then the value-added created can be appropriated away from the domestic firm (Mansfield et al., 1977; Cox, 1999).

Likewise, value-added may be created if a domestic firm is able to broaden its activity base by adding more functions to its in-house operations, for example, design or R&D. These functions allow the domestic firm to provide a more complete intermediary good to the MNE responsible for end market sales. This value-added can only be captured by the domestic firm so as long as it is reflected in the external transfer price. Once again, if the MNE is able to bargain for a lower price, the value-added created from the functional upgrading trajectory will be transferred to the MNE.

By treating upgrading trajectories as an indication for economic upgrading, prior studies have been making the implicit assumption that the creation and appropriation of value-added are always positively correlated. Gereffi (1999b) in his influential paper investigated instances of upgrading in the apparel global value chain in East Asia. He argued that domestic firm upgrading within the region was largely due to their ability to establish links with lead firms, typically MNEs. The author's definition of an upgraded domestic firm was one where the firm was able to move to more profitable niches, by means of advancements in both technology and skill level (Lee and Gereffi, 2015). Even so, the paper assessed upgrading by determining whether a firm moves into activities classified as higher value-added, as opposed to an understanding of whether value-added was actually being captured. For example, upgrading occurred if the firm was able to transcend simple assembly activities and move into those that involved full package supply to the MNE (functional upgrading according to Table 2.1) (Rossi, 2013). This notion of upgrading exemplifies the symbiotic assumption of value-added creation and its appropriation. Implicitly, it

advances the argument that if a domestic firm is able to move into activities of supposed higher value, then the value-added attributable to those activities will be captured by the domestic firm.

A critical reading of the study by Pavlínek and Ženka (2011) on the automotive GVC in Central and Eastern Europe illustrates the severity of potential imbalances between upgrading trajectories and value-added appropriation. Using data from the Czech automotive sector, the authors argue that various forms of upgrading trajectories had been undertaken by domestic firms. For example, the authors capture a process upgrading trajectory by measuring the turnover per employee. This ratio increased by 72% between 1998 and 2006 and was argued that domestic firms had become more efficient. However, this proxy merely indicates that over the period, domestic firms were able to generate more revenue per employee, that is, efficiency benefits which could *potentially* be captured by the domestic firms. Details on domestic value-added over the same period illustrate a different situation. In 1998, the average value-added across domestic firms stood at CZK 0.119 bn. This average increased to CZK 0.121 bn in 2006, a difference of CZK 0.002 bn in average value-added across all the domestic firms in the sector. This is merely a reader observation, greater analysis of the data is required to substantiate this observation. Even so, this negligible and less than proportional increase in value-added raises concerns regarding domestic firms' ability to appropriate value-added from its process upgrading trajectories.

This assumption of a positive correlation between upgrading trajectories and the ability to appropriate value-added has limited the focus of GVC research – biasing it towards positive findings of upgrading, presented uncritically (Brewer, 2015). The majority of upgrading studies focus specifically on the process of value-added creation (Ivarsson and Alvstam, 2011; Humphrey, 2004; Tokatli, 2013). These studies usually fail to theorize on, and analyse the extent to which this value-added

is being captured by the domestic firm or whether it is appropriated by other parties in the GVC. In the next section, I will discuss the influence of this implicit assumption – an assumption that underplays the role of bargaining power in the distribution of value-added. I make particular reference to the Gereffi et al. (2005) GVC typology. This is owing to the prominence of this typology in Appendix A’s summary of studies on economic upgrading. It has become the dominant “theoretical lens” to study economic upgrading from GVC participation – although it is more a categorisation than a theory.


4.2.1 GVC governance: The distributional and bargaining effects of upgrading trajectories

In line with the focus of this thesis, the GVC research on economic upgrading positions interfirm governance as an important factor. Existing studies are predicated on the supposition that the MNE orchestrates the value chain and controls the flow of knowledge and resources (Saliola and Zanfei, 2009). Even so, the problematic assumption regarding the creation and appropriation of value-added is also evident in this governance logic. I will demonstrate this by focusing on the dominant Gereffi et al. (2005) governance typology as it represents the most widely used framework to classify interfirm GVC relationships and generate the likely outcomes of upgrading trajectories.

The typology outlines the key factors that determine the likely governance mode that will be chosen by the lead firm. Beyond this, it predicts the likely degree of control and power asymmetry that will be present in each governance type. I have reproduced Table 2.2 for convenience as it effectively summarizes this widely used governance typology. This table was presented earlier in Chapter 2. At one side of the spectrum resides the market governance type, or what is commonly considered as arm’s length trade. Gereffi et al. (2005) argue that this is likely to occur when the transactions are not complex, can be easily codified and the MNE has suppliers with high capabilities. Being arm’s length trade between two independent firms, the

authors expect that there will be low levels of power asymmetry between both firms. On the other side of the spectrum is internalisation, where the transactional conditions are opposite. The complexity of the transactions is high and the ability to codify it is low. In addition, the MNE is unable to find a capable supplier to execute the activity. These conditions prompt the firm to establish a subsidiary where the headquarters is able to dictate the terms of the agreement (high power asymmetry).

Table 2.2 Key determinants of global value chain governance

Governance type	Complexity of transactions	Ability to codify transactions	Capabilities in the supply base	Degree of coordination and power asymmetry
Market	Low	High	High	Low  High
Modular	High	High	High	
Relational	High	Low	High	
Captive	High	High	Low	
Hierarchy (internalization)	High	Low	Low	

Source: Gereffi et al. (2005)

Of interest to this thesis is what Gereffi et al. (2005) positions as captive governance types. Given their low capability base, it is the governance type that underdeveloped firms from developing countries are likely to be classified within. This captive relationship is characterised by high degree of MNE coordination and power asymmetry. The MNE is incentivised to transfer knowledge and resources to the domestic firm so as to increase its ability to perform the externalised activity (process upgrading trajectory). Likewise, the MNE may encourage and provide support to facilitate the externalisation of additional activities (functional upgrading trajectory). As these capabilities increase, the typology posits that the relationship will transform into a more modular type (higher supplier capability).

As these capabilities increase, greater value-added is created in the process. The typology considers these improvements as upgrading given its assumptions around power asymmetry. From Table 2.2, it can be seen that a shift into a modular

governance type will reduce power asymmetry in the relationship. This perceived reduction in power asymmetry is what drives the typologies assumption around domestic firm value-added appropriation. More specifically, as the domestic firm upgrades, it is able to create value-added while simultaneously improving its bargaining position within the relationship. This bargaining improvement is what permits the domestic firm to capture the value-added from the upgrading trajectory.

However, scenarios may also exist where supplier capabilities can substantially increase but still experience many of the predefined captive effects that Gereffi et al. (2005) described, including, “a great deal of intervention”, “transactional dependency” and “lock-in”. A shift in any of the three factors does not necessarily mean that a given supplier will exit a captive governance mode (Buvik and Reve, 2001). Complexity, codifiability and supplier capability are important operational signals that inform governance modes but most appropriate for understanding the process of supplier choice. The typology implicitly assumes that lead firm vertical disintegration is driven by the desire for organisational economizing (Jensen et al., 2013; Williamson, 1991b). MNEs are usually confident on which activities they would prefer to externalize prior to actually engaging with any prospective supplier (Mudambi and Venzin, 2010). The three factors outlined by Gereffi et al. (2005) to a large extent allow the MNE to match the best supplier with the activity in question.

Ivarsson and Alvstam (2011) case of IKEA’s GVC operations in China provides ample evidence to raise concerns regarding the upgrading and power asymmetry predications proposed in (Gereffi et al., 2005). While Ivarsson and Alvstam (2011) integrate theoretical arguments from Gereffi et al. (2005), they also provide empirical evidence that is in contradiction to the typology’s expected outcomes. The authors explicate many forms of IKEA-led upgrading initiatives, ranging from (1) improved operational capabilities, (2) improved duplicative capabilities, (3) improved adaptive capabilities to (4) improved innovative capabilities (p. 738). These all increase firm

capabilities and should allow domestic firms to move from a captive governance structure to one that favoured more balanced power symmetry and value-added capture. Instead, the authors reported that post-upgrading, IKEA is still able to bargain extensively for lower prices (p. 741) to the extent where the domestic firms become dissatisfied with the value-added they capture from upgrading trajectories (p. 748). These insights while mentioned, were only passively acknowledged by the authors. As a result, it was not analysed further, despite its contradiction to the paper's underlying logic.

Such empirical contradictions signal the need to move beyond existing theorizations of economic upgrading. The ability to appropriate value-added transcends the three characteristics outlined in Gereffi et al. (2005). As I have argued, Gereffi et al. (2005) make a simple but profound assumption on the effect that an upgrading trajectory will have on a domestic firm's ability to appropriate value-added. More specifically, that improvements in the capability base of the supplier will enable the supplier to bargain for a greater share of the value-added. The empirical contradiction in Ivarsson and Alvstam (2010) raises questions around this aspect of GVC theorization. More explicit consideration needs to be given to the effect that upgrading trajectories have on the interfirm bargaining power (Crook and Combs, 2007).

4.3 Theoretical framework

The central task of this chapter is to construct a framework that is able to address the theoretical shortcomings of the assumptions underlying current work on economic upgrading. By problematizing prior studies, I have demonstrated that our understanding of economic upgrading is incomplete. This incompleteness transcends the conventional gap spotting approach of many studies. The arguments developed above do not simply highlight under-researched areas. Instead, they introduce a critique that casts doubt on conclusions derived from prior empirical studies. It impresses the need for a greater theoretical understanding of the value-

added appropriation implications of economic upgrading. To pursue this objective, the thesis's a-prior theoretical framework is constructed by incorporating insights from transaction cost economics (TCE) and power-dependence theory. The former theory is widely used within the international business research agenda (Coase, 1937; Williamson, 1975; 1985; 1996). The latter has its theoretical lineage in sociological studies with an emphasis on the study of interpersonal interactions. Even so, its utilization within a firm context is not uncommon (Dwyer and Walker Jr, 1981; Crook and Combs, 2007). Its core tenets are adopted from the seminal work of Richard Emerson (Emerson, 1962; Emerson, 1964).

Before elaborating on the framework, it is important to justify the theory selection. TCE provides the most developed theoretical lens for understanding and explaining how economic activity is governed (Crook, 2005). The behavioural assumptions of bounded rationality and opportunistic behaviour are in line with the perspective of this thesis. Much of the anecdotal evidence on GVC relationships offers empirical support for such firm behaviour (see Choksy et al. (2017) for a recent review of the literature). In other words, this thesis positions firms (both the MNE and domestic firms) as opportunistic entities seeking to maximise profitability. Managers make these profit maximising decisions in the presence of cognitive constraints coupled with asymmetric and limited information. Beyond this, TCE establishes a set of well-defined constructs that are able to explain and predict the most efficient governance structure – at least from a transaction cost minimising perspective. It provides a useful mechanism to determine the important attributes of interfirm arrangements. This will be elaborated on in section 4.3.1.

That being said, there are also some unresolved relationships within the TCE research agenda (David and Han, 2004). As I will argue in section 4.3.2, TCE on its own may not be able to provide a complete account of many observable GVC governance structures. Crook's (2005) meta-analysis of TCE suggests that while the

theoretical perspective is a potent predictor of interfirm governance, “other theoretical perspectives are also needed to provide a more comprehensive understanding of how firms govern economic activity” (pp. 108). Through a comprehensive aggregate empirical assessment, David and Han (2004) found that important relationships within TCE have been grossly under-researched. Some of these relationships are important to this research. For instance, the authors argue that there is little support or attention given to TCE propositions related to the performance implications of governance structures (David and Han, 2004). TCE may predict the structure that economises on transaction costs, where such economising may be an important factor in achieving above-average profitability. However, transaction cost in itself is not a proxy for firm performance or profitability. In fact, TCE does not directly account for the revenue potential of the various governance options available to the firm (Contractor, 1990; Brouthers, 2002). Profit maximisation via superior value-added appropriation is not solely determined by the transaction cost of three governance alternatives. One particular structure may be associated with higher transaction cost but can simultaneously allow the MNE to appropriate a greater proportion of the rents.

In section 4.3.2, I argue that the extent of relational dependence (between the MNE and domestic firm) determines the efficacy of the TCE transactional dimensions to explain a party’s value-added appropriation potential. For instance, the impact of asset specificity on unilateral hold-up can only be determined after interfirm dependence has been considered. This justifies the need for greater theoretical insight into bargaining power and the dependence aspects of interfirm relationships. Analysing transactional dimensions from a bilateral perspective underplays the extent to which each party to the contract is dependent on the other. Nesting core TCE tenets within a wider bargaining framework addresses this. A dependence based theoretical lens allows the analysis to capture the entire value chain, thereby transcending the conventional dyadic framing of TCE.

In the following three subsections, I will present and illustrate how both these theoretical perspectives will be melded together to create the a priori theoretical framework. In line with Chapter 3, this framework will be used to guide both the data collection and initial analysis phases of the thesis.

4.3.1 Transaction cost economics (TCE)

Firms exist because they are better able to manage transactions costs and control opportunism than externalised relationships (Ghoshal and Moran, 1996; Coase, 1937). This is however not the case for every activity needed to bring a final product to market. If it were, then GVC relationships would simply not exist. TCE provides a theoretical foundation to understand how these decisions are rationalised by the firm. As previously mentioned, TCE hinges on the behavioural assumptions of bounded rationality and opportunism. These assumptions justify the existence of transaction related costs and why it is necessary to institute the governance structure that attenuates its effects. Opportunism is commonly defined as “self-interest with guile”. According to Williamson (1985), it refers to “the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse” (Williamson, 1985). Bounded rationality exacerbates the effects of opportunism, as either party to the contract is unable to ex-ante devise a complete contract.

For certain transactions, the effects of opportunism become more pronounced. The incomplete nature of contracting makes it difficult to specify and control for specific forms of opportunism (Dequech, 2001). As such, either party may incur high transaction costs associated with monitoring performance and protecting themselves against potential opportunistic moves (Tsang, 2006). This is where the predictive advantage of TCE is most prevalent. The theory claims that by evaluating these transactional dimensions, it can predict the most efficient governance structure to

minimize exchange cost. These transactional dimensions are captured in asset specificity, frequency and uncertainty.

In the presence of opportunism and bounded rationality, these dimensions determine the adaptation, performance evaluation and safeguarding cost of alternative governance structures (Rindfleisch and Heide, 1997; David and Han, 2004). I will first present these three dimensions and then illustrate, from a traditional TCE perspective, how they combine to advance useful propositions on governance structures.

Asset specificity is often viewed as the most influential of all three dimensions (Joskow, 1988; Riordan and Williamson, 1985). The level of asset specificity is denoted by the extent to which the asset or investment can be deployed to alternative uses without sacrifice to its productive value (Williamson, 1991a). It can manifest itself in forms ranging from specific physical capital, specific human capital and site-specific capital (Minkler and Park, 1994). For instance, specific physical assets may manifest in machinery that is acquired solely to execute the activity or task in question. This does not necessarily imply that the asset cannot be reused for another purpose. Alternative uses may be possible should the transaction cease. However, this will not be costless for the capital owner as the next best alternative use will sacrifice significant productive value (De Vita et al., 2010). Similarly, specific human capital can ensue when a firm is required to invest in significant employee training and hiring. This training may be a prerequisite to performing a certain activity as part of the production process needed for the transaction. Should the transaction cease, the investing firm may be unable to repurpose this special knowledge (Chandler et al., 2009).

While it is seen as the most impactful transactional dimension, asset specificity on its own does not determine the cost-minimizing governance structure. If the transaction is infrequent or insufficiently continuous then it may not generate enough concern to warrant internalisation (Walker and Weber, 1984). Transaction frequency can be

considered as one-time, occasional, or recurring (Riordan and Williamson, 1985). It captures how often the activity is needed by the firm to conduct its operations.

The third transactional dimension is uncertainty. Transactional uncertainty intensifies the behavioural constraints of bounded rationality and opportunism. Information asymmetry and limitations on cognitive capability make contracts inherently incomplete. If the market is induced with uncertainty, it increases the difficulty of specifying the ex-ante contingencies that may affect adaptation (Williamson, 1975). Uncertainty is usually classified as either environmental or behavioural (Chiles and McMackin, 1996). Environmental uncertainties are attributable largely to the industry that the firm operates in. Such uncertainty can be captured in difficulties in forecasting demand, technological change or even consumer preferences (Bensaou and Venkatraman, 1995; Crook, 2005). Conversely, behavioural uncertainty manifests in the firm's inability to determine the performance aspects of the transaction in question (Williamson, 1985). Unlike environmental uncertainty, these behavioural aspects are endogenously imposed and arise within the context of the exchange (John and Weitz, 1988). They occur when there is difficulty in isolating or measuring the productive input of party performing the activity. Behavioural uncertainty becomes problematic due to potential opportunistic tendencies by contracting partners. In such instances, partners can make false claims about their performance, and may even pass off substandard work as satisfactory (John and Weitz, 1988).

TCE argues that together, these behavioural assumptions and transactional dimensions determine the cost-minimizing governance structure to be adopted. To reiterate, TCE is most concerned with the costs associated with the exchange process itself. This is captured in the cost of searching for potential partners, in addition to the costs related to negotiating with, and monitoring the chosen partner's performance (Brouthers, 2002). It is generally accepted that increases in any of the three dimensions is likely to increase the transaction costs associated with

transacting via external partners. As these transaction costs increase, internalisation even with its associated bureaucratic costs becomes the least costly organising mechanism. That being said, no single dimension dictates the transaction cost-minimising choice. While asset specificity is seen as the most influential, high levels of asset specificity does not, by itself, determine the ideal choice. Even if an activity requires specific assets to be executed, if such assets are used rarely, then the firm may choose to engage with external parties. Asset-specific transactions that occur infrequently do not require the firm to engage in constant monitoring of the exchange partner (David and Han, 2004). In such instances, the transaction costs of using the market are not enough to offset the bureaucratic costs associated with hierarchy. As the frequency of the transaction increases, the firm is likely to also increase the resources it devotes to monitoring the partner.

Bounded rationality and asymmetric information make uncertainty likely in many interfirm relationships. As with frequency, a similar argument can be mounted for instances of uncertainty. Take for instance a transaction where behavioural uncertainty is low. The firm is able to curb opportunistic behaviour by its ability to accurately measure the exchange partner's performance without incurring substantial monitoring and policing costs. Trust is frequently argued to be an uncertainty dampening mechanism. Researchers have noted that trust may mitigate against high transaction cost by reducing the need for monitoring and control (Brouthers and Brouthers, 2003). This may occur even when the transaction is difficult to measure, police or specify ex-ante. This notion of trust softens the opportunism assumption at the core of TCE (Ghoshal and Moran, 1996).

As previously stated, asset specificity is seen as TCE's "big locomotive" and a great deal of its predictive content is contingent upon it (Williamson, 1998). Asset specificity ignites opportunistic tendencies through hold up (King, 2007). When either party (buyer or seller) makes investments in specific assets, the relationship moves away

from a large numbers bargaining situation. This is replaced with a situation where its output now has a restricted buyer. Take for instance a case where a supplier invests in a specific piece of machinery to service the relationship. By definition, the supplier is unable to (1) sell the asset specific output to other buyers or (2) redeploy the specific assets without incurring a loss in productive value.

From a TCE perspective, this small numbers bargaining is not unilateral. Balakrishnan and Fox (1993) argued that investing in specific assets are usually made to enhance uniqueness and competitive advantage. For instance, a specific piece of machinery may permit productivity gains that are not achievable otherwise. In other cases, the input the buyer requires may not be otherwise available without this specialised machine. As TCE would posit, such specificity increases bilateral dependence and contracting hazards for both parties (David and Han, 2004). Opportunistic behaviour by either party can have significant transaction cost repercussions in the form of protracted negotiation, or even complete failure of the agreement.

The above is just one governance prediction that can be derived from TCE. The combinations are many. Table 4.2 provides an outline of various transactional combinations and the likely predictions based on key TCE tenets. This does not represent an exhaustive list of combinations, but is presented to elaborate on the TCE arguments presented above. In fact, I have chosen to focus on scenarios that exhibit instances of high asset specificity. This will maintain relevance with the discussions that will follow the table's summary.

Table 4.1 An application of TCE tenets

Transactional Dimension			Governance structure prediction	TCE Argument
Asset Specificity	Frequency	Uncertainty		
High	Low	Low	Arm's length trade	<p>If specific assets are infrequently required, then the likelihood of the firm internalizing the activity is low - even in situations of high asset specificity and holdup potential. It is unlikely that the utility derived will offset the cost of the specific investment (Teo and Yu, 2005).</p> <p>This more so the case when environmental and behavioural uncertainty is also low (Walker and Weber, 1984).</p>
High	Low	High	Arm's length trade	<p>High uncertainty may foster opportunistic behaviour, this is especially when considering activities that require the deployment of specific assets (Grover and Malhotra, 2003).</p> <p>Even so, an internalised governance structure may only become efficiency for recurrent transactions (Aubert et al., 1996)</p>
High	High	Low	Hybrid arrangements OR Internalisation	<p>Governance structures under these conditions have been inconclusive in the TCE literature (Hodgson, 2002)</p> <p>Formal contractual arrangements (hybrid arrangements) are usually argued for recurrent activities possessing intermediate levels of uncertainty and mixed investment characteristics (medium asset specificity) (Carter and Hodgson, 2006).</p> <p>As the level of asset specificity and/or uncertainty increases, the relationship is likely to favour internalisation.</p>
High	High	High	Internalisation	<p>High levels of all three transactional dimensions increase the costs required to have an efficient relationship under conditions of bounded rationality and opportunism (Grover and Malhotra, 2003). In such circumstances, internalisation is preferred.</p>

Source: Author

Of interest to this research is the impact that economic upgrading trajectories have on the governance relationship between the MNE and the domestic firm. Economic upgrading is an ex-post change to the inter-firm relationship that is likely to alter aspects of the transactional dimensions. I consider these trajectories ex-post as it is likely that they occur incrementally and usually after the initial contract has been agreed upon (Ivarsson and Alvstam, 2011). Of primary concern is the influence that upgrading trajectories have on TCE's most potent dimension - asset specificity. Evidence from various case studies has illustrated that MNE supported upgrading initiatives frequently take the form of capital deepening, where investments in technology, equipment and processes are common (Navas-Alemán, 2011; Ivarsson and Alvstam, 2010).

There is further evidence that investments may manifest themselves as specific assets. Giuliani et al. (2005) looked at domestic Latin American firms across various GVCs. The authors observed that there were certain patterns of learning and knowledge diffusion across the different industries. However, in many instances, the knowledge transfer focused on correcting deficiencies that offered production benefit to the MNE. For instance, in traditional manufacturing opportunity for domestic technological transfer was concentrated on improvements and modifications to production methods that were related to specific MNE designs (Giuliani et al., 2005). In the software industry in Mexico, domestic firms were able to access sophisticated software packages but were required to adapt these packages to the specific needs of the MNE (Giuliani et al., 2005). Based solely on a TCE logic, redeployability becomes a concern and transactions costs may begin to rise. TCE would posit that the MNE should be cautious of the level of specific assets that it allows the domestic firm to acquire – much less assist the domestic firm in its acquisition. That being said, the upgrading literature suggests that the MNE is not only incautious, but is actually supporting some of these asset specific investments (upgrading trajectories).

I have thus far illustrated that TCE provides strong theorization on the relationship between transactional dimensions and transaction-related costs – thereby predicting governance on a cost-minimising assumption. However, it stops short of fully integrating considerations around interfirm dependence, and is thus ill-equipped to theorize on the distribution of value-added. It's dyadic framing of governance has a tendency to assume symmetric dependency when specific assets are deployed by either party (Nooteboom, 1993b). Lock-in is assumed for both parties as discontinuity of the relationship means that either party will be left without an ideal trading partner (Pasternack, 2008). This dependency symmetry makes both partners bounded to the contractual relationship regardless of how inefficient the relationship becomes. For instance, either or both parties may become opportunistic or attempt to bargain for a greater share of the value-added. Without alternatives, considerable time can be spent haggling over price and other contract specifics that could not be specified ex-ante. Such inefficiency increases transaction-related costs and provides the justification for fiat via internalisation (Masten et al., 1989).

From this perspective, asset specificity gives rise to safeguarding problems as market competition no longer restrains opportunism (Rindfleisch and Heide, 1997). Rindfleisch and Heide (1997) also acknowledged that these issues are consistent with discussions related to dependence and bargaining. Even so, interfirm dependence is more nuanced than what TCE allows for (Shelanski and Klein, 1995). Transcending the traditional dyadic contextualisation of GVC relationships can achieve better theorization regarding the influence of the transactional dimensions on governance selection. The level of inter-dependence between the MNE and a domestic firm is not determined within the confines of the individual governance relationship. Instead, it is determined by considering that relationship in light of the other relationships that each firm is partied to.

In the next two sections, I will add a dependence based bargaining power element to TCE. This allows for greater theoretical utility of the core TCE transactional dimensions. I achieve this by arguing that power-dependence theory can produce governance predictions that are not entirely consistent with what a traditional TCE approach might suggest. These predictions are not only different, but may also better reflect the context of many GVCs. I demonstrate this by producing analytical illustrations that leverage on empirical insight from published GVC case studies. It shows that economic upgrading trajectories may increase the level of asset specificity, frequency and uncertainty within the relationship – all conditions that warrant internalisation. However, these upgrading trajectories may also relegate the domestic firm to a position of unilateral dependence, placing the MNE in a favourable position to appropriate the majority of value-added.

4.3.2 Integrating upgrading and interfirm bargaining power

To develop this aspect of the framework, I draw on the seminal work of Emerson (1962) and his theoretical insights on power-dependence relationships. For the purpose of this dissertation, power is defined as the extent to which a party (A) can get another party (B) to do something that party (B) would not otherwise do (Dahl, 1957). Here I am specifically concerned with value-added appropriation power, and the extent to which a party (A) can coerce the other party (B) to accept a share of value-added that they would not otherwise have agreed to. Utilizing this conceptualization, superior bargaining power is positively correlated with the ability to appropriate value-added. Both of which are derived from variations in the interfirm dependence of each contractual party (the MNE and domestic firm). Upgrading trajectories may create value-added by either minimising production cost or embedding added functions into the activities that the domestic firm provides. However, this value-added can only be captured by the domestic firm insofar as an upgrading trajectory is able to also improve the domestic firm's bargaining power position with the MNE. The strength of this value-added appropriation power will be

reflected in the contracted terms and price that is negotiated between the MNE and the domestic firm.

Adding this dimension of bargaining power through interfirm dependence addresses the theoretical shortcomings of a TCE centric approach to understanding GVC relationships. It allows the a priori framework to capture a more diverse range of governance motives. For instance, the MNE's ability to achieve superior bargaining power over a domestic firm may not always be consistent with a transaction-cost minimizing assumption. In fact, it is possible that the relationship with the lowest transaction related cost may not be the one that allows for the greatest level of MNE value-added appropriation. This MNE value-added appropriation potential can be captured in the contracted good/service price *plus* transaction costs (cumulative exchange cost) in comparison to the next best governance alternative. TCE emphasises the latter costs while an explicit bargaining element focuses on each party's ability to dictate the former (John and Weitz, 1988).

Though Emerson's work is grounded in the study of interpersonal interaction, the arguments can be extended to understand relationships at the group or firm level (Pfeffer and Salancik, 1978). The theory positions superior bargaining power not as a direct attribute of the actors, but rather as a property of the relationship (Emerson, 1964; Brass and Burkhardt, 1993). A particular MNE does not possess generalised bargaining power across all of its value chain relationships. It is more likely that it possesses favourable bargaining positions within certain nodes, while being in weaker positions within others. For example, a large and resource-rich MNE may assume a favourable bargaining position with some of its suppliers that provide inputs needed to conduct its operations. At the same time, this MNE may be in a less favourable bargaining position with a potential host country that it wishes to operate in. From this perspective, the bargaining power differential has less to do with the

firm characteristics of the MNE and more to do with the properties of the specific relationship (Emerson, 1962).

Wal-Mart provides a good illustration of this argument. The world's largest multinational retailer is often fingered for its controversial negotiations with many of its suppliers. These relationships are frequently characterised significant pressure to cut costs and provide precise delivery times (Reuters, 2015; Bloomberg, 2017). In the past, this bargaining pressure has been attributed to supplier failure and bankruptcy e.g. Vlastic – a pickle manufacturer (Crook and Combs, 2007). At the same time, Wal-Mart stumbled in its efforts to enter the Indian market – a plan they initiated in 2007. This difficulty was due to its inability to broker terms and conditions that were favourable to its operations. For retail operations, India requires firms to purchase at least 30% of its merchandise from local small and midsize businesses (New York Times, 2013). Despite intense efforts, in 2013 Wal-Mart announced that it would abandon any immediate plans to open consumer stores. As a key factor in this decision, Wal-Mart executives cited the unwillingness of lawmakers to make concessions on the regulation (Forbes, 2013).

Based on this relational bargaining assumption, the theoretical argument to be adapted for the purpose of this framework is as follows. The bargaining power of the domestic firm is positively related to the dependence of the MNE on the domestic firm. The dependence of the MNE upon the domestic firm is (1) directly proportional to the MNE's need for the product input mediated by the domestic firm and (2) inversely proportional to the availability of those inputs to the MNE outside of the MNE-domestic firm relationship (Emerson, 1962; Emerson, 1964).

Alternatively put³:

$$P_{md} = D_{dm} \text{ (m=MNE; d=Domestic firm)}$$

Power (**P**) of the MNE over domestic firm is equal to the dependence (**D**) of the Domestic firm on the MNE

Or

$$P_{dm} = D_{md} \text{ (m=MNE; d= Domestic firm)}$$

Power (**P**) of the domestic firm over MNE is equal to the dependence (**D**) of the MNE on the Domestic firm

Upgrading trajectories can only act as a positive appropriation mechanism for the domestic firm if it is able to alter the GVC relationship in a manner that increases the MNE's dependence on it. Applying Emerson (1962)'s logic: in addition to creating value-added, a trajectory must also act to unbalance the relationship dependency (Emerson, 1962). It must alter the power relation itself by increasing the MNE's dependence on the domestic firm. For the purpose of this research, I will focus on two⁴ elements of Emerson (1962) power-dependence theory. These are the ones most applicable to GVC relationships involving upgrading trajectories. An upgrading trajectory must be aligned with both elements in order to have a positive effect on the domestic firm's ability to appropriate value-added.

It should be noted that Emerson (1962) uses the term balancing operation as opposed to my reference to the term "unbalancing". This is owed to the framing of his theoretical discussion, that is, one which is positioned from an initial state of dependency asymmetry – where one party is more dependent on the other (hence the need for balancing). In the case of GVCs, the host country domestic firm predates the MNE's entrance. Prior to its entrance, no relationship is present between both

³ For reference, **P**_{md} signifies the **P**ower that the MNE (m) has over the domestic firm (d). Likewise, **D**_{dm} symbolises the **D**ependence of the domestic firm (d) on the MNE (m).

⁴ Emerson (1962) develops four generic aspects of balancing operations that can be used to shift interdependence. Only two operations are utilised in this research. The other two address social elements that are outside the scope of this thesis - such as legitimacy and status

entities and therefore insignificant interdependency exists. As such, it is imperative that upgrading in the domestic firm unbalances this initial state of interdependency.

The first aspect addresses the rarity of the value chain activity, post-upgrade trajectory (Wernerfelt, 1984). The upgrading trajectory must alter the relationship so that it becomes difficult for the MNE to source similar inputs from entities outside the relationship (Pfeffer, 1981). Take for instance a scenario where the trajectory manifests in the form of process upgrading (Blažek, 2015; Humphrey and Schmitz, 2002). The MNE may, for example, assist the domestic firm in funding and setting up complex machinery aimed at promoting less wastage and greater unit productivity. Continuous engagement ensues and the domestic firm becomes an integral part of the MNE's value chain. The input being produced the domestic firm may in final form still appear to be generic and easy to source. However, the rarity resides in the production function of the domestic firm and should the MNE seek to source the input elsewhere, it is unlikely that another supplier will be able to match the domestic firm's production efficiency (Pfeffer and Salancik, 1978).

However, this on its own does not significantly unbalance the relationship in the domestic firm's favour. In fact, it can shift the relationship from a generic arm's length engagement to one that approaches mutual dependence between the MNE and domestic firm (Williamson, 1996). I use the term mutual as the domestic firm may also find difficulty in selling the output to entities other than the MNE (Cook and Yamagishi, 1992). This may be due to the level of demand necessary to achieve minimum efficient scale.

Value-added is created through cost reduction and the MNE and the domestic firm are now in a position to bargain for a share of this added value. The MNE's dependence on the domestic firm increases marginally and it becomes willing to forego some of the added value so as long as it is still able to procure the input a cost lower than the market (Coff, 1999).

This type of arrangement is observable in Apple's interaction with its largest contract manufacturer, Foxconn (Denicolai et al., 2015). In the earlier stages of its operations, Foxconn focused on providing generic assembly service for many electronics brands, including Apple. Its technical capabilities developed as its relationship with Apple deepened. Pursuing various forms of process and product upgrading trajectories, Foxconn was able to develop engineering competencies while managing to achieve unmatched productivity with short lead times (The Economist, 2015; Financial Times, 2013). Over time, Apple began to find it difficult to source services from other contractors, thus facilitating an increase in Foxconn's bargaining power (Deutsche Welle, 2013; Wall Street Journal, 2013; Denicolai et al., 2015).

The second aspect of the unbalancing process occurs if the upgrading trajectory permits the domestic firm to cultivate and sell its outputs to alternative sources. This allows for an extension of the domestic firm's power network by dampening its dependence relationship with the MNE. This balancing process occurs when the upgrading trajectory allows for the upgraded activity to be redeployed across multiple GVC relationships.

Take for example, the MNE decision to assist a domestic firm in the development of a functional activity such as product design capabilities (Tokatli, 2007a). These activities are now performed within the domestic firm and attributable value-added should be reflected in the price proposed by the domestic firm. A rent-seeking MNE may be motivated to apply bargaining pressure to appropriate a greater share of the value-added by attempting to drive the purchasing price down. Assuming that the product design capabilities are pliable in other value chain relationships, the domestic firm will resist bargaining pressure and stand by its price. The domestic firm may eventually terminate the relationship if the MNE's offer price falls below what is offered in other GVC relationships. It should be noted that the MNE need not apply bargaining pressure in order to provoke a response from the domestic firm. The

domestic firm may come to realize that the activity can appropriate greater value-added outside the MNE relationship, thus motivating it to proactively seek a greater value-added share by bargaining for higher prices with the MNE.

In Section 4.3.1, I noted that prior case study evidence suggests a tendency for upgrading trajectories to manifest themselves as specific assets. If this assumption holds, then most MNE-instigated upgrading trajectories will fail to unbalance the relationship in the domestic firm's favour. The first unbalancing aspect creates mutual dependence. Beyond this, asset specificity and low redeployability will render the second balancing operation moot. Together they create a situation primed for high transaction cost and inefficiencies in contracting – thus providing the TCE justification for internalisation.

However, conceptualizing a GVC relationship as a bilateral interaction between one MNE and one domestic firm is the primary reason why prior studies have not been able to fully understand the dependency implications of economic upgrading. GVC relationships are more complex than an idiosyncratic non-equity relationship between two independent firms. Both the MNE and the domestic firm may have concurrent relationships with other firms during their arrangement with each other. Given the size and input demands of many MNEs, it is also common for a single MNE to have parallel relationships with multiple spatially distributed suppliers (Buckley, 2009). Restricting these relationships to isolated bilateral arrangements oversimplifies the issues around dependence and bargaining power in GVCs. In so doing, it is easy to fall into the trap of implicitly assuming that upgrading will contribute to mutual dependence, leading to balanced value-added sharing between the MNE and the domestic firm (Blair and Kaserman, 1987).

I will address the existing conceptual shortcomings by illustrating how an upgrading trajectory itself may create a situation of unilateral dependence on the part of the domestic firm. For this analysis, I will use a process upgrading trajectory scenario as

it represents the most common form of observed upgrading (Gereffi et al., 2005). I apply the traditional assumption of MNE superiority where the MNE is endowed with capital, knowledge and contracting experience (Li and Li, 2014; Merlevede et al., 2014). Subsequent to its contractual engagement with the domestic firm, a decision is taken to transfer specific resources and capabilities to the domestic firm. Capital may be lent to the domestic firm to purchase machinery in order to expand or automate aspects of the production process (Giuliani et al., 2005). Likewise, the MNE may decide to offer technical assistance on factory layouts and management practices in order to help streamline and improve the domestic firm's operations (Pavlínek and Žížalová, 2014).

Both examples create value-added by reducing the marginal cost of production. Regarding the dependence relationship, the domestic firm no longer provides a generic product offering to the MNE. Although similar inputs may be available from other suppliers, none are equipped with the superior technology and appropriate operational procedures required to replicate the domestic firm's production function. Given this, the MNE becomes increasingly dependent on the domestic firm in order to remain competitive in the end market. The domestic firm becomes an integrated cog in the value chain and is able to meet the high quantity, lead time or quality demands of the MNE.

It is expected that the domestic firm will also become dependent on the relationship resulting from increased difficulty in redeploying the upgrading trajectories outside the MNE relationship. Take for instance the case of IKEA in Ivarsson and Alvstam (2011). The authors describe situations where IKEA assisted local producers to rearrange their production layout to suit the needs of IKEA (p. 738; 741). This form of site-specific asset specificity (Dyer, 1996) made the domestic firm unable to reduce dependence by diversifying buyers. The ability to efficiently service other buyers would require the domestic firm to operate parallel manufacturing systems and

layouts. Ivarsson and Alvstam (2011) further grouped instances of technological upgrading into four categories (1) improved operational capability (2) improved duplicative capability (3) improved adaptive capability (4) improved innovative capabilities (p. 732; 738) of which many shared a similar level of relationship specificity (Williamson, 1985).

Framing this as a dyadic relationship positions upgrading as a mechanism that sets up the conditions for a bilateral monopoly (Williamson, 1996). Under these conditions, upgrading acts as an unbalancing operation for the domestic firm. It moves the relationship from one that is purely market-driven, where the MNE has the ability to source a generic input from a wide range of firms, all of which have a similar base of capabilities. Instead, the MNE now has a restricted source for its inputs and this will be negatively reflected in its ability to bargain for lower prices (Blair and Kaserman, 1987). The MNE and the domestic firm approach a situation of mutual and balanced dependency, where both entities exhibit a significant level of dependency on the other. Even under these circumstances, an upgrading trajectory can result in the ability for a domestic firm to capture greater value-added – as the MNE is more willing to forego value-added to sustain the relationship. Applying this argument to Gereffi (1999b), for example, provides a clearer understanding of how this dyadic framing can infer instances of upgrading. In this case, upgrading occurs when the domestic firm moves into activities that are deemed profitable and technologically sophisticated. If through MNE knowledge transfer, the domestic firm is able to move from a generic cut and trim garment manufacturer (mass supply market) into one that provides full package or OEM services to the MNE, then it has upgraded. Embedded in this argument is the assumption that not only does the domestic firm create new value-added by adding design, material sourcing and packaging activities to the product, but it is also able to capture the value-added (through price increases) as the MNE is no longer able to source these full package services in the open market.

However, an MNE's value chain is far more complex and usually involves many intermediaries. Buckley and Ghauri (2004) model of the Global Factory is able to capture the complexity of MNE led GVCs in a succinct manner. Intermediary firms are spread both vertically and horizontally across the MNE's web of activities (Buckley, 2011; Buckley and Ghauri, 2004). The MNE may choose to outsource *different* activities within its value chain to isolated individual contractors. For example, it may choose to outsource its online and technology support services to one firm while choosing to engage with another for dealing with warranty claims for its products. More commonly, however, the MNE may choose to outsource the *same* value chain activity to multiple suppliers. See for example (Ponte et al., 2014) and (Tokatli and Kizilgün, 2004).

Multiple supplier engagements by the MNE is important to my argument. An MNE may engage with a significant number of domestic firm suppliers in the initial periods of its activity fragmentation. It is also not uncommon for MNE-initiated upgrading trajectories to be spread across many suppliers over time. In the case of IKEA, the MNE assisted in upgrading hundreds of Asian suppliers, where most of their output was allocated to IKEA (Ivarsson and Alvstam, 2010; Ivarsson and Alvstam, 2011). The sampled suppliers on average allocated 70% of their production output to IKEA and the figure was 80%-100% for almost half of the sample (p. 737). Conversely, no single supplier was crucial to IKEA as they could reserve the option to re-allocate demand across multiple suppliers.

What initially appeared to be a mutually dependent and a favourable domestic firm relationship under a dyadic lens, now have different implications under a more practical contextualization of GVC participation. This is the traditional shortcoming of a TCE centric theorization – one where symmetric dependence from specific assets is assumed (Nooteboom, 1993b). However, multiple domestic firms pursuing similar upgrading trajectories makes each domestic firm unilaterally dependent on the MNE.

The domestic firm is unable to redeploy the operations to other buyers since its value-added creating upgrading trajectories are aligned to a single MNE. On the other hand, the MNE has at its disposal a range of suppliers from which it can choose from. The relationship can be represented by the following power scenario⁵:

$P_{md1} = D_{d1m} + D_{d2m} + D_{d3m} + \dots + D_{dnm}$ <p>Where: P=power; D= dependence and m=MNE; d₁=Domestic firm₁; d₂=Domestic firm₂; d₃=Domestic firm₃.... d_n=Domestic firm_n)</p>

Here, the power the MNE has over any one domestic firm is (1) inversely proportional on the MNE's need for the product input mediated by the domestic firm and (2) directly proportional to the availability of those inputs to the MNE outside of the MNE-domestic firm relationship (Cook and Yamagishi, 1992). While the MNE still has a significant need for the inputs provided by d₁, through upgrading replication, the MNE is now able to source this specific input from d₂, d₃...d_n. On the other hand, d₁ is not able to *effectively* sell its output or redeploy its upgrading trajectory outside the relationship due to its specificity. Herein lies the danger of assuming that value-added creating upgrading trajectories will be accompanied by domestic firm value-added appropriation. Framed within a dependence model, the conditions for value-added creation are met, but in the process, it has also created the conditions for unilateral lock-in and asymmetric dependence (Buvik and Reve, 2001). This unilateral lock-in is represented in the discrepancy in bargaining power between the MNE and any one of the multiple upgraded domestic firms⁶ that can provide the required input. The transactional dimensions of any one MNE-domestic firm relationship are not independent of the other relations in the network (or GVC) (Emerson, 1962). This bargaining differential can then be leveraged on by the MNE to appropriate the value-

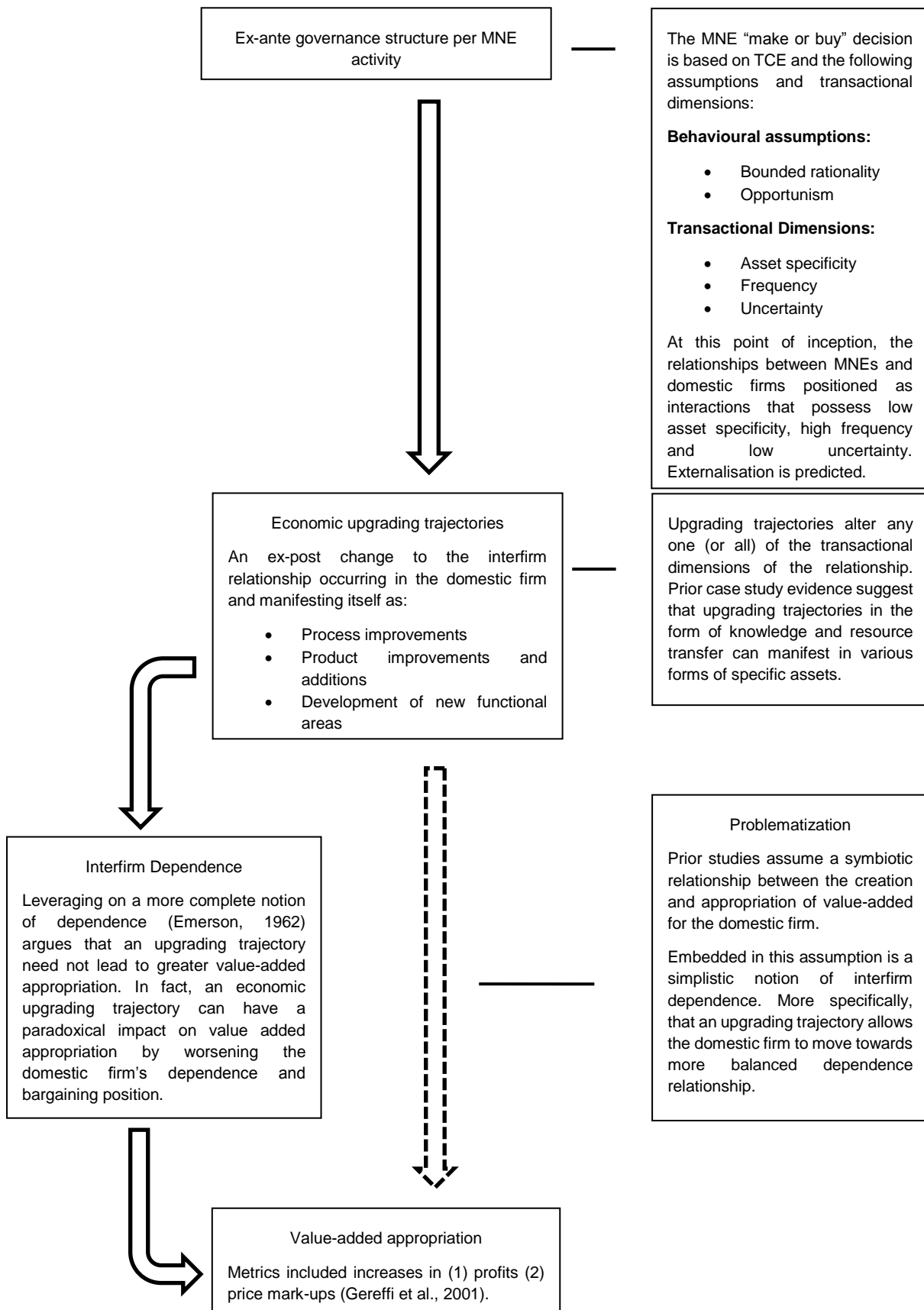
⁵ For reference P_{md1} denotes the Power that the MNE possesses over domestic firm₁. Likewise, D_{d1m} denotes the Dependence of domestic firm₁ on the MNE.

⁶ Supplier firms need not all be domestic. In fact, the MNE may have multiple suppliers that are geographically dispersed.

added that was initially created by the upgrading trajectory (Buckley and Strange, 2015).

Based on the thesis's problematization and the theoretical arguments presented in the previous two sections, Figure 4.3 is a graphical illustration of the thesis's a priori theoretical framework. The text boxes to the right-sided peripheral of the figure and guided by the (—) are intended to provide descriptive guidance. The main elements of the a priori framework are identified and guided by the arrows within the framework. The framework takes the perspective of the domestic firm within which the upgrading trajectory is expected to occur over time.

Figure 4.3 A priori theoretical framework



Source: Author

4.4 Theoretical anomalies

Thus far, this chapter has focused on problematizing studies on the phenomenon of economic upgrading. I argued that the work has been largely a-theoretical where implicit but profound assumptions are made. These assumptions were discussed and an a priori theoretical framework was introduced to ground the phenomenon on a stronger theoretical footing. For a moment, let us assume that this framework represented a complete articulation of the underlying relationship between economic upgrading and domestic value-added appropriation. If this were the case, then this thesis would have adopted a deductive, theory testing approach. The framework would have been tested against data collected from the case study. As discussed in Chapter 3, this thesis is in line with an abductive theory refining approach. By definition, this approach presupposes that there is scope for the underlying theories to be refined or elaborated upon. While the framework provides a good guide to navigate the empirical world, there are still aspects of the phenomenon that the theory is unable to reconcile within. In this section, I will present two of these under-explained areas and illustrate why greater theoretical development is needed. I will focus on what I argue to be (1) the conflict between MNE led upgrading and optimal interfirm contracting (2) the static nature of assuming asymmetry in bargaining. The discussion in this chapter has partially addressed some of these issues. Even so, greater theoretical development is needed. In Chapter 6 and 7, I will rely on the empirical data to shed light on these unresolved issues – a practice consistent with an abductive approach (van Hoek et al., 2005).

Transaction cost logic is usually framed as a firm's decision to make or buy. For every fine sliced activity, the MNE has to decide whether it should be executed internally or contract with an external party. The motive of seeking an efficient transaction cost contracting is a fundamental assumption of this decision process (Williamson, 2008). Here, the efficiency of transacting is frequently considered in terms of governance and bureaucratic costs (Martinez and Dacin, 1999). Martinez and Dacin (1999)

further stated that these costs could be visible, in that they are directly related to resources and production. Likewise, many of these costs may be hidden and associated with guiding, monitoring or policing the behaviour of the supplier (Martinez and Dacin, 1999).

In this sense, TCE sees economic organisation as a discrete choice between two alternatives, that is, using the market or internalising the activity. While this may be so, the theory does not fully consider that the cost of transacting may differ across potential contractual partners (suppliers in this case). In so doing, the theory makes one of two assumptions. On one hand, it may assume that the available supplier base comprises of a group of homogeneous suppliers, with identical capabilities (Bridge and Tisdell, 2004). Alternatively, it may suggest that proponents of the theory assume that while heterogeneity exists in the market, the firm will always engage with the supplier that offers the lowest cost of contracting (Nooteboom, 1993a).

Taking on board this argument, the existence of capability deficiencies in suppliers and the need for MNE assisted upgrading is a cause for theoretical concern. More specifically, significant scope for economic upgrading in supplier firms runs contrary to the notion of a transaction cost minimizing arrangement. The transfer of knowledge and resources in the form of economic upgrading trajectories are not costless for the MNE (Giroud et al., 2012). The MNE may choose to offer financial assistance to the supplier via loans. This arrangement may incur costs, ranging from establishing loan contracts to policing the payments. Other MNE assisted upgrading trajectories may require the MNE to devote resources to special training during its implementation. Post implementation, the MNE may also need to continuously monitor the supplier to ensure that they are able to meet the new requirements. These can all amount to significant governance related cost for the MNE (Williamson, 1985).

Teece (1977) crystallised these costs in his paper on the resource cost of transferring technological know-how. The paper argues that it is common for studies to assume

that transferring knowledge to other firms is costless. To test this argument, the author developed four groups to classify transfer costs. The first group includes MNE incurred costs related to pre-engineering technology exchanges. They are incurred in the initial phase of the process where the basic characteristics of the knowledge are revealed to the transferee. Likewise, engineering costs are likely to be associated with the respective product, process or functional upgrading trajectory, and will likely be borne by the transferor. These are usually incurred during the planning stage of knowledge transfer. The third group of cost are associated with resolving unexpected problems that may arise during the transfer process. And finally, Teece (1977) classified certain costs as pre-start-up training and excess manufacturing costs. Once the knowledge has been transferred, it is likely that the domestic firm will require special training to properly understand and operate the new technology. Once production commences the MNE may incur debugging cost associated with learning, which can manifest in incorrect specifications and other production errors.

These costs will differ depending on the on the nature of the technological know-how being transferred. That being said, an externalisation decision does not imply a homogeneous pool of suppliers. Potential suppliers vary in terms of their size, experience and capability base. This is more so for the domestic firms in developing countries that perform activities at the base of the “smile curve” (Pananond, 2013). For instance, Mudambi (2008) argued that the primary reason for low value-added appropriation ability of these emerging and developing country firms is the abundance of supplier choice. If an external market did not exist, an argument for incurring such transaction costs could be mounted. However, one can argue that an extensive pool of suppliers should minimise the need for such knowledge transfer. Many potential suppliers may have already engaged in endogenous upgrading, thus nullifying the need for MNE orchestrated upgrading trajectories – and the associated transaction costs. Considering the substantive body of theory of TCE, and the

arguments presented above, the logic driving the tendency to engage in upgrade prone relationships remains incomplete.

One might argue that the specific nature of the upgrading trajectories implies that even highly developed and technologically advanced suppliers would still require MNE assistance. Even so, this does not adequately explain why MNEs may tend to choose less developed and technologically weak suppliers. As I have established above, the actual knowledge and resource transfer process involve transaction costs. It is also generally accepted that more developed and technologically advanced firms may possess the capacity to better absorb external learning (Wang et al., 2012; Cohen and Levinthal, 1990). So while TCE may predict the MNE's propensity to externalize an activity, it is unable to provide an explanation for its proclivity towards its engagement of deficient suppliers.

The process of achieving acute asymmetry in bargaining, and by extension, the distribution of value-added is another area in need of theoretical clarity. In a recent paper, Buckley and Strange (2015) posited that MNEs may choose to externalize activities so as to appropriate full value-added from a smaller base of owned assets. There is ample case study research that illustrates the asymmetry in interfirm GVC relationships (see Choksy et al. (2017) for a recent summary). Many of these relationships involve suppliers from developing countries where the studies suggest that contract prices are only slightly above or equal to their marginal cost of production. In the context of interfirm relationships, this is an overly static proposition. The intensity of such asymmetry is likely to be dynamic and process oriented. The firms that participate in spatially dispersed GVC will typically predate the relationships themselves. Prior to engaging with the MNE, they would have been domestic firms that served the domestic market only. Buckley and Strange's (2015) argument of full appropriation of value-added implies that the relationship is one where the domestic firm faces immense bargaining pressure from the MNE. However, pre-existence

indicates that at initial engagement, the MNE is unable to exert such bargaining pressure. If this tactic is pursued, the supplier can exercise the option to walk away from the deal altogether if they are dissatisfied with the terms of trade being tendered (Masten, 2000). The supplier can then continue servicing its pre-existing domestic market.

Pre-existence is important to this argument and can be contrasted to the bargaining relationship between headquarters and a greenfield subsidiary. Subsidiaries of this nature are created by the MNE for a specific purpose. Goals and objectives are converted into subsidiary mandates that guide the strategic and operational direction of the subsidiary. At inception ($t=0$), the parent MNE is in control and enjoys the bargaining position needed to dictate the terms of the relationship (Yamin and Forsgren, 2006). However, this can change over time and the subsidiary's role can evolve in terms of its remit and responsibilities (Birkinshaw and Hood, 1998). This evolution of subsidiary charter is not always the intention of the parent MNE. Mudambi and Navarra (2004) argues that the subsidiary role within the MNE is contingent on its bargaining power relationship with the MNE parent. In this study, increases in subsidiary bargaining power occurred via the subsidiary's creation of knowledge assets that were of importance to the MNE as a whole. This bargaining power can then be used by the subsidiary to appropriate a large share of the rents from the MNE's resources. Increases in subsidiary's bargaining power had a significant and negative effect on the financial flows to the MNE parent (Mudambi and Navarra, 2004).

This comparison is meant to illustrate that bargaining power is not a static relationship dimension. A party's bargaining position at relationship inception is likely to evolve over time. Likewise, any asymmetry in bargaining that is currently observable may not have existed at inception. This has been recognised and studied extensively in parent-subsidary relationships (Bartlett and Ghoshal, 2002). The same cannot be

said for studies on GVC relationships between MNEs and host country domestic firms. In fact, little is known about how acute asymmetry in bargaining comes to fruition, or the role that upgrading plays in the process. The thesis's a priori theoretical framework is an attempt to explicate this process. However, it is likely to be only a partial explanation, one that can benefit from greater theoretical refinement from rich empirical insight.

4.5 Chapter conclusion

This chapter has engaged with a theoretical shortcoming regarding our understanding of economic upgrading from GVC participation. It has highlighted a problematic assumption embedded within much of the extant research on the phenomenon. Many studies fail to make a distinction between an upgrading trajectory and economic upgrading itself. In doing so they rely heavily on observational evidence of upgrading trajectories as signals for domestic firm upgrading. This chapter contends that economic upgrading must encompass both the creation and appropriation of value-added, and that upgrading trajectories are only an indication of creation.

A physical upgrading of the production process in the domestic firm (a trajectory) and the appropriation of the new value-added so created are not coterminous. Technical improvements, for example, through capital deepening and new embodied technology, generate increases in total product (and therefore productivity) but do not necessarily benefit the domestic firm in terms of the supplier's appropriation of value-added. Value-added creation and appropriation are liable to diverge in MNE-domestic firm relationships as a consequence of changes in bargaining power. Notwithstanding the fact that value-added is created in the value chain, this manipulation can create the unilateral lock-in of the domestic firm. Assuming a symbiotic relationship between value-added creation (upgrading trajectories) and its appropriation, prior studies have implicitly assumed away the implications of

bargaining power asymmetry – or at best assumed that an upgrading trajectory improves the domestic firm’s bargaining position.

To address this general oversight in the literature, this thesis’s a priori theoretical framework provides an initial roadmap for why a disparity in the appropriation of value-added can co-exist with a domestic firm’s apparent upgrading. Consistent with an abductive approach, the framework is constructed using theoretical insights from TCE and power-dependence theory. TCE represents the most widely used theoretical lens for understanding and predicting a firm’s chosen governance structure. However, this perspective is based on a cost-minimising approach where inadequate consideration is placed on interfirm-bargaining over time. To address this, I utilize the seminal work of Emerson (1962) to illustrate how deeper emphasis on the dependence implications of upgrading trajectories can enrich our theoretical understanding of the phenomenon. In combination, this framework will guide the data collection process that will be outlined in Chapter 5.

Chapter 5

Research methodology: Part 2

5.1 Chapter overview

This chapter represents the second part of the thesis's research methodology. Chapter 3 focused on what could be considered the conceptual methodological elements. It included a discussion around philosophical underpinning, as well as the manner in which theory will be positioned and used for the thesis. Mention of a theoretical framework is likely to induce the reader into making the assumption that the thesis aims to deductively test an extant theory. As such, it was important to articulate the abductive theory elaboration approach before progressing into Chapter 4's theoretical discussion.

In this second part, I will discuss the methodological aspects related to data collection and its analysis. This provides a seamless transition into the empirical content of the thesis (Chapters 6 and 7). I have already confirmed that a case study research strategy will be pursued. Section 5.2 and beyond is concerned with the mechanics of the research strategy. Section 5.2, in particular, discusses considerations around case sampling and why a single embedded case study is an appropriate sample for this thesis. In Section 5.3, I state the important ethical considerations that form part of the thesis. These considerations have been presented to, and approved by, the Faculty Research Ethics Committee. Maintaining anonymity is a key element of these ethical considerations. This was necessary to ensure that the respondents were willing to participate in discussions around value-added distribution and interfirm bargaining. Under the cloak of anonymity, Section 5.4 presents the case that will form the empirical foundation of the thesis.

Once the case context has been described, Section 5.5 explains the research methods that will be employed to gather the empirical insight needed to refine and elaborate on the theoretical framework. Data collected must then be organised,

analysed and abstracted to theory. I discuss this process in Section 5.6. This chapter concludes with Section 5.7 where I provide an overview of how the subsequent empirical chapters will be presented.

5.2 Sampling strategy

Case study sampling strategy involves consideration around (1) what to select – the unit of analysis, (2) how to select - the rationale on which case/s to select, (3) how many to include- the number of cases that should be integrated into the study (Fletcher and Plakoyiannaki, 2011).

The decision on “what to select” is instrumental in determining the boundary conditions and scope of the empirical investigation. Central to this decision is the issue of the unit of analysis. Fletcher and Plakoyiannaki (2011) proposed that the unit of analysis can be separated into four overlapping categories. This categorization is outlined in Figure 5.1. Regarding this thesis, the unit of analysis is not a singular object, rather, the investigation calls for more than one unit of analysis. A particular value chain may be a single unit where the value proposition is a lone product or range of related products (UNCTAD, 2013). Interconnectedness is a central theme of GVC analysis. Emphasis is placed on understanding the interconnected value-adding nodes of the chain and the role of each of these intermediaries in the creation of a good or service. Investigating economic upgrading from GVC participation makes understanding this interconnection crucial. For instance, a domestic firm at tier two of the value chain may have initiated a specific upgrading trajectory in the hopes of creating and appropriating greater value-added. Investigating the entire value chain allows me to determine the role that the lead firm has played in the process and the effect that it will have on their operations. An investigation across value-adding nodes also allows for a deeper understanding of market structure and how particular upgrading trajectories may alter this structure, and by extension the bargaining power within it.

Table 5.1 Unit of analysis classification

Unit of analysis classification	Description
Social	The social unit of analysis may be an individual or individuals, a group or committee, an organisation, a community or social specific social interactions (such as those existing in dyadic relationships)
Temporal	The temporal unit of analysis may be a particular encounter, episode or an event. Usually represented in a specific period of time
Geographical	The geographical unit of analysis may be represented in the form of countries, towns or states.
Artefacts	Artefacts in the form of books, photos, newspapers or technological objects

Adapted from Fletcher and Plakoyiannaki (2011)

The case study design that will be used for this study is in line with what Yin (1984) referred to as an embedded case study. An embedded case study design allows me to explore various sub-units within a larger case (Baxter and Jack, 2008). The value chain is the larger case under investigation, where this study is focused on the effects that GVC participation have on the ability for domestic firms to upgrade and appropriate greater value-added. Within this value chain, there are multiple levels of production, many of which involve the participation of domestic firms. The sub-units are the firms that participate in the GVC from which I will collect the data (Fletcher and Plakoyiannaki, 2011).

Determining which value chain will form the empirical basis for the case study is the next decision to be made. This decision is closely connected to the research approach outlined in Section 3.3. The research approach for this thesis is one of theory elaboration based on an abductive process. The initial research questions are derived by utilizing a problematization methodology, that is, by looking closely at and challenging an underlying assumption of studies on economic upgrading. The theoretical framework that is derived from the initial phase of this abductive process, though robust and defined, is not intended to be a complete understanding of the relationships among GVC participation, economic upgrading and the distribution of value-added. Instead, it is designed to guide the data collection but remain flexible enough to facilitate the process of theoretical elaboration.

It is imperative that the data collected from the case study strategy is well positioned to inform and develop the underlying theoretical framework. As such, this thesis adopts a sampling strategy that can be considered purposeful sampling (Fletcher and Plakoyiannaki, 2011). The thesis is not concerned with issues related to statistical sampling, as population generalisability is not the objective of this study. Instead, the sampling strategy is focused on appropriateness, purpose and access to good information (Marschan-Piekkari and Welch, 2011). Purposeful sample strategies are ideal for research questions that are aimed at analytical generalisability, that is, generalising to theoretical propositions (Yin, 2013).

Under the umbrella of purposeful sampling, the thesis will utilize a theoretical sampling strategy (Coyne, 1997). The underlying rationale of this sampling strategy is to select cases that are likely to provide insight that is useful to develop theory (Marschan-Piekkari and Welch, 2011). Theoretical based sampling has traditionally been utilised in studies that adopt a grounded theory approach (Glaser and Strauss, 2009). While this thesis utilises an abductive approach, the underlying sampling premise is similar. The case(s) is(are) selected based on its applicability and appropriateness, relative to the thesis's initial theoretical framework. In so doing, it provides alignment among the theoretical framework, empirical data and the analysis to create the interplay necessary to develop novel theoretical insights (Dubois and Gadde, 2002). In other words, the empirical setting was chosen on the basis of its ability to provide a context where the theoretical framework is most likely to be observable. It should be noted that the intention is not to achieve a replication or testing logic (Eisenhardt, 1989). Rather, the assumption is that the initial theoretical framework is a partial understanding of the phenomenon. Sampling the most appropriate context provides the rich data needed to contribute toward building a more complete theory (Welch and Welch, 2015).

Chapter 4 highlighted a fundamental assumption in the GVC economic upgrading literature that implicitly assumes a positive and coterminous relationship between the creation and appropriation of value-added from upgrading trajectories. Building on this problematization, a theoretical framework was constructed using insights from dependence base bargaining power and TCE (Emerson, 1962; Williamson, 1996). The framework applies a reconceptualization of economic upgrading and posits relationships that run counter to extant empirical conclusions. In order to develop this theory further, I need to identify a value chain that exemplified this divergence between conventional definitions of economic upgrading and the value-added capture of domestic firms. In other words, the thesis required a sampling strategy that was purposeful and theoretically driven (Coyne, 1997). Appropriateness, purpose and access to good information are important cornerstones of this sampling strategy (Fletcher and Plakoyiannaki, 2011). The empirical context needs to match a situation in which domestic firms were upgrading in a manner that was consistent with existing definitions, while at the same time indicating increasing asymmetry in the appropriation of value-added.

Thus far, I have provided a justification for (1) what to select – consideration around the unit of analysis, (2) how to select - the rationale on which case/s to select. Neither of these aspects deals with the controversial question of sample size. Regarding this thesis, I have chosen to undertake a single case study design. Even so, a commonly held view among many case study researchers is that larger sample sizes are more desirable. Probably the most common statement to this effect was made by Eisenhardt (1989), where she advocated for a case study size of between four to ten cases. The underlying argument of this suggestion is one based on a replication logic, largely derived from a positivistic underpinning (Fletcher and Plakoyiannaki, 2011). Yin (1984) argued that a large case sample would increase the chances of the empirical findings meeting the conditions for external generalisability. Depending on a study's research objective, it may indeed benefit from having a

“large-n” sample. For example, a study may be interested in the replication of findings, or theoretical relationships across a range of contexts. In such research circumstances, increasing the number of cases would be beneficial towards making a statement of external validity.

Large sample sizes have also been advocated in research studies that aim to build theory. For instance, Eisenhardt (1991) argued that good theory is partially the result of comparative multi-case studies, where the propositions developed are more robust with greater generalisability potential. However, developing theory from a large number of cases is not without internal contradiction. Depth of understanding is usually sacrificed in the pursuit of empirical breadth across a wide sample. Investigating large samples using qualitative research methods can compromise one of the core benefits of using a case study research strategy, that is, the opportunity to develop thick descriptions and explanations of associations between key concepts within the study (Fletcher and Plakoyiannaki, 2011).

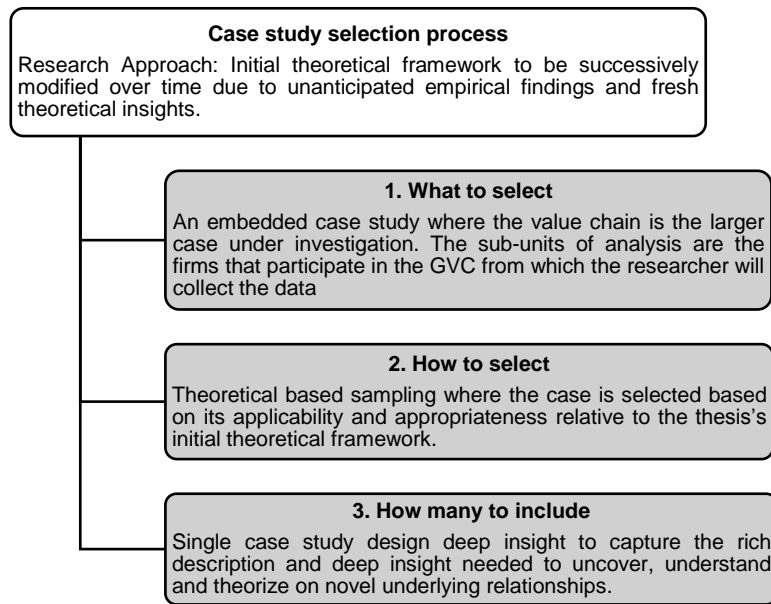
Economic upgrading is frequently positioned as most beneficial to domestic firms in developing countries. These firms are argued to be underdeveloped, where they lack the resources and experience necessary to be competitive in the global market (Gibbon, 2001). Even so, much of the research on economic upgrading have not given deep considerations to the importance of this context (underdeveloped capabilities resources and experience) on the upgrading decision-making process of these domestic firms (Tokatli, 2013). It is also important to gather insight into how the context changes after a particular upgrading trajectory has been undertaken. A particular trajectory will alter the makeup of the domestic firm and may change the structure of that firm. These changes may have implications on, for example, the options that the domestic firm has in terms of its supply market. Attempting to study these complex changes over a large sample of case studies may result in “thin”

descriptions that only provide surface data, as opposed to data that can help understand the deeper dynamics of economic upgrading (Dyer and Wilkins, 1991).

The overarching purpose of the research is instrumental in decisions of case sample size (Fletcher and Plakoyiannaki, 2011). The above issues are arguably less prevalent in studies aimed at explicitly testing a theoretical framework. In such situations, depth of insight and thick descriptions may be less of a concern as the relationships between constructs are already well defined. The underlying purpose of such research is external validity. For theory building objectives, as the one embedded in this thesis, then deep insight and rich description are necessary to uncover, understand and theorize on novel underlying relationships. The abductive process in the thesis explicitly positions the a priori theoretical framework as defined but flexible in order to allow for theory building. Theory guides the data collection process, but under the assumption that such theory is at best an incomplete understanding of the phenomenon under investigation.

Figure 5.1 highlights the decisions around case study selection and summarises the approach that this thesis will take. As with many methodological decisions, case study selection is closely tied to the approach of the study and the role that theory plays in the process.

Figure 5.1 The case selection process



Source: Author

5.3 Research ethics

The University of Leeds via the ESSL, Environment and LUBS (AREA) Faculty Research Ethics Committee reviewed and provided ethical approval for the data collection phase of this thesis. The ethics reference is AREA 15-035 and a copy of the approval is attached in the thesis's appendix. As part of the ethical application, I committed to providing anonymization to the respondents that agree to participate in the study. This involved presenting empirical evidence in a manner that cleanses it from detail which can be used to identify the respondent or the firms that they represent. In order maintain this level of anonymity, I will refrain from mentioning the exact industry or the country in which the domestic firms operate. While this level of anonymity may be considered unconventional, it was necessary in order to gain access to the respondents and their experiences and insights. This is primarily due to the nature of the discussion, as interviewees were questioned on a range on sensitive themes, including (1) MNE resource and knowledge assistance (2) collusion or market organisation (3) amendments to contractual terms (4) changes to shares of value-added.

Potential respondents were properly briefed on the context of the study and the discussion that is likely to emanate from the interviews. This was done verbally and in text via a participant information sheet. Prior to the interview, interviewees were asked for permission to record the interviews in audio form. Some respondents opted to not be recorded. In these instances, bullet points were taken during the interview and detailed insight was recorded immediately following the interview.

Interviews are an instantaneous method of data collection. Interviewees provide insight on the spot and may inadvertently say something that they may later regret having divulged. Although anonymity is offered, I allowed respondents a two week period during which they can withdraw their participation in the project, or withhold particular insights that they have previously provided. While this was offered, no respondent exercised this option.

5.4 The case

The value chain under investigation can be classified as the retail food sector in a developing country and is part of the global fast food industry. A global industry that generated over 540 billion United States dollars in revenues for 2016 (Zion Market Research, 2017). This particular chain is orchestrated by an MNE who is responsible for the brand name and recipes, that is, the brand owner (franchisor). The franchisor contracts with firms (franchisees) across the globe who are given the authority to operate under the brand within an agreed geographic area. More than half of the franchisor's revenue stream is derived from its global operations.

Specific to this case study, the franchisee is a regional MNE that owns and operates franchised stores across four countries within a common region. In many cases, the franchisee orchestrates a network of meat producers across the region who are responsible for processing the main ingredient (an animal-based protein product). In turn, the domestic meat producers contract with domestic farmers who rear livestock that is integrated into the production process. While the franchisee may need other

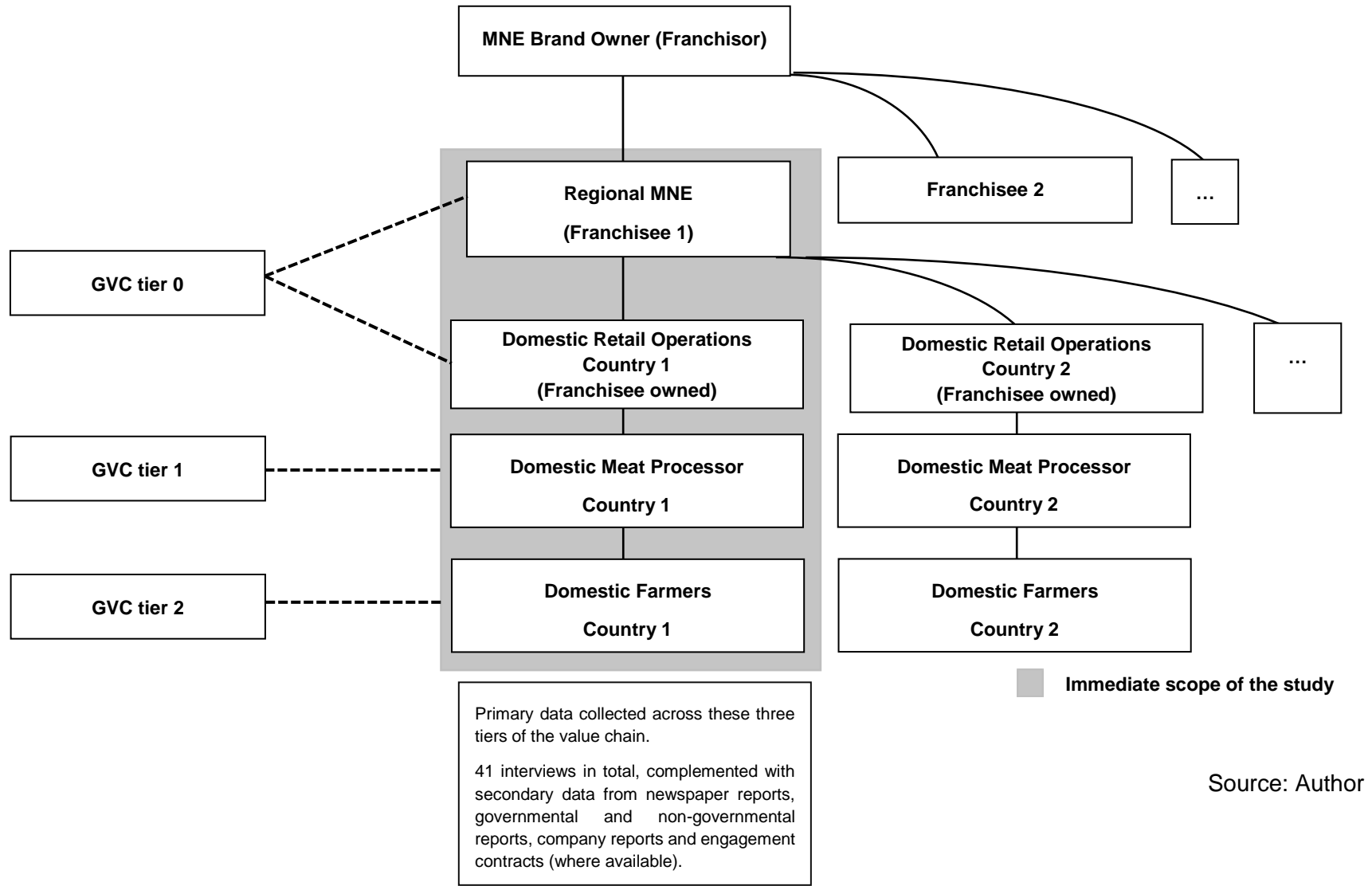
inputs to carry out its operations, this protein product represents the core input and is therefore the focus of this case study. Figure 5.2 provides an illustration of how the value chain is organised.

I use the term region as it represents a geographic space that denotes a cluster of smaller nation-states. While each country is an independent sovereign nation, there are single market regulations in place. This permits the free movement of labour and domestically produced goods and services. In the country of focus, the regional-MNE owns and operates 59 retail outlets that prepare and sell the meat-based fast food product. In absolute terms, domestic operations in the form of 59 outlets may appear as minute. However, this represents an average of 1 retail store per 22,000 persons. This average is specific to retail stores connected to the brand that is the focus of this thesis. In comparison, the United States of America had an average of 1 store per 70,000 persons in 2014. For the same fast food product, New Zealand had an average of 1 store per 41,000 persons in 2016. In terms of overall profitability, this domestic market is also significant. In 2015, the annual financial report for the regional-MNE confirmed a net profit figure of approximately 9 million USD. A local newspaper in 2016 asserted that the regional-MNE's capital city branch was the world's highest sales outlet in absolute terms, and the domestic market itself was the franchise's highest grossing overseas market per capita. These claims were supported by interviews with the supply chain manager at the regional-MNE.

The domestic processor is currently one of the largest processors of this type of meat in the country. The industry is dominated by four large processors, where produce is sold through various outlets, including (1) groceries and supermarket chains (2) fast food and quick service restaurants (3) "alive" market through small butchers and processing shops. In this case, the "alive" market refers to instances where the animal is sold by the domestic processor while it is alive. The animals are then processed independently by smaller processors and sold to end customers. The

relationship between the regional-MNE and the domestic processor began during 2000-2001. Even so, the data sources are able to capture the activities of these firms over time. This allows the empirical data to capture the operations of the domestic firm prior to its relationship with the regional MNE.

Figure 5.2 The case study industry breakdown



Source: Author

This case study matches well with the theoretical sampling strategy outlined in Section 5.2, where the criteria of appropriateness, purpose and access to good information were present. This fast food value chain permits me to investigate a complete value chain from genesis (farmers) to the end market (MNE franchising companies). While the value chain may be considered simplistic, it allows for the investigation and analysis of data that is beyond the MNE and 1st tier relationships that are common in the GVC literature (Ivarsson and Alvstam, 2011; Giuliani et al., 2005). The simplicity of the value chain minimizes distracting empirical data and permits me to undertake a deep investigation into the core relationships that exist across value chains, regardless of industry.

The a priori theoretical framework posits that variations in firm attributes are prevalent in GVC participation. Indeed, the prerequisite for economic upgrading via GVC participation is to a large extent dependent on variations in firm resources and capabilities. However, these variations also make the governance relationship increasing dynamic, as ex-post changes are more likely to occur as a result of economic upgrading or otherwise. How these changes affect value-added appropriation and bargaining power is a core objective of this thesis. It is imperative that the case matches or conforms to these prior notions of upgrading (Guerrieri and Pietrobelli, 2004; Humphrey and Schmitz, 2002; UNCTAD, 2013).

Media reports drew initial attention to the appropriateness of this case. National newspapers frequently report the success of the domestic firms and laud their development over the last decade. Applying the existing conceptualization of upgrading, one is likely to conclude that domestic firms have undergone significant levels of upgrading from its GVC activities. In my case, a regional MNE (franchisee) entered the developing country to conduct fast-food retailing to the general population. This franchisee has a large regional footprint and conducts similar retail activities across multiple countries under a common brand name with the support of

the brand owner (franchisor). Prior studies on upgrading have been noted to rely on visual indicators of firm development to signal instances of economic upgrading (Milberg and Winkler, 2011). These indicators may range from observations of physical capital deepening to entering into new functional areas. Evidence of these indicators are also present in the case study, where there is observational evidence of capital investment and functional upgrading trajectories within the domestic tiers of the value chain. A preliminary factory tour of the domestic meat producer revealed that various upgrading trajectories were apparent.

However, contradictory insight was also evident beyond the visual support for domestic economic upgrading. Unstructured initial interviews with key industry informants indicated that some value chain actors were increasingly under pressure to provide gate prices that were threatening their profitability. Seemingly, this occurred even in light of what could be classified as economic upgrading. For instance, an early respondent at the domestic meat processor mentioned that officials from the regional MNE (franchisee) were continuously making demands for lower prices. Such counterintuitive insights provide the justification for purposely selecting this case study based on theoretical grounds. The case not only fits well into the thesis's a priori framework, but it provided a fertile context to abductively develop it by investigating the thesis's research questions.

5.5 Data collection methods

The advantage of a case study research strategy lies in its ability to capture complex contextual relationships through rich empirical data (Eisenhardt, 1989). Even so, researchers are not always successful in capitalizing on this multifaceted approach to achieving thick description. Instead, it is common for many studies to claim case research, while at the same time relegating itself to narrowly collecting data through interviews (Voss et al., 2002). The lure of the interview is understandable, as it allows

the researcher craft the scope of the empirical data by having control over the interview questions and its structure.

This thesis investigates GVC issues that can be sometimes considered controversial. For fear of victimisation, firms from developing countries are not always keen to speak on issues of MNE involvement and the distribution of value-added (Ivarsson and Alvstam, 2011). My commitment to maintaining respondent anonymity is expected to assist in achieving openness from the interviewees. However, it is still unlikely that interview insight alone will provide the rich description and insight needed to facilitate theory elaboration.

Section 3.2 provided an overview of the thesis's ontological assumptions regarding the construction of reality. I assume an objectivist perspective in which a single truth exists within the confines of the case study. This truth is independent of the perceptions of the respondent. Triangulation is an important cornerstone of this objectivist positioning. While external validity in a generalizable sense is not the objective of the research (across a wide range of contexts), validity within the boundaries of the case study is needed. For example, a particular respondent may inadvertently provide subjective insight regarding their bargaining power position in the value chain. This may be influenced by only a partial understanding of the entire value chain. Likewise, the respondent may be pressured, socially or otherwise, to provide a response that they believe puts them in a favourable light. This response may be provoked by their desire to save face or to project an impression of personal achievement.

In both these scenarios, relying on multiple sources of data can be advantageous. Instances where the respondent is unwilling to provide a detailed account of particular relationships can be addressed by seeking complimentary insight from a range of other data sources. For example, respondents in the domestic meat producer were unwilling to speak on particular aspects of its contracting with domestic farmers. I

was able to gain deeper insight by retrieving written contracts from domestic farmers that were no longer actively participating in the value chain. Instances of perception based responses were also apparent and leveraging on multiple data sources assisted in achieving validity. For instance, certain respondents at the regional-MNE (franchisee) responded in a manner that implied a minimal level of input from the brand owner. The ability to corroborate this was possible through accessing secondary material available online from the brand owner on its franchisee support initiatives. The regional-MNE's annual report also provided insight that could be used to validate interview responses.

The above discussion is meant to illustrate the importance of embracing the full potential of multiple data sources in case study research. The examples are merely scenarios within the data collection process where leveraging on a range of data sources ensured that thick description and deep insight were maintained.

5.5.1 Print media and industry reports

Although the focal host country of this thesis is a developing nation, its prominent newspapers have been fortunate to retain an online presence. For the country's three major news houses, articles have been available online since the early part of the millennium. Media related to the value chain is searchable and easily downloaded for further analysis. This repository of text data is a source of empirical insight and can assist in filling voids in my contextual understanding. Beyond this, it provides longitudinal details on the industry's developments and challenges. For instance, it is likely newspaper outlets have reported on the regional-MNE's involvement in the domestic industry. This may include details on instances of upgrading as well as industry challenges such as industrial action.

Further to this, the national statistical office also provides a useful resource for economic and industry reports that are pertinent to the fast food value chain within the developing country. These reports are useful to understand the industry changes

over time - in terms of production output, employment and exports and imports. These reports may also be useful in determining the industry structure and how this structure has changed over time.

5.5.2 Engagement contracts

As previously mentioned, the thesis explores GVC issues that may be considered either controversial or in some regards confidential. Hurdles in data access are usually expected when the research focus is on value-added distribution, bargaining power and interfirm negotiation. To gain insight into these aspects, I was able to exploit novel sources of empirical insight. For certain tiers of the value chain, for instance the domestic farmers, there are individuals who are no longer active in the value chain. They may have retired or moved into other industries. In addition to interviewing these individuals, many of them were also willing to share documentation that they would have acquired during their involvement in the value chain.

These farmer records and documents include (1) short and long-term engagement contracts (2) standard operation procedures (3) training manuals (4) receipts for the sale of intermediaries. In some instances, domestic farmers were able to provide records of their basic bookkeeping and profitability over time. This was however not common, as many farmers were not trained in accounting, nor did they have the resources to hire specialists.

5.5.3 Website details and annual reports

The lower tiers of the value chain (domestic farmers and processor) were not limited liability companies and not mandated to make their accounts publically available. Most of the sample farmers did not keep proper records and the domestic processor was hesitant to disclose confidential financial records. However, the regional-MNE and the brand owner are both publically traded companies and were required by law to report their activity in annual reports. These reports help understand the

downstream value-added capture in light of the empirical data that will be retrieved from other domestic sources.

Other publicly disseminated information in the form of official websites were also considered valuable sources of empirical data. The brand owner is one of the largest franchising and restaurant management MNEs in the industry. They have taken a proactive stance on publically releasing information on their operations and interactions with franchisees. I was fortunate to have this level of publically available data on the brand owner as it was not possible to conduct interviews with persons at the organisation.

5.5.4 Interviews

Interviews were used as a core method to collect a significant amount of the empirical data needed for insight into both the context and the underlying GVC relationship. Of all the data collection methods, it is the element that I had the most control over. The scope of the responses could be focused based on the structure, framing and content of each interview question. The interview questions were guided by the thesis's theoretical framework and were semi-structured to facilitate an abductive approach. The semi-structured approach allowed for crafting focused and theoretically driven questions while permitting the respondents to speak openly without defined constraints on their responses. A summary of the interviewees is presented in Table 5.2. In appendix A, I have also included a copy of the interview protocol used at the domestic processor tier of the GVC.

Determining suitable respondents is an important aspect to consider when using interviews as a data collection method. The purposeful sampling strategy outlined in Section 5.2 was useful in rationalising the case study selection process. It is however relatively silent on the micro foundational considerations around respondent selection. Even so, the underlying criteria of appropriateness are still applicable (Turner III, 2010). Respondents needed to be in a position where they are likely to have

experiences that could inform the line of questioning. For example, when I sought to gain insight from the regional-MNE (franchisee) on its relationship with the brand owner (franchisor), it was necessary to have someone that was responsible for franchisor engagement. Likewise, when exploring the extent of process upgrading trajectories in the domestic processor firm, it was useful to request someone that was responsible for the operational aspect of production.

In the case of domestic farmers, decisions regarding “within firm” selection were less of an issue. Many of the farms in the industry function as sole trader businesses, where the owner is best positioned to provide both operational and strategic insight. The issues, however, reside in identifying appropriate farmers to interview. The industry is made up of a significant number of farmers. Not all these farmers engage in the value chain that is under investigation. Some sell to other domestic processors or attempt to sell directly to domestic groceries. I was fortunate enough to network with one domestic farmer that was in the process of setting up a local farmer’s trade union. In preparation for this, the farmer spent a considerable amount of time gathering population data on all farms in the country. He was generous enough to provide me with a copy of this database. This database was detailed and provided specifics on the farmer demographics, including (1) farm location and contact (2) farm size (3) processor that the farm sells to (4) current farm operation status. Using this data, I was able to select a representative sample of domestic farmers. This farmer level insight was not restricted to farmers currently in operation. Interviews were also conducted with farmers that were no longer in operation. These former farmers were a good source of data as they may be more open to discussing the issues that may be construed as controversial.

Many farmers have been in contractual relationships with the domestic processor for periods that pre-date the entrance of the regional-MNE. These respondents are thus well equipped to provide insight into the pre-MNE phase of the domestic processor’s

operations. Interviews were also conducted with both strategic and operational level staff at the domestic processor (see Table 5.2). Many of these staff members had been with the company before it began its relationship with the regional-MNE. An interview was also conducted with an industry informant/expert who has been involved in and has industry experience dating back over 40 years. This respondent's insight was used to elaborate on and corroborate interview data collected directly from informants at the domestic processor.

Table 5.2 Breakdown of interview data

Respondent ID	Value chain level	Level at firm	Length of interview
M1	Regional MNE	Supply chain management	1 hour 8 minutes
M1	Regional MNE	Supply chain management (follow up interview)	1 hour 12 minutes
M2	Regional MNE	Supply chain management	55 minutes
M3	Regional MNE	Supply chain management	1 hour 20 mins
M4	Regional MNE	Supply chain management	30 minutes
M5	Regional MNE	Franchiser engagement	45 minutes
P1	Processor	Director	1 hour 18 minutes
P1	Processor	Director (follow up interview)	2 hour 9 minutes
P2	Processor	Director	42 minutes
P3	Processor	Factory operations	1 hour
P4	Processor	Factory operations	1 hour 40 minutes
P5	Processor	Sales unit	Approx. 55 minutes
P6	Processor	Contract farming management	Approx. 40 minutes
P7	Processor	Factory operations	2 hours 12 minutes
P8	Processor	Quality assurance unit	30 minutes
P9	Processor	Integrated/downstream services	1 hour 35 minutes
F1	Farmer 1	Owner	57 minutes
F2	Farmer 2	Owner	2 hours 13 minutes
F3	Farmer 3	Owner	Approx. 1 hour
F4	Farmer 4	Owner	1 hour 15 minutes
F5	Farmer 5	Owner	1 hour 34 minutes
F6	Farmer 6	Owner	40 minutes
F7	Farmer 7	Owner	35 minutes
F8	Farmer 8	Owner	Approx. 50 minutes
F9	Farmer 9	Owner	1 hour 11 minutes
F10	Farmer 10	Owner	35 minutes
F11	Farmer 11	Owner	42 minutes
F12	Farmer 12	Owner	55 minutes

F13	Farmer 13	Owner	1 hour 13 minutes
F14	Farmer 14	Owner	1 hour 30 minutes
F15	Farmer 15	Owner	43 minutes
F16	Farmer 16	Owner	45 minutes
F17	Farmer 17	Owner	1 hour 2 minutes
F18	Farmer 18	Owner	41 minutes
F19	Farmer 19	Owner	58 minutes
FF1	Former farmer 1	Owner	42 minutes
FF2	Former farmer 2	Owner	47 minutes
FF3	Former farmer 3	Owner	1 hour 2 minutes
FF4	Former farmer 4	Owner	1 hour 14 minutes
FF5	Former farmer 5	Owner	58 minutes
IE1	Industry expert	Independent industry consultant	2 hours 12 minutes

Source: Author

5.6 Data analysis

Analysing qualitative data from case studies can be one of the most difficult phases of the research process (Ghauri, 2004). The advantage of rich contextual insight and thick description also means that the researcher is burdened with a mass of empirical data. An abductive research approach further complicates this as the investigation is not limited to testing particular theoretical relationships. If such were the case, having predefined and well-articulated hypotheses would provide a mechanism to navigate the large amounts of empirical data. Instead, this thesis has a theory refining objective, where emergent themes are crucial to advancing theoretical understanding. The data analysis process must be not only recognised these themes, but provide a means to organise and theorise on new relationships.

The data analysis for this thesis was done via a three-stage abductive process, namely data categorising, iterative matching and abstraction/theoretical refinement (Dubois and Gadde, 2002). Table 5.3 provides a summary of the data analysis process and highlights the key subtasks associated with each step.

5.6.1 Data categorisation

The categorisation stage of the data analysis process encompasses what Ghauri (2004) considers (1) coding - sorting data according to concepts and themes (2) clustering - categorising codes according to common characteristics. Nvivo, a computer-aided qualitative data analysis software (CAQDAS) assisted in this aspect of the data analysis process. First, all the data needed to be converted into a form that would facilitate the coding and clustering subtasks. 37 of the interview were available on recording and were transcribed verbatim. When asked for recording permission, four interviewees⁷ requested that the interviews not be recorded. Detailed notes were made during and immediately after the interviews in order to maintain the accuracy of these responses. Utilizing Nvivo as the analysis platform was not restricted to only interview data. Print data such as newspaper articles, contractual documents and company and industry reports were also scanned in text form and imported into the software.

⁷ These four interviewees are highlighted in grey in Table 5.2

Table 5.3 The data analysis process

Data Analysis Stage	Subtask	Details
Categorization	Transcribing/textual conversion	The process of converting audio recordings and other case study data into a common textual platform for analysis. Audio interviews were transcribed verbatim, photos uploaded, contracts and reports scanned into text form.
	Theory linked coding	Organising empirical data into coded themes. These themes were derived from the thesis's a priori theoretical framework.
	Emergent coding	The data drive aspect of the coding process. Themes that emerge from the data that were not informed by the theoretical framework.
	Clustering	Grouping both theory linked and emergent codes into themes. Each theme captures codes that are conceptually linked or share similar dimensions.
Iterative matching	n/a	Establishes the extent that the a priori theoretical framework is consistent with the empirical data. The objective is to determine whether the theory can be used to explain both the emergent and counterintuitive theory linked themes
Theorizing and abstraction	n/a	Focus is placed on unmatched themes and relationships where explanations provided for by extant theory are not consistent with the empirical data Elaborations or modifications to the underlying theories to develop a more robust theoretical perspective

Source: Author

The coding process for this thesis was both theory and data-driven (Welch and Welch, 2015; Gibbs, 2008). Both coding mechanisms are represented in the theory linked coding and emergent theme coding subtasks respectively. The objective of coding remains the same in both cases, that is, organising the data into manageable and meaningful analytical units (Suter, 2011). The difference between the two subtasks is in the manner in which the codes are derived. In the case of theory linked coding, the codes are shaped by the thesis's a priori theoretical framework. This theoretical framework is meant to provide a defined but flexible compass for conducting data collection and analysis. The framework's utility is not limited to crafting interview questions and selecting the case study context. It is also an integral part of data analysis phase, where empirical insights are coded using guidance from the thesis's theoretical framework. It should be noted that I do not position theory linked coding as an exercise in testing the degree to which elements of the theoretical framework

are supported. Likewise, instances where the a priori codes are not represented, or when the case study insight provides counterintuitive are also important. Emphasis is placed on capitalising on the rich detail to understand the deeper nuances of the relationships.

This thesis positions the role of theory as a tool for articulating the core concepts and constructing the initial framework of relationships. It is meant to act as a device for maintaining control over the significant amount of data that is collected (Dubois and Gadde, 2014). At the same time, I am cautious of being blinded from discovering novel insight that may arise from the empirical investigation. The semi-structured approach to interviews was deliberately chosen to facilitate such emergent insight. Consistent with an abductive research approach, the framework is expected to evolve due to changes inspired by the empirical data (Dubois and Gadde, 2002). Recognising and capturing emergent themes are thus important aspects of this evolutionary view to theory elaboration (Fisher and Aguinis, 2017). It is expected that the original framework will be successively modified, credited in part to themes that emerge from confronting reality (Dubois and Gadde, 2014). These themes provide the empirical insight needed to discover and delineate relationships that were not well defined or have been omitted from extant theory.

Determining appropriate theory linked codes is a defined process, in that they are deduced from the thesis's theoretical framework. Distilling the empirical data through the use of emergent codes is less straightforward. These codes are expected to manifest in the form of salient issues that arise from the text itself, and are not influenced by a priori theory (Attride-Stirling, 2001). In this thesis, emergent codes are partially identified based on the recurrent nature of the subject matter, and whether such issues are common across case study data. I use this method cautiously as it assumes that each respondent is knowledgeable about the GVC network in its entirety and is able to provide a complete understanding of the salient

relationships. This is not always the reality, as it is common for many GVC participants to have experience and knowledge that is restricted to their immediate tier - and very little beyond that (Pietrobelli and Saliola, 2008). Seemingly independent issues may share a common underlying relationship and identifying emergent themes based on count significance can minimise the ability to recognise these novel theoretical relationships. To control for this, I also consider emergent codes based on possible analytical significance, and the extent to which they are likely to be logically interrelated to other emergent or theory linked codes. Such analytical significance may or may not be initially correlated to count significance. This approach is especially important in the initial stages of the data collection and analysis. Emergent issues can be identified and the data collection mechanisms adjusted, so as to capture greater insight into these aspects of the case.

Once the text data has been transcribed and coded, it is necessary to cluster the codes into related categories. Clustering is necessary for abstraction and is an important step in identifying relationships among concepts that can be theorised (Bowen, 2009). For example, many of the theory linked and emergent codes were collapsed and partially organised under themes such as (1) longitudinal insight into firm development (2) market structure in which the firm operates (3) value-added creation initiatives (upgrading trajectories) supported by lead firm or otherwise and (4) asymmetry in information across GVC actors (5) bargaining power reflected in firm dependence. These themes were to a large extent consistent with extant theory. In other cases, new themes were created as they were could not readily fit into the theoretical framework that I developed a priori.

It should be noted that even though codes were not readily consistent with the theoretical framework, it does not necessarily imply that the theory itself is silent on such themes. It may be instances where my a priori framework omitted important concepts and relationships that the theory has addressed (van Hoek et al., 2005).

The abductive approach is a pragmatic one and it is likely that the iterative matching stage will capture whether these non-consistent themes are reconciled with current readings of the theory, or whether and to what extent, is elaboration or refinement needed.

5.6.2 Iterative matching

Section 5.6.1 described an important phase of the data analysis process. The categorization phase is needed to navigate and condense the mass of case study data into relevant themes that could then be looked at more closely. It sets the foundation for the iterative process of comparing and moving between theoretical knowledge and insights from the empirical data (Cornelissen et al., 2014). Subsequent to categorization, it is expected that aspects of the empirical data and the theoretical framework may not match up (Dubois and Gadde, 2002). The likelihood of this happening is significant given the purposeful sampling strategy implemented in this thesis. The possibility of uncovering new theoretical dimensions is also probable given the opportunity to tap into multiple sources of empirical insight. Regarding this thesis, the core objective of iterative matching is to (1) establish the extent to which the a priori theoretical framework is consistent with the empirical data (2) determine whether the theory can be used to explain both the emergent and counterintuitive theory linked themes.

As previously explained, this thesis adopts a defined but flexible theoretical framework. It is expected that some of the findings will conform to logic explicated in the framework. It is also likely that some of the themes and their codes embedded will not provide any insight that supports the a priori arguments. The possibility also exists that the empirical data provides insights that run counterintuitive to those that have been explicated in the theoretical framework. In a purely deductive sense, both of these latter circumstances would render the theoretical framework unsupported. The framework would be scrapped and a new one developed from appropriate bodies

of theory and tested with the hopes of better understanding the phenomenon. In the process of iterative matching, however, both these instances are not seen as problems. Rather, they are seen as opportunities to tap into the rich data to understand why this theoretical misfit exists.

The theoretical framework may also act as a constraining factor and received theory may have provided guidance on understanding these emergent themes. As such, the matching process requires the researcher to look beyond the narrow framework that was initially created, and to consider the substantive body of theory (Dubois and Gadde, 2002). For example, the theoretical framework may overlook concepts or relationships that have been well developed in the theory. Without confronting the empirical world, I may have been under-informed of the significance that these concepts in explaining the empirical observations. As such, it would not have been well represented in the theoretical framework, the interview questions or the theory-linked coding. Even so, this oversight does not negate the fact that the overarching body of theory, from which the framework is derived, is still equipped to understand the emergent themes.

At the end of this process of back and forth, it is expected that one of two conclusions will be made. On one hand, the thesis's theoretical framework, and by extension extant theory, precisely matches the empirical data from the case study. The contribution of the study is then relegated to confirming the contextual application of a general theory (Timmermans and Tavory, 2012). On the other hand, even after a recursive process of attempting to make sense of the empirical data through the lens of the focal theoretical framework, there is still data that cannot readily be explained by theory. If the latter conclusion is made, then the empirical data needs to be abstracted and theorised on.

5.6.3 Theorizing and abstraction

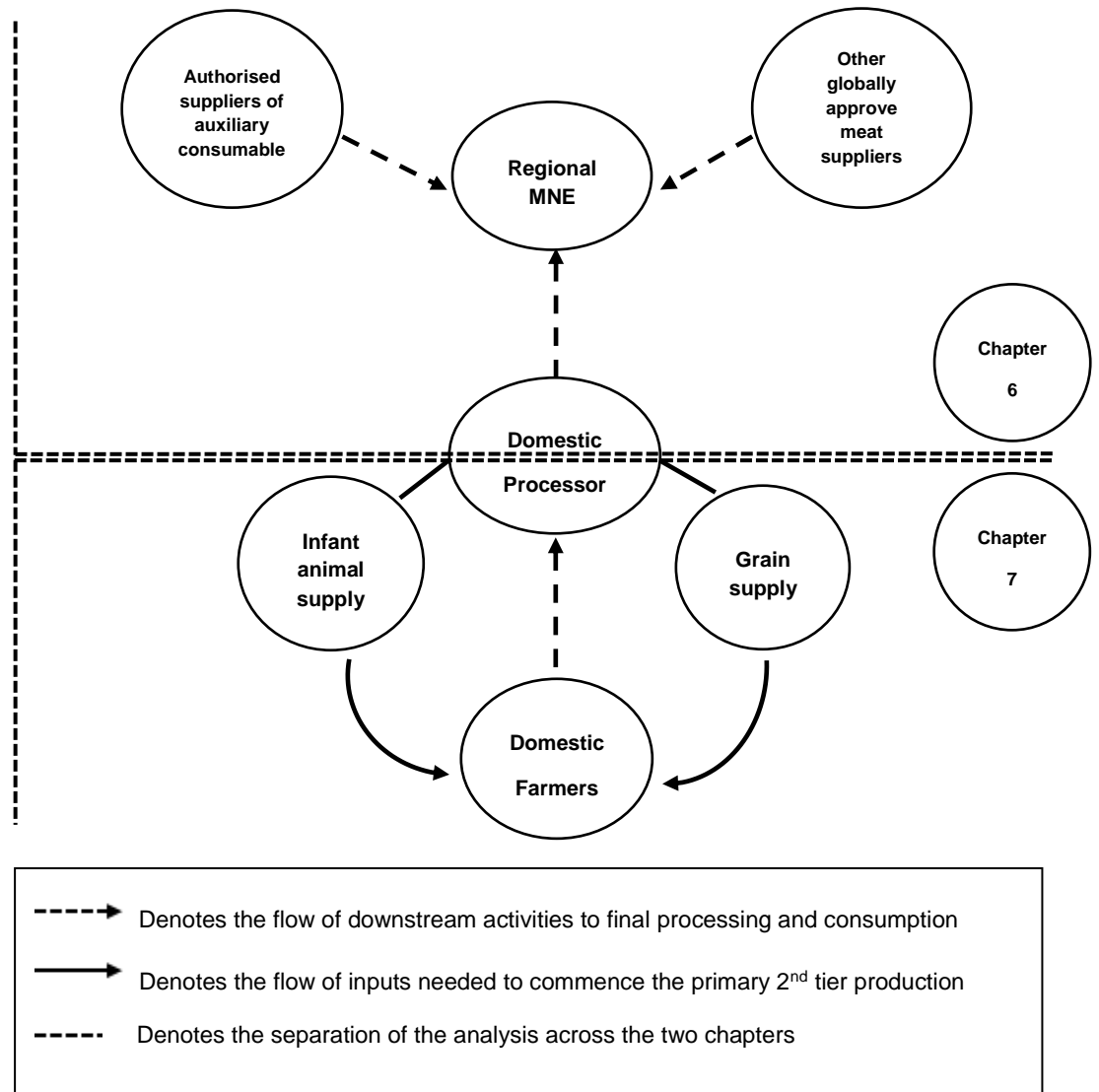
I do not position the theorizing and abstraction phase as a means to create a refined or elaborated *general* theory. Instead, it is positioned as a necessary step in refining the findings of a single anomaly in order to reconsider the manner in which we consider the general theory – pending subsequent testing. This anomaly may manifest itself in changed circumstances, additional dimensions, misguided preconceptions or mis-specified assumptions (Timmermans and Tavory, 2012). The intended theoretical contribution of this tedious abductive process, such as this thesis, is the identification of a singular case where accepted readings of the theory are inadequate to properly explain the phenomenon under investigation.

This theorization process is guided by what could be considered a narrative strategy towards theorization (Langley, 1999). This approach to theorization bridges the dichotomous trade-offs between over-contextualisation and over-generalisability. This is useful when applied to processual data, such as the insight that will be derived from this single embedded case study. On the surface, its insights will offer thick description and a rich contextualised case of GVC participation. If unexplained aspects of the empirical phenomenon are to be of theoretical value, it cannot simply be presented in a descriptive form. This is the main task in the theorizing and abstraction phase of this abductive approach. The descriptive data capturing unexpected findings must be inductively conceptualised and articulated in terms of its relationship with other concepts within the extant theory. In this phase, I am in what might be considered uncharted territory, where the guidance of extant theory is largely absent from the process. Instead, I rely on the logic and coherence of good argumentation, supported by empirical evidence from the case study. The overarching goal of this approach is to end up with a theoretical logic that transcends an idiosyncratic story that offers thin conceptual contributions (Langley, 1999; Golden-Biddle and Locke, 1993).

5.7 Presenting the case study findings

As previously stated, this thesis utilizes data from four levels of the value chain. For three of these levels, primary data was collected and combined with various secondary sources. These levels include the regional-MNE, domestic processor and the domestic farmers. Empirical insight for the global brand owner (4th level) was largely collected from data that was publicly available through secondary sources. Given the complexity of the case context, it is important that the data is presented and analysed in a structured manner. To achieve theoretical efficacy, the data will not be reported in a purely a-theoretical or overly descriptive manner. This is not to discount the value of description and rich insight, as these attributes are important elements of qualitative case study research. However, description must confront existing theory if we are to advance our understanding of any international business phenomenon. The theoretical framework presented in Chapter 4 guides the data collection process. Once the data has been collected, it is necessary to revisit the a priori theoretical framework and substantive theory in general. Inconsistent empirical and descriptive data needs to be discussed, abstracted and ultimately integrated into existing theories. This is how more refined theories are built. For the purpose of this thesis, I will report and discuss the empirical data in two chapters. Figure 5.3 provides an illustration of this presentation.

Figure 5.3 Focus of the empirical chapters



Source: Author

The first empirical chapter (Chapter 6) will focus on the regional-MNE, its role in domestic firm upgrading and the extent to which the domestic firm benefits. Different dimensions of domestic firm benefit will be considered. This chapter focuses on the interactions between the regional-MNE and the domestic processor. Data relevant to the global brand owner is also discussed here. I have isolated the domestic processor as they are the only domestic actor that has direct interaction with the regional-MNE. This provides a context to understand the formal aspect of GVC interactions and the direct effect of MNE led upgrading trajectories on domestic value-added

appropriation. Beyond this, the chapter explicitly investigates the dependence aspect of interfirm relationships. The case study provides an opportunity to take a longitudinal perspective to understand how the upgrading trajectories alter the transactional dimensions of the relationship. This insight can help refine and advance the theoretical value of the a priori framework.

The majority of studies on GVC participation and economic upgrading focus on the firms that have direct interaction with the MNE. This has contributed to the overwhelming number of studies on MNE-1st tier relationships. However, there are other firms involved in the GVC that do not have direct interaction with the MNE. This perspective has been largely absent from studies on economic upgrading. The second empirical chapter (Chapter 7) will shed some light on the impact that GVC participation has on these firms. I have chosen to address these firms separately, as it is difficult to ascertain the effect that the MNE has on its operations. In principle, the MNE does not contract, bargaining or provide direct assistance to these firms. Even so, any pressures or improvements occurring at other tiers of the GVC should manifest itself or have implications at this level.

Chapter 6

The MNE's role in domestic firm upgrading

6.1 Chapter overview

This chapter represents an integral part of the abductive approach to theory refinement. To facilitate the iterative process, the chapter is presented in five distinct sections. In GVC studies, it is typical for the analysis to commence at the point of MNE engagement. In doing so, it ignores important contextual insight that pre-dates the GVC relationship. These insights provide a crucial baseline for understanding the implications of various upgrading trajectories. The initial part of Section 6.2 is used to address this oversight. The section then goes on to mimic prior studies on GVC participation and economic upgrading. It evaluates the extent to which economic upgrading trajectories were pursued by the domestic processor, and the role of the regional-MNE in this process. Analysing case detail allow me to not only determine its presence, but also to gain insight on exactly how the trajectory has altered the domestic firm's operations. The section is intentionally a-theoretical so as to (1) maintain comparability with prior studies on economic upgrading, and (2) emphasize the implicit tendency to align upgrading trajectories to value-added appropriation.

Section 6.3 sheds lights on what was previously argued to be a fundamental assumption in GVC studies on economic upgrading, that is, the symbiotic relationship of value-added creation and its appropriation. Applying the a priori theoretical framework, the case study provides insight on this assumption by demonstrating a paradoxical effect of economic upgrading. While value-added was created, it also weakened the interfirm bargaining and value-added appropriation of the domestic processor. The section goes on to juxtapose these findings against the a priori framework to explain why negative effects on bargaining and value-added appropriation were only unilateral.

As part of the iterative process of abductive research, Section 6.4 engages with elements of the case study insight that were not considered in the a priori framework. Here I focus on the issue of suboptimal contracting and argue that the regional-MNE, for a period of time, engaged in what could be considered a suboptimal relationship. This argument is developed by employing case study insight. The substantive theoretical agenda was revisited to determine the extant rationales for this type of firm behaviour. Once they are presented, I contend that these alternative rationales are ill-equipped to explain the evidence from the case study. This forms the foundation for what I position as a novel theorization of suboptimal contracting. This theorization provides important refinements to TCE and illustrates a dynamic and process-oriented explanation for bargaining power asymmetry in GVCs.

6.2 The pursuit of upgrading from GVC participation

This section provides a descriptive account of the case study and is split into 6.2.1 and 6.2.2. Subsection 6.2.1 focuses on a time period of the domestic firm (the domestic processor in this case) that is frequently overlooked in most GVC studies. It is common for GVC studies to commence investigation from the point of MNE engagement. While this is indeed the focal point of any GVC analysis, it must not be devoid of historical context. This “pre-MNE” phase is important for two reasons. First, it provides a comparative element for understanding the effect that various upgrading trajectories have on the domestic firm’s operations. The second reason is important to the research objectives of this thesis. A proper account of this phase of the domestic-processor’s operations allows for an assessment of its interim dependence before engagement with the regional-MNE. As I have argued in Chapter 4, dependence is a core element of interfirm bargaining, and the ability for contracting parties to appropriate value-added.

Subsection 6.2.2 is presented in a manner that is consistent with prior studies on economic upgrading from GVC participation. As such, it has been intentionally

descriptive and a-theoretical. Navas-Alemán (2011) stated that the GVC literature considers upgrading as the movement into activities that are associated with higher remuneration (better margins) and low replicability of skills (Navas-Alemán, 2011). The empirical insight from this section is in line with this approach of aligning activities deemed to be of higher value-added to that of increased value-added appropriation. 6.2.2 presents insight that is consistent with this approach. Most GVC studies would conclude at this point. Instead, this is the empirical foundation for the chapter. A foundation that provides the insight needed to apply and refine the thesis's a priori theoretical framework.

6.2.1 Domestic processor operations - pre regional-MNE

The domestic processor has been in operation for the past 50 years. The firm has had formal interaction with the regional-MNE for 17 of these years. The other 33 years predates the GVC relationship itself. Even so, it is important to understand this era of the firm operations as it provides a basis to evaluate the particulars of MNE driven development. Interviewee *P1* is a director at the domestic processor, and was the main informant for this aspect of the contextual insight. He has been with the company for over 25 years, having married into the family business. As with many firms from developing countries, the company's start was a humble one. It was initially a small processing shop that dealt only with "alive market" sales. *P1* outlined the firm's initial strategy as follows:

"We would buy the [animals] from [processors 1, 2, 3 or 4] and then redistribute, so we were like a distribution agency that supplied depots and we also owned a few depots ourself.

What we did as well is that we would attempt to re-grow the [animals]. For example, we would buy [animals] on Monday at a weight of 3.8lbs, place them into a holding farm and put them on good grain, water, little bit of extra vitamins and sell a 4.75 lb [anima]l on Friday. This allowed us to increase our margins over a short space of time."

At this early stage, the company would buy animals from the processor before the processing had occurred, usually directly from the processor's farms. The animals were then taken their own holding farms where they would attempt to accelerate the size of the animal in a short space of time (typically a week). These larger animals would then undergo basic processing by the company themselves and sold to the general public for home use. During this time period, the company also acted as a "bulk breaker", where they sold the larger live animals to community processing shops across the country. These community shops were usually too small to deal directly with the larger processor 1, 2, 3 or 4. This arbitrage type business strategy proved to be successful for the company. In the late-1980s an opportunity arose for the company to purchase a grain/feed processing mill that also had a small number of farming facilities. This mill was operated by another domestic firm that had shut down its operations. The investment allowed the company to become more integrated into the domestic meat industry. *P1* mentioned this in the following statement:

"...then [a smaller local processor] was going under, which was a [meat] company out of [the capital city] which was also a fully integrated operation - feed mill etc. We bought that initially and we turned it around and it started to do pretty well."

Leveraging on this investment, the company was able to rear more of its own animals and also supplement the supply of grain/feed to the four main processors. It was via this ad-hoc grain supply that the company was able to make significant inroads into the domestic market. Over time, it forged a close grain supplying relationship with one of the larger domestic processors. A line of credit was offered to the processor, who was unable to repay the accumulated debt. This processor was a family owned business that frequently had internal squabbles that hampered productivity and weakened its profitability. The then small grain supplier was able to negotiate with part of the processor's ownership, where a deal was struck to transfer ownership of the company to the creditor. *P1* was not willing to share the particulars of the deal,

but confirmed that it was a combination of debt forgiveness and a cash payout to the private majority shareholders. This essentially transformed what was once a small bulk-breaker into one of the larger domestic processors for this meat-based product. Insight from respondent *FM1* supported this major turn of events by providing the following details:

“[the domestic processor] was involved in buying [animals] from purchased from the large processor and would either resell in the live market or do some semi-processing himself. They were involved in another feed mill at the time.

[This large processor] began a relationship with them and they started to lend the company money when it faced difficulty. Eventually, the company owed a very large sum of money to them and they made a move to take over the company after acquiring the shares of some of the other family members.”

This takeover occurred in the mid-1990s. During this time, the newly owned domestic processor was involved in three main segments of the domestic market. Its core interest was providing packaged meat to the large local groceries chains. Serving the “alive” market was also core to its business. It was the segment that the new management had the most experience in. Third, the company services the small parlours and convenient shops across the country. These shops usually bought in small but consistent quantity.

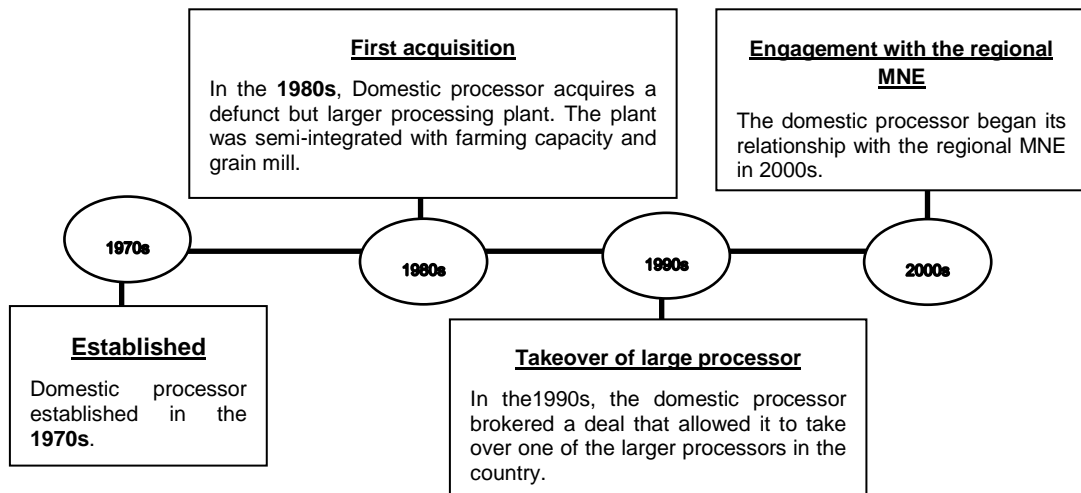
At the time of acquisition, the domestic producer was a significant player, relative to the industry landscape. It was one of the three large players in the domestic market. Even so, its operations were still unsophisticated and manually driven. For instance, the animal was still butchered, cleaned and packaged by hand. Its range of products was confined to two offerings. On the one hand, it would continue to sell to the “alive” market with direct sale to small processors and depots. Otherwise, the live animal would be brought to the processing plant where it would be slaughtered, sanitised

and cleaned in a semi-manual process. The carcass would then be manually cut to standard cuts for distribution to grocery chains and community shops.

I presented similar questions to other industry actors who did not have a similar personal link to the company. Interviewee *IE1* and *FM1* are both independent of the processor. They were active in the industry during these developments and are thus well positioned to either support or contradict the story of *P1*. When I posed similar questions, they both provided details that were largely consistent with the timeline described by *P1*.

This historical timeline is important to understand the context of the case study. I have also provided an illustrative summary of this pre-MNE era in Figure 6.1. The intricacies of this particular context will not be uniform across all domestic firms from developing countries. Each firm will have a different developmental trajectory and not all may permit indigenous growth. Even so, to the best of my knowledge, none of the prior studies sought to provide pre-MNE insight into the domestic firms that they were investigating. This became evident from the literature summary that was conducted in Chapter 4. It is instead conventional for upgrading studies to start its analysis from the point of MNE engagement. As such, the reader either ignores or is left to assume the circumstances of the domestic firm's operations prior to MNE engagement. Integrating details on pre-existence into the analysis allows for a baseline to evaluate the MNE-led upgrading trajectories. Beyond this, it permits an evaluation of the initial dependence relationship and the extent to which coercive bargaining by the MNE is possible.

Figure 6.1 Historical overview of domestic processor: pre-MNE era



Source: Author

6.2.2 Domestic processor operations - post regional-MNE

This section mirrors prior studies on economic upgrading. Focus is placed on determining whether upgrading trajectories were pursued by the domestic processor and extent to which the MNE may have facilitated such. Leveraging on the rich insight of case study approach affords a great level of description and detail. This, in turn, has theoretical value as it provides a mechanism to evaluate the trajectories against the a priori theoretical framework. It sets the foundation for the iterative process of theoretical refinement – consistent elements are matched to the framework and unexplained aspects are theorised. In both instances, rich description is needed.

Once the domestic processor began its relationship with the regional-MNE, various upgrading trajectories became observable. In the remainder of this section, I will make the case, with empirical support, that these firm-level changes conform to the leading notion of MNE-led economic upgrading. These changes will be evaluated against the conventional process, product and functional upgrading trajectories that are common in the GVC research agenda (Navas-Alemán, 2011). These trajectories were presented in Chapter 2 and summarised in Table 2.1.

Process upgrading

Process upgrading is positioned as the most common form of upgrading that occurs from GVC participation (Staritz and Reis, 2013). As it relates to this case study, there is strong evidence for the presence of process-oriented upgrading. P2 worked at the domestic processor for 23 years and was responsible for the production facilities at the firm. During the interview, P2 noted that in 2003, the domestic process was able to acquire a piece of state of the art processing machinery:

“In 2003, we put in the 9 piece cut machine. This machine cuts 90 [animals] a minute. This is how fast it is, so literally in less than a second 1 animal drops out the machine fully cut into 9 pieces. That machine gave us the ability to supply them everything so they now had a meat almost ready to cook.”

Prior to this, the animals were cut manually into the sizes required by the buyer. This was a time-consuming process that frequently resulted in wastage and inconsistent output. The inconsistency was a problem as each cut of the animal needed to be a specific size. This ensured that the meat could be marinated fully and cooked within the franchisor’s specified time. If the meat was cut too large, then the marinade would not fully penetrate, and the meat ran the risk of being undercooked. The opposite happened if the meat cuts were undersized.

This investment conformed to the conventional notion of process upgrading, that is, the ability to transform inputs into outputs more efficiently through technological deepening or reorganised production systems (UNCTAD, 2013; Humphrey and Schmitz, 2002; Schmitz, 1999). Reduced wastage meant that the processor’s input-output ratio improved and its average production cost was reduced. The rate of production was also improved. The older cutting system comprised of a manual cutting station. Workers would stand around the table and manually cut the carcass into the required cuts. The total output per minute was between 45-50 animals per

minute for the entire table. The new system increased the production rate by 45% on average.

The role of the regional-MNE in this upgrading trajectory was also openly acknowledged by P2 in the following response:

"[The regional-MNE] arranged for us to visit other production facilities in the [United] States to observe how their operations were structured and the machinery that was used. Their input was necessary to facilitate these developments. Because obviously, we had to be able to produce to their specifications. For example, we went a production plant in the USA. It was the biggest plant in the US actually and they were able to arrange this by working with the franchisor.

They also provided financial assistance. They gave us funding via a loan to purchase the cutting machine. They paid for the machinery up front and then it was worked out over a period."

P2 noted that there was no interest attached to the loan. From the respondent's comments, it is evident that this process upgrading trajectory was made possible by the resource transfer afforded by the regional MNE. While P2 did not provide an actual cost figure, the respondent alluded that it was not an investment that could otherwise be afforded by the domestic processor at that time. The regional-MNE was also able to employ its network links through the global brand owner to ensure that the domestic processor was well trained and understood how to properly implement the new technology. This was facilitated through foreign site visits and consultancies. The regional-MNE also provided post-setup technical support.

Functional upgrading

Aside from this instance of process upgrading, the case study also provided evidence of functional upgrading. I make this separation by considering process oriented upgrading as trajectories that improved the productivity and input-output efficiency of existing activities. Functional upgrading trajectories occur when new value-adding

functions are performed by the domestic firm (as it relates to a particular product). P3 is a factory floor operator who was responsible for performing one of these newly added functions. He described the following:

"In 2004-2005 we began to do the marinating for the [regional-MNE]. We got some new tumbler marination machines that did around the clock marinating for them."

Being a floor employee, P3 was not able to provide much insight into the strategic process that led to the decision. Even so, the respondent's description was important in highlighting these additional areas of domestic development. P1 supported this insight and noted that in late 2004, the company agreed to perform the marinating services for the regional-MNE. Again, he stated that it required the purchase of special injection and tumbler marinating systems. The function itself was highly technical as it affected the overall taste and favour of the final product. The regional-MNE confirmed this and provided greater context through M1, the manager of supply chain relationships.

"I remember sitting in a meeting with the outlet manager and the team from the [domestic processor]. The outlet manager was saying that sometimes they couldn't marinate the [animals] fast enough at the peak times. So they started to give the domestic processor more and more product to marinate. It got to a point where even the domestic processor could not handle the volume because they had limited resources, in terms of vacuum tumblers."

"Some of the guys from the [domestic processor went] up to the [United] States and saw the injection marinating process and they became very excited and approached us to determine if they would be able to assist them with developing the inject marinade. We said not a problem if the global headquarters gave the go ahead then we can work on it. They put in a machine and we developed the inject marinade for the process."

M2, the assistant to the regional-MNE's supply chain manager, provided further detail regarding some of the operational challenges initially faced with promoting this functional upgrading trajectory.

"The initial marinating setup at the [domestic processor] was not perfect. It took a lot of time to adjust it. We had to call in a specialist company from Costa Rica that the brand owner recommended. They had to adjust the formula to match the required taste. Before it was too strong and the product was too spicy and people did not like it. We eventually got it right though."

In terms of value-added, a functional upgrading trajectory such as marinating activities should affect the contract price of the meat production. Prior to this, the domestic processor was only responsible for the preparing the cuts of meat. The marinating process was still being internalised by the regional-MNE. Transferring these value chain activities to the domestic processor increased the scope of its involvement in the GVC. Beyond this, the domestic process was now performing activities that were more technical in nature, moving it away from the preparation of a narrow raw material. From the interview insight, the marinating process requires precision and a supplier that is able to execute the function with the right concentration of flavour. This blend of herbs and spices is the differentiating element for the regional-MNE. Their value proposition to consumer leverages on this unique but consistent flavour profile. A supplier that is able to provide these added functions is able to charge a higher price for its output – thereby having a positive effect on its value-added (Blažek, 2015).

Product upgrading

During the data collection phase at the domestic processor, I was afforded a tour of the production facilities to witness the production process. During the tour, I observed what appeared to be an isolated section of the factory that had above average hygienic requirements. When I enquired with the guide, the respondent informed me

that it was a new “cook” room that was established at the factory. This was the processors most recent addition, and was implemented during the 2006-2007 period. When questioned more about it, the guide stated that it was an industrial kitchen that prepared cooked meat products for the regional-MNE. In line with prior studies, I classify this as a product upgrading trajectory (Humphrey and Schmitz, 2004). This new facility permitted the domestic processor to work with the regional-MNE to develop and produce new products for outlet sale. This is different from the functional upgrading trajectory that was presented earlier. While new functional areas were also added by way of this initiative (e.g. research and development), these functions were part of a distinctively new product offering.

P4 provided some more context⁸ for this particular firm development:

“In the cook rooms, we make products for the [regional MNE] to sell at their outlets. We handle everything for them, including the preparation of the [meat], the seasoning and the cooking. All they need to do is sell it in their store.”

P1 explained the background of this particular initiative:

“In 2005, the [regional MNE] approached us to work with them to develop a range of items that could be sold in the stores. These were supposed to be special offer products. They would not be year-round products but would be sold at specific periods. They wanted us to do the testing and the development of the product. What was new was that they wanted us to cook it for them and they would just reheat it.”

This was clearly an area that the domestic processor did not have experience in. They were meat processors that provided uncooked meat to buyers that handled final preparation themselves. Producing products that were now fully cooked and ready for consumption was beyond their initial activity scope. *P2* confirmed that they obliged because they were keen to deepen the relationship with the regional-MNE. *M5* was

⁸ Quote is not verbatim as *P4* refused to be recorded

the regional-MNE's point person with the global brand owner. The respondent explained the circumstances around this particular initiative.

"These seasonal products were not based on directive from the global brand owner. They allow each franchisee to adapt certain products or create new ones specific to the market. They were not able to provide us with tried and true products, so we needed to create it. We also did not intend to offer these products year round. Only as specials. Working with the domestic-processor allowed us to get help in developing this."

P2 noted that this initiative also required the domestic processor to invest in other equipment. They were also required to undertake modifications to the production facility in order to maintain proper health, safety and food requirements. The cook area needed to be isolated from the rest of the production facility to ensure that there was no chance of food contamination with raw meat after the products had been cooked. Even so, the trajectory conforms to the existing notion of product upgrading. According to GVC studies, product upgrading is usually captured in (1) introducing new products (2) changing designs (3) improving quality (4) producing a more sophisticated final output (Navas-Alemán, 2011; Humphrey and Schmitz, 2002).

Table 6.1 provides a summary of the various domestic process upgrading trajectories. Details on these firm-level changes are summarised with authority from the literature on the classification of the upgrading. I have also provided the relevant respondents that provided the insights. These identification codes can be referenced to Table 5.2 for more detail on the respondent's position.

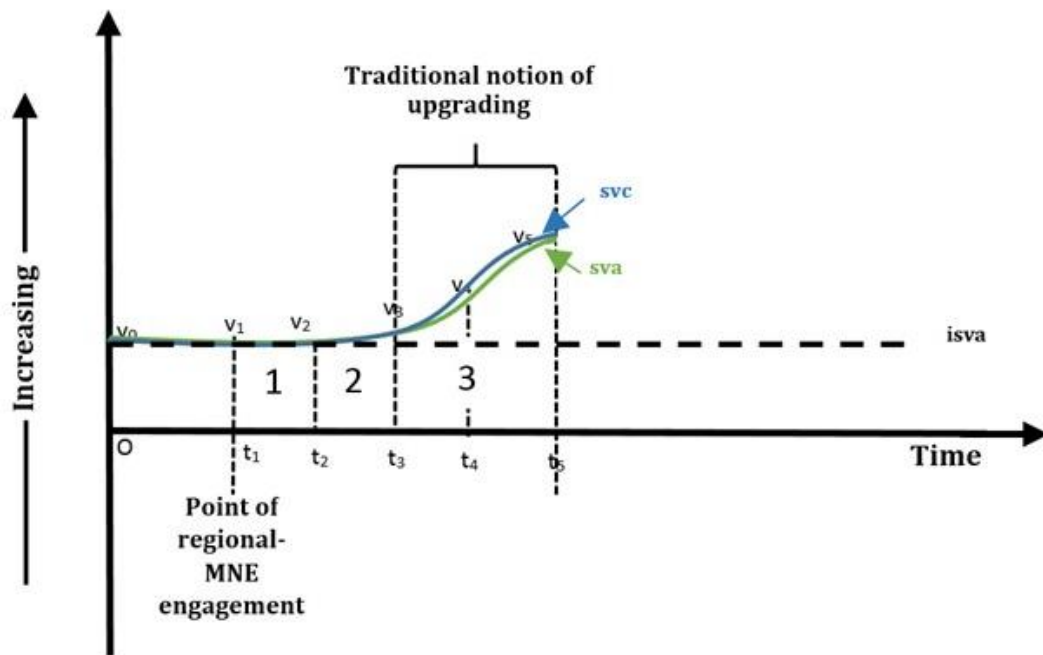
Table 6.1 Processor level upgrading trajectories

Structural firm level change	Details	Type of upgrading trajectories	Respondent providing information
<p><u>Process upgrading</u></p> <p>New machinery and operational techniques</p>	<p>The regional-MNE was instrumental in helping the domestic processor access production machinery to help improve output and efficiency. Facilitated through:</p> <ul style="list-style-type: none"> • Visits to other contracted processors in the United States to receive training, demonstrations and equipment sourcing advice • Interest-free loans provided to facilitate equipment purchase 	<p>Process (UNCTAD, 2013; Humphrey and Schmitz, 2002; Schmitz, 1999)</p>	<p>M1, M2, M3, M5 P1, P2, P7</p>
<p><u>Product upgrading</u></p> <p>Launching new goods</p>	<p>The regional-MNE worked with the domestic processor to launch specific products that were not originally offered by the domestic processor. They assisted in helping them venture into producing cooked food options by facilitating knowledge transfer related to acquiring appropriate equipment, preparation techniques and recipes.</p>	<p>Product (Gereffi, 1999b; UNCTAD, 2013)</p>	<p>M1, M2, M3, P1, P2, P4, P7, P8</p>
<p><u>Functional upgrading</u></p> <p>Performing new functions</p>	<p>Within the processor's core business activity, the regional-MNE assisted knowledge transfer to allow the domestic processor to perform related activities it had not done before.</p>	<p>Functional (Kaplinsky and Morris, 2002)</p>	<p>M1, M2, M3, P1, P2, P4, P7, P8</p>

Source: Author

Figure 6.2 provides a graphical illustration of this mainstream view of economic upgrading (Khan et al., 2015). Not only does it ignore the pre-MNE aspect of the domestic firm (t_0 to t_1), it also emphasizes the surface benefits of the upgrading trajectories. This is largely due to its assumptions around coterminous value-added creation and appropriation. At t_1 , the regional-MNE engages formally with the domestic processor. In this case, shortly after (t_2) various upgrading trajectories are pursued by the domestic-processor. These trajectories are summarised in Table 6.1. During the initial phases of upgrading (t_2 to t_5 in this case) the domestic processor is able to appropriate the majority of the value-added from the upgrading initiatives. This is represented by the close alignment of the supplier value-added creation (svc) and the supplier value-added (sva) curves. I have labelled this as the “traditional notion of upgrading”.

Figure 6.2 The conventional view of upgrading



svc- supplier value-added creation
 sva- supplier value-added appropriation
 isva- initial supplier value-added appropriation
 t_n - various points in time during the interfirm relationship

Source: Author

It is at this point that most GVC studies would terminate the analysis (t_5). The focus of these studies is to determine whether domestic firms have benefitted from resource and knowledge transfer from MNE interaction. A premium is placed on the existence of capital deepening in the domestic firm.

The motive of this description laden presentation was not only to mimic prior studies of economic upgrading. Rather, these insights provide an empirical foundation to abductively apply the a priori framework. In Chapter 4, an argument was mounted to demonstrate the pitfalls of assuming a symbiotic relationship between value-added creation and its appropriation. In the next section, I will leverage on additional case study insight to understand the effect that these upgrading trajectories had on the domestic processor. Emphasis will be placed on changes to (1) the transactional dimensions of the relationship (2) dependence and bargaining power.

6.3 The theoretical matching process

Thus far, I have illustrated two important aspects of the domestic firm's GVC participation. First, I highlighted a traditionally overlooked aspect, that is, pre-existence. Section 6.2.1 demonstrated that the domestic processor had a history that predated its relationship with the regional-MNE. 6.2.2 then described the various firm developments that occurred subsequent to the involvement of the regional-MNE. Detailed insight was provided on the nature of these upgrading trajectories and the role of the regional-MNE in the process. Building on this, Section 6.3 will be separated into 6.3.1 and 6.3.2. Each section will focus on a particular aspect of the a priori theoretical framework.

6.3.1 examines additional case study insight to determine the value-added distribution aspect of the relationship. This explicit consideration around value-added distribution has been lacking in prior studies. The central task is to investigate whether the domestic processor was able to continue appropriating the value-added that was created from these three upgrading trajectories. I evaluate the upgrading trajectories based on its changes to the transactional dimensions that underpin the interfirm relationship (David and Han, 2004; Williamson, 1996). Understanding the changes to these TCE dimensions indicates the extent to which opportunistic inclinations can be pursued.

TCE provides important conceptualisations around core dimensions that determine the cost minimising governance structure. However, one of its fundamental shortcomings lies in the bilateral framing of its analysis. This dyadic framing oversimplifies the extent of dependence that may exist in the relationship (Nooteboom, 1993b). Without explicit considerations around interfirm dependence, a TCE centric framework can produce incomplete theorization around bargaining power and the distribution of value-added. 6.3.2 addresses this by considering the dependence aspect of the a priori theoretical framework.

Together, these two subsections represent the matching phase of the abductive approach to theory refinement. Here, I am not attempting to deductively test the a priori framework. Indeed, the matching process is undertaken to determine the extent to which the framework is consistent with the case study insight. However, is also intended to highlight unexplained elements of the case study, so that theoretical refinement can be facilitated.

6.3.1 The upgrading effect on value-added distribution

In this subsection, emphasis is placed on determining if the domestic firm was able to (1) increase its value-added appropriation and, (2) maintain this position over time. The scope for assessing upgrading was adapted from Gereffi et al. (2001). The two dimensions included increases in: (1) overall profits and (2) price mark-ups. These two dimensions were outlined in Section 2 of Chapter 4.

P1 was asked whether the domestic processor was satisfied with the contractual terms when they first began its relationship with the regional-MNE. The response was as follows:

“At that point, meat prices were not consistent. We found it difficult to plan because we could not predict where the prices would have been. Sometimes we made money, sometimes we made less. It had a lot to do with demand and supply. With [the regional-MNE], we created a relationship that paid by the “head”. We offered a fixed animal size that we sold to them by the head which meant that they paid, say, 20 dollars a head all the time. This was regardless of the fluctuations in the market. These were the contract terms.

The [regional-MNE] was happy with this too because they didn't want to change their prices based on market fluctuations. Overall, this was a good deal.”

When asked about how the initial arrangement compared with its current satisfaction with the relationship. *P1*'s response was as follows:

“Yes, we were happy with the terms of the initial arrangement and for some of the years that followed. But now we are not happy at all. Currently, they will fight us for the last cent if they could. For example, if they hear feed [is] a little cheaper, they come back and demand lower prices. While the contract has become a bit more open now, they are looking to save pennies and cents.

The contract itself doesn't mean anything anymore. For example, they follow the grain market more than us and they understand that because they are 60-70% of our business that if grains drop then we are saving money on our activities or that we can make more money. They do not want us to have this and they do whatever they need to to take it.”

These responses highlight a shift in the level of satisfaction with the arrangement the domestic firm has with the regional-MNE. The dissatisfaction stems from what the domestic processor describes to be an unfavourable distribution of value-added. It is important to note that the unfavourable conditions were not present at initial engagement. P2 noted that this unfavourable arrangement began to manifest around the year 2007 and progressively became worst over the subsequent years. Over the course of a seven-year period, the domestic processor moved from a relationship that it was motivated to enter, into one that they were increasingly dissatisfied with. The source of discontent for the domestic processor was linked to contract volatility and weakened value-added appropriation. First, they were apprehensive about the increased volatility in the contract prices. The relationship went from having fixed one-year terms, conditions and prices - to having no written contract in place. P2 revealed the following:

“When we first started, it was every year that contracts were renegotiated. Currently, they try to renegotiate every month. Because they are looking and playing the market, grain prices change, [infant animal prices] change and they come back to us for lower prices. They only wish to renegotiate when the prices drop though. So we do not have a long-standing contract anymore with them. There is actually nothing written at all. Before we used to have detailed contracts and they were long and comprehensive,

now there are no written contracts in place. We want one, but they do not want to sign anything.”

P2 is outlining a situation where there is currently no contract in place with the regional-MNE - a situation that was not present during the initial periods of engagement. Beyond this, the regional-MNE is seemingly monitoring the input markets of the domestic processor to identify possible surplus that it can bargain for and appropriate. Once these potential gains are identified, it revisits the pricing structure with the domestic processor in a bid to gain lower prices. The regional-MNE did not wish to reveal much information on their negotiation process with the domestic processor. However, the parsimonious detail that they did disclose was consistent with the responses from personnel at the domestic processor. For instance, M3, a contract officer at the regional-MNE, said the following:

“I will be frank with you. We negotiate hard in the interest of the business and its shareholders. You can push your suppliers to reduce cost etc., it is important for us to know this limit.

We monitor the input markets for the animal and feed production. We look at the prices for corn and soya bean and negotiate or re-negotiate based on these fluctuations. We sometimes do this in between prior agreements if the fluctuations are too large to ignore.”

This bargaining pressure on the domestic firm is not restricted to the regional-MNE’s desire to appropriate unforeseen value-added from fluctuations in the input market. Interview insight suggests that this pressure is also applied to value-added that was traditionally captured by the domestic firm. This included value-added that was created by the various upgrading trajectories. Both the domestic processor and the regional-MNE confirmed that the bargaining pressure got so intense for one particular product that the domestic firm could not go any lower without sustaining a significant loss on the production. The regional-MNE was not willing to reduce the pressure

placed on the domestic processor, who was then forced to stop supplying that particular boneless meat product to the regional-MNE.

P5 noted that the relationship escalated to a situation where the operational staff no longer had a pricing schedule to create invoices for the regional-MNE. Every week, they were required to check with one of the directors to verify if any new prices were in effect. The respondent's insight is consistent with *P2's* and *M1's* and illustrates the operational repercussions the asymmetry in bargaining. At this point, the regional-MNE began to intensify bargaining pressure to constantly drive the price downwards. *P1* noted that the negotiation became so hostile and coercive that they were forced to hire a specialist negotiation team:

"Our late CEO and owner built a team around the people who dealt with our major clients. Two of those people is one of our lawyers and the other is our marketing director. So this is the face that [the regional MNE] and our other big clients would see and they would meet with. So we don't just send anybody, these people are professionals and they understand the issues that need to be considered when we negotiate...we have created that in the sense and [the regional MNE] is made to know that we are sending our best person to handle our negotiation.

This wasn't always the case, we used to have regular office staff handling all our accounts. But these were basically paper pushers you know. They were not trained or had experience in negotiating. When [the regional-MNE] started to play hardball, we needed to bring in this special team."

This reactive decision signals the extent of the bargaining pressure that the domestic processor is currently facing. They were forced to hire a specialist team to handle their negotiation in an attempt to attenuate the loss in value-added. Even so, it does not appear to have had a significant effect on the terms of the agreement. At the time of the field data collection, the domestic processor was clear on the poor terms that they were required to accept. This included the increasing volatility of constant price negotiations, without a formal or binding contract in effect. As previously mentioned,

this bargaining pressure was not limited to appropriating value-added from unforeseen fluctuations in input costs. The regional-MNE is also keen to appropriate value-added that was traditionally captured by the domestic processor.

Some of the bargaining pressure was not directly manifested in the appropriation of value-added. For instance, *P5* noted that the regional-MNE has successfully negotiated for an extension of the credit terms of the relationship.

“They used to pay us net 30 days, this was mutually accepted for a long period. Some time ago they told us that they want to pay net 45 days. It was not something that was good for us and our cash flow.”

During the early period of the relationship, the regional MNE had credit terms that were conventional within buyer-supplier contracts of this nature. Full payment within 30 days of the initial invoice was then changed to 45 days of initial invoice – a decision that was not supported by the domestic processor. This does not have a direct effect on the unit value-added or overall profitability of the domestic processor. However, it affects their cash flow and presents added pressure when meeting its short-term obligations.

Hiring a specialist negotiation team had little effect in increasing returns or stabilizing income. In order to buffer its profitability, the domestic processor has been forced to extend the level of risk that it takes. As respondents at the regional-MNE mentioned, they monitor the domestic processor's input markets to determine if commodity prices change. As no formal contract is in place, they use downward shifts in commodity prices as a signal to demand better prices. *P1* stated that in order to maintain profitability, they have been forced to experiment with the futures market for grains.

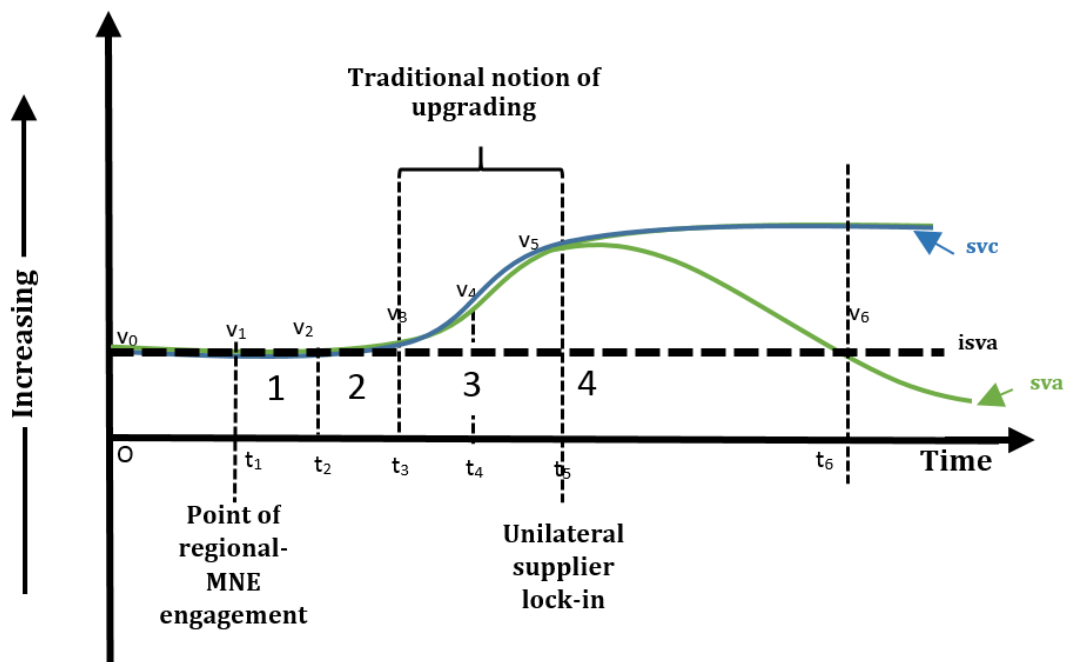
“Well, we have to find some way to save on the inputs. We currently do some futures buying on the grains. So we actually go into the market and try to forward buy so we lock in prices for some of our inputs. We do gamble a little bit but we don't tell

[regional-MNE] about this. They demand adjustments based on what the real-time prices are. We do play the game a little bit to try and make some extra money. So if we believe the market trending down then we gamble a bit and try to make something extra. If we lose then we lose. But given our current returns, it a risk we have to take to survive.”

Figure 6.3⁹ illustrates this aspect of the relationship. This is an extension of Figure 6.2 and captures the longer term effects of the upgrading trajectories. Subsequent to the short period of cordial negotiation, the domestic processor was faced with an intensification of bargaining pressure. This is captured from t_5 onwards. The figure demonstrates a sharp diversion in the value-added that is being created by the domestic processor and the share that it is able to appropriate. I refer to this as the point of supplier lock-in and is represented at time t_5 in Figure 6.3.

⁹ The table's value-added curves are based on relative value-added (compared to its initial value-added appropriation).

Figure 6.3 The paradox of upgrading



svc- supplier value-added creation
 sva- supplier value-added appropriation
 isva- initial supplier value-added appropriation
 t_n - various points in time during the interfirm relationship

Source: Author

Juxtaposing these findings to the metrics presented by Gereffi et al. (2001), it is clear that one of the metrics for economic upgrading has not been satisfied, while the second one is increasingly threatened. The domestic processor is now operating at lower product mark-ups than it did at t_1 . This reduction is more acute when compared to $t_3 - t_5$. These pricing pressures have direct repercussion for the domestic processor's share of value-added in the regional-MNE's final product. Over time, the domestic processor has been offered lower remuneration for its output, despite this output becoming more sophisticated.

Their overall profitability outcome is also under threat should the regional-MNE continue to intensify its bargaining pressure. Testimonials across the firm support the conclusion that *relative sva* has decreased to a level that is now beneath what was

originally received by the domestic processor at t_1 . This is based on unit consideration where the value-added is captured as the difference between the unit cost and the price that the regional-MNE pays for the input. More specifically, the profit margins that the domestic processor now received is at its lowest point. As depicted in Figure 6.3, this return is below the domestic processor's initial *sva* with an even greater disparity from the initial periods of regional-MNE engagement. However, *P5* noted that the overall profitability of the domestic processor is higher than what was originally captured at t_1 . Even so, the respondent contended that this too has faced a sharp decline and at t_6 was marginally higher than the absolute *iva* at t_1 . What is of concern, is how ineffective the domestic processor is in its ability to fend off bargaining pressure from the regional-MNE.

I refer this diversion in *svc* and *sva* as the *paradox of upgrading*. While the trajectories were effective in creating value-added, it also seemingly locked the domestic processor into the relationship. For instance, *P1* saw significant initial benefit from the process upgrading initiative:

"The nine-piece machine was a critical improvement for us. The ability to cut 90 [animals] in 1 minute with precision and no damage was excellent. At one point we had increase productivity and lower wastage."

However, *P1* currently compares the upgrading trajectories to a "ball and chain". For instance, the nine-piece cutting machine is tailored to serve the needs of the regional-MNE. The cuts are specific to their cook process and not something that is widely used anywhere else in the market. Beyond this, the machine's minimum efficient scale is unachievable without the quantity and frequency of the regional-MNE sales account. Even if the domestic processor were to find an alternative use for the machine, they would not be able to find a buyer with enough demand to make it feasible to continue utilizing the machine in production.

Layering the a priori theoretical framework over these insights partially reveals the role of asset specificity in this paradoxical observation. Low redeployability restricts the productive use of the asset in alternative relationships (De Vita et al., 2010). Similar lines of asset specificity can be drawn from the other instances of economic upgrading trajectories. As part of the case study investigation, I was offered a tour of the production facility. I was able to interview the production tour guide (*P7*) on the operational specifics of all the upgrading initiatives that were described by the other respondents. Both the process and functional upgrading trajectories are both tied to the regional-MNE. Redeploying these assets to other buyers or markets would be difficult. For instance, the tumbler and injection marinating equipment have been developed and optimised for the specific marinating blend that is provided by the regional-MNE. This optimisation is also dependent on the meat sizes produced by the cutting machine. The marinating system is designed to work in tandem with the precise meat sizes that the cutting machine is able to produce. As such, its utility is tied to the continued operation of the cutting machine itself – thus intensifying the re-deployability constraint.

Transactional frequency further escalates the domestic processor's negative exposure (Williamson, 2008). The domestic processor noted that the regional-MNE had become its core buyer. *P5* provided a breakdown of their weekly demand and the figures are consistent with this position.

"We currently process on average 250,000 heads of [animal] per week. At least 140,000 to 160,000 heads goes to [the regional-MNE] alone [56-64%]. [A large grocery chain] does another 40,000 heads. the rest of it is shared up with our distributors which sell to various small and medium-sized groceries. Anybody that has a massive demand are dealt with in-house. While we process 250,000 heads, we sell another 60,000-80,000 heads on the alive market."

Low re-deployability and high frequency offer only a partial explanation for the adverse value-added appropriation of the domestic supplier. While manipulation of

the relationship's transactional dimensions is evident, this manipulation on its own cannot explain the asymmetry in the bargaining power. From a TCE-centric perspective, the upgrading trajectories do not create small numbers bargaining for only the domestic processor (Anderson and Gatignon, 1986). The specificity of each upgrading trajectory provides non-substitutability and competitive advantage for the regional-MNE (Crocker and Masten, 1996). For instance, the cutting machine that manifests itself as process upgrading is critical to the regional-MNE's product offering. Its demand is substantial, the equivalent of 160,000 animals per week. Domestically, they are no other processors that can meet this demand requirement without undergoing a similar upgrading trajectory. More importantly, is the need for precise and consistent meat size. Manual or semi-automated cutting typically results in irregularity in the supply of animal pieces. As explained by *M4*, this is crucial for ensuring that the final product is in line with the global brand owner's criteria for quality, taste and safety. The interviewee noted that the equipment at the outlet stores is calibrated to cook each piece meat to a precise temperature of "doneness". If the meat is not of this exact size, then under or overcooking will occur.

The process upgrading trajectory not only allows for a lower unit cost of production with increased efficiency. Beyond this, it ensures that the regional-MNE receives an input that meets its preparation requirements. A similar line of argument can be applied to the functional upgrading trajectory that the domestic processor undertook. The marinating process is a cornerstone of the regional-MNE's product offering. In many of their public advertisements, they boast of the well marinated and fully penetrated flavours that make the product different from its competition. This is an outcome that only the elaborate marinating system at the domestic processor can produce. Other domestic suppliers are not equipped with the machinery or the experience required to ensure this precise flavour profile.

The knowledge transfer from this bilateral relationship has created a situation where both parties *should* be exposed to small numbers bargaining (Blair and Kaserman, 1987). The domestic processor is bounded to the relationship owing to its (1) significant investment in low-redeployable assets and, (2) ballooning size and production output, making it difficult to achieve minimum efficient scale without the regional-MNE's account. Likewise, and as demonstrated above, the regional-MNE is also bounded to the relationship. Given the specialised nature of the product, the input provided by the domestic processor has low substitutability. This creates the bilateral monopoly that is predicted by TCE (Williamson, 1985). In the presence of opportunism, both parties are able to hold up the other as they bargain for a higher share of the value-added. In theory, this collapses into protracted negotiation where no clear consensus can be made regarding price and other contractual specifics (Nootboom, 2000). High transaction cost ensues and the relationship fails to achieve the transaction cost minimising objective. This justifies the theoretical push to an internalised or hierarchical mode of governance (Hill, 1990).

In light of this theoretical perspective, my empirical data offers contradictory insights to the mainstream TCE prediction. Instead of protracted negotiation and bilateral holdup problems, the case study illustrates the opposite. In fact, on the request of the regional-MNE, the relationship has moved away from any system of formal contracting. The regional-MNE can dictate pricing and re-negotiate the terms at will, with little indication of holdup. Subsequent to time period t_6 (Figure 6.3), the regional-MNE incurs little transaction cost in the pursuit of its opportunistic motive to appropriating maximum value-added. On the other hand, the domestic processor is unable to mount any resistance to the demands of the regional-MNE, despite its valiant efforts. The pricing structure is complied with, and the domestic processor has to resort to risk and secretive strategies to create value-added buffers.

6.3.2 Why unilateral supplier lock-in?

In this subsection, I will continue the matching phase of the abductive approach to theory refinement. The theoretical framework presented in Chapter 4 was two prong. TCE insight was combined with dependence based bargaining theory to provide a more complete theoretical rationale. In Section 6.3.1, the evidence suggests that only the domestic processor was under extensive bargaining pressure. This occurred even in light of the predictions of TCE (Nooteboom, 1993b). The widely used GVC typology advanced by Gereffi et al. (2005) predicts a similar increase in interfirm bargaining for the domestic processor. A rise in supplier capabilities through economic upgrading should have shifted the relationship from a captive governance structure into one that is modular. This shift should be accompanied by an increased level of domestic processor bargaining power (Gereffi et al., 2005).

Here lies the shortcoming of a TCE centric approach to theorizing all GVC relationships. The bilateral framing underplays the importance of dependence in determining the extent of bargaining power asymmetry in an interfirm relationship. This became evident when *P1* succinctly summarise the evolution of its relationship with the regional-MNE.

“Back then we would then deliver this whole perfect animal to the store and then they would take it from there. In growing, we added a machine and we started to cut the animal into 9 pieces and supply it to them in that form and they would handle the marinating and prep. Then into the cutting now we started to select the [animal parts] for them also, so we started to sort out the bad pieces from the good ones and take out the pieces that may not be good enough.

It then went a little further, we were now certified by the franchisor to become an approved supplier. This came with certain standard requirements, production procedures and quality assurance. This helped us by increasing our own standards. So now we are approved to supply meat to other franchise branches around the globe should they contact us [emphasis added]. We then

moved into doing their marinating for them, we brought in some machinery to do this as well. We also do different types of packaging for them depending on the type of product we are supplying.”

Being an “approved supplier” suggests that there may be a more extensive network of regional-MNE relationships outside the one under investigation. Respondents at the domestic processor were acutely aware of this. *P1* noted that it was common for supply chain employees at the regional-MNE to introduce the possibility of sourcing elsewhere when the domestic processor was not quick to accept new terms. This threat became a reality when the regional-MNE began to work with another regional processor for a specific boneless meat product. *P2* stated the following:

“We used to supply all of [the regional-MNE] needs in terms of their other products as well. Now we are only 100% bone in [meat] but at one time we were supplying all the raw material for products [...]. But they would always want lower prices and would be fighting down the bottom line figure. It came to a point where we could not meet their price demands so they went to their import market instead. Because I mean at one point in some boneless products we were only making 50 cents and they want to fight us for 45 cents of it. So it comes to a point where we just could not go any lower.”

This move by the regional-MNE represented a stark reminder to the domestic processor that they are replaceable. Even so, the domestic processor appeared to have acquired limited knowledge of the regional-MNE’s GVC network – other than alternatives exists. For instance, they referred to the import market in a generic term without being able to provide specifics of the regional-MNE’s global sourcing strategy. None the less, this provided detail which was used to garner deeper insights from the regional-MNE. In an interview with *M5*, I asked if it was possible to explain the company’s global sourcing network and the system that it had in place for procurement. This respondent confirmed that the global brand over provides a very extensive supply network that every franchisee can access. This network is two prong. One aspect of supply deals with the standardised consumables, packaging and

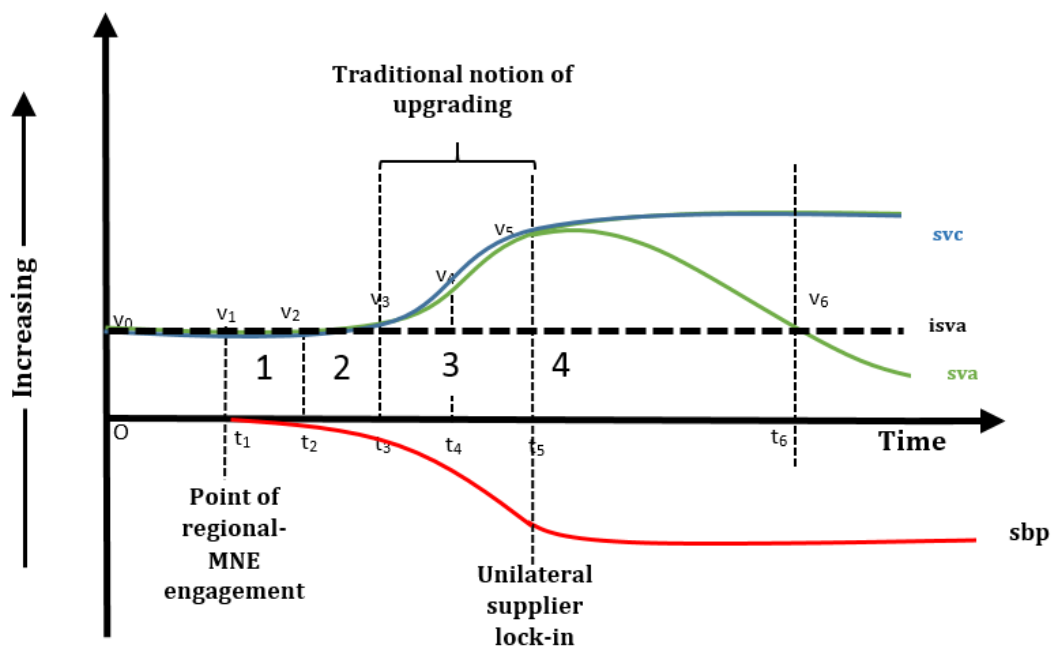
condiments. The global brand owner has negotiated a long-term arrangement with one of the USA's biggest restaurant suppliers. This company works with the regional-MNE to provide the auxiliary inputs that are needed for cooking, preparation and sale. The network is closely orchestrated for the core meat input that the franchisees need. This network of relationships is managed internally by the global brand owner. Each franchisee may create domestic relationships for core input but they must adhere to the global brand owner's standards. As suppliers become accredited, they are then added to a global database of suppliers that can be leveraged on by any franchisee that requires such input:

“The global brand owner has a [supply chain support department] and they would provide support if we discuss sourcing a product or selecting a new supplier out of the USA or otherwise. They would also lend support in via certain supply chain management programs. For example, they have something called the spend-smarter program. This was a two-day workshop, they not only look at pricing but it looks at innovative ways of doing things differently, they teach you ways to think outside the box. It is highly unlikely that we would go to any sort of consultancy firm to help us negotiate or develop strategies.”

The domestic processor is but one of many “upgraded” suppliers capable of providing the inputs needed for the regional-MNE to carry out its operations. Even if the regional-MNE did not cultivate the relationships themselves, the global brand owner is able to make these suppliers available to them. This creates the conditions necessary for unilateral lock-in. A situation that is consistent with the dependence based bargaining element of the a priori theoretical framework. This franchisor orchestrated supplier network renders the two balancing operations ineffective. The economic upgrading trajectories while successful in creating additional value-added, have not created the interfirm dependence relationship to permit the domestic processor increased value-added appropriation. In fact, the upgrading trajectories themselves have acted as the impetus for unilateral lock-in.

Figure 6.4¹⁰ introduces a supplier bargaining position (*spb*) to illustrate this aspect of the argument. Given the extensive nature of the regional-MNE's supplier network, the upgrading trajectories that occurred from t_3 to t_5 have created a unilateral case of small numbers bargaining. This is captured by the sharp decline in *spb* that mirrors the rise in value-added creation from the investment in specific assets. The point of unilateral lock-in occurs at the point where the supplier bargaining position is at its lowest.

Figure 6.4 Interfirm dependence and asymmetric value-added appropriation



svc- supplier value-added creation
 sva- supplier value-added appropriation
 isva- initial supplier value-added appropriation
 sbp- supplier bargaining position
 t_n - various points in time during the interfirm relationship

Source: Author

This deterioration of domestic processor bargaining power is reflective of the violation of the two core aspects of balancing outlined in Chapter 4. Emerson (1962) first

¹⁰ The table's value-added curves are based on relative value-added (compared to its initial value-added appropriation).

aspect of balancing addresses the rarity of the value chain activity, post-upgrade trajectory (Wernerfelt, 1984). The upgrading trajectory must alter the interfirm relationship so that it becomes difficult for the regional-MNE to source similar inputs from entities outside the relationship (Pfeffer, 1981). Bilaterally, it may appear that this has successfully “unbalanced” the relationship in the domestic-processors favour and should have allowed the domestic processor increased interfirm bargaining – or at a minimum move it into a state of bilateral dependence. However, deeper contextualisation of the GVC illustrates that the regional-MNE, through global support, is able to tap into other suppliers. This dampens the effect of rarity for *only* the regional-MNE. Even so, the product still remains relatively rare, in that the domestic processor is unable to find another buyer that is able to be substituted for the regional-MNE.

The second aspect of balancing emerges when the upgrading trajectory permits the domestic firm to cultivate and sell its outputs to alternative sources. This allows for an extension of the power network and dampens the domestic firm’s dependence relationship with the regional-MNE (Crook and Combs, 2007). This can be facilitated when the upgrading trajectory allows for the upgraded activity to be redeployed across multiple value chain relationships (global or domestic). As the previous sections have illustrated, the specificity and frequency dimensions of the interfirm relationship have been altered. This increase in specificity was a product of the MNE-led upgrading trajectories themselves. This effectively altered the domestic firm’s operations in a manner that dampened its ability to serve alternative markets.

Combining TCE with deeper consideration around interfirm dependence has demonstrated that non-equity arrangements can persist with a combination of transactional dimensions that would otherwise suggest internalization. These relationships can also allow the dominant party to appropriate the majority of the value-added without being exposed to protracted negotiation and hold up.

6.4 Theoretical refinement

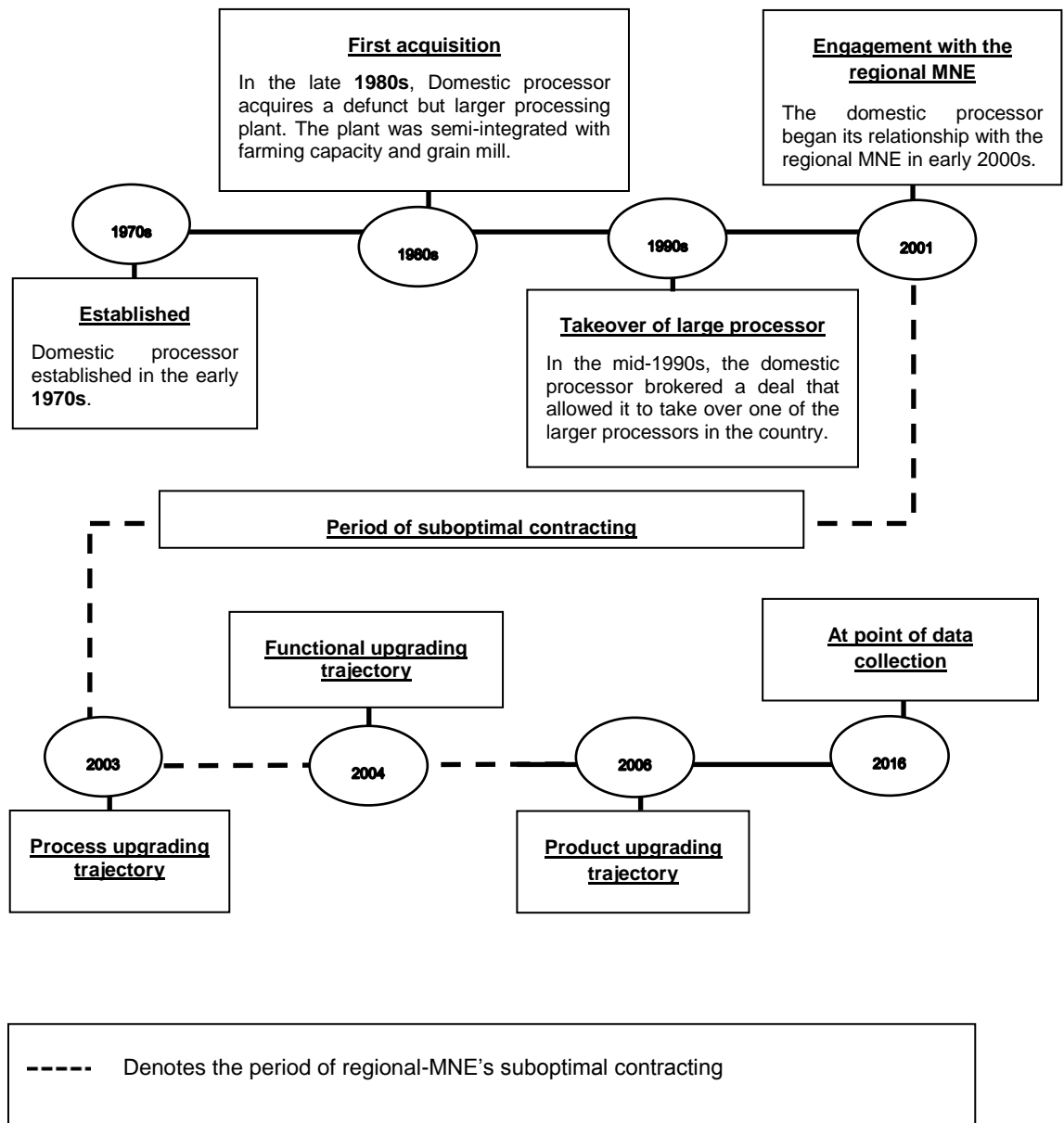
An abductive approach is fruitful if it is the researcher's objective is to discover new things (Dubois and Gadde, 2002). Section 6.3 engaged in the matching phase of the abductive process. While the a priori theoretical framework fits the case study well, it was not equipped to fully understand the two theoretical anomalies online in Chapter 4. I identified these anomalies as (1) the conflict between MNE-led upgrading and optimal interfirm contracting, and (2) the static nature of assuming asymmetry in bargaining.

In the following three subsections, I will work towards theorizing the residual case study insight to help resolve these anomalies. 6.4.1 illustrates that for a distinct period in the GVC relationship, the regional-MNE engaged in what amounts to a suboptimal relationship. I define this notion of suboptimality and provide empirical insight to support this argument. Having specified the dimensions of this instance of suboptimality, I use 6.4.2 to revisit the substantive body of theory for an explanation. Four alternative explanations are considered. Even after considering these extant theorizations, I contend that these anomalies remain unresolved. Building on 6.4.1 and 6.4.2, subsection 6.4.3 advances what I position as a novel theoretical rationale for suboptimal contracting.

6.4.1 Relationship dynamics: an account of inefficient contracting

I identify this period of suboptimal engagement as: subsequent to (t_1) and prior (t_5) (Figure 6.4). In terms of the case study context, the period captures detail from years 2001 to approximately 2005. This covers the regional-MNE's initial engagement with the domestic processor and terminates just before the product upgrading trajectory was undertaken by the domestic processor. Data from various respondents suggest that during this time, the regional-MNE engaged in what could be considered an inefficient and suboptimal relationship with the domestic processor. Figure 6.5 maps the entire development path of the domestic processor. I have highlighted this period of suboptimal contracting by use of the broken line.

Figure 6.5 Historical overview of domestic processor: post MNE era



Source: Author

This notion of suboptimal engagement is based on two dimensions. The first aspect is ingrained in a TCE logic and is represented in its core *transaction* cost efficiency seeking assumption. Engaging in a governance mode or specific relationship that does not yield the lowest transaction cost is seen as suboptimal. These costs conform to the widespread assumption of TCE and are captured in the cost of searching for potential partners in addition to the costs related to negotiating with, and monitoring

the chosen partner's performance (Brouthers, 2002). Beyond this, I explicitly include an aspect of TCE that is often ignored or assumed to be homogeneous across governance modes, that is, production-related costs (Demsetz, 1988). The market rarely offers a homogeneous group of suppliers with identical production functions. Suppliers are heterogeneous in their technical capabilities and thus provides the buyer with inputs that vary in quality and unit production cost. The decision is not merely to "make or buy". A decision to externalize requires deeper consideration around the choice of an appropriate contracting partner. For the purpose of this thesis, I consider a suboptimal engagement to be an interfirm relationship that fails to minimise or economize upon both the *transaction* and *production* related costs (Walker and Kwong Wing, 1999; John and Weitz, 1988). Using this definition of suboptimal engagement and a qualitative assessment of the case study evidence, I argue that the regional-MNE for period identified above, engaged in what can be considered suboptimal contracting.

I will focus first on the transaction cost related to (1) the knowledge transfer process, and (2) monitoring and policing the exchange. In Chapter 4, I argued that the transfer of knowledge and resources in form of economic upgrading trajectories are not costless initiatives for the MNE (Giroud et al., 2012). Teece (1977) argued that it is common for studies to assume that transferring knowledge to other firms is costless. Insight from the case study, some of which have been presented in Section 6.2.1, illustrates that the knowledge transfer process was not costless for the regional-MNE. Most noticeable is the commitment of financial resources to facilitate the process upgrading trajectory at the domestic processor. The loan was interest-free and diverted capital away from other investments that *may* have had a higher return at that point in time. Aside from the opportunity cost of the loan itself, the regional-MNE was required to draft a contract, outline the specifics and police repayment over the stipulated period of time. Both of which attracts a non-trivial level of transaction costs.

Even before an agreement for the process upgrading was struck, the regional-MNE had to organise multiple site visits to other production plants for various personnel at the domestic-processor. Once the machinery was procured, the regional-MNE, with the global brand owner's support, arranged for installation, training and initial maintenance of the machine. Once production commences the regional-MNE also incurred debugging cost associated with domestic processor learning and manifested in incorrect specifications and other production errors. Teece (1977) referred to these costs as pre-start-up training and excess manufacturing costs. These debugging costs were also present in the marinating system that the domestic processor adopted (functional upgrading trajectory). This was captured in M2's earlier insight:

"The initial marinating setup at the domestic processor was not perfect. It took a lot of time to adjust it. We had to call in a specialist company from Costa Rica that the brand owner recommended. They had to adjust the formula to match the required taste. Before it was too strong and the product was too spicy and people did not like it. We eventually got it right though."

The functional upgrading trajectory and the knowledge transferred by way of it was not seamless. As M2 explains, the process had hiccups that required the regional-MNE to incur debugging cost associated with incorrect specifications and other production errors (Teece, 1977). Assuming that the actual cost associated with wastage was borne by the domestic processor, the regional-MNE was still burdened with product inconsistencies that made its way to market. This burden manifested itself in increased levels of consumer dissatisfaction.

The above insights were focused on the transaction cost related to the transfer of resources and knowledge to the domestic processor. There is also evidence that during the initial periods of the relationship, the regional-MNE was required to police and monitor the operations of the domestic processor. These transaction costs were not related to the knowledge transfer process itself. Instead, the monitoring process necessary to ensure that the domestic processor was not knowingly cheating or

providing raw material that was not of the agreed quality. P8 provided the following response in support of this conclusion:

“For many years, [the regional-MNE] had a unit of four to five people that would be full time at the company. They were very active and would monitor the production process and quality assurance to make sure that everything was done to the agreement we had with them. They checked the orders to make sure that nothing was short or held back. They were here every day, it was almost like they were full-time employees with us.”

From a production cost perspective, this initial phase of the relationship also suggests sub-optimality. The various upgrading trajectories did not merely serve to standardise the operations at the domestic processor. Instead, each upgrading trajectory brought with it productivity gains through capital deepening. Section 6.2.1 went in depth into these value-added gains that accompanied each of the trajectories. These gains were not present at t_1 or the immediate years that followed. In fact, they only commenced at t_3 . Deducing from Figure 6.4, the domestic processor was only able to achieve its minimum efficient scale and maximum value-added creation at t_5 . The period of engagement that preceded t_5 required the regional-MNE to engage in a relationship that did not offer the production cost minimising option.

Also related to contract pricing. Respondents at the domestic processor noted that the initial terms offered by the regional-MNE were generous and beyond what they were already receiving through existing supply markets. Among these favourable terms were (1) above market “per head”¹¹ prices (2) prompt net 30 credit payments, and (3) fixed one-year contract terms and prices. Specific to this initial period of engagement, the data suggests that even within the domestic market, the regional-MNE may have been able to attain better “per head” prices.

¹¹ Per head is industry jargon that represents per animal or per pound prices

In combination, these insights build a strong argument for suboptimal contracting. The relationship with the domestic processor, at least for this period, did not represent the optimal engagement for the regional-MNE. To give this argument weight, it requires an alternative relationship for which to compare. This is owing to the static, comparative-efficiency underpinnings that are typical of TCE (Roberts and Greenwood, 1997). This alternative relationship is captured in the global brand owners “approved supplier” list. In order to be considered an “approved supplier”, these alternative processors would have to undergo similar upgrading trajectories. In doing so, they already benefited from similar knowledge and resource transfer initiatives, albeit from another franchisee with global brand support. The costs associated with this period of transacting could have thus been avoidable.

Having presented the specifics of this case of suboptimal engagement, it is necessary to revisit the substantive body of theory. This is consistent with abductive research and the iterative approach to theory refining. The a priori framework was unable to provide a proper theorization, in part due to an incomplete understanding of the phenomenon itself. Engaging with the empirical data has assisted by providing greater context.

6.4.2 Extant arguments for suboptimal contracting

The notion of suboptimal contracting is not in itself a novel observation. Reverting to the substantive body of theory reveals specific arguments regarding a firm’s decision to enter into a relationship that may be considered inefficient. In this section, I will present four competing arguments for the engagement of suboptimal contracting. I will then argue that these extant arguments are incompatible with the findings of this case study.

The first argument supporting the existence of suboptimal contracting is that of regulatory restrictions by the host country governments. Host countries may institute trade restrictions that are meant to promote certain types of foreign market entry by

MNEs. This may be done to maintain domestic control of the activity or to increase the likelihood of knowledge transfer to domestic actors (Griffith et al., 2001). Chinese regulations in the 1990s are frequently cited as an example of such suboptimal engagement. More specifically, early Chinese FDI policy prohibited the formation of wholly foreign-owned enterprises and favoured international joint ventures (IJVs) (Pajunen and Fang, 2013). The automotive industry in China was once a prime example of regulatory-induced suboptimal contracting (Sun et al., 2010). This is not to say that all MNEs are coerced into IJVs or modes of governance other than wholly owned subsidiaries. It is also possible that for many arrangements, an IJV is the most appropriate governance structure (Lee et al., 1998). However, there is a strong argument within the literature to suggest that host government ownership restrictions can box the MNE into less optimal relationships, even when transaction cost analysis would predict otherwise (Gomes-Casseres, 1990).

Local content regulation can act as a similar regulatory restriction on how an MNE may orchestrate its value chain. Conventional local content laws dictate that firms producing a good or service within a country must procure a certain proportion of intermediate inputs domestically (Belderbos and Sleuwaegen, 1997). Such regulations do not restrict the MNE's mode of entry, but instead, limit the extent of its intermediary linkages. Global relationships cultivated outside the host country cannot be leveraged on by the MNE. Under these circumstances, the MNE is obligated to engage with domestic firms that may be suboptimal. This sub-optimality may be manifest itself in both high levels of transaction and/or production related costs (Walker and Kwong Wing, 1999). Even so, the MNE may still wish to operate within the domestic market. For instance, the market may be of strategic importance for long-term growth potential (Agarwal and Ramaswami, 1992).

Another argument for suboptimal contracting lies in the assumption that every domestic asset can be freely purchased or acquired. Country-specific assets (CSAs)

are seen as an integral element of foreign market entry and subsequent operations (Dunning, 2000; Rugman and Verbeke, 1998). Hennart (2009) posited that prior studies were “MNE centric”, in that they overlook the role of domestic owners of these complementary local assets (Hennart, 2009). These complementary assets may not be freely acquirable by the MNE. The MNE’s objective of exploiting FSAs across markets is thus constrained by the access to local complementary assets. The local asset owners may not be willing to forgo ownership, thus restricting the governance modes available to the MNE. As such, a decision by the MNE to engage in a non-equity or arm’s length arrangement with a domestic firm should not be taken as a manifestation of the MNE’s assessment of efficient contracting. Instead, it may actually indicate the domestic firm’s unwillingness to relinquish control of the asset to the MNE. In such instances, the transactional dimensions of the activity may be indicative of a hierarchal governance mode. However, this ownership constraint may relegate the MNE to a less efficient governance structure.

Argyres and Liebeskind (1999) coined the term governance inseparability. The authors argue that TCE focuses on cost minimizing analysis of isolated transactions to determine the scope of the firm (Argyres and Liebeskind, 1999). However, the governance of a new activity may be linked with or influenced by another transaction that is already under engagement (Argyres and Liebeskind, 2002). This is largely a path dependence argument that has been adapted to TCE (Foss and Klein, 2005). Its applicability is stressed by the static and activity isolated approach that is typical of TCE.

Governance inseparability may manifest itself in two way. First, it may prohibit a switch in governance modes for a given transaction, even when changes in the transactional dimensions dictate such an adjustment. The case of Coca-Cola and its franchisees illustrated this aspect of inseparability. In the 1980s, the company decided to forward integrate into markets where it had earlier entered into franchising

agreements with other entities. These franchisees had territorial jurisdiction over the bottling and sale of the product. In order to switch governance modes, Coca-Cola was required to buy out the franchisees on the open market. In some cases (1) they were unable to broker an acquisition deal, or (2) the cost of the acquisition was unfeasible (Argyres and Liebeskind, 1999). Eden and Molot (2002) applied this aspect of governance inseparability to the negotiations occurring between MNEs and host country governments. They propose that latecomer firms may be faced with less favourable deals than those attained by first movers. This was predicated on the argument that governance inseparability would “constrain the host government’s ability to negotiate new contracts with the latecomers” (Eden and Molot, 2002),

The second manifestation of governance inseparability restricts the firm’s governance modes for new transactions. In this scenario, the firm may be forced to use an existing governance mode for a fresh transaction – even when TCE would dictate that another mode would result in more efficient governance (Eden et al., 2004). Argyres and Liebeskind (1999) use failed internal new venture initiatives as an example. The authors argue that existing arrangements between corporate management and established divisions may affect the conditions offered to new internal ventures. Differential treatment within the organisation (e.g. incentives) can give rise to interdivisional conflicts that undermines the stability of the entire organisation. Such potential repercussions may make it difficult for the firm to internalize new venture activities, thereby forcing the firm to acquire these new activities in the open market.

Lastly, institutional factors are frequently posited as drivers of suboptimal contracting. Of all three competing arguments, the institutional perspective has garnered the most support. For instance, Roberts and Greenwood (1997) advanced what they argued to be the constrained-efficiency framework. The authors argue that TCE adopts what can be considered a comparative efficiency framework for choosing ideal

relationships. In doing so they contend that the theory “implicitly assume that institutional influences play no part in determining which organizational designs are adopted” (Roberts and Greenwood, 1997). Martinez and Dacin (1999) argue that TCE transaction cost minimising assumption is predicated on a purely economic rationale. In doing so, the authors claim that this approach underplays the influence and constraints that social construction imposes on this economic rationale (Martinez and Dacin, 1999). TCE may produce an under the socialised view of contracting and interfirm engagement (Granovetter, 1985). Organisations may be pressured to conform to certain institutional norms which can lead to inefficient organisational decisions and structures (DiMaggio and Powell, 1983). Many of these pressures may be coercive and arise from societal expectations (Martinez and Dacin, 1999). For instance, an MNE may be pressured to conform to societal expectations of significant local sourcing. Such coercive isomorphism may result in the MNE engaging with domestic suppliers to appease the desires of the wider society (Mizruchi and Fein, 1999). These domestic relationships need not be efficient, but are required for the MNE to successfully operate.

These societal norms may not always manifest itself in a coercive manner. For instance, trust within a given context is usually positioned as a transaction cost dampener. As previously argued, transactions with significant levels of asset specificity would be conventionally assigned to a hierarchal or internalised mode of governance (Ouchi, 1980). Chiles and McMackin (1996) contend that in the presence of trust, these activities may be assigned to a hybrid or inter-firm governance structure. In this sense, trust relaxes the behavioural assumption of opportunism. Hypothetically, the potential for hold-up and protracted negotiation is still present. However, each party to the contract can trust that the other will not succumb to opportunistic behaviour, even in the face of short-term incentives (Chiles and McMackin, 1996). Inzerilli (1990) observed this in interfirm arrangements in Northern Italy. These relationships occurred predominantly among small, family-run

businesses. In this context, relationships were steeped in “trust-based social exchanges, involving diffuse, informal, non-contractual obligations” (Inzerilli, 1990). This resulted in governance modes being observed that were counterintuitive to TCE predictions. So much so, that relationships primed for opportunistic behaviour, existed without formal contracts.

6.4.3 A novel argument for suboptimal contracting

The alternative explanations presented in section 6.4.2 share a commonality. They are positioned as constraints on the firm’s governance options. In other words, the firm adopts the next best alternative because the ideal arrangement is not possible. For instance, government regulatory restrictions result in the MNE adopting a less than efficient structure due to bureaucratic boundaries on the scope of the MNE’s domestic activity. Both manifestations of governance inseparability have the same effect on governance choice. The inability to easily (1) switch the organisation of existing activities, or (2) choose the mode of new activities, are both based on this constraint logic. Lastly, as the phrases connote, osmophoric pressures and a constrained-efficiency framework are both positioned as burdens on the operational scope of the firm. These institutional dimensions can force the MNE into adopting suboptimal relationships in order to satisfy contextual conformity.

The coercive lineage of these arguments is clear. However, the insights from the case study do not suggest that such pressures were present in the regional-MNE’s engagement with the domestic firm. For instance, the host country does not have any local content laws or regulations that would mandate the regional-MNE to engage with a domestic firm. Consulting host country trade regulation confirmed this. *M1* also noted that much of the consumables for the franchise are imported. This mass importation of auxiliary consumables further negates the existence of institutional or socially driven pressure for domestic non-equity relationships.

An argument for governance inseparability is also inadequate. For a moment, let us assume that the regional-MNE had path dependent constraints that prohibit internalization. As such, the regional-MNE is restricted to externalisation when TCE predicts that internalisation is the transaction cost minimising mode for this activity. Even if a non-equity engagement was forced upon the regional-MNE, it still does not explain the choice of supplier. As the case study insight reveals, at t_1 , the regional-MNE had at its disposal a list of “authorised” processors. These processors would have, in many cases, already undergone the upgrading trajectories and thus able to offer a needed input at a lower cost to the regional-MNE. The premise of upgrading and its accompanying productivity gains is counterintuitive to the decision of choosing an underdeveloped domestic processor over alternative “authorised” suppliers. More specifically, at time t_1 in Figure 6.6, the domestic processor was not the most optimal choice. Yet it was the option that the regional-MNE *opted* to select.

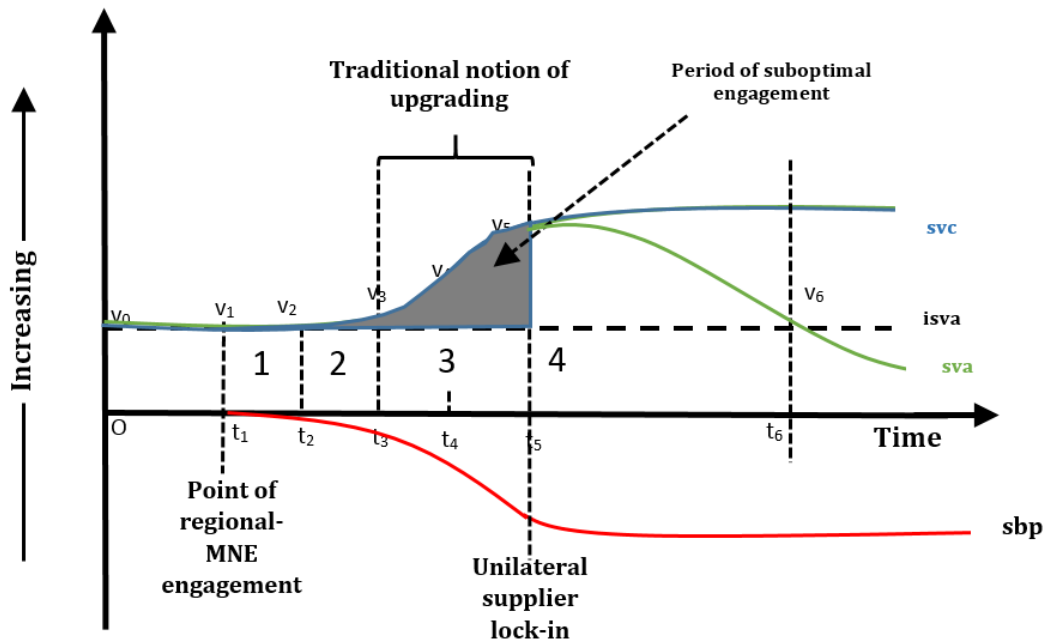
There is one caveat to this constraint approach to interfirm governance. I acknowledge that the institutional argument regarding the transaction cost damping effect of interfirm trust does not conform to this coercive lineage. Instead, it is an intentional and mutually agreed decision by both contracting parties. One may be tempted to assume that in the later time periods (beyond t_5), that this trust element is present in the GVC relationship (Chiles and McMackin, 1996). For instance, the relationship moved from one with a formal contract to a state where no formal contract was in place. This occurred even in light of increasing levels of asset specificity – an indicator of a higher probability of hold-up (Williamson, 1975). Even so, I maintain that it also does not satisfy the deeper evidence emanating from the case study. Interview insight suggested a relationship where the domestic processor is pressured continuously to offer better terms whenever it suits the regional-MNE. Respondents at the domestic processor went as far as to explicitly state that they prefer a formalised contract but the regional-MNE refuses to agree. As it relates to

this case study, it is actually dangerous to assume that the absence of a formal contract is an indication of bilateral trust.

In light of these inadequacies, I advance the argument that the period of suboptimal engagement was a strategic decision by the regional-MNE. In the absence of such a period, the regional-MNE would not be able to enjoy the favourable bargaining position observed during the later periods of the interfirm relationship. Reintroducing Figure 6.6¹², I define this period of suboptimal engagement as t_1 to t_5 and have highlighted it in grey. A dynamic perspective of the GVC relationship is needed to capture this argument. More specifically, this period of inefficient contracting was required to create the relationship conditions to foster asymmetry in bargaining power and the distribution of long-term value-added. This period promoted three specific adjustments to the GVC relationship: (1) a position of monopsony (2) domestic processor upgrading trajectories in the form of specific assets, and (3) unilateral lock-in. I will illustrate this using case study insight.

¹² The table's value-added curves are based on relative value-added (compared to its initial value-added appropriation).

Figure 6.6 Intermfirm dependence and asymmetric value-added appropriation



svc- supplier value-added creation
 sva- supplier value-added appropriation
 isva- initial supplier value-added appropriation
 sbp- supplier bargaining position
 t_n - various points in time during the interfirm relationship

Source: Author

The relationship between the regional-MNE and the domestic processor commenced at t_1 . I denote this as the point of lead firm engagement. At this point, it is reasonable to posit that the regional-MNE did not benefit from asymmetry in bargaining power. I assume this given that historical account of the domestic processor that was presented in Section 6.2. Pre-existence on the part of the domestic firm supports the argument that the regional-MNE was not in a position of favourable dependence. The absence of this dependence relationship failed to provide the leverage needed to appropriate the majority of the value-added (Emerson, 1962). Should the regional-MNE demand opportunistic contractual terms at t_1 , the domestic processor could simply exercise the option to walk away from the negotiations. At t_1 , there is no prior investment in the relationship by either party, making it a simple exchange. In such

circumstances, parties may choose to haggle or walk away altogether if they become dissatisfied with the terms of trade tendered (Crocker and Masten, 1996).

This ability to walk away is predicated on the fact that the domestic processor had an established range of markets that it could continue servicing. Based on this logic, the supplier bargaining power position curve (*sbp*) rests in a neutral position at t_1 . The lack of a favourable bargaining position is one reason why the regional-MNE may not resort to any coercive attempt at value-added appropriation. Beyond this, any premature coercive actions may affect the willingness for the domestic-processor to engage in any MNE-led upgrading trajectory at a future date. This is more so the case when such upgrading trajectories manifest in the deployment of relationship-specific investments.

I have already demonstrated that the domestic processor initially received favourable contractual terms. During the early phases of the relationship, the contracts were year-long where the price and other key aspects were held constant. This motivated the domestic processor to continue and deepen its relationship with the regional-MNE. Relational deepening in the earlier periods took the form of supply concentration in the regional-MNE's favour. For instance, *P1* noted:

"Now we had to give up a lot of market share in plenty other markets to deal with that order fully. We backed out from many orders, for example, [grocery chain 1 and 2] used to deal with us, but we had to forego the account to deal with the regional-MNE."

The stable terms of the arrangement were relatively favourable when compared to what the market was offering. As such, the domestic processor was willing to forego other established clients and markets that it serviced prior to t_1 . For the domestic processor, this made it easier to plan their production schedules and forecast overall profitability. To them, this provided enough incentive to narrow its supply base to a point where the regional-MNE was in a monopsonistic position.

Comparatively better terms and supply concentration creates the impetus for economic upgrading. It makes the domestic processor willing to amend the transactional dimensions of the relationship through capital deepening (accepting knowledge and resource transfers from regional-MNE). Up until this point (t_3), the domestic processor has not invested in any specific assets. The absence of such investments makes it possible for the domestic processor to revert to prior relationships if needed. On the surface, these upgrading initiatives offer strong empirical support for the traditional notion of upgrading (Ivarsson and Alvstam, 2011). In Figure 6.6, these upgrading trajectories are captured in the sharp increase in *svc* and *sva* curves during time period t_3 to t_5 . This is the period that is typically the focus of many GVC studies, see Ivarsson and Alvstam (2010) and Humphrey and Schmitz (2002) for examples. During this time period, the domestic processor is allowed to appropriate the value-added from these upgrading trajectories. This is captured in the close alignment of both the *svc* and *sva* curves.

As I argued in Section 6.5, this period of upgrading was accompanied by an increased level of transaction related cost for the regional-MNE. This intensified suboptimal contracting conditions. Even so, it simultaneously created the transactional conditions necessary for unilateral lock-in (Buvik and Reve, 2001). This is captured in the downward shift in the supplier bargaining power (*sbp*) curve. This increase in non-reciprocal dependence on the part of the domestic processor creates a point where its bargaining power is lowest. Up until t_3 , the processor is able to access a large number of qualified buyers for its product (Williamson, 1985). At t_5 , a paradoxical effect of upgrading takes shape. The domestic processor is unilaterally in a position that fosters small numbers bargaining (Ouchi, 1980). More specifically, the domestic processing is now supplying 60%-70% of its output to a single buyer with assets that have little productive use in that buyer's absence.

Subsequent to t_5 , the regional-MNE is able to leverage on its superior bargaining position to begin appropriating the additional value-added from the upgrading trajectory. This is represented in the diverting *svc* and *sva* curves following the lock-in point (t_5). Over time, appropriation is not restricted to the value-added from the upgrading trajectory only. The regional-MNE is also able to encroach on a portion of the value-added that was initially being captured by the domestic processor at t_1 . This is relative to initial value-added appropriation on a unit basis, and is captured by the point t_6 .

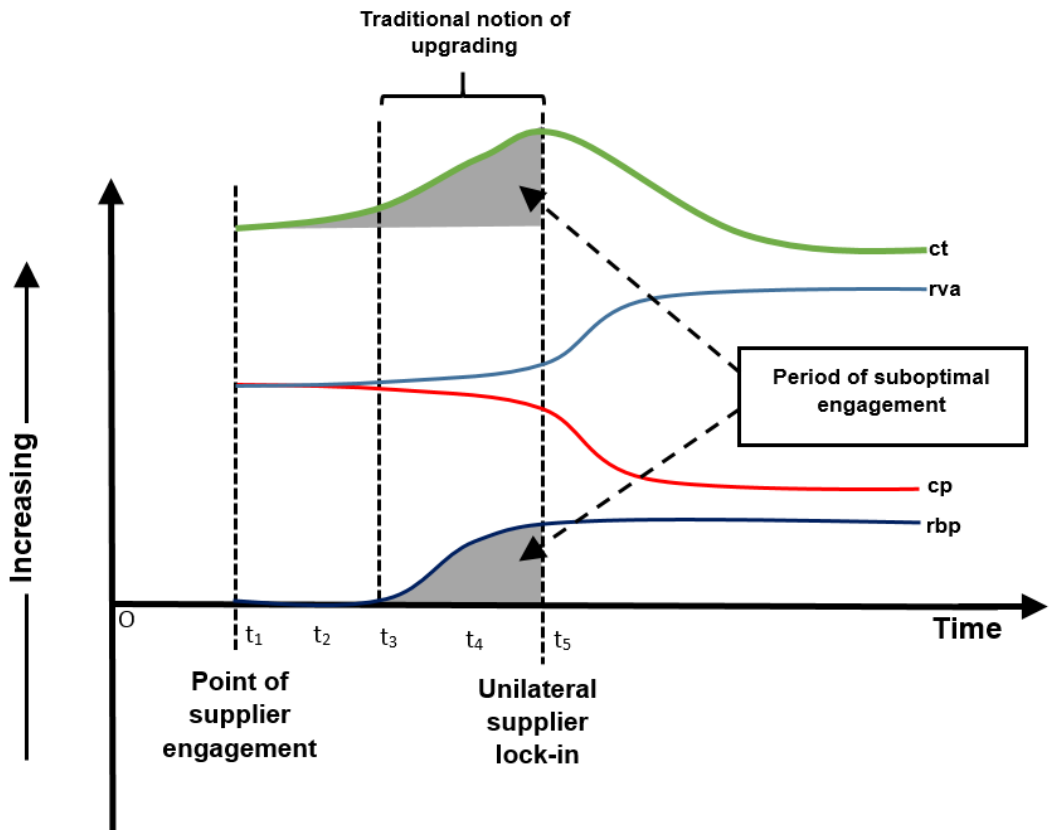
Transaction-related costs also diminish once unilateral lock-in is achieved. For instance, the regional-MNE has removed its contingent of staff that were initially stationed at the domestic processor's facility. This may be due to the successful knowledge transfer, to an extent where no further assistance is needed. However, it also indicates that post lock-in, the regional-MNE need not police or monitor the operations of the domestic processor. The submissive position of the domestic processor dampens the desire to behave in an opportunistic manner (Nyaga et al., 2013). The absence of formal contracts is also indicative of a reduction in transaction related costs. Haggling and protracted negotiations are now absent from the relationship. Post lock-in, the regional-MNE is able to broker better prices when it is convenient for them. The potential for hold-up is minimal given the extensive global network of upgraded suppliers that can be leveraged on. From the perspective of the regional-MNE, the process model can be captured below in Figure 6.7.

In contrast to the graphical illustrations presented before, Figure 6.7¹³ takes the perspective of the regional-MNE. In the earlier phases of the GVC relationship, one can see the positive correlation between the cost of transacting and the interfirm bargaining power of the regional-MNE. Both of which simultaneously occurred during the period of suboptimal engagement (t_1 to t_5). The regional-MNE forgoes value-added via suboptimal engagement, both in terms of transaction costs and the

¹³ I have maintained similar time periods (t_1 , t_2 , t_3 etc.) to allow for comparability between both illustrative iterations

tendered terms of the contract. The latter costs encapsulate the willingness to offer generous contractual terms and pricing in the presence of more cost-effective suppliers. These costs are incurred even before upgrading is pursued by the domestic firm. The former is manifested in the costs associated with the transfer of knowledge and resources during the upgrading process. It also represents the costs associated with monitoring and policing the activity of the domestic-processor during this period of suboptimal engagement. Even so, this period of increasing engagement costs also provided a mechanism to shift the dependence relationship in a direction that was favourable to the regional-MNE (Emerson, 1962). This is represented in the upward slope of the regional-MNE bargaining power curve. This curve peaks at the point of unilateral supplier lock-in (t_5).

Figure 6.7 Suboptimal contracting: the regional-MNE's perspective



ct- cost of transacting
 rva- regional-MNE value-added appropriation
 cp- contract price
 rbp- regional-MNE bargaining power
 t_n- various points in time during the interfirm relationship

Source: Author

Once lock-in has been achieved, the regional-MNE's cost of transacting decreases at a rapid rate. The transaction costs associated with knowledge and resource transfer ceases to exist. Moreover, the regional-MNE no longer engages in acute monitoring or policing of the relationship. This is instead guarded by the submissive position that the domestic processor has found itself in. Beyond this, the regional-MNE has opted for an open and contract-less relationship. Terms that it can effortlessly renegotiate at will, without incurring the inconvenience of haggling, holdup or protracted negotiations. Exploiting this position of interfirm bargaining power, the regional-MNE is able to appropriate an asymmetric share of the value-added (post

t₅). This is captured in the inverse relationship between the regional-MNE's contract price and its value-added appropriation.

This theorization of an indulgent view of suboptimal contracting provides the means to resolve the anomalies outlined in Chapter 4. When I refer to an indulgent, I suggest a form of suboptimal contracting that does not conform to the constrained perspectives that dominate the TCE literature. See for example; Gomes-Casseres (1990), Argyres and Liebeskind (1999), Roberts and Greenwood (1997).

The first theoretical anomaly was introduced as the apparent conflict between MNE led upgrading and optimal interfirm contracting. In Chapter 4, I contended that the existence of capability deficiencies in suppliers and the need for MNE assisted upgrading was a cause for theoretical concern. I made an argument that any significant scope for economic upgrading in supplier firms ran contrary to the notion of a transaction cost minimizing arrangement. This concern is amplified given the argument used to justify the low value-added appropriation of developing country suppliers. For instance, Mudambi (2008) argues that this was due to the abundance of suppliers competition for activities that were of low innovation and perfectly substitutable. This economic rationale still does not explain the MNE's choice to engage with firms that lag significantly behind the productivity frontier (Porter, 1996).

This thesis's rationale provides an alternative reasoning for this anomaly. It suggests that the decision for the regional-MNE to engage with a deficient supplier permits scope for organisation manipulation. Contrary to Mudambi (2008), the case study insight illustrates that post-upgrading, the developing country firm executes an activity that has low substitutability, with a substantial level of technological sophistication. These changes essentially *remove* the supplier from the market by creating small numbers bargaining. The supplier is then quasi-internalised into the regional-MNE's complex supplier network. The extent of this quasi-internalization is greater than what is typically advanced in the extant literature. For instance, Scott-

Kennel and Enderwick (2004) define quasi-internalisation as the involving the transfer of key resources by the MNE for *joint* exploitation by both the MNE and domestic firm. The evidence in this thesis describes a quasi-internalisation mechanism that allows the regional-MNE to appropriate the majority of the value-added from the relationship without any ownership (Buckley and Strange, 2015).

The second anomaly bares an overlapped with the first anomaly. Frequently, the literature on interfirm bargaining power positions acute asymmetry in bargaining as the outcome of a weak firm's interaction with stronger firms (Ireland and Webb, 2007). This perspective views bargaining power distribution as an outcome of the attributes of the respective chain actors. For instance, the contracting partner with superior attributes (e.g. market share, financial capital, intangible assets) will assume the dominant position in the GVC. However, I have argued that bargaining power is a property of the relationship that exists between the firms, and not directly based on the characteristics of the actors (Emerson, 1962). The party less dependent on the other will assume the superior bargaining position. However, these conditions of dependence do not necessarily exist when the initial contractual terms tendered. Therefore, any one party to the contract may not possess the bargaining power advantage (reflected in unilateral dependence) to appropriate the majority of the value-added. This is more so the case when both parties pre-exist the contract being negotiated.

This argument is captured in insights from the case study. Figure 6.1 describes a 30 year period in which the domestic processor operated in the absence of the regional-MNE. During this time, the domestic processor served a diverse range of buyers. At t_1 (point of initial engagement) the regional-MNE did not possess the dependence relationship needed to assume a position of superior bargaining. If the regional-MNE tried to coerce exchange terms that were unfavourable, then the domestic firm could

exercise the option to walk away from the negotiations (Farrell and Shapiro, 1989; Raiffa, 1982).

The theorization in this section has provided a processual perspective on how this asymmetry in bargaining power comes to fruition. In this case, the regional-MNE was required to *nurture* a relationship that supported asymmetric dependence. To create this dependence relationship, the regional-MNE foregoes value-added at the initial phase of the relationship through suboptimal conditions. As Figure 6.7 illustrates, this period of suboptimal engagement also functioned as the impetus to create the unilateral dependence needed to appropriate most of the value added ($>t_5$).

6.5 Chapter conclusion

To avoid monotony, I will not be offering a simple summary of the key theoretical elaborations – this has already been developed in the sections before. Instead, I will relate these insights to the wider research agenda, and illustrate how they can aid in (1) resolving pre-existing empirical conundrums or (2) developing novel theoretical relationships.

Within the GVC research agenda, a generally accepted argument exists. Authors posit that MNEs are willing to assist suppliers in process and product upgrading trajectories, but deter suppliers from entering into activities that afford the MNE a “competitive” advantage (Lund-Thomsen and Nadvi, 2010). For instance, the MNE may provide support for suppliers to improve their productive capabilities, but prevent the supplier from developing capabilities in R&D, branding, design and marketing (Choksy, 2015). This argument has also been advanced by other GVC researchers, see; Humphrey and Schmitz (2004); Bazan and Navas-Alemán (2004); Özatağan (2011); Brandt and Thun (2011); Zhu et al. (2017).

While this consensus exists, little is known about the means by which such “determent” is carried out by the MNE. Tokatli (2013) noted that the GVC research agenda has not yet provided an explanation for “...manner in which buyer firms make

their suppliers act in certain ways, and especially the manner in which they prevent their suppliers from encroaching on their domains...” (Tokatli, 2013 pp. 1002). At the time of this thesis, no explanation has emanated from the research agenda despite the knowledge void being first acknowledged in 2007. Tokatli (2007a) initially raised the concerns around the failure of GVC researchers to explain “...exactly how lead firms construct and reproduce barriers to entry within their competency areas...” (Tokatli, 2007a pp. 69). The author found this statement irreconcilable with the tendency for GVC relationships involving developing country firms to lack formal contracting. Here the assumption was that non-competition and restrictive clauses in engagement contracts were the only established mechanisms that could explain how this deterrent mechanism might manifest itself.

The abstracted insight from this thesis can provide an explanation to resolve this longstanding empirical conundrum. The paradox of upgrading presented in Section 6.3.1 and developed theoretically in Section 6.4.3 provides this explanatory utility. MNEs/lead firms can encourage “productive capability upgrading” not to *exclusively* improve value-added creation. In the process, this upgrading can create the lock-in mechanism needed to prevent suppliers from encroaching on activities that the lead firm guards closely. This deterrent can manifest itself in two ways. With the unilateral dependence that is created by the upgrading paradox, the MNE can explicitly threaten withdrawal from the relationship should the domestic firm try to engage in any protected activities. The MNE’s monopsonistic position coupled with low-redeployable production assets makes it challenging for the domestic firm to continue its operations should the MNE withdraw from the relationship. The second deterrent is less explicit. The upgrading paradox places the MNE in a position of superior bargaining power. This bargaining power can be used to appropriate the majority of the value-added from the interfirm relationship. Even if the MNE permits the domestic firm to independently develop new capabilities, it is unlikely that the domestic firm will

possess the capital slack needed to engage in costly and highly uncertain activities such as branding or research and development.

Beyond resolving questions such as the above, the insight from this chapter provides novel theoretical explanations for what might otherwise be considered well-understood issues. The lack of formal contracting is a prime example. Issues such as: when might an interfirm relationship not be underpinned by a formal contract?

Extant research provides a theorization based on mutual consent and bilateral trust (Lumineau, 2017). Here trust is construed as the willingness of a party to become vulnerable to another party owing to positive expectations of the latter's actions (Rousseau et al., 1998). In a general sense, formal contracts are positioned as substitutes for trust-based inter-organisational relationships. When a party does not have positive expectations of the other party's actions, a formal contract is required to safeguard against conflict and opportunism (Lumineau and Quélin, 2012). The need for these formal safeguards is likely to intensify as transaction specific investments increases within the relationship (Mesquita and Brush, 2008). Conversely, trust can replace formal contracting as a mechanism to regulate interfirm exchange (Heide and John, 1992). In this instance, a party to a contract is willing to make itself vulnerable to the other party's actions due to the former's positive expectations.

This thesis's case study describes a situation where the interfirm relationship between the domestic processor and the regional-MNE moved from formal contracting, to one where no formal contract existed. In this case, theory suggests that formal contracts can facilitate trust building by encouraging initial cooperation between both parties (Poppo and Zenger, 2002; Gulati and Nickerson, 2008). As this trust increases, a formal contracting becomes unnecessary. However, the dynamic GVC perspective in this thesis provides insight that is contradictory to this logic. The case study evidence suggests that distrust increased during the time that a decision

was taken to forego formal contracting. The decision to forego formal contracting was a unilateral decision made by the regional-MNE. The theorization advanced in Section 6.4.3 argues that this decision was not facilitated by trust, but rather by adverse bargaining asymmetry in the inter-firm relationship. The process by which this adversity comes to fruition is one of the main takeaways from this chapter's analysis. In the absence of this novel theorization, it is easy to appreciate how the case study's insight could be exposed to theoretical misspecification.

The final discussion point is linked to the qualitative nature of this thesis. Employing this research methodology provides rich insight that allows for a nuanced perspective of key issues. While this perspective has been derived from a single case, its potential value to wider theoretical cannot be ignored. In Section 6.3.1, I noted that the domestic processor's appropriation of *relative* value-added has decreased to a level that is lower than when it initially contracted with the regional-MNE. Even so, insight from the case study suggested that the *absolute* value-added that the domestic processor appropriates, while decreasing, is still higher than initial engagement.

An empirical analysis based on *absolute* domestic value-added would support a hypothesis that suggests a positive linkage effect from GVC participation. Even so, this empirical focus sanitizes the relationship of factors that may have a material impact on the domestic firm's development. As the case study has illustrated, this absolute increase in value-added can be accompanied by unilateral lock-in. In such instances, the domestic firm becomes beholden to the MNE, and in the process forgoes a great deal of organisation control.

These are some of the conclusions that can be drawn from this chapter's empirical analysis and its theoretical development. It is important to reiterate that these insights have been derived from the context of a single case study. The theoretical elaborations suggested are not proposed with the intention to instantly reposition

extant theory. Further testing is of course required to determine the extent of generalisability.

Chapter 7

The invisible hand of the MNE: influence beyond the 1st tier

7.1 Chapter overview

The thesis's a priori framework and the theoretical contributions thus far have focused on understanding direct interactions of the regional-MNE with the domestic processor (1st tier supplier). In Chapter 6, I illustrated that economic upgrading, as defined in prior studies (Navas-Alemán, 2011), can create an interfirm bargaining situation that disadvantages the domestic processor. This bargaining power asymmetry inhibits the domestic processor from appropriating the majority of value-added it has created.

GVCs rarely comprise value-adding processes that involve only the MNE and a single tier of producing firms. It is common for production tiers to exist beyond MNE-1st tier relationships (Barrientos and Smith, 2007). Even so, GVC and linkage studies have focused on understanding the effects of interactions between the MNE and its immediate suppliers (Gibbon and Ponte, 2005). The result is an accumulated amount of insight into the MNE's direct contracting in GVCs. It is not my intention to discredit this approach. Most GVCs are buyer-driven and the direct influence of the MNE represents the focal point of the analysis (Gibbon et al., 2008; Henderson et al., 2002). However, this influence is not always captured solely in the MNE's direct and contractually bounded relationships (Mares, 2010). Interactions between the MNE and 1st tier suppliers have ripple effects and broader implications for a wide range of upstream actors (Gibbon et al., 2008).

In this chapter, focus is placed on understanding the influence of the regional-MNE on the 2nd tier of the value chain. Section 7.2 provides contextual insight into this 2nd tier of the case study's GVC. I offer descriptive detail into the structure of the relationships between the domestic processor and the domestic farmers that rear and provide the live animals. Section 7.3 makes an argument for an extension of the scope of the MNE's influence. GVC analysis is frequently positioned as interactions

between independent firms (Ponte and Sturgeon, 2014). Chapter 6 has shown that it is possible for the MNE to assume control of an independent entity in the absence of equity or ownership. While there have been discussions around control without ownership, these discussions have been largely relegated to the MNE's direct contractual relationships (Strange and Newton, 2006; Johanson and Mattsson, 1987; Contractor and Kundu, 1998). Using empirical insights from the case study, I show that this highly quasi-internalised relationship can have implications for the lower tiers of the GVC. The bargaining pressure applied to key suppliers does not remain at the 1st tier of the GVC. Instead, this pressure can be passed on to lower tiers of suppliers (Wad, 2008). Through the lock-in of central value chain nodes (such as the domestic processor), the MNE can appropriate value-added indirectly from these lower tiers.

7.2 2nd tier engagement

This section will provide a contextual understanding of the relationships between the domestic processor and the farmers that it contracts with. In 2005, a local newspaper quoted the domestic processor as saying that it had recurring engagements with over 100 domestic farmers. *P6*, the processor's contracting farming manager, noted that in 2016 the figure sat at around 75 contracted farmers.

The farmers provide two main productive inputs: (1) capital and (2) labour. The written contract between the farmer and the domestic processor defines the farmer as an entity "desirous of growing [animals] at his/her premises for [the domestic processor]". The agreement goes on to state that "[the domestic processor] will deliver [the animals] to the farmer who shall manage and properly care for [the animals] for the prescribed period of time". Using data from print media, engagement contracts and interviews, I will provide a brief overview of two important aspects related to this tier of the GVC. I will focus on the (1) semi-integrated structure of engagement and (2) manner in which payments are determined. As I will illustrate, both these aspects are important in understanding the distribution of value-added.

Moreover, I will track changes to these areas to illustrate the indirect influence of the regional-MNE. An influence that extends the commonly held view that MNEs rely on 1st tier suppliers to primarily formalize, communicate and enforce quality and delivery standards throughout the chain (Kaplinsky, 2010; Gibbon and Ponte, 2008)

7.2.1 Semi-integrated engagement

The farmer provides the labour, land as well as the farm equipment and housing needed to nurture the animal to the predetermined market size. The other inputs are provided directly by the domestic processor. The contract states that “all [the animals] and supplies furnished under this agreement shall remain the property of [the domestic processor].” During the rearing period, the farmer is bounded to the relationship with the domestic processor, and is not permitted to rear animals for any other processor. *IE1*, a domestic industry expert, noted that this arrangement is common across all the processors in the domestic industry.

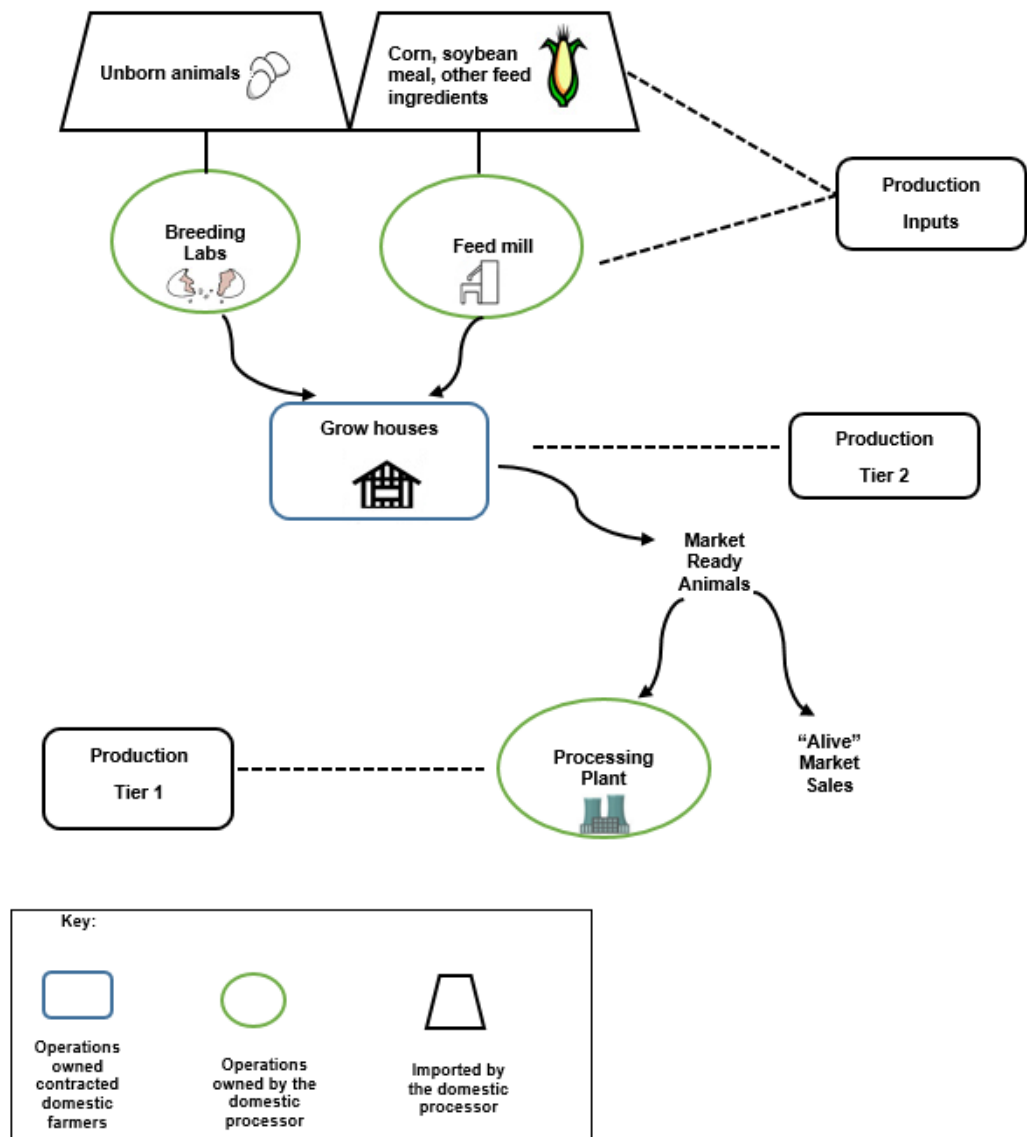
In Chapter 6, I noted that the regional-MNE aggressively monitored the various input markets to signal the appropriate time to renegotiate prices with the domestic processor. This is due to the integral role that the domestic processor plays in the acquisition of farming level inputs. As part of the agreement with the farmers, the domestic processor is responsible for providing infant animals, grains, and any vaccines and medication that the animal may need throughout its life. This is an arrangement that is conventional for the industry under investigation (both domestically and internationally). To accommodate this arrangement, the domestic processor has ownership stakes in key areas of breeding labs and grain mills. *P1* provided the following details:

“We have a feed [grain] depot in the USA. However, they do not do the full processing abroad. They do most of it but we have a feed mill on [the port], so it comes into the port and we do the final processing. There are some additional taxes if we bring in complete products as opposed to intermediate goods but it also allows us to mix the final product ourselves. This way we have more direct control over the mix of the feed.

We do not grow any of [mature animals] ourselves for [offspring]. We buy [offspring] from the USA from a few suppliers and we ship it via containers. Currently, the [offspring] come from the US and they are [nurtured] locally. We have a [breeding facility] locally that we use to [nurture] the [offspring]. We hatch weekly up to about 450,000 [off springs].”

This insight suggests that the domestic processor operates a semi-integrated operation. They control the supply of the inputs and the farmer is responsible for bringing the animal to marketable specifications. A review of the various literature on agricultural economics revealed that this industry structure is a common approach globally for organising this level of the value chain. For instance, farmers in the USA and UK operate under a similar arrangement with processors – the inputs necessary to bring the animal to market are supplied to the farmer by the processor. During rearing, the animals remain the property of the domestic processor and the farmer is not allowed to use any third party grain, nutrition or medication on the animals. Figure 7.1 captures the flow of inputs and outputs at this tier of the value chain. While the domestic processor’s core activity is meat production, the diagram illustrates its stake in the intermediate inputs necessary to bring the animal to a level that is suitable for processing or “alive” market sale.

Figure 7.1 1st – 2nd tier engagement



Source: Author

7.2.2 The remuneration structure

The manner in which the domestic farmer is compensated is the second aspect of the relationship that requires deeper consideration. While the infant animals and grains are supplied by the domestic processor, the farmer does not purchase these inputs through an outright sale. Instead, domestic farmers are paid for their labour and capital input based on predetermined conversion ratios. This conversion ratio is

meant to capture how efficiently the farmer is able to convert grains fed, into animal weight. A clause in the contract describes this as follows:

“For the calculation of the payment the term “average weight” shall mean the total live weight in pounds (lbs) collected from the farm divided by the number of [animals] that is collected from the respective farm. The term “conversion efficiency” shall mean the total number of pounds (lbs) of grain [administered] divided by the total live weight of [animals] collected from the respective farm.”

Table 7.1 represents an excerpt of this payment schedule. At the end of a growth cycle, a farmer may, for example, produce 10,000 lbs of live weight. If the farmer provided 2,500 animals, the average weight would be four pounds. During the cycle, the domestic processor may have provided the farmer with 20,000 lbs of grain. Based on this, the conversion ratio would be 2:1 and be interpreted as the farmer’s ability to convert 2lbs of grain into 1lb of meat.

Every probable conversion ratio is represented in the complex matrix where individual ranges attract a specific price. At an average weight of four pounds and a conversion ratio of 2:1, the farmer is able to achieve a conversion price of \$1.48 per animal. The conversion price is then applied to the number of animals that were initially collected from the farmer. In this example, the farmer would have received a total payment of \$3,700 (in local currency). The lower the conversion ratio, the higher the price that the farmer will receive - signifying a more efficient use of farming inputs. The contract stipulates that the domestic processor reserves the right to withhold any remuneration in cases where the conversion ratio exceeds 2.45:1 (where a farmer uses more than 2.45lbs of grain to produce 1lb of meat).

Table 7.1 Farmer payment schedule

Avg. Weight Range (lbs)	FEED CONVERSION RANGES																
	≤1.89	1.90 to 1.94	1.95 to 1.99	2.00 to 2.04	2.05 to 2.09	2.10 to 2.14	2.15 to 2.19	2.20 to 2.24	2.25 to 2.29	2.30 to 2.34	2.35 to 2.39	2.40 to 2.44	2.45 to 2.49	2.50 to 2.54	2.55 to 2.59	2.60 to 2.64	≥2.65
	PAYMENT PER ANIMAL [IN LOCAL CURRENCY]																
2.50 to 2.80	1.54	1.40	1.26	1.12	0.98	0.84	0.70	0.56	0.42	0.28	0.14	0.00	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.
2.81 to 3.00	1.57	1.43	1.29	1.15	1.01	0.87	0.73	0.59	0.45	0.31	0.17	0.03	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.
3.01 to 3.10	1.60	1.46	1.32	1.21	1.10	0.99	0.89	0.81	0.73	0.66	0.59	0.62	0.55	0.48	0.41	Ref To Mgr.	Ref To Mgr.
3.11 to 3.20	1.63	1.46	1.35	1.24	1.13	1.02	0.92	0.84	0.76	0.69	0.62	0.55	0.48	0.41	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.
3.21 to 3.30	1.66	1.52	1.38	1.27	1.16	1.05	0.95	0.87	0.79	0.72	0.65	0.58	0.51	0.44	Ref To Mgr.	Ref To Mgr.	Ref To Mgr.
3.31 to 3.40	1.69	1.55	1.41	1.30	1.19	1.08	0.98	0.90	0.82	0.75	0.68	0.61	0.54	0.47	0.40	Ref To Mgr.	Ref To Mgr.
3.41 to 3.50	1.72	1.58	1.44	1.33	1.22	1.11	1.01	0.93	0.85	0.78	0.71	0.64	0.57	0.50	0.43	Ref To Mgr.	Ref To Mgr.
3.51 to 3.60	1.75	1.61	1.47	1.36	1.25	1.14	1.04	0.96	0.88	0.81	0.74	0.67	0.60	0.53	0.45	0.39	Ref To Mgr.
3.61 to 3.70	1.78	1.64	1.50	1.39	1.28	1.17	1.07	0.99	0.91	0.84	0.77	0.70	0.63	0.56	0.49	0.42	Ref To Mgr.
3.71 to 3.80	1.81	1.67	1.53	1.42	1.31	1.20	1.10	1.02	0.94	0.87	0.80	0.73	0.66	0.59	0.52	0.45	Ref To Mgr.
3.81 to 3.90	1.84	1.70	1.56	1.45	1.34	1.23	1.13	1.05	0.97	0.90	0.83	0.76	0.69	0.62	0.55	0.48	Ref To Mgr.
3.91 to 4.00	1.87	1.73	1.59	1.48	1.37	1.26	1.16	1.08	1.00	0.93	0.86	0.79	0.72	0.65	0.58	0.51	Ref To Mgr.
4.01 to 4.10	1.90	1.76	1.62	1.51	1.40	1.29	1.19	1.11	1.03	0.96	0.89	0.82	0.75	0.68	0.61	0.54	Ref To Mgr.
4.11 to 4.20	1.93	1.79	1.65	1.54	1.43	1.32	1.22	1.14	1.06	0.99	0.92	0.85	0.78	0.71	0.64	0.57	Ref To Mgr.
4.21 to 4.30	1.96	1.82	1.68	1.57	1.46	1.35	1.25	1.17	1.09	1.02	0.95	0.88	0.81	0.74	0.67	0.60	Ref To Mgr.
4.31 to 4.40	1.99	1.85	1.71	1.60	1.49	1.38	1.28	1.20	1.12	1.05	0.98	0.91	0.84	0.77	0.70	0.63	Ref To Mgr.
4.41 to 4.50	2.02	1.88	1.74	1.63	1.52	1.41	1.31	1.23	1.15	1.08	1.01	0.94	0.87	0.80	0.73	0.66	Ref To Mgr.
4.51 to 4.60	2.05	1.91	1.77	1.66	1.55	1.44	1.34	1.26	1.18	1.11	1.04	0.97	0.91	0.83	0.76	0.69	Ref To Mgr.
4.61 to 4.70	2.08	1.94	1.80	1.69	1.58	1.47	1.37	1.29	1.21	1.14	1.07	1.00	0.93	0.86	0.79	0.72	Ref To Mgr.
4.71 to 4.80	2.11	1.97	1.83	1.72	1.61	1.50	1.40	1.32	1.24	1.17	1.10	1.03	0.96	0.89	0.82	0.75	Ref To Mgr.

Reproduced from farmer's contract

The domestic processor contends that this is a fair remuneration structure, while simultaneously controlling for opportunistic behaviour by contract farmers.

Compensating farmers on a conversion ratio minimizes loss against potential

shrinkage and theft by farmers. All grains sent to the farmer over the course of the growth period are logged by the domestic processor. Should a farmer attempt to sell grains to third parties, the discrepancy will be accounted for in the farmer's conversion ratio. Likewise, the sale of live animals without the domestic processor's approval will also worsen the farmer's conversion ratio.

7.3 Selective quasi-internalisation: the upstream effects

Studies have noted the importance of the 1st tier supplier in orchestrating key upstream production activities of the value chain. Humphrey and Memedovic (2003) described 1st tier suppliers in the automotive industry as being responsible for organizing the rest of the value chain. These firms were instrumental in managing the 2nd tier suppliers, and developing supply systems in many different locations (Humphrey and Memedovic, 2003; Gereffi, 1999a).

In this section, I look at the effects of GVC participation on the upstream actors in the value chain (domestic farmers). I continue to take a dynamic perspective by providing insight into two key areas. First, I investigate whether any instances of upgrading occurred in this GVC tier. Second, I examine the upstream effects of the regional-MNE's quasi-internalisation of the domestic processor. The insights emerging from the case study suggest an indirect influence by the regional-MNE. Meanwhile, prior studies have under-researched this aspect of GVC participation (Khan et al., 2015). It is common to treat lower tiers as an isolated context – one that is divorced from the GVC and the MNE (Coe and Hess, 2013). As such, some studies underplay the impact that the MNE's 1st tier engagements have on the rest of the value chain (Wad, 2008). Others tend to assume that the lack of formal or contractual relationships with lower tiers of the GVC negates any meaningful influence by the MNE (Mares, 2010). In Sections 7.3.1 and 7.3.2, I will demonstrate the regional-MNE's influence in this wider system of production. I argue that through the lock-in of a central value chain node, the regional-MNE is able to appropriate value-added that once resided beyond

the domestic processor. The domestic processor's unilateral dependence on the regional-MNE alters aspects of the domestic processor's relationship with the domestic farmers. These 1st–2nd tier changes mimic the demands and bargaining pressure that is placed on the domestic processor post lock-in. Section 7.3.3 decontextualizes these insights by drawing parallels from other published case studies on GVC participation. Here the aim is to illustrate that a more abstract interpretation of the case study context suggests that similar value chain structures may exist across other industries. In instances where central value chain nodes become captured by MNEs, the scope for upstream bargaining pressure and value-added appropriation can also occur.

7.3.1 The mechanics of 2nd tier bargaining asymmetry

Chapter 6 revealed that the relationship between the regional-MNE and the domestic processor was accompanied by various upgrading trajectories. This is manifested in various forms of capital deepening and knowledge transfers to the domestic processor. I pursued a similar line of investigation regarding the relationships between the domestic processor and the various farmers. All 24 farmers noted that little to no upgrading initiatives had been pursued over the last two decades. Four farmers reported shifts into semi-automated watering and grain dispensation systems. For instance, *F1* & *F3* described initiatives where they invested in small pumps to facilitate the replenishment of water vessels without the need for extensive manual effort. Likewise, *F2* invested in a grain dispensing machine that allowed for the easier administering of daily grains to the animals. In all three instances, the upgrade initiatives were facilitated through soft agriculture loans from a governmental agency. None of these farmers reported assistance from the domestic processor that conformed to conventional definitions of product, process, or functional upgrading trajectories (Ivarsson and Alvstam, 2010).

This is not to say that assistance from the domestic processor was completely absent. Individuals interested in setting up new operations were able to access assistance from the domestic processor. For instance, *F4* noted the following:

“If you need any kind of assistance or equipment they might be willing to help. Like if you’re setting up and you need feeders and building material, they will help. But the help is really a loan because they take it out of your payment every time you produce the grow-out¹⁴. They also help you get started by providing some ideas on farm construction and how to grow good [animals]”

Other farmers, including *F10*, *F8* and *FF1*, reported similar types of assistance from the domestic processor. For the purpose of this study, this form of assistance does not conform to an upgrading trajectory (or economic upgrading). An upgrading trajectory is a movement into activities deemed to be of *higher* value-added (Rossi, 2013). Economic upgrading itself is construed as the actor’s ability to create and appropriate *greater* value-added from its operations. The domestic processor’s willingness to aid in the setup of new farmers does not fit with either notion. For instance, an upgrading trajectory would imply that there is a positive *improvement* in the operations of the farmer. However, the resource and knowledge transfer by the domestic processor was only instrumental in setting up the farms. Once the farms were established, the farmers explained that no other forms of assistance were offered to increase value-added creation or appropriation.

In Chapter 6, I argued that the upgrading trajectories themselves facilitated the unilateral lock-in of the domestic processor. This was achieved through a period of suboptimal contracting where the regional-MNE created an interfirm relationship that promoted asymmetric dependence. A *process* was required to create this dependence due to the presence of contractual pre-existence. More specifically, the domestic processor pre-dated the GVC relationship, making it difficult for the

¹⁴ A grow-out refers to one growth cycle. The period from which the infant animals are released in the farmer’s care to the point where they are collected by the domestic processor for processing.

regional-MNE to exert bargaining pressure at time t_1 . This was in part due to the diversified buyer network of the domestic processor at t_1 (Choksy et al., 2017). Over time, the regional-MNE needed to persuade the domestic processor into concentrating its buyer base, with a sizable portion of its output being allocated to the regional-MNE.

A reversed logic can be used to understand the bargaining relationship between the domestic processor and the farmers. In this tier, pre-existence is less of a contentious issue for the domestic processor. According to *IE1*, the population of domestic farmers were established to provide services to a domestic processor. Prior to the 1970s, meat supply in this developing country was met through subsistence farming. Over time, income and demand for the commodity grew, giving rise to large-scale processing. As such, the farmers did not possess a diverse buyer network or any other relational factor that could afford a greater level of interfirm bargaining.

In this sense, the domestic processor and its farmers share an initial interfirm bargaining dynamic similar to the MNE HQ and its greenfield subsidiaries (Mudambi and Navarra, 2004). In this circumstance, the burden is on the newly established entity (subsidiary or contract farmer) to introduce balancing operations that can improve its bargaining position (Emerson, 1962). In the case of subsidiaries, Mudambi and Navarra (2004) argue that knowledge creation can facilitate such balancing. Especially if the knowledge created by the subsidiary is of strategic importance to headquarters and/or other subsidiaries (Holm and Pedersen, 2000). When this dependence relationship shifts in the subsidiary's favour, it is able to bargain for, and appropriate a greater share of the rents.

Evidence from the case study suggests that domestic farmers have restrictive scope for pursuing any balancing operation that may result in greater bargaining power (Crook and Combs, 2007). This is attributable to two factors. First, the integrated operations of the domestic processor create a "closed" sourcing system. If the

farmers wish to continue rearing animals for the domestic processor, they must rely on the processor for the supply of inputs. This relegates the farmers to a submissive position, where they are unable to develop input relationships outside of the contract, even if such inputs could be acquired elsewhere under more favourable terms. *F14* noted the following:

“Sometimes [local retail farm shops] import grain that seems to be a better quality. This is what they sell to regular people rearing [animals] for their own use. But we can’t use this grain, if we use it and [the domestic processor] finds out, we will lose our contract. And if we try to take a chance and buy it then the money coming from our pockets, since we still have to take [the domestic processor] grains.”

It is reasonable to propose that farmers can gravitate to another domestic processor in cases of adverse contractual conditions with a particular processor. There are three other large domestic processors. Case study evidence suggests that farmers have restricted scope when attempting to move between domestic processors. I asked *P1* about the industry structure and the company’s interaction with other domestic processors. The response was as follows:

“To maintain order in the industry, we have a gentleman relationship with other processors such as [domestic processor 1] and [domestic processor 2]. We don’t go to their farmers and customers and they don’t go after ours. I won’t say it’s a written arrangement but it is something that has been honoured for some time.”

The farmers and the industry expert supported the existence of this “gentlemen’s agreement”. The terms of the contracts are largely uniform across the processors. This standardised system provides little incentive for informed farmers to switch. Beyond this, 15 of the interviewed farmers have reported unfavourable interactions when the possibility of switching was raised or pursued. These unfavourable interactions originated from the domestic processor themselves, as well as the other local processors that the farmer was considering switching to. For instance, *F8* noted that there was an outright refusal from a competing processor to engage in any

consideration of a relationship. Likewise, *F7* was given an ultimatum by the domestic processor. That is, should *F7* pursue any alternative relationship with another domestic processor, it would not be possible to return to in the future.

Farmers noted that over the last decade, there have been many failed attempts to organise a collective bargaining association. 18 of the interviewed farmers linked this unionisation failure to either direct intimidation or fear of intimidation. *F9* went on record saying that threats were levied by the domestic processor when they became aware of his interest in unionising:

“They heard that I was part of the farmers meeting that happened last month. The farm officer that comes around to the farms told me that [the processor] informed him to tell me that if I continue to be part of these meetings then I would never farm for anyone again.”

Other farmers such as *F4*, noted that they themselves have never been personally intimidated by the domestic processor. Even so, they have refrained from partaking in any attempt to establish a union for fear that it may provoke a negative reaction from the domestic processor.

Together, these circumstances provide the conditions necessary to maintain favourable interfirm bargaining for the processors. The lack of pre-existence on the part of the domestic farmers negates the presence of buyer diversity. From the farmer’s perspective, at the point of inception, they are bounded to a single party – both in terms of inputs and output sale. Both balancing operations outlined in Chapter 4 are irreconcilable with the industry dynamics outlined above (Emerson, 1962; Crook and Combs, 2007). For instance, rarity among the domestic farmers is purposely constrained by the domestic processor. All farmers provide a uniform intermediary where they are restricted to sourcing their value-adding inputs directly from the domestic processor. Domestic farmers are also not able to cultivate relationships or sell its outputs to alternative sources. The contract with the regional

processor explicitly prohibits the farmer from simultaneously rearing animals for other buyers. Moreover, the ability for farmers to move between processors during rearing cycles is dampened by the informal collusive agreement among processors.

7.3.2 The MNE's indirect appropriation of value-added

The regional-MNE became actively involved in the domestic industry during the early 2000s. Since then, there has been an increase in both raw material and final consumption demand for the meat product. Even with this growth in the industry, domestic farmers have reported that their incomes have decreased significantly. I have already noted that the bargaining asymmetry between the domestic processor and the farmers predates the entrance of the regional-MNE. Even so, farmers only began to report significant reductions in incomes at or around the year 2005/2006. This timing coincides with the point in which the domestic processor began to experience the negative effects of unilateral lock-in.

The rest of this section will present empirical data that links the bargaining pressure faced by the farmers to the unilateral lock-in of the domestic processor. Before doing so, it is necessary to clarify the underlying assumption of this argument. First, I do not rule out the possibility that the domestic processor would not have acted in an opportunistic manner in the absence of the regional-MNE's bargaining pressure. The mechanisms that sustain the asymmetric bargaining relationship between the domestic processor and the farmers are independent of, and older than the regional-MNE's involvement in the industry. Based on the empirical data, my argument is merely that the observed reduction in farmer income is indirectly driven by the MNE's relationship with the domestic processor- and the demands and bargaining pressures placed on the latter.

As value-added is being appropriated away from the domestic processor, it is likely that pressure is passed on to the lower tiers of the value chain as a means to

recapture lost income (Wad, 2008). F3 offered the following comment when asked about the current state of income generation from contract farming activities:

“Let me tell you, a lot of farmers have moved on, just as I am looking to move on now. The return is just not worth the work and effort that is put into the business. Not all can walk away though. I am old in age and I am looking to retire anyhow. But some farmers have no other option so they have to continue and accept what they are getting.

Fortunately for me, I was employed elsewhere and I was able to supplement my income. Some demolished their farms and went into other businesses and some sold out and move on. For the last 10-15 years, I wouldn't think that there is one private farmer who has entered the industry.”

In order to appropriate value-added from the lower tier of the GVC, the domestic processor can take three strategies. They can choose to (1) directly reduce the remuneration farmers receive per conversion ratio, (2) manipulate the factor inputs that determine the conversion ratios, or (3) adjusting the contractual terms to externalize greater risk to farmers. Post lock-in, the evidence from the case study suggests that the domestic processor pursued the latter two strategies as a means of recovering value-added lost through adverse bargaining conditions.

In the mid-2000s, the industry received a great deal of domestic media attention. Various contract farmers lodged anonymous complaints with a national media outlet. The claim was that farmers were being provided underweight grain supplies. A journalistic investigation revealed that over an eight-month period, farmers were being provided bags of grain that were incorrectly weighted. Bags of 100lbs of grain were provided to the farmers as part of the contractual agreement. It was eventually revealed that the bags of grain weighed as little as 90lbs when tested on the farms. This action by the domestic processor did not affect the growth cycle of the animal. In principle, there was no material change in the animal's ability to convert grain consumption into weight. Even so, farmers experienced conversion ratios that were

on average 10-15% worse than before the lock-in. Underweighted bags of grain meant that the farmers needed more bags of grain to achieve the usual conversion ratios. Actual grains supplied to the farmer and the quantity logged by the domestic processor varied. Eventually, the domestic processor acknowledged the shortcoming and offered the farmers partial compensation.

This strategy was an explicit mechanism to appropriate value-added from the domestic farmers. Farmers were provided quantities of grain that were inconsistent with the aggregate amounts used to determine their conversion ratio. The mechanisms used by the domestic processor evolved as its relationship with the regional-MNE deepened. With each new iteration, each mechanism became more closely aligned with the demands of the regional-MNE.

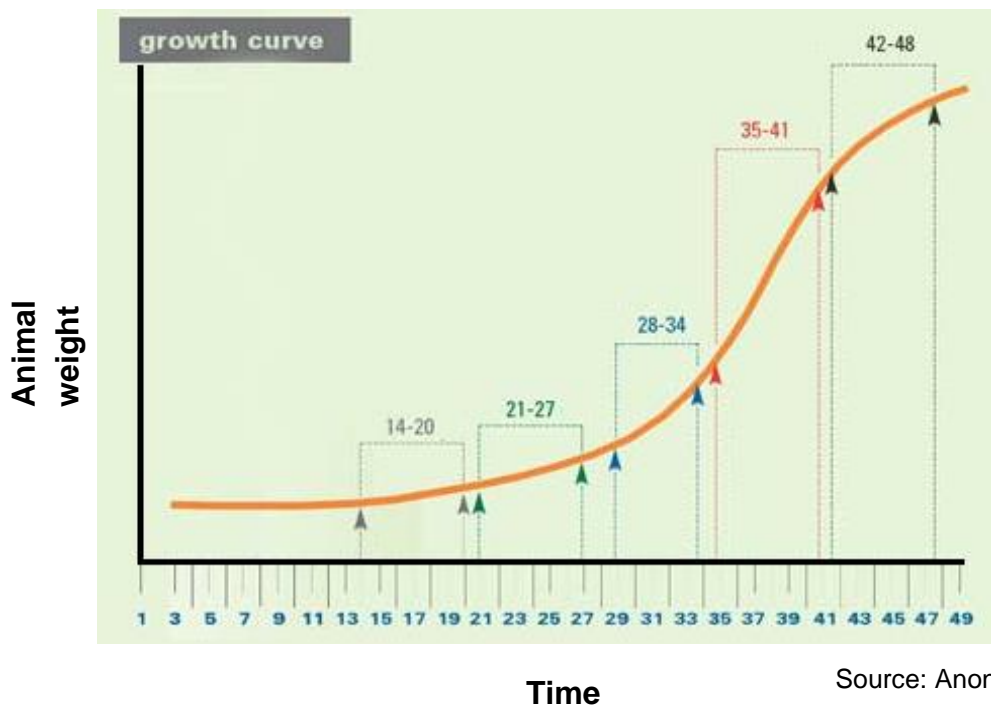
I have previously noted that the regional-MNE was able to negotiate for a lengthier credit period (net-45 days as opposed the conventional net-30 days). The regional-MNE accounted for on average 64% of the domestic processor's weekly output. This placed a significant cash flow constraint on the firm once the credit extension was agreed to. To mitigate against this constraint, the domestic processor began to rely on the "alive" market to generate sufficient cash flows. This was necessary to keep the company operational, pending payment from the regional-MNE. As P6 described:

"The alive market is a cash-only market. We do not give any credit to these customers. As soon as [the animal] is collected from the farms, the live sale clients are required to pay us immediately."

The "alive" market prices vary from week to week. Avoiding this volatility was one of the factors behind the domestic processor's decision to commence and then deepen its relationship with the regional-MNE. Bulk "alive" market sale executed in one week over another can translate into significant increases in cash flow for the domestic processor. However, earlier contracts between the domestic processor and the farmers stipulated a fixed period for which the animals must be collected by the

processor. The domestic processor was bounded to retrieving the animals at that time, regardless of what the “alive” market was offering. An analysis of more recent contracts (post-2008) revealed that this contract clause had been removed by the domestic processor. What could be construed as a superficial amendment, allows the domestic processor the option to retrieve the animals from the farms at their convenience. This convenience is predicated on its ability to fetch a favourable “alive” market price. Figure 7.2 was published by a respected North American council that provides technical support for industry stakeholders. *IE1*'s explanation and the experiences of the farmers are consistent with this growth curve.

Figure 7.2 The animal's growth curve



Source: Anonymised¹⁵

The growth cycle of the animal can be graphically captured as an inverted “U” shaped curve, with varying slopes across the cycle. If the animal is withdrawn from the farm early, the farmer is not able to benefit from the period where the animal is best able to convert grain into live weight (period 35-41). Farmers contend that this is the period of the growth cycle that determines if they are able to make a profit. Earlier iterations

¹⁵ The source of this illustration has been anonymised. Contextual information in the figure as well as the source will identify the exact industry under investigation.

of the contract stipulated that the animals would be retrieved during the time period 42-48. Subsequent to this period, the animal is less efficient at converting the grains into weight and becomes more susceptible to death (forcing the aggregate curve downwards). Likewise, animals withdrawn from the farm prior to, or in the early part of period 35-41 do not experience efficient conversion.

The generous credit terms obtained by the regional-MNE forced the domestic processor to deepen its exploitation of “alive” market price fluctuations. The risk associated with varying the animal’s time on the farm is borne by the farmer and is reflected in their conversion ratios. 14 of the interviewed farmers noted repeated instances over the last eight years where they have had to keep animals on the farms beyond the conventional time period. *FF2* explained that it was such an instance that forced the closure of his farm:

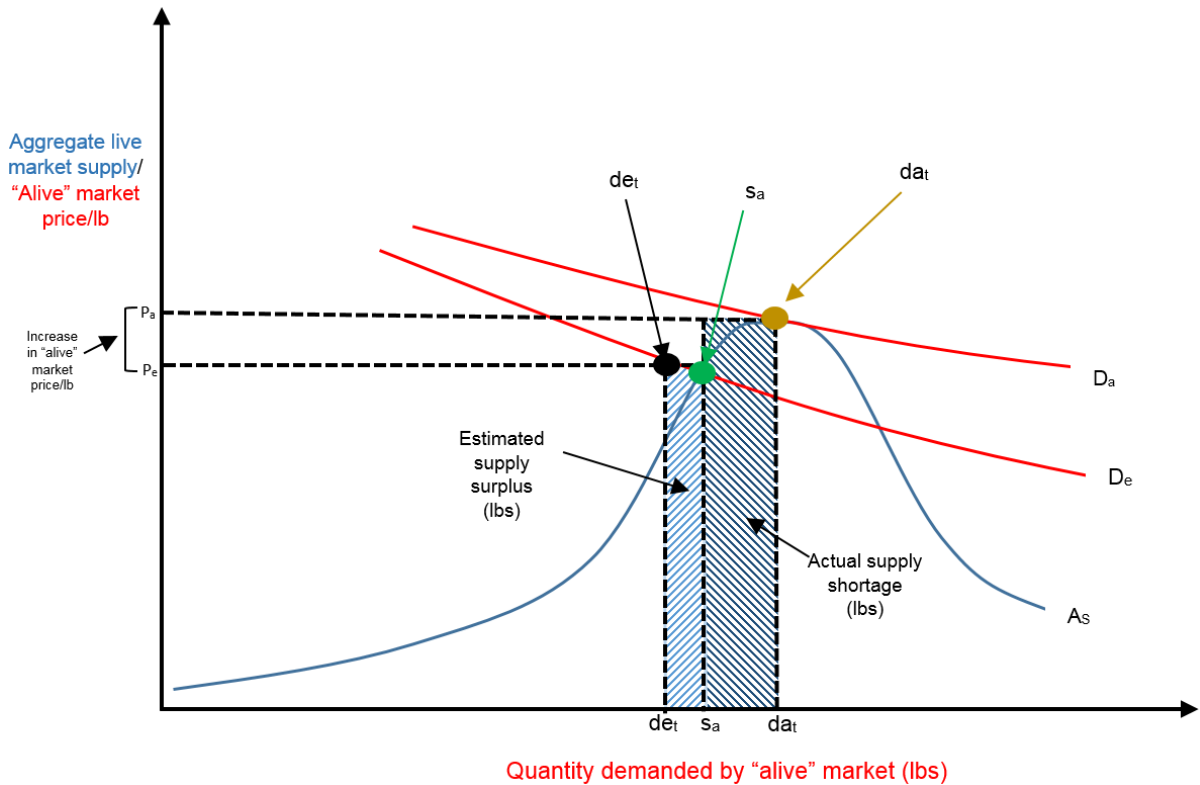
“I had a grow-out that was due to end during the last week of [a religious fasting period]. People were not eating meat so the alive market prices were low. [The domestic processor] refused to come and collect [the animals]. Over the next week, my mortality rates were high and didn’t make any money from the cycle. [The domestic processor] actually refuse to pay me anything. This was not my fault.”

Similarly, other farmers noted the domestic processor’s eagerness to remove animals prematurely from the farms when the “alive” market prices become favourable. This also hurts the farmer’s income generation potential as the animal has not experienced the phase it’s growth cycle that maximises the conversion ratio yield. I have created Figure 7.3 to illustrate the economic effect of this cash flow maximisation strategy.

The green node on the graph (S_a) denotes the actual amount of mature animal supply. This supply represents animals that have already gone through the period of efficient growth. At that point in time, the domestic processor estimates that “alive” market demand will be D_e and with a corresponding price at P_e . Here the domestic processor

envisions a surplus of “alive” market supply ($S_a - D_e$). This minimal surplus would be left on the farm or processed and frozen for sale to the regional-MNE. However, in this scenario, actual “alive” market demand was D_a and is represented by both outward shifts and movements along the demand curve – increasing actual price to P_a . *IE1* explained that this change can occur for a number of reasons. For instance, imported meat sold by some grocery chains may be unexpectedly delayed in shipment or held up at domestic customs. Alternatively, other domestic processors with more concentrated sales in the “alive” market may be unable to supply the market. This shortfall may be the result of a high demand period (e.g. national holiday) not syncing with the predetermined growth cycles.

Figure 7.3 The farming repercussions of retrieval manipulation



P_e - estimated "alive" market price per lb
 P_a - actual "alive" market price per lb
 D_e - estimated "alive" market demand curve
 D_a - actual "alive" market demand curve
 A_s : Domestic processor's aggregate supply of animals for "alive" market
 d_{e_t} - estimated quantity demanded at time t
 d_{a_t} - actual quantity demanded at time t

Source: Author

These short-term shocks to demand and supply have shifted the actual demand curve outwards. Consumers are not only demanding more meat, but are also willing to pay a higher price for the commodity. However, the domestic processor has already planned for an allocated a fixed amount of animals to the "alive" market (S_a). This is the maximum amount of mature animals that the domestic processor can supply the "alive" market. In light of the dire need for liquidity, this supply shortage ($S_a - D_a$) is met by removing premature animals from the farms. While the overall meat demands are met (in lbs), it is done by utilizing animals that have not yet experienced

the efficient conversion period. The farmers' conversion ratios are high at this point in time and receive lower returns for their capital and labour inputs.

The next instrument deals with input sourcing. Chapter 6 noted that the regional-MNE monitored the market prices of the inputs used in the farming process. This was utilised by the regional-MNE as a signal to initiate renegotiation. To minimise the loss of value-added to the regional-MNE, the domestic processor sometimes sources inputs that are of both low quality and price. P9 was responsible for the domestic processor's integrated/upstream services and noted the following:

"Over the last few years, we have had to look into other places to source [input 1] and [input 2]. We could not continue sourcing from the United States for all the input, then we just would not make any money. We started to look to other countries in [region 1] and [region 2] to get cheaper stuff."

I followed up by asking whether sourcing from these new suppliers affected the operations in any way. P9 then mentioned that the supply from these alternative sources is not as good in quality or consistency as the previous inputs that were being used. The inconsistency is so pronounced that they still maintain a partial supply from the US suppliers to ensure that a constant animal supply is not jeopardised. P6 explained that over the last two years, the domestic processor has been dealing with an intermittent case of fungus in the grain supply. The presence of this fungus affects the animal's health and the conversion ratios that the farmers are able to achieve.

What I have described thus far are more explicit instances of the domestic processor's reaction to the bargaining pressures of the regional-MNE. This final manifestation is more tacit. The data in this case study did not include laboratory tests to support this argument. Even so, it is worth mentioning given how consistent the insight is with the rest case study data. The regional-MNE accounts for, on average, 64% of the domestic processor's production capacity. The regional-MNE has a demand cycle that fluctuates throughout the year. This fluctuation is predictable and

usually coincides with (1) holiday and festive periods, (2) religious and fasting periods. In the latter, demand from the regional-MNE drops. Likewise, the former drives an above average increase in the demand for the meat products. Many farmers contend that these periods are accompanied by conversion ratios and remunerations that are inconsistent with what they have been accustomed to. This is so even though the number of animals reared remains constant. *F14*, *F1*, *F7*, *FF2* and *FF3* allowed me to peruse their payment receipts and there is indeed a general trend that reflects this allegation. To rationalise this, the farmers argue that the quality of grains supplied varies based on these periods of demand peaks and slumps.

Even so, their evidence is instinctive and based on smell and observation. *F14* and *F7* note a difference in the smell of the grains and argues that it sometimes lacks the needed “fishmeal”, a key source of protein for the animal. At other times, the grains have a pungent odour that is reminiscent of this key protein ingredient. *F11* and *F1* noted that in addition to variation in the smell, they observe differences in the animal’s excretion patterns. Their rationale is that the lack of protein in the grains affects the animal’s ability to convert food into mass. This inability to retain mass is thus manifested in a higher than usual level of animal excrements – and greater grain consumption to maintain target weights.

This accusation was posed to *P1* who denied that such actions occur at the domestic processor. *P6* noted that his employer, the domestic processor, does not engage in grain manipulation but he is aware of other domestic companies pursuing such strategies. While I was unable to conduct laboratory testing on the various feed samples. This proposition is plausible given two pieces of empirical insights that were previously presented. In Section 7.2, I revealed that the domestic processor runs a semi-integrated operation. This included a domestic mill that is responsible for mixing the various ingredients to produce grains for farmers. This gives the domestic processor a great deal of control over the end product – as opposed to buying a

standardised product from a supplier. Such control can facilitate, if desired, the need to alter the composition of the grain. In Section 6.2, *P1* provided a historical overview of the processor's development. The respondent noted that the company fuelled its initial growth by pursuing "arbitrage" type income by purchasing animals, holding them for short periods and administering "good feed". As such, the domestic processor possesses not only the capability of grain manipulation, but also the intimate knowledge of how to execute such strategies (derived from experience).

A strategy of engineering growth cycles is necessary for meat being sold exclusively to the regional-MNE. Unlike the "alive" market, animals reared for the regional-MNE cannot be left on the farm for extensive periods (reduced demand periods). This is due to the strict requirements on meat size imposed by the regional-MNE. These requirements do not exist in "alive" market sales. Even so, feed engineered to dampen growth cycles result in higher overall consumption by the animals. This is the cumulative effect of longer periods on the farm and lower relative feed quality. This negatively affects the conversion ratios of the farmers – resulting in lower remunerations. The effects of this regional-MNE demand volatility are not purely negative. For instance, demand spikes require the domestic processor to provide a specific animal size in a shorter period of time. In such instances, the farmer conversion ratios are driven downwards.

In Section 7.2, I noted that the farmer population had decreased by approximately 25% over the period 2005-2016. This occurred despite an overall increase in production and demand (from the regional-MNE's domestic activity). With this gradual reduction in the farming operations, it is reasonable to assume that a significant shortfall in domestic supply would ensue. This assumption was considered, and adequate insight was sought to clarify the extent of this supposition. Respondents at both the domestic processor and farming tiers confirmed that the number of annual "grow-outs" had increased. Prior to 2008, domestic farmers were

required to carry out six grow-out per calendar year. The animals on average require six weeks (42 days) before they are ready for processing (see Figure 7.1). A 14-day “cool-down” period between each grow-out was required. This period is necessary to prepare and sanitise the farms to facilitate the next grow-out. Together, these recurrent activities amounted to 48 calendar weeks. The remaining four weeks were given to farmers as personal time.

Over time, the number of farmers began to decrease while the regional-MNE’s input demands increased. To address this, the domestic-processor increased the “grow-outs” per calendar year to seven on average. This change is captured in Table 7.2. In order to accommodate the additional six-week grow-out, farmers were required to reduce their cool-down and sanitization periods from two weeks to one week. Their personal time also diminished from four to three weeks.

Table 7.2 Post regional-MNE grow-out adjustments

No.	Old grow-out schedule		Amended grow-out schedule	
	Grow-out duration	Cool-down duration	Grow-out duration	Cool-down duration
1	6 weeks		6 weeks	
		2 weeks		1 week
2	6 weeks		6 weeks	
		2 weeks		1 week
3	6 weeks		6 weeks	
		2 weeks		1 week
4	6 weeks		6 weeks	
		2 weeks		1 week
5	6 weeks		6 weeks	
		2 weeks		1 week
6	6 weeks		6 weeks	
		2 weeks		1 week
7	n/a		6 weeks	
				1 week
	Total 48 weeks		Total 49 weeks	

Source: Author

The effects of this shift on the 2nd tier were twofold. First, it contributes to a reduction the income generated by the farmer’s factor inputs (labour and capital). *F6* and *F10* noted that this additional grow-out helped minimise the decline in income from the conventional six grow-out cycle. This reduction can, to a large extent, be attributed to the other three mechanisms outlined in this section. An additional grow-out

assisted in stabilising the absolute value-added that the farmer is able to appropriate. Even so, the relative gains are increasingly negative, as the farmer now has to devote additional labour resources to farming process (by way of an additional grow-out). Beyond this, the additional grow-out accelerates physical capital depreciation of the crucial farming structures and equipment.

IE1 suggested a second issue with this increase grow-out cycles, one that has far-reaching implications for the value-chain:

“It is actually dangerous to have such short rest periods between grow-outs to the point where in a little while we can experience one of the greatest shortages of [animals] in the country. This is based on biosecurity risks that arise from this. The owners of [the domestic processor] know that they are on a knife edge when it comes to rotation and farm capacity. You are talking about a farm cycling in 5 days!”

The industry standard of a two-week “cool-down” period is not meant to provide the farmer with a period of resting. In fact, it is meant to allow adequate time to properly sanitise and prepare the farms to receive the volatile infant animals. Without proper sanitisation, the domestic industry exposes itself to disease generation and a potential epidemic. Shifting from a six cycle production schedule to a seven cycle schedule has reduced the cool-down period by half. Farmers now have less time to prepare their farms and ensure that they are of an acceptable standard to grow healthy animals.

As I have argued before, the domestic processor owns the means to execute any of the above value-added appropriation tactics without the MNE’s involvement. The regional-MNE did not provide any tool or instrument that would enhance the domestic-processor’s bargaining position with farmers. However, the case study insight demonstrates a clear alignment of the domestic processor’s aggression towards the domestic farmers and the lock-in phase outlined in Chapter 6. Table 7.3

demonstrates the alignment between domestic processor lock-in and the adverse conditions being experienced by the domestic farmers.

Table 7.3 The upstream effects of 1st tier lock-in

Action by the domestic processor	Impact on the domestic farmers	Link to the regional-MNE's relationship
Misrepresenting input supply by providing underweighted grain supplies	Net grains used by farmers overstated. Farmers' conversion ratios become higher, leading to a reduction in their remuneration and value-added capture.	The link with the regional-MNE is based on correlation only. According to newspaper reports, this tactic was pursued in 2005. According to the case study timeline, 2005 marked the initial year of post-lock in bargaining pressure by the regional-MNE.
Volatile collection periods based on "alive" market prices	Collection periods outside of the efficient animal growth period affects farmers' conversion ratios, remuneration and value-added capture.	<p>The regional-MNE was able to use its bargaining position to access lengthier repayment periods (net 45 days). This negatively affected the domestic-processor's cash flow position.</p> <p>This adverse bargaining pressure presented liquidity problems, forcing the domestic-processor to exploit "alive" market volatility by amending the collection periods with farmers.</p>
Questionable input sourcing strategies by the domestic processor	<p>Increased low-quality sourcing affects the farmers' ability to produce consistent quality animals. This inconsistency is reflected in their conversion ratios, remuneration and value-added capture.</p> <p>Farmers are restricted to accepting input from the domestic-processor regardless of its quality. The risk associated with low-quality sourcing is borne by the farmer</p>	Respondent insight from the domestic processor note that the decision to look into lower price/quality sourcing was influenced by the bargaining and value-added appropriation pressure faced by the domestic processor.
Input manipulation by the domestic processor ¹⁶	<p>Input manipulation has mixed impacts for the domestic farmers. When the grain quality is superior, the farmers are able to produce good conversion ratios.</p> <p>Likewise, poor grains leads to unsatisfactory conversion ratios. This results in poor remunerations. In certain cases (ratios in excess of 2.50), payment is withheld by the domestic processor.</p>	<p>This variation in inputs is synced with the demand cycle of the regional-MNE. The regional-MNE accounts for, on average, 64% of the domestic processor's demand.</p> <p>In periods of high demand, the domestic processor is pressured to increase output. Failure to meet the regional-MNE's orders jeopardises the domestic processor's existence.</p> <p>In periods where the regional-MNE reduces its demand, the domestic processor needs to dampen production with minimal internal repercussions. A manipulation in input quality supply allows for (1) slower growth period or (2) higher farmer conversion ratios. In both cases, the disadvantages of demand concentration are externalised to the farmers.</p>
Increase in the "grow-out" yearly cycle	Additional grow-out period helps stabilize absolute losses brought about by 1-3 above. Even so, the farmer's relative value-added appropriation decreases. The farmers' income attributable to its capital and labour factor inputs also diminishes.	The population of domestic farmers faced pressures owing to actions 1-3. Farming numbers decreased by 25% while demand from the regional-MNE steadily increased. Regional-MNE demands were facilitated by increasing the number of grow-out cycles (beyond the industry standard).

Source: Author

¹⁶ Justification based on farmers' experience and other case study insight. No laboratory testing was performed to test this relationship. The domestic processor has also denied this action. Even so, it is presented here since the action is consistent with other details provided by the domestic processor.

Table 7.3 summaries what could be interpreted as a downstream transfer in value-added – a transfer that starts at the domestic farmers and terminates at the regional-MNE. The regional-MNE's quasi-internalization of the domestic processor provides a mechanism to extract value-added at will. This value-added appropriation pressure on the domestic processor has seemingly activated a latent asymmetric bargaining relationship with the domestic farmers. The end result is one where the regional-MNE is able to extract value-added from the domestic farmers in the absence of a formal or direct relationship with them. Any additional value-added captured by the domestic processor (from the farmers) can be renegotiated for and appropriated by the regional-MNE at will. The reduction in income by farmers is not merely a passive complaint. I began identifying potential interviewees one year prior to conducting the fieldwork. 24 farmers were identified during this process. When I arrived in the host country, five of these farmers had already closed their farms and four others are actively trying to sell their farms.

The domestic processor is acutely aware of the reduction in contract farmers. *P1* noted that they have recently had to build some of their own farms to deal with the shortfall in animal supply from closures. Two reasons were put forward by the domestic processor when questioned about the motivation behind the closures. One reason is the lack of personal investments by the farmers. *P1* argued that:

“Many of these farmers are not investing in their farms. Labour is a high cost now and to make money they need to automate their farms and invest in some of the new technologies that are on the market.”

This justification is not reconcilable with the insight summarised in Table 7.3. For instance, the decision to remove animals prior to the ideal growth phase is independent of the improvements that the farmer makes to the farm. Regardless of how well a farmer is able to rear the animals, a decision to withdraw the animals early will still negatively affect the conversion ratio. For instance, *F3* invested significantly in his farm through government loans and retirement pensions from his primary job.

When asked about the benefits attained from the improvements, the response was as follows:

“Well, this is the part that has disappointed me the most. I can see the material benefit from the new pens, the raised floors and the automation. My [animals] are growing better and I have less mortality but I am not seeing this in terms of return. Probably at first I noticed more money in grow outs but then that too started to drop. Now I can’t say that I am making any more money from all these changes”.

P9 offered a second rationale for the increase in farm closures over the last decade. The respondent noted that many of the farmers are approaching the age of retirement. In these circumstances, the inheritors of the estates, do not see farming as a glamorous profession. The respondent argued that rather than continue with and develop the business, many individuals are opting to downsize or divest from the industry. F17 offered a logical rebuttal to this supposition. The farmer noted that if this was indeed true, then the retired farmer can choose to hire management for the farm – under the condition that it was a profitable venture. Alternatively, a farmer could exercise the option to sell the farming operations to parties interested in entering the industry. But this is not possible given the minuscule income streams that the farms are currently generating.

7.3.3 Distilling the idiosyncrasies

The value chain under investigation has seen an increase in overall demand, coupled with knowledge and resource diffusion from the regional-MNE. These are all positive hallmarks of MNE host country activity (Javorcik, 2004). Even with these conventional positive indications, I have demonstrated that domestic actors within the chain are not able to reap benefits from these chain developments. In the previous section, I provided contextual insight to illustrate that this inability to capture value-added was not restricted to the domestic processor. Instead, the regional-MNE superior bargaining position with the 1st tier supplier acts as a mechanism to indirectly appropriate value from even lower tiers of the value chain. This was the primary

motive of this chapter – to provide a deeper understanding of the upstream effects of 1st tier lock-in and quasi-internalisation.

Even so, the empirical insight provided in this chapter can be construed as a contextualised account of the 2nd tier GVC engagement. The specific instruments by which the domestic processor is able to appropriate value-added from the farmers are unique to the industry under investigation (see Table 7.1). For instance, one can argue that it is the nature of the intermediary input that permits these actions by the domestic processor. The farming industry is a special case where the 1st tier supplier can opt to withdraw work-in-progress before its ideal state of readiness. In other industries, intermediate inputs may be characterised by a binary scale, where the input is only useable in a fully completed form.

I recognise that these contextual idiosyncrasies are significant enough to conclude that the findings are only relevant to the case study in question. These appropriation instruments will vary by industry and are contingent on, among other things, the characteristics of the intermediary good being exchanged. When I say instruments, I refer to the strategy that the 1st tier processor employs to exert the bargaining pressure needed to increase its appropriation of value-added. While these operational mechanisms may differ, the broader contextual conditions may have utility across industries. These are the conditions that aid 1st tier suppliers in its pursuit of value-added appropriation, namely the institutional voids common to developing nations and the frequency of 1st tier suppliers as integrators.

In line with this thesis, studies investigating economic upgrading are frequently conducted within a developing country context. While this thesis focuses on the interfirm relationships themselves, these relationships are embedded within a broader institutional framework (Pietrobelli and Rabellotti, 2011). That being said, developing countries are commonly positioned as having weak formal institutional frameworks (Mair and Marti, 2009). These weaknesses are reflected in the legal

framework and its enforcement, property rights and regulatory regimes (Williamson, 2000; Kafouros and Aliyev, 2016). Meyer et al. (2009) argued that institutions are 'weak' if they fail to ensure effective markets or even undermine markets (for instance, corrupt business practices). That being said, the bargaining and value-added appropriation mechanisms in Section 7.3.2 can be construed as manifestations of institutional deficiency. Two aspects stand out, namely collusion among domestic processors and raw material consistency.

Collusive behaviour among competitors is generally seen as anti-competitive (Siltaoja and Vehkaperä, 2010). These horizontal arrangements can undermine effective markets, disrupt the efficient allocation of scarce resources and dampen innovation (Baker, 2007). While developed countries enact and enforce policies to curb collusive behaviour (see Bruneckiene et al. (2014) for an overview), the developing world has lagged behind. This chapter has shown how this manifestation of institutional weakness can allow domestic firms to collectively close markets and extend bargaining power (Dunning and Rugman, 1985). Interview insight supports the existence of collusive behaviour among processors that serves to inhibit mobility and choice among farmers – thereby weakening their interfirm bargaining power. Similarly, extensive and prolonged quality issues within the industry inhibited 3rd tier firms from capturing value-added. These issues flourish in the absence of solid regulatory regimes and quality control apparatus. When these voids endure, they create opportunities for actors in the value chain to purposely externalise risk and appropriate value-added.

While the instruments exploited by the domestic processor are distinct (collusive behaviour and input inconsistency), they are facilitated through a broader institutional framework – one that is weak and unregulated. Other appropriation instruments are likely to emerge in different industries under a similar institutional context. This may

be especially so when domestic entities face downward pressure from the MNEs that orchestrate the GVC (Reinecke and Donaghey, 2015).

The international fashion industry provides a comparable illustration of how institutional deficiencies in developing countries can translate into appropriation instruments. Rossi (2013) investigated the Moroccan garment industry to determine whether there was a link between economic upgrading and the social welfare of domestic workers. It should be noted that the study positions upgrading as performing activities *deemed* to be of higher value-added. Even so, the author discovered that knowledge and resource transfers by the MNE did not always translate into better social welfare for the employees at lower tiers of the GVC (Sinkovics et al., 2016). In many instances, various tiers of supplying firms exploited local labour regulatory and enforcement voids to satisfy the growing requirements of the MNE (Barrientos et al., 2011). For instance, cyclical periods of increase MNE product demands drove domestic suppliers towards offering discriminatory working conditions to subsets of workers (Rossi, 2013). These workers were required to accept payments below the minimum wage while working longer than the standard recommended hours. They were also denied union representation and laid off when the MNE demand normalised or dipped.

There is a second general condition that can allow 1st tier suppliers to assume superior bargaining positions with lower tiers of the GVC. This thesis provided insight into a case study that featured a semi-integrated 1st tier supplier. Control over the flow of inputs to the lower tiers gave the domestic processor an added dimension to appropriate value-added. This GVC structure is not unique to the thesis's case study. For instance, Neidik and Gereffi (2006) noted that 1st tier garment manufacturers in Turkey functioned as semi-integrated entities. In addition to trimming and final packaging, they were also responsible for the fabric manufacturing aspect of the GVC (Neidik and Gereffi, 2006). This fabric is produced by the 1st tier suppliers and sold

to subcontractors who then undertake the majority of the garment manufacturing. Another iteration of an integrated sourcing approach is observable in the automotive value chain. Humphrey and Memedovic (2003) noted that the 1st tier supplier produced for and provided specific components directly to the assemblers (brand owners). Beyond this, they were also responsible for the management of 2nd tier suppliers and subcontractors (Humphrey and Memedovic, 2003). This included the sourcing the multitude of components needed by these lower tiers.

In both these cases, the 1st tier supplier controls component sourcing – either through manufacturing or direct procurement. This provides the semi-integrated scope that 1st tier suppliers may need to appropriate value-added from the lower tiers of the GVC. This scope can range from inflating the price of inputs supplied to subcontractors, to sourcing or manufacturing inputs of subpar quality.

This section provided parallel examples for both of the contextual dimensions observed in the thesis's case study. These parallel examples are not meant to infer that 1st tier suppliers in other industries will behave in a similar manner. Instead, it suggests that a broader set of conditions can be abstracted beyond the confines of this thesis's case study. Should the theorisations put forth in Chapter 6 have broader merit, then the upstream effects of 1st tier quasi-internalisation may be observable across various country and industry context.

7.4 Chapter conclusion

In this chapter, I investigated the upstream effects of GVC participation. As I have established elsewhere, these effects are studied within a value chain that has experienced 1st tier MNE quasi-internalisation. The insight provided in this chapter offers insight on how the strategic lock-in of key value chain nodes can extend an MNE's influence beyond direct engagement with the 1st tier.

Regarding this thesis's case study, the evidence from 1st and 2nd tier engagements illustrate a transfer of value-added appropriation pressure along the value chain. This

pressure coincides with the post lock-in period of the domestic processor's relationship with the regional-MNE. Making a statistical statement regarding causality between these two events is beyond the scope of this thesis. Even so, the qualitative insight from the case study suggests an alignment with the pressures faced by domestic farmers, and the demands made on the domestic framers by the regional-MNE. This alignment was described and illustrated in Section 7.3.2.

As the regional-MNE began to apply bargaining pressure, certain conditions were coercively agreed to by the domestic processor. As these demands intensified, the domestic processor was unable to meet its operational demands without adjusting its relationship with the domestic farmers. These adjustments increased uncertainty for the farmers while simultaneously reducing the value-added they were able to appropriate from the contractual relationship. I further argued that the asymmetric dependence relationship between the domestic processor and the farmers predated the regional-MNE's involvement. It, however, remained latent until the bargaining pressure by the regional-MNE was introduced within the value chain.

Through selective control of a key value chain node, the regional-MNE is able to extend its influence beyond its direct relationship with the domestic processor. None of the interviewed farmers has ever interacted or is familiar with the management at the regional-MNE. Even so, they remain beholden to its demands, albeit indirectly.

Chapter 8

Thesis conclusions

8.1 Connecting the thesis's contributions

This dissertation is a comprehensive investigation into the phenomenon of economic upgrading from GVC participation. Evident from Chapter 2, this phenomenon has not been a casualty research oversight. On the contrary, it has been a “front burner” issue in both academic and policy spheres for almost two decades (UNCTAD, 2011; 2013). Prior studies have adopted one of two framings to investigate these vertical host country implications of MNE activity – economic upgrading or linkage effects. As part of this study, I reviewed both these framings. This review suggested that much of the work on vertical linkage effects adopts an aggregate empirical analysis that prioritises absolute value-added gains. As a consequence, it has provided little insight into interfirm governance and the distribution of value-added (between the MNE and domestic firm).

The literature on economic upgrading is better positioned to shed light on the micro level organisation of GVCs. This is reflected in the case study insight on GVC governance and the process by which upgrading trajectories occur. Notwithstanding, I identified two key shortcomings within this literature stream. These shortcomings catalysed what I consider to be the foundation of this dissertation. First, issues of bargaining power and value-added distribution, while considered, are underdeveloped conceptually. In fact, studies frequently assume that economic upgrading fosters an interfirm relationship where the creation and appropriation of value-added are symbiotic. Second, the research agenda surprisingly lacks a well-articulated theoretical underpinning. In its absence, relationships have been theorised on simple logic and intuition.

These voids have provided an opportunity to problematize existing studies, and introduce a more complete conceptualisation of what firm-level economic upgrading

should represent (Chapter 4). To address the under-theorisation, I have adopted an abductive research approach where an a priori theoretical framework was constructed. Insights from TCE and power-dependence relations have been incorporated into this a priori framework. Approaching the phenomenon of economic upgrading and the context of GVCs from an abductive theory elaborating approach provides scope for multifaceted contributions. The application of a theoretical framework to a particular phenomenon is not only an opportunity to assess the applicability of extant theory. Instead, phenomena that have been previously studied in the absence of a strong theoretical underpinning also provide scope for the empirical insight to inform and develop existing theory.

This has been the approach throughout this research. The theoretical framework developed in Chapter 4 allowed for a more complete understanding of economic upgrading. Through stronger theoretical underpinning, we now have a deeper and nuanced understanding of the effect that upgrading trajectories may have on the domestic firm's ability to appropriate greater value-added. I will summarise this aspect in Section 8.1.1. Confronting the empirical world has also provided an opportunity to inform and elaborate on existing theory. Regarding this research, I argue that certain aspects of the data were not readily reconcilable with current readings of theory. This had provided scope for iterative matching, and an opportunity to elaborate on and develop extant theory. I will summarize this aspect in Section 8.1.2.

8.1.1 Contributions to our understanding of GVC participation and economic upgrading

The contributions in this section can be categorised as empirically related. While they conform to extant theorisation, the analysis provides important insight into how the phenomenon of economic upgrading is considered in both academic and policy spheres.

By problematizing empirical studies on economic upgrading, I have illustrated that there is little separation between value-added creation, and the domestic firm's ability to appropriate said value-added. Instead, it is frequently assumed that the latter will accompany the former. By disentangling the two core elements of economic upgrading, I have shown that it is possible for value-added creation and its appropriation to diverge – owing to changes in interfirm bargaining power. Consistent with the a priori theoretical framework, my case study data suggest that the domestic firm may find itself in this unfavourable bargaining position as a consequence of the upgrading trajectory itself. An upgrading trajectory may take the form of a specific asset or investment, one that has low redeployability and productive value outside of the MNE-domestic firm relationship. Even so, the MNE may reproduce similar relationships across geographic space. This can create unilateral dependence on the part of the domestic firm, thus locking it into the MNE's GVC.

The qualitative dimension of such lock-in has also been underdeveloped in prior empirical studies. Evidence from this thesis suggests that the paradox of upgrading was applicable to relative value-added. Respondents at the domestic processor noted that while absolute value-added on a sharp decline, the amount was still higher than what was earned before the MNE's entrance. I initially justified this research by arguing that studies focused on assessing aggregate gains to value-added fail to capture the distributional effects of upgrading (or linkage effects). Beyond asymmetry in the distribution of value-added, the empirical analysis illustrates a beholden aspect of unilateral lock-in. It not only restricts the domestic firm's ability to appropriate value-added from the relationship, but also quasi-internalizes its decision-making process.

A second empirical contribution emanates from the data collected at the 2nd – 3rd tier of the value chain. The GVC research agenda has offered little insight into economic activity that occurs outside of the MNE's direct engagement – usually 1st tier firms (Ponte and Gibbon, 2005). Research has only recently started to investigate the

effects of economic upgrading on the social actors within the domestic firm (Lee and Gereffi, 2015; Gereffi and Lee, 2016). The majority of these studies focus on the effect that economic upgrading has on the workers employed at the domestic firm that directly engages with the MNE (Rossi, 2013; Milberg and Winkler, 2011; Barrientos et al., 2011). Beyond this, little is known about the effects GVC participation on the upstream actors (firms \geq tier 2 of the GVC).

Chapter 7 of this dissertation provides insights that contributes towards filling this empirical void. The empirical analysis suggests that in the presence of 1st tier lock-in, the MNE can extend its control beyond its direct contractual relationships. The bargaining pressure that ensues post lock-in, can act as a mechanism to appropriate value-added from upstream actors. The empirical insight from the case study suggests that the conditions necessary for the 1st tier supplier to spread bargaining pressure to the 2nd tier predated the MNE's domestic involvement. However, its effects remained latent until post lock-in.

The mechanisms facilitating 2nd tier indirect appropriation may be idiosyncratic to the industry under investigation. Even so, I contend that these mechanisms are manifestations of more abstract conditions that share commonality across many developing countries that participate in GVCs. Using evidence from published studies, I categorised these conditions into two main aspects, namely the institutional voids common to developing nations and the frequency of 1st tier suppliers to act as integrators.

While reconcilable with extant theory, these insights offer meaningful contributions to studies on economic upgrading from GVC participation. To reiterate, the analysis suggest that it may be problematic to assume that *all* MNE-led upgrading trajectories can be constituted as an improvement in the domestic firm's ability to improve value-added. Upgrading as conceptualised in prior studies can actually constrain value-added appropriation for the domestic firm. These effects may not only reside at the

1st tier. The unilateral lock-in of 1st tier suppliers may represent selective control of key value chain nodes. These suppliers are well poised to act as surrogates - where value-added appropriation pressure can be transferred further upstream, on behalf the chain orchestrator (Wad, 2008).

8.1.2 Contributions to theory

The contributions summarised in Section 8.1.1 suggests that the a priori theoretical framework was able to explain much of the insights emanating from the case study. More specifically, the framework was consistent with, and able to explicate how an upgrading trajectory could facilitate the domestic firm's unilateral lock-in. However, I acknowledged at an early stage (Chapter 4) that certain aspects of GVC participation and economic upgrading were not reconcilable with mainstream readings of the theory. Consistent with abduction, I considered this misalignment as an opportunity for the empirical data to inform and assist in the elaboration of the two underlying theories that formed the basis for this investigation. I will revisit some of these theoretical insights in the following text.

The majority of the TCE driven literature posits that minimising the total cost of exchange drives the firm's choice of governance mode. This allows for maximising benefit from a given activity (Carter and Hodgson, 2006). While focus is usually placed on the cost of transacting, Williamson (1979, pp. 245) clearly states that cost economising "takes two parts: economising on production expense and economising on transaction cost". Beyond this, the firm's objective of accessing the lowest cost option – either through external procurement or internalisation is treated as a static assumption within prior studies (Roberts and Greenwood, 1997). This thesis adopts a dynamic perspective to investigate the GVC interaction between an MNE and a domestic firm. This investigation provided novel insight into this efficiency seeking assumption.

Redefining the cost minimising assumption

The insights afforded by this dissertation illustrates a case where the MNE may *intentionally* engage in an interfirm relationship (for a period of time) that undermines the core but static tenet of TCE. During this period of time, the relationship may fail to satisfy both of the cost economising elements outlined by Williamson (1979). This conforms to a manifestation of suboptimal contracting (Argyres and Liebeskind, 1999). While suboptimality has been the subject of theoretical discussion, it is usually considered from a constrained perspective, that is, the option of last resort.

Analysis of the case study evidence demonstrate that the MNE may *choose* suppliers that are underdeveloped in order to secure long-term appropriability. In the initial stages of the relationship, the process of MNE supported economic upgrading can alter the transactional dimensions of the governance relationship to facilitate unilateral lock-in. In other words, this insight shows that the MNE may not contract with the cost-minimising supplier, but rather the one that possesses scope for transactional manipulation. In this initial stage, the MNE forgoes private efficiency gains – both in terms of production costs and transaction-related costs.

Scope for economic upgrading itself can be considered as counterintuitive to the production cost aspect of TCE. It suggests that the domestic firm is not well equipped to offer the lowest cost alternative and the MNE is required to assist in remedying this capability deficiency. In terms of transaction-related costs, the analysis also suggested that the MNE is required to engage in substantial knowledge transfer, coupled with relationship monitoring and policing. These initiatives were not costless for the MNE (Teece, 1977). Such arguments become more pronounced when we consider the scope of the MNE and options for supplier engagement (Buckley and Ghauri, 2004). With this case study in particular, the MNE had an extensive supplier network at its disposal and was thus not constrained to enter into a suboptimal relationship. The process of replicating relationships, even at the expense of short-

term suboptimality, strengthens the MNE bargaining power across all of its 1st tier suppliers.

The key theoretical insight from this study revisits the cost minimising assumption that is frequently cited in academic studies (David and Han, 2004). When TCE refer to production cost expense, this need not be consistent with the supplier's production function. Instead, it may simply reflect the MNE's ability to negotiate for a lower contract price. Conversely, the governance structure that economises on transaction costs need not be the relationship that provides the MNE with the means to negotiate a lower contract price. Instead, the *net* cost minimising option will be reflected in the relationship that offers the MNE the most favourable interfirm bargaining position.

Suboptimality: a means of achieving bargaining asymmetry

The manifestation of suboptimal contracting is tied to the explanation for how the MNE may be able to assume a favourable interfirm bargaining position. This provides a contribution to our theoretical understanding of interfirm bargaining power. Studies commonly assume the MNEs dominate role in GVCs and its ability to appropriate the majority of value-added (Gereffi, 1994; Buckley and Strange, 2015). Even so, little is known of the manner in which this dominant position is attained. Instead, bargaining power is implicitly ascribed to the characteristics of each actor, where the MNE is positioned as having generalised power (Emerson, 1962). This thesis does not only conform to the theoretical argument that interfirm bargaining power is idiosyncratic, and is a property of each relationship (as opposed to the actors themselves). Instead, it provides a contextualised account of how this position of superior bargaining power can be achieved.

At the point of the MNE's entrance to the local market, the domestic firm's dependence on the MNE is insignificant. If the MNE attempted to negotiate for the majority of value-added then the domestic firm can exercise the option to walk away and continue supplying its existing market. Instead, I have illustrated a dynamic case

where the MNE is required to create a relationship of unilateral dependence – regardless of how underdeveloped the domestic firm may appear. The analysis demonstrates that suboptimality is a key component of constructing this dependence relationship. During this period of suboptimal engagement, the MNE is able to create what could be construed as an “unbalancing” operation. Favourable contracting terms and highly specified knowledge and resource transfers can act as a mechanism to remove the domestic firm from the market. It weans the domestic firm off its pre-existing supply base while simultaneously dampening its ability to redeploy operations, should the relationship be terminated.

8.2 Limitations of the study

As with any piece of academic research, certain limitations exist within this thesis. In certain instances, mitigating strategies were adopted to minimise its influence. In other instances, limitations were brought about simply by the research approach of the thesis and were less mitigatable. In both circumstances, it is important that full transparency be maintained. I have separated these limitations into sub-sections. 8.2.1 discusses the limitations related to the thesis’s methodology. It also provides some insight into how the effects of these limitations were addressed. 8.2.2 outlines the limitations of the thesis that are aligned with theory and its theoretical contribution.

8.2.1 Methodological limitations

The first methodological limitation is that of data coverage. As illustrated in Figure 5.2, the immediate scope of the thesis lies among the regional-MNE, domestic processor and the domestic farmers. Immediate scope refers to the value chain nodes where the collection of primary interview data was possible. The global brand owner (franchisor) was not part of this immediate scope as they were not receptive to participating in the data collection process. I was able to minimise the implications of this by drawing on the interview data provided by the regional-MNE and supplementing it with information that was publically available (annual reports and

media release). None the less, this impediment restricted my ability to gather deep insight into their strategic role in the orchestration of the GVC.

As previously mentioned, a core data collection method was interviews. I acknowledge that in many instances, the data used to piece together the dynamic perspective was derived from the interviews of high rankings members of the respective companies, many with personal ties. This was especially so for respondents at the domestic processor and farmers. This can expose the data to certain validity issues. A prominent one is that of interviewee exaggeration and embellishment (Berry, 2002). For instance, the domestic processor may be inclined to under-report the extent to which the MNE might have assisted their development. Likewise, the regional-MNE may feel obligated to overstate the role in helping the domestic processor. To dampen this effect, I ensured that there was overlap in the questions posed to all nodes of the GVC. This allowed for an element of within-method data triangulation (Mathison, 1988).

Interviews were conducted with other industry actors who did not have a similar personal link to any of the interviewees in the sample. This allowed for richer detail and also provided an opportunity to validate the authenticity of the responses. The industry expert (*IE1*) is a good example of this. The respondent is an independent actor and was in the industry during the developments that are of interest to this research. The respondent was thus well positioned to either support or contradict the story of the other interviewees with personal ties. Newspaper reports were also leveraged on to aid triangulation and provide richer contextual understanding.

It is also noteworthy to mention the manner in which changes in value-added were captured throughout the data collection process. Given the research context, the availability of financial data is limited. This is due to two main factors. First, the nature of the investigation deterred certain firms from providing material evidence related to their interaction within the GVC. Under the condition of anonymity, they were

prepared to speak about their experiences. Beyond this, they were not willing to make available paper documents or evidence that could be traced back to the establishment. The second factor is related to poor record keeping and is common at the farmer level of the value chain. While farmers were more willing to share documents (e.g. contracts), many of them did not retain proper accounting records. Given these limitations, insight on value-added changes was based on qualitative responses from the interviewees – rather than quantifiable numbers. This limited my ability to determine the exact effect that changes in interfirm bargaining had on value-added appropriation.

Another methodological limitation is related to potential conflicts with the philosophical underpinning of this thesis. The objectivist ontological stance of this thesis assumes that the phenomenon is an objective occurrence, one that can be observed across individuals, regardless of their individual perceptions. Qualitative primary data such as interview insight can introduce elements of subjectivity, based on respondents' personal experiences or emotional predispositions. For instance, a key element of this thesis involves asking respondents at the domestic processor and regional-MNE whether they were satisfied with the returns they were receiving from their interfirm relationship. Probing issues such as satisfaction with value-added distribution can introduce subjective responses that may be based on relational aspects not directly tied bargaining power and value-added appropriation. For example, a particular respondent at the domestic processor may have little affection for their regional-MNE counterpart thus triggering a personal dissatisfaction with the regional-MNE relationship. To address this, the interview questions were designed to solicit examples from the respondents on specific aspects of the relationship that created bargaining pressure and dissatisfaction. This allowed for more objectivity in the analysis process as solid evidence could be used to justify the source and relevance of the dissatisfaction.

Subjectivity can be introduced beyond considerations around misdirected satisfaction. This is especially so when a research project confronts issues such as value-added creation and its appropriation. Issues of a “fair” distribution are usually contentious and can be construed based on individual perception (Daverth et al., 2016). For instance, respondents at the domestic processor may not believe that the value-added they appropriate from their participation in the GVC represents a fair compensation for the factor inputs devoted to the relationship. However, this thesis was not concerned with assessing the fairness of the distribution of value-added. Instead, it is interested in understanding how this distribution changes over time and the role that economic upgrading plays in the process. Even so, it is likely that such “fairness” dissatisfaction manifested itself in the interview insight. Added effort was required to delineate the objective factors that affect the value-added distribution. Interviewees were asked to provide a clear idea of whether value-added appropriation was increasing or decreasing and how these changes compared to pre regional-MNE situations. Interviewees were encouraged to provide descriptive examples to illustrate these changes.

The final methodological issue relates to my role in the collection of primary data. Interviews were conducted personally where I was able to interact with and gain insight directly from actors in the GVC. In certain regards, this personal engagement allows for richer data collection potential. For instance, observations gathered from being on production sites fed into the interview protocol and allow for greater insight. A benefit that could not be realised from remote interviews or surrogate interviewers. Even so, this approach to primary data collection can give rise to potential methodological issues. While this thesis did not aim to test theory, it did incorporate a framework that posited an a priori logic. This provided a degree of structure to the interview protocol. While effort was made to avoid leading questions, any noteworthy structure to an interview is likely to induce respondents into making assumptions regarding the ideal responses. This may be more so the case when the project owner

conducts the interviews. Elements of the framework may unconsciously find its way into the discussion. To minimise the effect, I adopted two strategies. First, I encouraged respondents to provide clear examples to justify particular responses. Second, any response that was susceptible to lead question enticement was quickly flagged and reintroduced with a different framing at a later point during the interview. Both responses were then compared to determine consistency.

8.2.2 Theoretical limitations

This thesis has been empirically informed by data from a single embedded case study. This research strategy presented a theoretical compromise. In Chapter 3, I argued that a single embedded case study design was necessary to provide depth and richness of empirical insight. This was crucial to facilitate the development of novel theoretical insight. To avoid monotony, I will not rehash these arguments.

However, leveraging on depth came at the expense of claiming statistical generalisability. For instance, the abstraction in Chapter 6 has provided a novel theoretical argument for suboptimal contracting in TCE. This theorisation provided an explanation of the relationship and the conditions under which it is likely to occur. By focusing on this aspect of a theoretical contribution, I am unable to determine how often it occurs. Moreover, I am restricted from making any statistical claims on its validity across other contextual dimensions (for example industries). To make these claims, further testing is necessary.

I, however maintain, that the findings contained in Chapter 6 and 7 are legitimate within the conditional boundaries articulated throughout the analysis. These conditions were outlined at various points of the thesis. For instance, Section 6.4 elaborated on our current understanding of suboptimal contracting. I presented the extant arguments and contended that they were inadequate to explain the relationship observed in the empirical data. I then presented an alternative theoretical explanation which is better aligned with the abstracted conditions observed. Similarly,

Section 7.3.3 accepted that the insight from Chapter 7 could be construed as a contextualised account of the 2nd tier GVC engagement – owing to the descriptive insight presented throughout the chapter. Section 7.3.3 addressed this by attempting what I coined “idiosyncratic distillation”. While this was not a claim to generalisability, it was intended to illustrate the potential for wider applicability- owing to what could be considered common conditions across contexts (based on prior published insight).

8.3 Implications of the research

A doctoral thesis is usually positioned a piece of work aimed at making a contribution towards theory. This has been the theme throughout this document. Even so, it is necessary that these the research findings offer utility to a wider demographic. I will focus on the implications to (1) national policy makers (2) domestic firms in developing countries. This will be outlined in sections 8.3.1 and 8.3.2 respectively.

8.3.1 Policy implications

The domestic host country implications of international business have always been neatly separated into potential positive and negative effects. These relationships and the various moderating factors were discussed in Chapter 2. Despite the potential for both negative and positive consequences, recent policy positions have always been favourable towards foreign investment and MNE activity (Mattoo et al., 2004). In fact, encouraging international business activity is frequently the goal of most developing country government agencies charged with trade development. The desire to achieve this goal is usually supported by many forms of government incentivising (Goodspeed et al., 2007).

There are prominent government initiatives that support the assumption that aggregate increases in foreign activity are beneficial to the host country. The “Make in India” program that started in 2014 is a good example. Official governmental literature contends that the campaign will aid in the facilitation of investment, foster innovation and enhance local skill development (PM India, 2017). This position is

also adopted by many developmental agencies charged with offering policy advice to nations. In 2014 for instance, the OECD released an Investment Policy Review on Myanmar where it sort to prescribe strategies for growth and development. In the report, the organisation suggested that an improved climate for foreign investment would “promote linkages with local companies that will trigger skills upgrading, technology and knowledge transfer” (OECD, 2014b pp. 149).

In both of the above policy examples, a key aspect of perceived benefits is consistent with the notion of upgrading trajectories. This thesis has argued for greater attention to the value-added appropriation facet of upgrading – a key shortcoming of the existing conceptualisation. It has illustrated, through a single case study, that the linkage and upgrading effect of inward international business activity may have a paradoxical effect. What was considered a core and clear benefit to policymakers, now require deeper consideration. As previously noted, the findings and theoretical insight emerging from this thesis require empirical testing. Even so, these initial findings suggest a need to move away from blanket policies aimed at soliciting all manners of international business activity.

8.3.2 Managerial implications

Imperfect information in interfirm relationships is a frequent reality. This is the assumption that underpins the argument of incomplete ex-ante contracting (Lim, 2001). As this research has illustrated, one party to the contract may have more complete information than the other. For firms in developing countries, this asymmetry of information is usually more pronounced. This variation can, for instance, be partially attributed to their lack of international experience.

My research findings provide a dynamic view of how bargaining power can come to fruition. The possibility exists for domestic firms to translate these findings into strategic guidance as they embark on the complex process of contractual negotiation. Bargaining power is a function of dependence and it essential that new interfirm

relationships do not negatively influence the domestic firm's dependency structure. For instance, GVC participation should be seen by domestic firms as an opportunity for market development or extension. It should not constitute market replacement - even with the lure of knowledge transfer and learning opportunities.

8.4 Future research directions

The research approach guiding this dissertation was multi-pronged, thus making it an inherently complex process. As such, it was important that the focus is restricted to ensure that ample attention is placed on each element of the research process. Such restraint leaves scope for future research opportunities. The following are some of these opportunities.

Regarding this project in particular, additional insight from other actors within the GVC will provide deeper insight on the manner in which the chain is orchestrated. In particular, the role of the global brand owner is underrepresented in the current study. The regional-MNE has acknowledged their role in linking globally disbursed franchisees. Even so, greater insight on their capacity as a transferor/facilitator of key knowledge will be useful to the theorisation process.

As I have acknowledged in the limitations section of this chapter, the theoretical arguments advanced has been derived from a single embedded case study. These insights require further testing so as to determine its generalizable utility. This can be done in the form of additional small sample case studies across different industries and contexts. Alternatively, the theoretical insights can be tested on quantitative secondary data. The latter will require the researcher to further operationalise core constructs and acquire suitable data sources. Beyond this, the empirical evidence and theoretical discussions have been presented in a narrative manner. While this has facilitated deeper discussion and argumentation, more precise and testable propositions will need to be developed for testing.

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Appendix A: A review of economic upgrading

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
Gereffi (1999b)	The author cites the “global commodity chains framework”. No mention of an underlying or substantive theoretical logic	Empirical paper: The apparel industry in Asia is the context of focus	Organizational learning to improve the position of firms or nations in international trade networks. It facilitates the domestic firm’s movement into more profitable and/or technologically sophisticated capital and skill-intensive niches	At the firm level, the author proxies upgrading as (1) movement from simple to complex products, (2) movement from small to large orders (3) movement assembly to OEM and OBM export roles
Kessler (1999)	The author cites the “global commodity chains framework”. No mention of an underlying or substantive theory	Empirical paper: The apparel industry in Mexico post-NAFTA is the context of focus	Upgrading as the manifestation of knowledge/technological transfers and skills development to foster development	The movement up the chain into activities that are deemed to be of higher value-added.
Gibbon (2001)	A review paper of works that are conducted from the “global commodity chains” perspective	Analytical review paper. Takes stock of the “global commodity chains” agenda	The concept of industrial upgrading is used multiple times throughout the paper. However, no formal definition has been proposed	Upgrading proxies suggested include (1) capturing higher margins for unprocessed commodities, (2) producing new forms of existing commodities
Humphrey and Schmitz (2002)	Interfirm governance is seen as the moderating factor for upgrading. TCE is introduced to explain why certain governance structures may exist in certain exchange relationships	A literature review paper synthesizing the GVC and Industrial clustering literature streams.	Learning by doing through the allocation of new activities by lead/MNE firms. One of the first papers to proposed the now widely used trajectory classifications: (1) process upgrading, (2) product upgrading, (3) functional upgrading and (4) inter-sectoral upgrading	Upgrading manifested in improved products, processes or new functional areas
Bessant et al. (2003)	Reference is made to GVC theory. Proper theoretical development is absent from the paper. Underlying logic is driven by the presence of MNE FSA and knowledge transfer through engagement	Exploratory case study with focus on the timber industry in South Africa	Upgrading defined as learning and capability development from GVC participation	Specific dimensions highlighted: (1) process efficiency, (2) Introducing new products, (3) developing new function areas (4) moving into a new value chain
Bair and Gereffi (2003)	Authors cite the “global commodity chains framework”. No mention of an underlying or substantive theory	Empirical paper: The apparel industry in Mexico and the Caribbean Basin post-NAFTA are the contexts of focus	Industrial upgrading defined as the movement to higher-value activities in global supply chains	In the context of the apparel industry, the authors operationalize upgrading as instances where the domestic firms move from standardised assemblers to original equipment manufacturers to eventually own brand manufacturers
Lorentzen and Barnes (2004)	Proper theoretical development is absent from the paper. Underlying logic is driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: The South African automotive industry is the context of focus	Upgrading as learning and innovation	Investments in R&D activities, including (1) In-house product development (2) R&D expenditure (3) International standards e.g. ISO 9000
Hassler (2004)	Authors cite the “global commodity chains framework”. Four dimensions of global commodity chains are highlighted (1) input-output	Empirical paper: Indonesia’s clothing/apparel industry is the context of focus. Data is qualitative	Emphasis placed on upgrading as a production efficiency improving mechanism.	Evaluating firm-level strategies to determine its ability to achieve higher performance of production units. These strategies include (1)

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
	structures (2) territoriality (3) governance structure (4) institutional framework. No mention of an underlying or substantive theory			training and skills improvement (2) improving manufacturing processes
Tokatli and Kizilgün (2004)	Authors cite the "global commodity chains framework". No mention of an underlying or substantive theory	Empirical paper: Turkey's clothing/apparel industry is the context of focus. Data is qualitative	The authors propose three classifications of upgrading (1) doing things better (2) Making better things (3) moving into higher value-added stages of the value chain	Focus on observable instances of shifts into what could be considered process improvements (new machinery), new products or new activities (R&D or marketing)
Giuliani et al. (2005)	Reference is made to governance with mention of three governance structures (1) network (2) quasi-hierarchy (3) hierarchy. Proper theoretical development is absent from the paper. Underlying logic is driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: Various Latin American clusters are the contexts of focus. Mixed data sources (quantitative and qualitative)	Upgrading construed the capacity of a firm to make better products, make them more efficiently, or move into more skilled activities. Paper employs convention classifications of process, product, functional and inter-sectoral upgrading	Process upgrading captured in developments such as (1) certification and process improvement initiatives. Product upgrading proxied by the entrance into new product. Functional upgrading captured by moves into marketing activities
Pickles et al. (2006)	No mention of an underlying or substantive theoretical underpinning	Empirical paper with focus on functional upgrading: East European apparel industry is the context of focus	A staged approach to upgrading as the movement from export-oriented assembly to more integrated forms of manufacturing and marketing	Empirical evidence that suggests a move from assembly, or full-bundle activity, to OEM, which may involve more in-house design or full package manufacturing.
Tokatli (2007b)	No mention of an underlying or substantive theoretical underpinning	Empirical paper: focus on functional upgrading: Turkish apparel industry is the context of focus. Data is qualitative	No explicit definition offered by the author. Implicitly, upgrading is treated as the firm's ability to move into activities of higher value-added	Author uses the movement into functional activities such as design, marketing and own brands as a proxy for upgrading
Tokatli (2007a)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: focus on functional upgrading: Turkish apparel industry is the context of focus – with particular focus on the case study of Hugo Boss's relationships in Turkey. Data is qualitative	No explicit definition offered by author. Implicitly, upgrading is treated as the firm's ability to move into activities of higher value-added	Performing activities more efficiently or adding new products to the manufacturing process are positioned as instances of upgrading. Particular focus is placed on the movement into functional activities such as design, marketing and own brands as a proxy for upgrading
Evgeniev and Gereffi (2008)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: focus on the textile and apparel industry and firms in Turkey and Bulgaria. Data is a mixed between qualitative and quantitative export data	Upgrading classified as the movement into higher value-added roles. The definition emphasizes the desired outcomes of (1) profits (2) price mark-ups (2) value-added	The authors contend that it is difficult to access data on the profit and mark-ups levels of domestic firms. Paper relegates upgrading to the execution of activities deemed to be of higher value-added.
Gibbon (2008)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic driven by the presence of MNE FSA and knowledge transfer through engagement.	Empirical paper: focus on the apparel industry in Africa. Data is qualitative	Upgrading as (1) the acquisition of capabilities and accessing of new market segments through GVC participation. It permits domestic firms to shift into more rewarding functional positions, or by making products that have more value-added	Proposed operationalization leverages on observational evidence of shifts in the operational scope of the domestic firm.

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
	MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance			
Morrison et al. (2008)	This paper is a review of the existing work on GVC analysis and economic upgrading	Critical review of the global value chain (GVC) literature	Upgrading positioned as capability development. It includes the conventional "climbing up" the value chain but should also encompass the deepening the capabilities within the same functions or in additional functions	This is not an empirical paper. However, the authors call for greater focus on capturing the learning and innovation that occurs within the domestic firm
Selwyn (2008)	The author cites the "global commodity chains framework". No mention of an underlying or substantive theory. Chain governance positioned as a key determinant of upgrading	Empirical paper: focus on Brazilian Horticulture Industry. Data are qualitative	The author considers upgrading to be the ability for firms in less developed countries to integrate into global markets on a higher value-added basis	Manifestation of upgrading captured in (1) higher quality products (2) produce more efficiently (3) developing or adding to the activities performed by domestic firm
Sturgeon and Gereffi (2009)	Paper is a call for greater focus on improved measures of industrial upgrading and technological learning	A perspective paper on GVC and the need to develop measurements within the research agenda	Learning positioned as the cornerstone of upgrading. For countries that are behind, the authors posit that learning, at least in part, must come from absorbing knowledge created elsewhere (i.e. GVC participation). This facilitates the process of moving from low-value to relatively high-value activities	The authors do not propose measures for upgrading per say. Instead, emphasis is placed on developing new ways to measure and analyse the global fragmentation of trade brought about by rising GVCs.
Saliola and Zanfei (2009)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic and hypotheses driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: focus on various industries in Thailand. Data is derived from Productivity and the Investment Climate Survey (PICS)	The authors define upgrading as domestic firm innovation to increase value-added	This paper does not examine the factors that affect upgrading. Instead, it analyses the factors that affect the governance mode that the MNE may choose to adopt. The domestic firm capability is seen as a key factor in the MNE governance mode chosen. Domestic firm capability captured through domestic patents filed or new technologies developed
Ponte and Ewert (2009)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic and hypotheses driven by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: Findings are on South African Wine. Data is mixed	Upgrading is approached from a broader perspective and taken to mean the domestic firm's ability to achieve "a better deal"	Product upgrading captured in measures such as the unit price of the product, overall intrinsic quality, Process upgrading measured by improvements in managerial systems, winemaking practices and viticultural practices. Authors argue that many of these measures of upgrading did not necessarily translate into higher value-added
Ivarsson and Alvstam (2009)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the	Empirical paper: focus on the GVC linkage effects of Swedish MNEs in emerging countries	No explicit definition of upgrading provided. Implicitly, upgrading is positioned as the ability of the domestic firms to improve their position in	MNE assisted upgrading captured by, for example, (1) improvements to existing production technologies (2) collaborative

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
	presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance		the GVC by process, product and function improvements.	R&D projects with the MNE (3) assistance with achieving quality assurance standards
Ivarsson and Alvstam (2010)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance	Empirical paper: focus on the GVC linkage effects of Swedish MNE IKEA with Chinese and South East Asian domestic firms. Questionnaire data used by authors	The opportunity for domestic firms to seize opportunities from value chain participation. These opportunities permit the improvement of operations and market positions	Upgrading is operationalised in the form of MNE led learning and assistance. The authors captured this in, for example, (1) support to improve production technology (2) training programs for suppliers (3) advice on production layouts (4) financial assistance to purchase upgraded machinery
Ivarsson and Alvstam (2011)	This paper is an extension of Ivarsson and Alvstam (2010). In this case, the authors use primary interview data to provide a more contextualised and descriptive perspective of the GVC participation by the Chinese and South East Asian domestic firms. The definitions and operationalisations is consistent with of Ivarsson and Alvstam (2010)			
Fernandez-Stark et al. (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement.	Empirical paper: focus on the upgrading of service-oriented firms in the various developing countries	Upgrading is positioned as the process of moving into more profitable and/or technologically advanced niches	Trajectories are considered to be instances of upgrading. For instance (1) shifting from basic services to services of higher value-added (2) new functional areas e.g. the shift from information technology outsourcing (ITO) to knowledge process outsourcing (KPO)
Özatağan (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance	Empirical paper: focus on the upgrading of automotive component suppliers in Bursa. Survey and interview data used.	Upgrading classified as the movement into higher value-added roles. The traditional typology of process, product and functional upgrading is used.	The empirical evidence used to suggest upgrading included (1) suppliers' ability to gain competence in design and product development (2) Improvements in the production processes (3) innovation in human resource management
Navas-Alemán (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance	Empirical paper: focus on the upgrading of firms in the Brazilian Furniture and Footwear Industries. Data collected by way of interviews and a questionnaire survey	Upgrading is construed as the ability for domestic firms to move into higher value-added activities. These activities offer better remunerated (higher margins) and have higher entry barriers because the skills required are difficult to replicate	Upgrading is operationalised by use of specific categorizations. These include, for example, (1) new production machinery (2) employee training (3) increased product quality (4) reduced delivery times (5) introduction of new management techniques Responses solicited on a scale of 1–5

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
Fold and Larsen (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement.	Empirical paper: focus on the upgrading of agro-food producers in Africa.	Employs the widely used trajectory classifications: (1) process upgrading, (2) product upgrading, (3) functional upgrading and (4) inter-sectoral upgrading	Proxies utilised include (1) increasing the quality, volumes and reliability of supplies, and (2) producing new forms of existing commodities.
Azadegan and Wagner (2011)	Hypotheses developed from intuition and logic. No reference to a substantive body of theory.	Empirical paper: focus on the upgrading of manufacturing firms from Far East countries.	Reference is made to industrial upgrading. Industrial upgrading is framed as a learning mechanism.	Data collected via survey responses from domestic firms. Instances of upgrading were captured by (1) the number of new products introduced by the firm (2) percentage of sales attributed to this new line and (3) R&D intensity.
Barrientos et al. (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	The paper can be considered perspectives oriented. It discusses the extent to which economic upgrading can lead to social upgrading for other actors in the GVC.	Upgrading is treated as the movement into higher value-added activities in production. This movement improves technology, knowledge and skills.	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Frederick and Gereffi (2011)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement	Empirical paper: focus on upgrading in the apparel industry with emphasis on Asia and Central America.	No explicit definition offered by the author. Implicitly, upgrading is treated as the firm’s ability to move into activities of higher value-added	Upgrading is said to be captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Morris et al. (2011)	The paper provides descriptive insight into the domestic industries. No mention of theory is made.	Empirical paper: focus on upgrading in the clothing sectors of Lesotho and Swaziland.	Upgrading is defined as moving to higher value activities in GVCs in order to increase the benefits (e.g., security, profits, skill, technology or knowledge transfer).	Upgrading is said to be captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Herrigel et al. (2013)	The paper utilizes insights from organisational learning theory	Historical perspective on the upgrading of Chinese manufacturing firms. Data collected through interviews domestic firms and MNEs.	Upgrading is positioned as a process of learning. This learning process allows firms to transform their operations into more sophisticated areas	No measures or proxies were explicated.
Marchi et al. (2013)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper.	A perspective paper connection between environmental performance and economic upgrading. Authors use insight from case studies	Authors consider economic upgrading as the process by which economic actors – nations, firms and workers – move from low-value to relatively high-value activities in global production networks	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
De Marchi et al. (2013)	Reference is made to the “global value-chain perspective”. Proper theoretical development is absent from the paper. Underlying logic by the	The paper looks specifically at the role that lead firms in GVCs play in shaping the green and environmental	Economic upgrading is positioned as improvements in the technical and operational capabilities of domestic firms.	As economic upgrading is not the primary focus of the paper, no proxies were proposed.

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
	presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	activities of features of upstream activities Case study insight from Swedish furniture manufacturer, IKEA is incorporated.		
Kadarusman and Nadvi (2013)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	Empirical paper: focus is on upgrading in the Indonesian electronics and garment sectors	No explicit definition of upgrading is provided. However, its use of conventional upgrading trajectories as proxies can lead one to assume the upgrading is treated as firm's ability to move into activities of higher value-added	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Ponte et al. (2014)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	Empirical paper: focus is on upgrading in aquaculture value chains. Beyond the influence of lead firms, the paper also investigates the role of domestic regulatory frameworks in facilitating upgrading. Interviews conducted across four countries (Bangladesh, China, Thailand, and Vietnam).	Upgrading is approached from two perspectives: 1. From a broader perspective and taken to mean the domestic firm's ability to achieve "a better deal" 2. As moving to higher value activities in GVCs in order to increase the benefits (e.g., security, profits, skill, technology or knowledge transfer).	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Ravenhill (2014)	No theory applied, tested or developed.	Commentary paper that discusses the adaptation of GVC frameworks by Multilateral Economic Institutions	Economic upgrading is positioned as improvements in the technical and operational capabilities of domestic firms.	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Puppim de Oliveira and de Oliveira Cerqueira Fortes (2014)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper.	Empirical paper: It discusses the extent to which economic upgrading can lead to social upgrading for other actors in the GVC. Focus is on Brazilian agro-industrial sector.	Economic upgrading is defined as the process that enables local producers to achieve higher levels of productivity and to move into higher value-added aspects of production	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Morris and Staritz (2014)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement.	Empirical paper: focus is on upgrading in Madagascar's export apparel industry.	Upgrading is broadly defined as moving to higher-value activities in value chains to increase the benefits from participating in global production.	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.

Author/s and year published	Theoretical lens used	Paper classification	Economic upgrading definition	Economic upgrading proxies used/proposed
	MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.			
Lee and Gereffi (2015)	MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	Review paper on the link between economic and social upgrading	Upgrading is defined as the process of improving the ability of a firm or an economy to move to a more profitable and/or technologically sophisticated capital- and skill-intensive economic niche.	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
(Khan et al., 2015)	Reference is made to prior studies on upgrading, linkages and knowledge transfer. No reference to a substantive body of theory.	Empirical paper with focus on automotive parts suppliers in Pakistan	The paper defines upgrading "the firm's ability to move up in the value chain, by designing and introducing advanced product lines, superior technological processes and logistics systems and by elevating to become a system and advanced design suppliers."	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Blažek (2015)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	Review paper on the various upgrading strategies pursued by firms in GVCs	Upgrading is defined as a shift to higher value-added activities in production, to improve technology, knowledge and skills, and to increase the benefits or profits deriving from participation in GPNs'	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.
Barrientos et al. (2016)	No theory applied, tested or developed.	Editorial paper discussion the "new dynamics" of upgrading in GVCs	Upgrading is defined as suppliers moving to higher value activities	No measures or proxies were explicated.
Gereffi and Lee (2016)	Reference is made to the "global value-chain perspective". Proper theoretical development is absent from the paper. Underlying logic by the presence of MNE FSA and knowledge transfer through engagement. MNE governance is seen as a moderating factor, the typology by Gereffi et al. (2005) is used to explain interfirm governance.	Perspectives paper discussing the importance of governance for economic and social upgrading from GVCs	Economic upgrading is defined as the process by which countries and firms moving to higher value activities in GVCs with improved technology, knowledge, and skills.	Upgrading is captured in the traditional trajectory view of: (1) Product, (2) Process, (3) Functional and (4) Chain.

Source: Author

Appendix B: Project ethical approval

Performance, Governance and Operations
Research & Innovation Service
Charles Thackrah Building
101 Clarendon Road
Leeds LS2 9LJ Tel: 0113 343 4873
Email: ResearchEthics@leeds.ac.uk



UNIVERSITY OF LEEDS

Miguel Dindial
International Division, LUBS
University of Leeds
Leeds, LS2 9JT

ESSL, Environment and LUBS (AREA) Faculty Research Ethics Committee University of Leeds

Dear Miguel

Title of study: Global value chain (GVC) participation and economic upgrading: a developing country perspective
Ethics reference: AREA 15-035

I am pleased to inform you that the above research application has been reviewed by the ESSL, Environment and LUBS (AREA) Faculty Research Ethics Committee and I can confirm a favourable ethical opinion as of the date of this letter. The following documentation was considered:

Document	Version	Date
AREA 15-035 Ethical_Review_Form_Miguel Dindial.pdf	1	22/10/15
AREA 15-035 DRAFT_Information sheet_Miguel Dindial.pdf	1	22/10/15
AREA 15-035 Participant_consent_form_lowrisk_Miguel Dindial.pdf	1	22/10/15
AREA 15-035 fieldwork_assessment_form_low_risk_2013_Miguel Dindial.pdf	1	22/10/15

Please notify the committee if you intend to make any amendments to the original research as submitted at date of this approval, including changes to recruitment methodology. All changes must receive ethical approval prior to implementation. The amendment form is available at <http://ris.leeds.ac.uk/EthicsAmendment>.

Please note: You are expected to keep a record of all your approved documentation, as well as documents such as sample consent forms, and other documents relating to the study. This should be kept in your study file, which should be readily available for audit purposes. You will be given a two week notice period if your project is to be audited. There is a checklist listing examples of documents to be kept which is available at <http://ris.leeds.ac.uk/EthicsAudits>.

We welcome feedback on your experience of the ethical review process and suggestions for improvement. Please email any comments to ResearchEthics@leeds.ac.uk.

Yours sincerely

Jennifer Blaikie
Senior Research Ethics Administrator, Research & Innovation Service
On behalf of Dr Andrew Evans, Chair, [AREA Faculty Research Ethics Committee](#)
CC: Student's supervisor(s)

Appendix C: Participant information sheet

PARTICIPANT INFORMATION SHEET

PROJECT TITLE: Global value chain (GVC) participation and economic upgrading: a developing country perspective

Dear sir/madam,

My name is Miguel Dindial and I am a PhD candidate at the University of Leeds, UK. I am a native of Trinidad and Tobago and my research is being funded by the government of Trinidad and Tobago. My research involves an investigation into how multinational enterprises (MNEs) organise their value chains and the role that firms in developing countries play in this process. In the process, the study will look at the implications for the domestic firms and the extent to which they have been able to upgrade from participation. The study is case-based and I have identified the [specific industry and country] industry as an appropriate industry to study.

Your firm has been identified as an integral actor in the [industry] value chain and your participation in the research project would add substantial value to its contribution. As part of the study, you would be asked to share your experiences as a participant in the industry. More specifically, your feedback would be appreciated in areas such as:

- the size and scope of your business as it relates to the [specific] industry
- your primary intermediate interactions (buyers and sellers)
- general details on the contractual arrangements with these primary buyers and sellers
- any organisational changes that have occurred as a result of these contractual arrangements and the impact it has had on your ability to generate greater profitability

Your experiences will be solicited via an interview and/or questionnaire. All data collection will be undertaken by me personally and I estimate that the entire process will not exceed one hour in duration. Please note that your participation will offer no monetary compensation. However, should you be interested, I would gladly provide a summary of the research findings. The process is entirely voluntary and you can refuse to answer or respond to any question that you deem inappropriate. Once the interview/survey has been completed, I will offer you an additional window of two weeks in which you can withdraw your participation.

I also wish to advise you that your input is strictly confidential and will not be used for any purpose outside of this project. Your responses will be anonymised and no details will be included that may allow others to identify you as a participant in the project. We also understand that some of the firms operate in value chain segments that have few other competing companies. As such, you may assume that this will allow readers to narrow down potential respondents. However, I wish to reassure you that extra effort will be made to ensure anonymity. This will include:

- ensuring no specific detail regarding firm size, geographic location or clients is included
- providing no specific detail regarding organisational structure or hierarchical positions

I would like to take this opportunity to thank you for considering participating in this research project. I am also available to answer any further questions that you may have. I can be contacted via the following channels:

- Telephone: +44(0)7999293979
- Email: bn10m2d@leeds.ac.uk

Best wishes,
Miguel Dindial
PhD Candidate
University of Leeds

Appendix D: Participant consent form



Leeds University Business School (LUBS)

UNIVERSITY OF LEEDS

Consent to take part in an investigation into the prospects for upgrading via global value chain (GVC) participation

	Add your initials next to the statements you agree with
I confirm that I have read and understood the information sheet/ letter dated [insert date] explaining the above research project and I have had the opportunity to ask questions about the project.	
I agree for the data collected from me to be stored and used in relevant future research in an anonymised form.	
I understand that relevant sections of the data collected during the study, may be looked at by individuals from the University of Leeds or from regulatory authorities where it is relevant to my taking part in this research. I give permission for these individuals to have access to my records.	
I agree to take part in the above research project and will inform the lead researcher should my contact details change.	

Name of participant	
Participant's signature	
Date	
Name of lead researcher	Miguel Dindial
Signature	
Date*	

<i>Project title</i>	<i>Document type</i>	<i>Version #</i>	<i>Date</i>
Global value chain (GVC) participation and economic upgrading: a developing country perspective	consent form for participation		

Appendix E: Sample semi-structured interview protocol (anonymised)

Domestic processor protocol¹⁷

Aspect to be captured	Category	Interview questions
Level of firm development	Firm attributes (historical & current)	A1- What is your position in the company?
		A2- How long have you been employed at this company?
		A3- When was your company established?
		A4- Can you provide an overview of your firm's history
		A5- How many persons did you initially employ?
		A6- What would you say was the firm's core business activity when first established?
		A7- Aside from this core activity, what other areas of business where you involved in at the time?
		A8- Who were your main markets/clients at that time?
		A9- What was your initial production capacity at that time and how was this allocated?
		A10- How has your business evolved over time? Are you currently involved in new industries/ activities e.g. feed production; breeding labs etc.
		A11- Can you provide an overview of your company's current operations, and its organisational structure (divisions e.g. production, administration etc.)
		A12- Has the scope of these core activities increased or decreased over time? If so, can you provide some examples?
		A13- How many employees do your firm currently employ?
		B1- Can you provide a breakdown of your current market and what percentage of output they represent?
		B2- Does your firm have a specific division that deals with supply chain management (farmers and buyers)?
		B3- If yes to B2, what would you say is the overall objective of this division?

¹⁷ This interview protocol reflects the questions that were prepared prior to conducting the interviews. The semi-structure approach allows for “on the fly” question construction based on insight received during the interview. Given the semi-structured approach, the questions were not necessarily administered in the order that they appear in the protocol. In certain instances, questions were omitted based on prior responses from the interviewee.

	<p>Insights into limits on bounded rationality</p>	B4- Do you have any special division that deals with the [regional-MNE]?		
			B5- If yes to B4, Can you provide more details on what their role is?	
			Would it be possible to speak with someone from the team?	
			B6- How many persons are employed in this division?	
			B7- Can you outline the hierarchical structure for this division?	
			B8- Do employees in this division undergo any specific training to better execute their tasks?	
			B9- If yes to B8, can you provide details of such training?	
			B10- Does your firm solicit external advice (consultants etc.) on strategic planning regarding supply chain matters?	
			B11- If yes to B10, can you provide details of these services?	
			B12- You mentioned that [the regional-MNE] was your client, have you ever deal with large foreign firms before?	
			B13- If yes to B12, can you provide some more details on these past clients?	
<p>Value-added creation</p>		<p>Upgrading and buyer support mechanisms (from regional-MNE)</p>	C1- Regarding your largest client, did this buyer approach you for business, or did you approach them? - Can you provide details on how the relationships started?	
				C2- Do you know where they sourced their input from previously?
				C3- Did you start with main core [activity] for [the regional-MNE]?
				C4- Can you provide an overview of this initial arrangement?
				C4- How long has this relationship been going on?
				C5- How did the activities evolve over time (if at all)? Can you provide some examples?
				C6- Before agreeing to do business, what did you envision would be the main benefit from this contract?
				C7- Back then, did you company process for [the regional-MNE] on a daily basis?
				C8- If yes to C7, can you provide more details on what was included?
				C9- How much of your initial production capacity was devoted to [the regional-MNE]
				C- - How does this allocation compare to current?
				C10- Did [the regional-MNE] provide any technical assistance to your firm during the initial periods?
		C11- If yes to C10, can you provide some more details and examples?		
		C12- Where there any technical and implementation issues with this assistance?		

		C13- Has this assistance change as the relationship progressed?
		C14- If yes to C12, can you provide some more details and examples?
		C15- *Follow-up with questions to determine specificity*
		C16- How have these changes affected your operations?
		C17- Is [the domestic processor] exploring new markets?
		C18- If yes to C15, can you provide some more details on these new potential markets?
		C19- If large clients increased production demand, what has been the impact on your own brand?
		C20- Have you been doing less own branded sales versus your supplier sales?
	Justification of firm boundaries regarding value-added creation	D1- What are the crucial inputs and downstream activities are necessary to effectively carry out your core business?
		D2- How involved are you in the organisation of these downstream activities? Can you provide examples?
		D3- Does your company have equity/ownership stake in any of these upstream or downstream activities related to your core business
		D4- If yes to D3, can you outline the factors that dictate which activities are worthy of ownership?
		D5- If no to D3, can you explain why your firm has not decided to vertically integrate into these areas?
	Supplier selection motives (farmers)	E1- What factors matter when deciding on the number of farmers? For example, if one large farmer can furnish your needs, would you choose this option or decide to engage with multiple smaller suppliers?
		E2- Do you think that only [your company] can handle the output from large-scale farmers?
		E3- Are farmers inclined to work with you as opposed to other processors?
		E4- If yes to E3, What do you offer them that other processors don't?
		E5- Has your number of farmers increased or decreased over time?
		E6- For the activities not directly owned, what factors matter in the selection of appropriate suppliers?
		E7- How many farmers do you currently work with? What sizes do they range from?
E8- Why has this number increased/decreased?		
E9- Is there an association of domestic processors?		
E10- What sort of policy is discussed and agreed upon by this association?		
E11- Do you have required standards for your farmers?		
E12- Have your core farmers been able to meet your standards?		

		E13 - If no to E12, what have you done to try and address this?	
		E14- As it relates to your inputs for your business, are you actively involved in production planning within the contract farmers? Do you hold regular meetings?	
		E15- What sort of quality control measures are in place?	
	Supplier upgrading as a value-added creation mechanism	F1- Given that you also rear your own [animals], do you believe your farms are more efficient/productive than contract farmers?	
		F2- Does your firm provide any kind of assistance to farmers	
		F3- What kind of assistance do you offer to farmers?	
		F4- How does this assistance affect the farmer's operations	
		F5- If yes to F3, why does your firm see it necessary to assist suppliers?	
		F6- Can you provide details on what type of assistance has been provided?	
		F7- How often do you provide assistance? Can you provide a chronological breakdown of the major initiatives per supplier?	
		F8- What has been the result of this assistance? How has your firm benefited from the farmers' improvement?	
	Degree of control and value-added appropriation	Governance and dependence relationship with regional MNE	G1- How contract prices and terms of engagement with buyers decided?
			G2- How often are prices renegotiated and which party normally initiates renegotiation talks?
			G3- Would you say that prices are negotiated more often as your tenure with a particular supplier increases?
			G4 – How satisfied were you with the initial contract terms you had with [the regional MNE]
G5- Could you provide some examples of this satisfaction and how it affected your business?			
G6- How did this satisfaction change? Are you more or less happy now with the terms of the contract?			
G7- If dissatisfied, what has changed? Ask for examples			
G8- Has any situation ever arose in which legal proceedings were necessary? Are you able to provide additional details?			
G9- if you are increasingly pressured, why do you not end the relationship with [the regional MNE]?			
G10- Has the quantity/amount of input you demand from individual suppliers increased over time?			
G11- Has the scope of activities for any of your buyers increased over time (you do more processing, marinating etc.)? Can you provide examples and details?			
G12- What factors led to this decision to allow for increased scope?			

		G13- Has any assistance included the following (1) technical advice on factory reconfiguration for efficiency (2) Sourcing or financing of specialist, high volume equipment (3) specialised training for suppliers' employees. Can you provide details and examples?
	Governance and dependence relationship with domestic farmers	H1- Can you explain the contractual relationship that you have with farmers?
		H2- How are farmers paid for their inputs?
		H3- Are farmers satisfied with the contractual arrangements and payments they received? Can you provide examples?
		H4- What issues does {the domestic processor} face that prevents them from offering a higher price than what is currently offered?
		H5- Do farmers frequently move between domestic processors?
		H6- Are you aware if there is any association or union of farmers?