Lecture 13

Relative Role of Actors in Shaping the Global Economy (I): Role of the State

KEY QUESTION:

Can states influence economic activities?

With the completion of this lecture, attached readings and tutorial, you should be able to discuss the:
- influence of states on TNCs' operations through their role as regulators of economic activities; and
- varying degree of states' influence over the operations of TNCs

Lecture Outline

An artist's impression of the Jurong Innovation District (JID) in Jurong West.

The 600-ha JID is a recent and large scale example of the Singapore government's effort to stimulate manufacturing in new growth areas, such as advanced manufacturing, robotics, urban solutions, cleantech and smart logistics.

To date, despite the pandemic, JID has attracted close to $2 billion in private investment. Among the entrants are major players in the advanced manufacturing sector, including: Hyundai Motor Group, Konica Minolta, Nvidia, and Omron.

The effort here is an example of a state taking steps actively to provide key infrastructure that will enable the country to attract FDIs from TNCs, so as to remain competitive and to upgrade or strengthen the local talent pool. **How else does a state influence TNCs?**

13.1 Introduction

- In **Lecture 12**, we learnt that the GPNs of TNCs contribute to flows of trade, capital and labour, which connect different places in the global economy. Such connection also contributes to interdependence. In tutorial, we learnt that the flows of trade, capital and labour are uneven, resulting in different impacts on home countries, as well as host countries in different macro-regions.
- In **Lecture 13**, we will find out **how states can also shape the global economy** through their **influence on TNCs**. This is because a state very often does not directly participate in the economy, as its role is largely in governing a country. However, the policies, initiatives and measures adopted by states can affect TNCs' locational decisions, thereby affecting their GPNs and how TNCs connect places in the global economy. States can also affect how TNCs behave in their countries, influencing the development levels of their countries. This will then affect the variations in development levels across the world.
- As you consolidate this chapter, you should understand **how states shape the global economy**. In the process, you will also be able to discuss **the extent to which states are able to exert their sovereign power over TNCs**.
- By the end of Topic 1.2, we will be able to discuss the **relative influence of the different actors** (states, labour, multilateral institutions and TNCs) in **shaping the global economy**.

13.1 How Do States Regulate Economic Activities?

- According to the Cambridge Dictionary, to regulate something means *to control it, especially by making it work in a particular way*. States regulate economic activities by means of **rules**, **policies** and **strategies**.
- States are the primary regulators of the economic activities that take place **within**, and **across**, their borders.
- States regulate economic activities based on economic, environmental, social, and ethical considerations.

13.2 How Does the Regulation of Economic Activities by A State Influence TNCs?

The global economy is characterized by flows of trade, capital and labour. The flows are largely coordinated by TNCs through their GPNs. At the same time, **state regulation** can influence TNC behaviour and operations.

i. **One way** is through influencing the (direction and magnitude of) flows of trade, capital and labour within a TNC's GPN, thereby shaping the global economy.
ii. **Another way** is through 'capturing' the benefits of TNCs in a country. This influences a country's level of development, which would then affect the variations in development levels in the global economy, thereby shaping the global economy.

When reviewing this section, **it is important to bear in mind how states affect TNCs, which then shapes the global economy, as opposed to ~~how a state affects its national economy~~.**

13.2.1 Trade policies

- States often actively manage trade *in the interests of domestic producers*. In most cases, the result is **policies** that seek to **stimulate exports** while being **restrictive to imports**. **Fig. 1** summarises the major types of trade policy pursued by national governments.

Policies towards imports	Policies towards exports
1. Tariffs	Financial and fiscal incentives to export producers
2. Non-tariff barriers	Export credits and guarantees
Import quotas (e.g. 'voluntary export restraint', 'orderly marketing agreements')	Setting of export targets
Import licences	Operation of overseas export promotion agencies
Import deposit schemes	Establishment of Export Processing Zones and/or Free Trade Zones
Import surcharges	'Voluntary export restraint'
Rules of origin	Embargo on strategic exports
Anti-dumping measures	Exchange rate manipulation
Special labelling and packaging regulations	
Health and safety regulations	
Customs procedures and documentation requirements	
Subsidies to domestic producers of import-competing goods	
Countervailing duties on subsidised imports	
Local content requirements	
Government contracts awarded only to domestic producers	
Exchange rate manipulation	

Fig. 1 Major types of trade policy

- In terms of *imports*, while World Trade Organization (WTO) rules mean that **tariff barriers** have been dramatically **reduced** across the global economy (see **Lect 14**), states may implement a variety of non-tariff barriers to **curtail imports** - including, for example, quotas, licensing regulations, labeling and safety requirements.
- Policies on ***imports*** fall into two distinct categories:
    - **Tariffs**. These are *taxes* levied on the value of imports that increase the price to domestic consumers and make imported goods less competitive (in price terms) than otherwise they would be.
        - In general, the tariff level tends to rise with the stage of processing, being lowest on basic raw materials and highest on finished goods. The purpose of such 'tariff escalation' is to protect domestic manufacturing industry while allowing for the import of industrial raw materials.
        - Thus, although tariffs may be regarded simply as one means of raising revenue, their major use has been to protect domestic industries: either 'infant' industries in their early delicate stages of development or 'geriatric' industries struggling in the face of external competition.
        - For instance, the US in the Trump era has placed tariffs on billions of dollars' worth of good from abroad in order to protect US's industries. China's imports of the US goods in 2019 fell 31.4% from 2018, while exports to the US declined 7.8% amidst a tariff war.

    - **Non-tariff barriers (NTBs)**. While tariffs are based on the value of imported products, NTBs are more varied: some are quantitative (e.g. import quotas), some are technical (e.g. health and safety regulations). Although, in general, tariffs have continued to decline, the period since the mid-1970s witnessed a marked increase in the use of NTBs. Indeed, it has been estimated that NTBs affect more than a quarter of all DC imports and are even more extensively used by LDCs.
- For ***exports***, the state may get involved in promoting exports through its various agencies, or manipulating the cost of exports through subsidies and exchange rate policies. For instance, the low exchange rate of the Chinese *renminbi*, particularly with the U.S. dollar, is a huge ongoing geopolitical issue given its effect on the relative cost of Chinese manufacturing exports.
- A state's regulation of imports and exports could influence where TNCs locate, thereby affecting flows of trade, capital and labour in the global economy. **Table 1** shows how some firms have relocated from China to countries in Southeast Asia in response to increases in tariffs. Such a shift involves a shift in capital flows and would result in changes in trade flows. In addition, these shifts could affect the relative development levels of China versus the countries where firms have shifted to.

Company	Nationality	Industry/activity	Host Country	Year	Remarks
Alpan Lighting	United States	Industrial products	Indonesia	2020	Shifted production from China to escape higher tariffs triggered by trade tensions
Kyocera	Japan	Electronic components Printers	Thailand Viet Nam	2019	• Relocated part of its automotive camera modules and displays production to avoid impact of the trade tensions • Moved production of United States-bound copiers and multifunction printers, mainly to avoid tariffs
Zhejiang Hailide New Material	China	Apparel and textile products	Viet Nam	2021	Moved to avoid the risks of anti-dumping cases and tariff hikes

Table 1 Diversification of Production from China to ASEAN due to United-States-China Trade Tensions and Other Reasons (Selected Cases)

(Source: ASEAN Investment Report 2020–2021 – Investing in Industry 4.0)

- Other trade-related policies include local content requirements, where a state mandates that a product must be made from a specific amount of local content (as opposed to wholly imported raw materials) to quality for preferential (lower) tariffs. By stipulating **local content requirements**, states can determine the number of **local linkages** that a TNC forges by implement local content or local partner requirements. For example, in Thailand's automotive industry, locally assembled automotive vehicles had to have locally produced parts equivalent to 25% of the total value of the vehicle. Local partner requirements refer to ownership of the operation or land. For example, Thailand allows for 100% of foreign ownership of land in industrial areas. However, China does not allow for full foreign ownership of automotive firms. Until 2023, foreign automotive firms had to enter in a 50:50 joint venture with local automotive firms. However, that requirement has been scrapped in 2023.
- Deepening local linkages can be beneficial to the national economy. This would affect the variations in development across the global economy as one country increases in development relative to others.
    - For example, due to regulations on foreign ownership, the 5 largest automotive firms in China were all local and state-owned. However, this may not always be the case. For example, the local content requirement for the automotive industry in Thailand resulted in many inefficient local firms that did not survive the abolition of the local content

requirement scheme in 1998. New, more efficient Thai firms replaced them. This shows that local content requirements may not always be beneficial.

13.2.2 Foreign direct investment (FDI) strategies

- In a world of TNCs and of complex flows of investment at the international scale, national governments have a clear vested interest in the effects of FDI, whether positive or negative. Few governments operate a totally closed policy towards FDI, although the degree of openness varies considerably.
- In many cases, states combine tax incentives, the availability of prime land, and supporting industries and workforce characteristics *to form an attractive package* for foreign investors. States may also, however, seek to capture the gains from inward investment by insisting on certain levels of local purchasing and technology transfers, and/or by trying to limit the repatriation of profits (Recall: Impact of TNCs in **Lect 12**). **Fig. 2** summarises the major types of national FDI policy.

Fig. 2 Major Types of FDI Policy

- Historically, there have been large differences in national policy positions towards inward FDI. In general, DCs have tended to adopt a more liberal attitude towards inward investment than LDCs, although there were exceptions (e.g. France). Among NIEs and LDCs, Singapore had a particularly open policy, far more so than most other Asian countries (see **Box 4**). In particular, Singapore has been keen to attract high technology and high value-added industries through the development of economic clusters (see **Example 1** on **page 6**).
- Other countries such as China and India too have been proactive in attracting FDI. A manifestation of this is in the setting up and development of Export Processing Zones (see **Example 2** on **page 8**).

- States frequently use trade policies together with FDI strategies to attract foreign investment. A spatial strategy that reflects this combination is **Export Processing Zone** (discussed in **13.3.2**). Such strategies serve to **influence the locational decisions of TNCs**.
- Despite such deliberate attempts to attract FDI, the relationship between TNCs and the states should not be seen as benefitting the TNCs only. For instance, when the Canadian mining company Glencairn Gold sought approval from the Costa Rican government to develop a mine site in the early 2000s, not only were there no concessions but the company had to overcome significant roadblocks to begin the extraction process. There is often a balancing of power between these two players.

Example 1: Economic Clusters

- Economic clusters are **geographic concentrations of interconnected companies and institutions in a particular field**.
- Economic clusters include **linked industries and other entities important to for the cluster to compete with other clusters**. They include, for example, suppliers of specialised inputs such as components, machinery, and services, and providers of specialised infrastructure. Clusters also often include distribution channels, customers and manufacturers of complementary products and to companies in industries related by skills, technologies, or common inputs. Finally, many clusters include governmental and other institutions—such as universities, standards-setting agencies, think tanks, vocational training providers, and trade associations—that provide specialised training, education, information, research, and technical support.
- Economic clusters can come about because of **state action**; they can also develop due to other reasons such as **geographical location, prior location of related industries, rise of one or two innovative companies.**

***Box 2*: Seletar Aerospace Park, Singapore**

In the early 2000s, Economic Development Board (EDB) believed the time was right to develop Seletar Air Base. This would be a visible symbol of Singapore's commitment to the aerospace industry, which was recovering from the throes of 9/11 and the 2003 SARS. At the same time, the global aerospace industry was a fast-growing one, valued at about $350 billion by 2027, making the aerospace industry an important one for Singapore's continued economic success.

At present, the 320-hectare Seletar Aerospace Park is home to 70 TNCs and local enterprises employing over 6,000 aerospace professionals. One TNC that decided to set up its operations in the Park is Rolls-Royce. In 2010, Rolls-Royce set up the S$700mil Rolls-Royce Seletar Campus. It comprised an Assembly & Test Unit, a Wide Chord Fan Blade manufacturing facility, an Advanced Technology Centre, and a Regional Training Centre. This was the single largest investment by an aerospace company in Singapore, and a watershed moment for our industry as it signalled the advent of leading-edge aerospace manufacturing in Singapore.

TNCs chose to locate in Seletar Aerospace Park for three reasons.

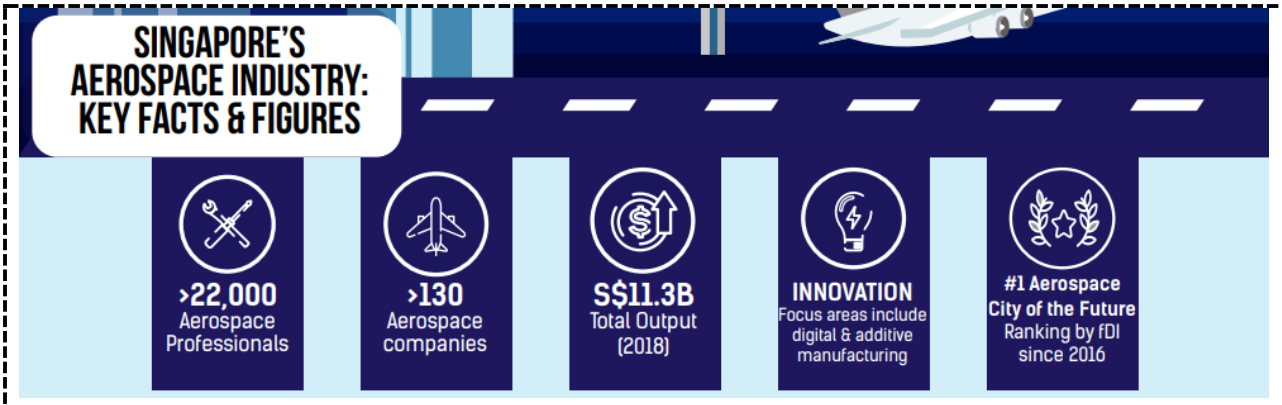
1. **Access to R&D Ecosystem**
   Establishing themselves in the Park and Singapore enabled TNCs to locate within a community of companies, public research institutes, start-ups and regulators innovate and develop new products, technologies and services. To date, over 140 R&D projects have been completed.

2. **Availability of Skilled Labour Force**
   There is an abundance of skilled manufacturing and 'maintenance, repair and overhaul' (MRO) talent in Singapore. In addition, the future workforce is also equipped with emerging skills to support industry needs of the future. Aerospace courses are popular engineering programmes at Singapore's institutes of higher learning. Over 2,000 students graduate from aerospace courses across ITE, polytechnics and universities annually. Aerospace companies have also partnered schools to develop courses and offer attachments and on-the-job training.

3. **Specialised Infrastructure**

   The park has standard facilities that offer "plug-and-play" solutions for manufacturing and MRO. The Park is also in close proximity to Changi East Industrial Zone (CEIZ), which allows for MRO, air cargo and air freight activities.

The success of the Park can be seen through the Park's achievements and accolades **(see figure below)**.



Sources:

- EDB Aerospace Industry Brochure
- How Singapore got a modern aerospace park with 'old world charm' in Seletar

Example 2: Export Processing Zones

- The attraction of FDI has been an integral part of development strategies in many developing countries, although to varying degrees. Among all the measures used by many developing countries to stimulate their export industries and to attract foreign investment one device in particular – the *export processing zone* (EPZ) – has received particular attention.
- The EPZ may be defined as:

  Industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being (re-)exported again.
- **Fig. 3** shows the rapid growth in EPZs, especially during the past 30 years.
  - Some 90% of all EPZs in the developing countries are located in Latin America, the Caribbean, Mexico and Asia.
  - However, in terms of employment, Asia is by far the most important region for EPZs, with 85% of the total.
  - Of these, the biggest concentration is in China, which has 40 million of the world total of 66 million EPZ workers.

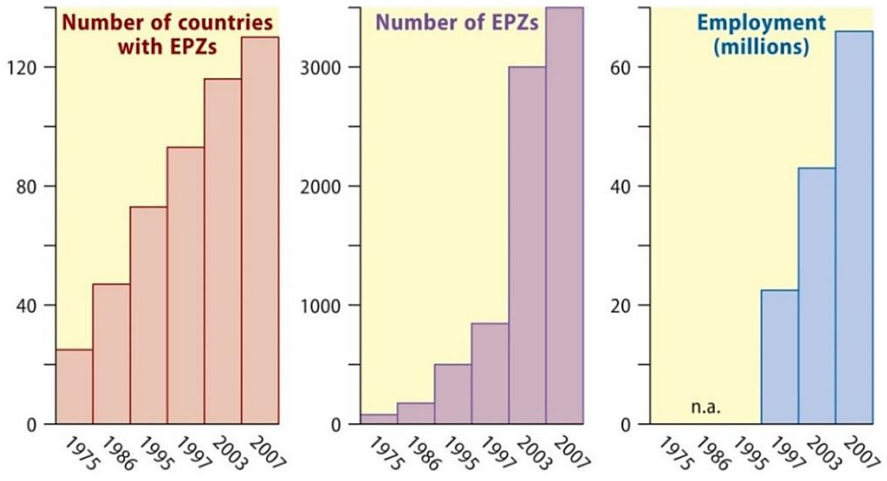


Fig. 3 Growth in EPZs

- EPZs come in a number of different forms: 'free trade zones, special economic zones, bonded warehouses, free ports and *maquiladoras*'.
- Within developing countries, EPZs have been located in a variety of environments.
  - Some have been incorporated into airports, seaports or commercial free trade zones or located next to large cities. Others have been set up in relatively undeveloped areas as part of a regional development strategy.
- EPZs themselves vary enormously in size, ranging from geographically extensive developments (e.g. Shenzhen in China; see **Box 1**) to a few small factories; from employment of more than 30,000 to little more than 100 workers. However, they are similar in the provision of conditions intended to increase industrial output and exports, such as:
  - tax incentives on imports and exports of goods
  - exemption from various sales and services taxes
  - better supply of power, water, sewerage and sanitation
  - infrastructure linking EPZs to non-EPZs areas via railways, roads and telecommunications
  - improved port facilities
  - safety and security measures
  - liberalisation of economics laws regarding employment, *etc*.

***Box 1*: The Development of Special Economic Zones (SEZ) in China**

China's Special Economic Zones (SEZ) are areas in which foreign and domestic companies can trade and invest without the same control and regulations from Beijing as other parts of China. These areas are designed to encourage overseas investment in China and boost the country's economic growth.

SEZs were first developed in 1980 as part of Deng Xiaoping's drive to open up China to the rest of the world and cement China's place on the global stage as a major economic player.

Shenzhen, in Southern China near the border with Hong Kong, was among the first 4 locations in China to be given SEZ status. At the time Shenzhen was just a small town, now, 33 years on, it is a booming trade hub and one of China's largest cities. The other 3 areas are also situated in the south of China in Guangdong and Fujian provinces.

The Chinese government aimed to encourage foreign investment in the SEZs by introducing more relaxed regulations in these areas but the scheme had a rocky beginning.

Shenzhen first became an SEZ in 1980 and was expected to attract investors from across the globe however, by the end of 1981, 91% of all foreign investment in the city came from Shenzhen's neighbour, Hong Kong. This was due to a lack of proper regulations concerning wages, employment and the firing of employees. Foreign companies, unfamiliar with Chinese business culture were unwilling to take the risk and they felt there was still too much red tape to contend with. Hong Kong based companies were more inclined to take the risk of opening up offices in Shenzhen due to familial and cultural connections as well as having a better understanding of how business worked on the mainland.

Another problem Shenzhen faced was the lack of diversity of investment sectors. As most investment was coming from Hong Kong there was a severe bias towards the real estate sector with 71% of all investment concentrated in this one area. The bias was due, in large part, to exorbitant land prices in Hong Kong which was causing a population overflow into neighbouring Shenzhen.

The early setbacks that China's SEZs were faced with caused many investors to withdraw their investment and close their offices in China. The withdrawal of investment caused the PRC to wake up to regulation problems and by January 1982, five new regulations had been approved which simplified red tape in SEZs, especially with regards to entry and exit procedures and wage guidelines. These improvements led to a sharp increase in overseas investment in SEZs and ultimately contributed towards the success of the zones in China.

Another factor that can be apportioned to the eventual success of SEZs in mainland China was the fixed 15% income tax applied to partly foreign owned enterprises as opposed to the 33% tax in the rest of China or 17% in Hong Kong. This was a huge incentive to overseas investors. Companies were also given exemptions from other local taxes and were allowed to export goods duty-free.

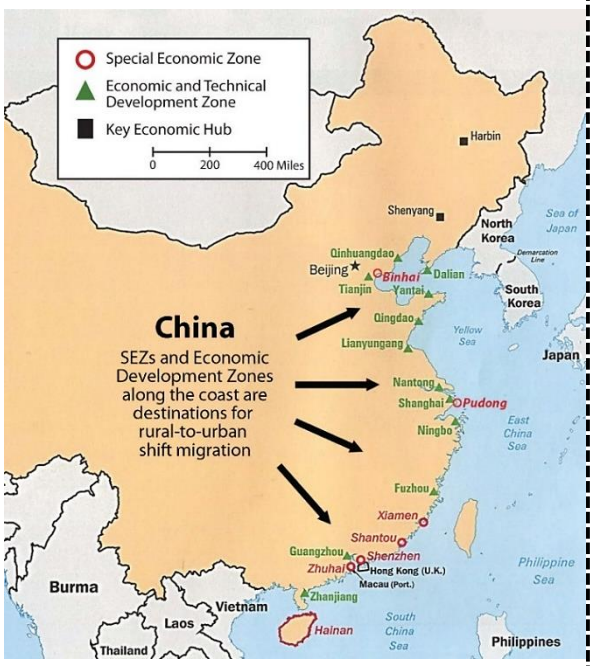
Since 1982 China's SEZs have all been developing at an incredible speed. Shenzhen itself has been especially successful. In 1992 Shenzhen attracted 14% ($4.3billion) of China's total foreign investment. The city is now one of China's main import-export hubs as well as a leading manufacturing base. The initial success of the SEZs led the Chinese government to sanction more foreign trade areas in cities including Shanghai, Dalian, Ningbo and Tianjin.

These newer zones are known as Economic and Technological Development Zones (ETDZ). They are generally smaller than SEZs and place a larger emphasis on specific industries, particularly on developing high-tech research and development. There are 54 ETDZs around China and they have, for the most part, carried on the success of the original SEZs.

However, SEZs haven't proven to be a complete success story. A 2013 investigation presented to the Royal Economic Society into the viability and success of SEZs found that whilst it is undeniable that SEZs have helped to increase GDP in China by up to 10%, they have not led to increased productivity within the regions where they are located.

The next step in the development of SEZs will be the creation of Free Trade Zones (FTZ). In recent years cities across China, including Shenzhen and Shanghai have been vying for the opportunity to become FTZs. These new areas are expected to have more relaxed regulations on the exchanging of currencies as well as less stringent rules on the types of companies that can be set up. For example, foreign owned companies may no longer need a Chinese owned partner to help them develop their business on the mainland.

At the beginning of September 2013, Shanghai was named as the first city to be given the opportunity to trial a Free Trade Zone in the Pudong area of the city. The area will have fewer restrictions on currency converting and it is hoped that it will bring even more foreign investment into China and take the focus away from Hong Kong where the government has less control.



Beijing has also said it may lift the ban on websites like Twitter and Facebook in the FTZ to encourage foreign companies to come to China, as well as making it easier for Chinese companies to enter foreign markets and promote themselves abroad.

The Chinese government will be keeping a close eye on the FTZ trial in Shanghai with a view to developing more zones in other cities in the near future. If the Shanghai trail does prove to be successful then Shenzhen is likely to be the next city to create an FTZ given its success as an SEZ. The future of SEZs is uncertain but if Shanghai is successful in its latest venture, many of the current SEZs are likely to develop into FTZs in the future.

13.2.3 Labour market strategies (see **Lect 14)**

- Policies in this area have sought to promote enhanced **labour market flexibility**, i.e., for the labour market to better meet the needs of TNCs.
- States, especially in older DCs in Europe and the US, are recognising the need to remove rigidities in the labour market to make it more in tune with what are seen to be the dominant characteristics of a globalising world economy to remain competitive, thereby attracting TNCs. As a result, a variety of labour market measures, employed in various combinations has emerged. (See **Fig. 4**)
- TNCs tend to comply with labour regulations in places with robust governance, especially for high-skilled labour.
- The influence of states on TNCs' labour practices should not be viewed merely from the perspective of ethics in this chapter. Instead, consider how **state regulation on TNC labour practices influences TNC location, which influences flows of trade, capital and labour,** as well as relative development levels. Remember that 'development' includes human development. Therefore, **the extent to which states can influence TNCs in ensuring labour rights** would affect development. This would then **affect variations in development levels in the global economy**.

The range of potential labour market policies

- The use of more temporary and fixed term contracts
- The introduction of different forms of flexible working time
- Moves to encourage greater wage flexibility by getting the long-term unemployed and the young to take low-paid jobs
- Increased vocational training to provide more transferable skills
- Reforms in state employment services
- Incentives to employers to take on workers
- Measures to encourage workers to leave the labour market
- Reductions in the non-wage labour cost burdens on employers
- Specific schemes to target the long-term unemployed

Fig. 4 Elements of Labour Market Policies

13.2.4 The State as a Business Owner: State-owned enterprises (SOEs)

- With a few exceptions, states also directly engage in owning economic activities. This is an obvious and yet often overlooked aspect of state involvement in the economy; put another way, in some areas the state *is* the economy.
- It also challenges the notion that globalisation is driven by private corporations, as **some of these state-owned enterprises are actively globalising as well**.
- Different countries, however, experience different levels of state involvement in business enterprises.
- SOEs are **public enterprises** that are **directly owned and managed by the state**.
  - CNOOC, the Chinese National Offshore Oil Corporation, provides a good example. One of China's largest oil companies, CNOOC was founded in 1982 and is headquartered in Beijing. In 2019, it had approximately 18,703 employees and a total assets of US$11.5 billion. (http://en.cnooc.com.cn/, accessed March, 2021).
  - The Chinese state not only owns a substantial 70% stake in CNOOC, but also directly appoints its top management.
- It is important to note that state ownership rarely means that the state owns 100% of a corporation – Enel and Gazprom have been part privatised, for example – but rather has a controlling stake.
- SOEs have been rising in influence in the global economy over the past decade, more than 10% of the world's largest firms are state-owned. As seen in **Fig. 5**, the proportion of SOEs among the Fortune Global 500 has grown from 9% in 2005 to 23% in 2014.

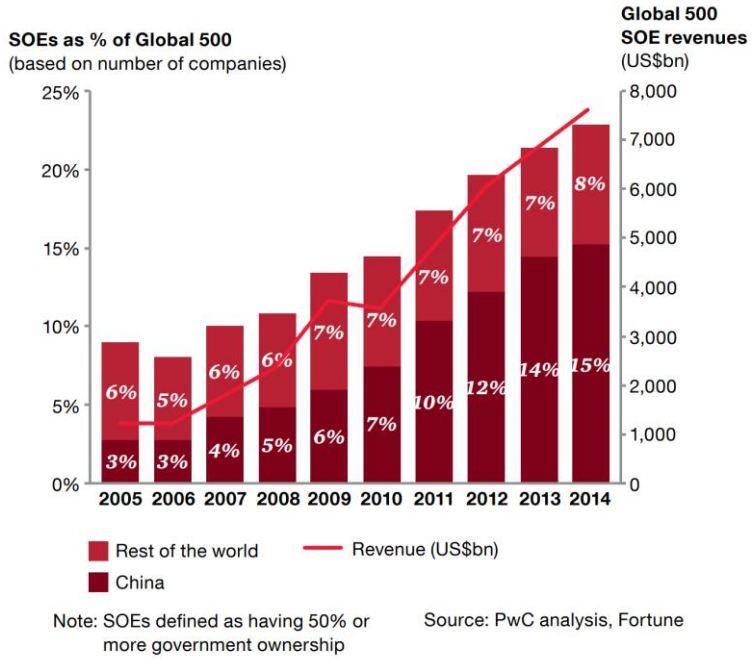


Fig. 5 Share of SOEs in the Fortune Global 50

- Geographical spread of SOEs:
  - SOEs are commonly found in developing countries throughout the world, where the state has immediate developmental goals that can be achieved through direct state ownership and management of business enterprises. They are found in such diverse developing economies as Brazil (e.g., Petrobas), China (e.g., China Ocean Shipping), India (e.g., Indian Railways), Malaysia (e.g., Petronas), Mexico (e.g., CFE, an electricity monopoly) and Russia (e.g., Gazprom).
  - However, SOEs are also found in developed countries as the examples of Statoil (Norway), Systembolaget (alcohol, Sweden), Enel (electricity, Italy) and Amtrak (U.S.) demonstrate.
- One important dimension of SOEs is the extent to which they are now a global force. Many, if not most, large SOEs are active internationally and engaged in trade, with some emerging country governments pursuing explicit policies of internationalisation. Increased global competition for finance, talent and resources are seeing some countries turning to SOEs as tools to better position themselves for the future in the global economy. In this way, states are able to regulate the activities of TNCs through direct ownership.

13.2.5 Hold TNCs Accountable for Wrongdoings

TNCs can be held accountable in their home countries or their host countries. However, TNCs often locate their operations in places with more lenient penalties on labour or environmental transgressions, as compared to their home countries. In this way, TNCs can avoid accountability for their actions in foreign jurisdictions. In other words, home economies are more effective in regulating the actions of TNC operations within their jurisdictions since host countries may be less likely to hold TNCs accountable for fear of TNCs shifting their operations elsewhere.

However, the victory of Nigerian victims in the UK and the Hague courts against Royal Dutch Shell shows that home economies can hold TNCs accountable for the actions of their overseas subsidiaries (see **Box 3**). However, such prosecution is more likely for wrongdoing that originates intra-firm, rather than transgressions that originate inter-firm.

The ability of states to hold TNCs accountable for wrongdoings shapes the global economy in terms of affecting where TNCs choose to locate (thereby affecting flows of trade, capital and labour), as well as influencing relative levels of development.

***Box 3*: Holding Shell Accountable in Nigeria – case study**

In a historic ruling against the oil giant Shell, a Netherlands court has found in favor of four Nigerian farmers along with environmental activists in an oil spill case that was first filed in 2008.
The Niger Delta has been polluted by oil spills for decades, since Shell began its operations in Nigeria.

- In 2011 the UN concluded it would take 30 years to clear up the vast amounts of pollution in the Niger Delta.
- The Ogale community of about 40,000 people are mostly fishermen or farmers who rely on Ogoniland's waterways. But pollution has all but destroyed fishing, turning their lush home into a toxic wasteland.
- There have been at least 40 oil spills from Shell's pipelines since 1989, lawyers say Shell's records reveal.
- UN scientists have found an 8cm (3 inch) layer of refined oil floating on top of water that supplies the community's drinking wells - vastly higher than is legally permitted.
- The water is now too dirty for people to drink. Despite promises to provide clean water, people must often either shell out for bottled water or drink from contaminated sources.
- Thick crusts of ash and tar cover the land where oil spills have caused fires. Planting new vegetation to replace burnt crops or plants is almost impossible.

In the verdict delivered in 2021 at the Court of Appeal in The Hague, the appeals judge sided with the farmers in finding Shell's Nigerian subsidiary responsible for four out of six pipeline leaks covered by the lawsuit, as well as declaring that the parent company, Royal Dutch Shell, had violated its duty of care.

Shell will pay an unspecified amount in damages to the farmers, who claimed the spills had ruined the livelihoods of villagers in the area. The company was also ordered to install leak detection equipment in its pipelines.

... One of the Nigerian plaintiffs, Eric Dooh from the village of Goi, told the media: "Finally, there is some justice for the Nigerian people suffering the consequences of Shell's oil. It is a bittersweet victory, since two of the plaintiffs, including my father, did not live to see the end of this trial. But this verdict brings hope for the future of the people in the Niger Delta."

Friends of the Earth Netherlands, which helped to bring the case, said the verdict "exceeds all expectations." Director Donald Pols said: "This is fantastic news for the affected farmers ... This is also a warning for all Dutch transnational corporations involved in injustice worldwide ...

Royal Dutch Shell said in a statement that it was "disappointed" by the verdict. The company claims that the leaks were caused by sabotage.

Friends of the Earth said it was the first time a Dutch multinational had been held responsible for a duty of care overseas...

13.3 Conclusion

- Even though states largely only have sovereign power over their countries, state regulation over TNCs allow them to have an impact on the global economy.
- At the same time, it would be an exaggeration to claim that states have equal ability to influence TNCs. Very often, a state's ability to influence TNCs depends on the **bargaining power** that states have.
- On the one hand, the effectiveness of the state influencing the behavior of TNCs is well-exemplified in the NIEs, including the first-generation ones such as Singapore (see **Box 4**) and recent ones such as China (**Box 5**).
- On the other hand, the experience of Nigeria and Bangladesh (see **Box 6**), shows that some states experience challenges in effectively regulating the behaviour of TNCs.
- As a closure to this chapter, **what do you think are some factors that allow a state to have greater bargaining power over TNCs and thereby a commensurately larger role in influencing the global economy?**
- To foreshadow what you will learn in a later chapter, states can shape the global economy not only through state regulation of TNCs, but through their membership in multilateral institutions (see **Chapter 15**).

Box 4: Singapore – case study

Singapore is a small country of a population of about 5 million, yet with its GDP per capita standing at US$56,286 in 2014, it is also one of the richest. Much of this growth rides on the backs of TNCs, which has continued to pump in phenomenal amounts of FDIs into the country since it first became independent in 1965.

Despite the recent financial crisis, the economy managed to attract US$16,809 million worth of FDI and a net inflow of US$10,830 in 2010, topping the list among its other Southeast Asian neighbours. With an economy that is overwhelmingly dominated by foreign companies, Singapore illustrates well how FDIs work with local conditions to help a country excel economically.

In the early years of independence, Singapore faced problems in social, political and economic dimensions. One major problem is that of high unemployment which direly needs to be solved. Without any natural resources and supported only by a very small market, Singapore had no better choices then to take on an export-oriented approach (see Section 7.4.1) to its economy, and to actively woo TNCs to set up labour-intensive manufacturing operations to help create jobs for the locals. The agency responsible was the Economic Development Board (EDB), which still plays an extremely influential role in Singapore economy.
In order to make it appealing for TNCs, the Singapore government made two main moves.

- First, it granted a series of tax cuts, such as reducing the income tax from 40% to 4% for selected industries. This made the country very attractive cost-wise to TNCs.
- Second, it dealt with labour relations, for instance, by establishing the National Trade Union Congress which effectively incorporated workers' unions under one umbrella and into the governance system. Such a move helped to assure TNCs of a disciplined workforce that is also free from politics.

While countries such as Taiwan and South Korea required TNCs to engage in joint ventures with local firms, Singapore differed by taking a softer stance towards TNCs. Although TNCs are given the liberty in how they run their operations, by putting in place a well-educated workforce, TNCs are encouraged to choose working with local firms. Thus, a focus on educating the population also increases the chances of attracting TNCs looking for skilled labour which is more able to contribute to the their growth (and conversely, locals able to learn more from the TNCs too).

Moreover, Singapore attracts FDIs with its high quality physical infrastructure and efficient transport networks within and beyond the country. The rule of law also takes precedence in the country, with political stability and extremely low levels of corruption as its key characteristics too. Hence, both the hardware and software for businesses are in place.

In addition, not allowing the initial relationships established with TNCs remain stagnant, Singapore continues to review its focus. Although FDIs in the initial years have been effective in generating employment, the government soon realised that these jobs needed only a low level of skills. A push towards high-tech industries (such as pharmaceuticals and biotechnology) and the tertiary sector soon ensued. That is, Singapore has decided to take the 'high-road' strategy. The result of this shift can be seen in 2011, with 40% of FDIs in financial and insurance services and 23% in manufacturing. However, manufacturing is still important, employing more than a fifth of the Singapore workforce.

Today, Singapore promotes itself as a global business centre on the basis of the very high quality of its physical and human infrastructure, its strategic geographical location and its business-friendly policies. Government policy incorporates an explicit strategy to 'regionalise' the Singaporean economy by encouraging domestic firms to set up operations in Asia, while Singapore develops as the 'control centre' of a regional division of labour. The government introduced a series of initiatives using government-linked corporations to develop major infrastructural projects in Asia and, more broadly, to develop international networks.

***Box 5*: China – case study**

China only started to open its economy to foreign investments after 1978. Prior to 1978, China was largely isolated from the international economy and global markets, which was aggravated by poor allocation of resources and rampant inefficiencies. These were largely due to China's planned economy, whereby pricing, volume and sales of goods are mandated by the government, depriving producers from competition with rival suppliers and the opportunity to expand operations.

These took a turn in 1978, when China began its gradual transition from a planned economy to the market economy, and also began its 'open door policy'. A distinctive feature of the open door policy was the explicit use of geography, to steer Foreign Direct Investments (FDIs) to specific locations. As such, China set up Special Economic Zones (SEZs), restricting the areas where foreign and domestic companies can trade freely without regulations. The first four SEZs in the Southern provinces of Guangdong and Fujian became the experimental ground of China's open-door policy. These zones quickly became drivers of national growth due to the investments of Hong Kong and Taiwan entrepreneurs that were in search of lower production costs. The success of these few SEZs led to the further development and geographical spread of Economic and Technological Developments Zones (ETDZs). The progression towards extensive openness to international trade and investment also allowed for imported technology, equipment and expertise, which empowered Chinese businesses to compete in global markets. *[See **Box 1** for an elaborated version of this paragraph]*

Despite these massive flows of capital and technologies, China remains a centrally controlled economy, in which State-owned Enterprises (SOEs) predominate. Particularly, China has remained largely in control of many large state enterprises and manipulated its economy by controlling its banking system, cross-border trades and capital movements. Rather than the immediate dismantling of institutions under central planning, China's transition happened very gradually and is perhaps still in the midst of transition to become a market economy. For instance, large-scale privatisation of large State-owned Enterprises (SOEs) only begun in 1996, 18 years after 1978, giving time for the state to continue directing and supporting these SOEs while they build up experience in operating in a market economy. A major problem however, was the inefficiency and high levels of corruption within many of the SOEs.

Today, only about one-fourth of industrial output is derived from SOEs, and there are continuous reforms to break up SOEs and turn them into private entities given that SOEs have been continuously underperforming as compared to private firms. Profitability of SOEs have fallen while private firms have grown in strength, returns are now half the non-state-owned firms, as seen in the graph. However, China would likely still retain its control in the "strategic sectors" such as aviation, energy and telecommunications. An example of which would be PetroChina, the country's largest oil producer. These strategic sectors while used to be led by Chinese Communist Party (CCP's) officials for "vested interest", or corrupt personal gains, have since been cleaned up under President Xi Jinping's anti-corruption campaign.

When China joined the World Trade Organisation (WTO) in 2001, China was obligated to give up some aspects of its state directed transition strategy and align with WTO's principles of non-discriminatory open market and fair competition. Although it greatly enhanced China's economic potential it also imposed severe stresses on domestic economy and institutions, exposing Chinese enterprises to intense competition. It is notable that the Chinese government now actively encourages Chinese businesses to invest overseas and there have been a number of significant Chinese acquisitions of foreign businesses, notably the IBM PC business by Lenovo in 2001.

Financially, China continues to be under pressure to revalue the *renminbi*. To ensure competitiveness of exports amidst the weak global economy, China's central bank has been devaluing the yuan and controlling the value of the yuan so as to help Chinese exports remain less expensive in the overseas market. This practice has persisted despite criticism from the United States and economic blocs such as the European Union, which have long claimed that the Chinese currency is too weak, allowing their goods to be sold artificially cheap, creating unfair competition.

***Box 6:* Bangladesh – case study**

Bangladesh's textile and garment industry is a major contributor to the country's economy, and it is a vital player in the global textile and apparel market. In the fiscal year 2021-2022, Bangladesh exported garments worth US $42.613 billion, making it the second-largest apparel exporter in the world (Export Promotion Bureau data).

In addition, the garment industry is also a significant source of employment and income for Bangladesh, with more than 4 million people (about twice the population of New Mexico) working in the sector.

The Bangladesh Garment Manufacturers and Exporters Association (BGMEA) reported that in the first eight months of 2022, BD ready-made garment (RMG) exports totaled $29.825 billion, up by 38.39% compared to the same period in the previous year.

The United States is the largest export destination for Bangladeshi garments, accounting for around 21.50% of total exports. The European Union (namely Spain, Germany, Italy, France, Belgium and Netherlands) is the second-largest export destination for BD apparel, followed by UK and Canada.

Bangladesh is home to more than 4,000 factories that supply global brands ranging from fast fashion retailers such as Zara-owner Inditex and Gap Inc to the more upmarket Hugo Boss and Lululemon. The garment factories in Bangladesh are hence part of the GPNs of TNCs in the fashion industry.

In 2013, a wave of protests and strikes lobbied for more emphasis on workplace safety, fair wages, union rights and worker welfare after the Rana Plaza collapse. In response, Bangladesh's government raised the minimum salary for garment workers from 3,000 to 5,300 taka (then USD$68) a month in 2013. Five years later, this sum rose again to 8,000 taka (then USD$95), as the garment industry is legally bound to review wages every five years.

When it was time for the next review in 2023, Bangladesh raised the minimum wage for garment workers by 56.25%, the first hike since 2019, the junior labour minister said on Tuesday after a week of protests calling for higher salaries.

The minimum wage for workers increased from 8,000 taka to 12,500 taka ($114) per month from Dec. 1, State Minister for Labour and Employment Monnujan Sufian said. There will also be a 5% annual increment. Workers, however, are not happy with the rise at a time when inflation is running at 9.5%. Workers demanded a 23,000 taka (USD$209) minimum.

There are several challenges to enforcing the wage increase in Bangladesh. Firstly, local laws may regulate fire safety, pay and working conditions, but enforcement is often weak because there are not enough inspectors and there is significant potential for the corruption of officials. At the same time, workers can struggle to raise awareness of issues as a result of low levels of union recognition and fear of reprisals. Secondly, while fashion brands may express their commitment to implementing responsible purchasing practices, they may in practice impose additional demands upon factory owners that may prevent factory owners from paying their workers fair wages.

Several fashion brands including Abercrombie & Fitch, Adidas, Gap, Hugo Boss, Levi Strauss, Lululemon, Puma, PVH and Under Armour told Prime Minister Sheikh Hasina in a letter they were "committed to implementing responsible purchasing practices" to enable higher wages.

"We continue to recommend that the government of Bangladesh adopt an annual minimum wage review mechanism to keep up with changing macroeconomic factors," the letter said. In addition to the wage increase, the government has said that workers would be given a 5% annual increment.

But Abdus Salam Murshedy, managing director of the Envoy Group that sells to Walmart (WMT.N), Zara and American Eagle Outfitter (AEO.N) among others, said buyers were unwilling to pay the "right price, the fair price" with major economies slowing and the wars in Ukraine and in the Middle East raising geopolitical concerns.
"Words from buyers are fine but when they place orders, they say there are many other competing suppliers, so you better do this, do that," said Murshedy.

The example of Bangladesh's attempt to increase the minimum wage of workers in the garment industry illustrates the challenges that developing countries experience in regulating TNCs. Developing countries often rely on TNCs for economic growth and employment. At the same time, developing countries may have weakly developed governance structures.

Sources:

1. https://www.worldfashionexchange.com/blog/rise-of-bangladesh-textile-and-garment-industry/
2. https://en.wikipedia.org/wiki/Rana_Plaza_collapse
3. https://www.ilo.org/infostories/en-GB/Stories/Country-Focus/rana-plaza#intro
4. https://www.cnn.com/style/article/rana-plaza-garment-worker-rights-accord/index.html
5. https://www.reuters.com/sustainability/global-fashion-factories-bangladesh-resigned-slimmer-margins-ahead-wage-hike-2023-11-08/
6. https://www.reuters.com/world/asia-pacific/bangladesh-hikes-minimum-wage-garment-workers-after-protests-minister-2023-11-07/
7. https://www.theguardian.com/business/2019/jan/21/low-wages-garment-workers-bangladesh-analysis