Expanding the International Trade and Investment Policy Agenda: The Role of Cities and Services*

Christine Cote
London School of Economics

Saul Estrin
London School of Economics

Daniel Shapiro
Simon Fraser University
Beedie School of Business

Final, April 15th, 2020

* Ideas in this paper were developed as part of a Knowledge Synthesis Grant, ES/S008373/1, funded jointly by Canada (SSHRC) and the UK (ESRC) entitled: "The (New) Geography of International Trade and Investment: Exploring the extent to which 'distance' matters in the establishment of economic relations". We are grateful to Angelina Borovinskaya, Celine Tang, Tianna Li and Ines Alvarez Boulton for outstanding research assistance and to Kieran Shah for help when it was needed most. Thanks to the editor, the area editor, and to three anonymous reviewers for constructive comments.

Abstract

We explore the public policy implications of two new, significant, and inter-related global phenomena. First, the rising share of services, particularly innovation-driven digital and knowledge-based services, in foreign trade and multinational enterprise activity; and second the increasingly important role of global cities as home and hosts to these activities. Our framework distinguishes between national economic policies to promote trade and FDI, referred to as economic diplomacy, and comparable policies originating in cities, referred to as city diplomacy. National economic diplomacy has traditionally promoted trade and investment in goods, often through trade agreements and promotion agencies, and we explore the limitations of these tools as trade in services becomes more important. However, we also note that trade in services, particularly innovation-driven services, is concentrated in global cities, and traded between them, often within MNEs. We conclude that national policies on trade and investment cannot be divorced from innovation and knowledge strategies, and these strategies cannot be divorced from cities. We emphasize that national economic diplomacy should be better aligned with city diplomacy. We also discuss how the transition to stronger city diplomacy may have consequences for firms and their strategies for corporate diplomacy.

Keywords: services, trade and investment policy; economic diplomacy; city diplomacy; global cities; MNEs; corporate diplomacy

1. Introduction

The process of globalisation has meant that international trade and investment increased rapidly in the post-war period, and especially after 1990, as transportation and communications costs fell (Rodrik, 2018a), allowing the emergence of Global Value Chains (GVCs) that supported greater trade and foreign investment in goods (Baldwin, 2016; Gereffi & Fernandez-Stark, 2016). The post-1990 period also witnessed a policy transition away from multilateral agreements like The General Agreement on Tariffs and Trade (GATT) (Krugman, 1991; Rose, 2004) and towards Regional Trade Agreements (RTAs) and International Investment Agreements (IIAs) (Baier & Bergstrand, 2007; Glick & Rose, 2016) designed to support trade and investment in goods and services.[1] Most countries supported these arrangements domestically with agencies designed to promote international trade and investment, the number of which has tripled since 1990 (OECD, 2018: 20; van Bergeijk & Moons, 2018).

The evidence broadly supports the view that this mix of treaties and national promotion agencies, which we refer to as *economic diplomacy*, acted to stimulate trade considerably, especially between countries that are relatively close to each other (Baier & Bergstrand, 2004; 2007; 2009; Baier, Bergstrand & Clance, 2018; Bergstrand & Egger, 2013; Bruno, Campos & Estrin, 2019; Egger & Merlo, 2007, 2012; Globerman & Shapiro, 1999; Moons & Van Bergeijk, 2017; Rose-Ackerman, 2009). There is also evidence that growth in international trade and foreign investment has recently been slowing (The Economist, 2019; McKinsey Global Institute, 2019), raising issues over the possible policy responses, reflected for example in the most recent *World Development Report* (World Bank, 2020).

[1] The number of RTAs increased over ten-fold from 225 in 1990 to over 302 in 2019 (WTO, 2019) while the number of IIAs reached 3317 by 2018 (UNCTAD, 2019), including 2932 Bilateral Investment Agreements (BITS) and 385 Treaties with Investment Provisions (TIPS) both of which represent substantial increases since 1990.

Thus, the post-war world, notably after 1990 saw a dramatic increase in trade and foreign direct investment (FDI) in goods and services, accompanied by equally dramatic increases in trade and investment agreements and promotion agencies. However, the nature of globalization is changing. First, while trade and foreign investment may have slowed in total, trade in services has been growing faster than either trade in goods or FDI (Donnan & Leatherby, 2019; McKinsey Global Institute, 2019; van der Marel, 2016); it has more than doubled since 1970, and now accounts for some 25% of total exports being predicted to rise to 33% by 2040 (Gervais & Jensen, 2019; World Trade Report, 2019)[2]. The growing importance of trade and investment in services (Buckley & Majumdar, 2018) has not been widely studied, nor have the implications for policy received much attention, despite its relationship to the knowledge economy (Mudambi, 2008).

At the same time, there is now a better understanding of the nuanced role of geography, so that countries are not necessarily the prime geographic unit of interest for various policy decisions by firms and governments (Mudambi, Li, Ma, Makino, Qian & Boschma, 2018a). In particular, scholars and policy makers have pointed to the pivotal role of cities in facilitating the creation and trade of knowledge-based services, a core activity for many contemporary MNEs (Iammarino, McCann & Ortega-Argilés, 2018; Santangelo, 2018; Trujillo & Parilla, 2016). Cities can generate strong agglomeration economies in both physical and knowledge infrastructures (Davis & Dingel, 2019; Glaeser, 2008; Bryan, Glaeser & Tsivanidis, 2019), leading to the co-location of MNEs, and in particular knowledge-based professional service firms as well as the knowledge-based parts of MNE GVCs, in these cities (Belderbos, Sleuwaegen, Somers & De Backer, 2016; Belderbos, Du & Slangen, 2020; Mudambi, Narula &

[2] These estimates are likely understatements since they do not measure the value of services embedded in goods.

Santangelo,2018b). This has led to the emergence of what have been called global cities (Ljungkvist, 2016; Sassen, 1991; Taylor & Derudder, 2016), and this is an emerging market as well as a developed economy phenomenon (Bryan, et al, 2019). In this paper, we focus on three characteristics often ascribed to global cities. They are defined by the presence of advanced multinational business service providers (Sassen, 1991); by the associated interlocking networks of cities (Taylor, 2004); and by the presence of innovation clusters that promote both the location of knowledge-based activities and the creation of new knowledge-based firms that can serve international markets at an early stage (Cantwell, 2017; Mudambi et al, 2018a). Global cites are therefore defined by the location decisions of business service multinational enterprises (MNEs), the degree to which their activities are connected across cities, and their capacity to host innovation clusters. Thus, global cities combine local resources with global linkages and networks (Bathelt, Malmberg, & Maskell, 2004; Mudambi et al, 2018a).

Explanations of the global city phenomenon centre on the idea that these cities can reduce spatial transactions costs and therefore "distance" for trade and FDI, particularly in knowledge-based goods and services (Estrin, Nielsen & Nielsen, 2017; Mudambi et al., 2018b; Nielsen, Asmussen & Weatherall, 2017). Thus, although the spatial scale of knowledge sourcing may be local, the spatial scale of knowledge flows can be global (Mudambi et all, 2018a). The increasing significance of cities in global trade and FDI also has important implications for trade and FDI policy. Although cities cannot sign treaties in the same way as countries, they do create both bilateral and multilateral agreements among themselves (Acuto & Rayner, 2016), they participate in city networks defined by the location decisions of MNEs (Sassen, 1991; Taylor, 2004) and they mount significant efforts to promote and attract investment to their cities, often in knowledge-based services (Tavares-Lehmann & Tavares, 2017). Thus, cities, recently labelled as

"nation cities" (Emanuel, 2020), now engage in their own forms of economic diplomacy, which we refer to as *city diplomacy*.

In this paper, we offer a perspective on the ways in which traditional trade and investment policy frameworks may need to be modified to consider these increasingly significant new phenomena. We provide an organizing framework that first considers a national policy context which we use to illustrate current policy options for enhancing trade and FDI at the country level based on the international economics and international relations literatures (Bayne & Woolcock, 2016; van Bergeijk & Moons, 2018). We define two broad categories of national policy options: *trade diplomacy,* whereby nation states sign RTAs, which define the rules of the game, and *commercial diplomacy* whereby these agreements are supported by the creation of trade and investment promotion agencies (TIPAs) designed both to promote exports by domestic firms and to attract new inward FDI. Collectively, we refer to these elements as *economic diplomacy*. MNEs respond to these actions by choosing the appropriate locations for trade and investment and by negotiating conditions for market entry, a process that may require negotiation with relevant local stakeholders, or corporate diplomacy (Henisz, 2014). We consider the twin policy options of trade and investment deals and trade and investment promotion activities and emphasize services as well as goods. This framework involves two tiers, whereby countries first set the rules of the game, and firms respond to those rules by choosing and negotiating location strategies.

We then extend this to propose a three-tier framework that incorporates *city diplomacy* into the framework. City diplomacy defines the ways in which cities can represent their interests internationally, both with other cities, and with other relevant organizations. City diplomacy therefore includes formal and informal agreements among cities together with activities

surrounding city-level TIPAs including efforts to promote the city as a home to networks of MNEs. This third level is of growing significance because global cities rather than countries have become the locational decision point for much, if not most, of the knowledge- and innovation-based activities at the heart of modern trade and FDI (Berube & Parilla, 2012; Sassen, 1991; Taylor & Derudder, 2016). As noted by Trujillo & Berube, "understanding global market currents requires an understanding of the economic dynamics playing out in the world's cities." (2016:9)

We conclude that global cities can ameliorate many of the distance-related obstacles to trade and investment growth, notably in services, and that much greater attention to city-based trade and investment policies is warranted. In particular, we highlight the need for deeper understanding of the nature, structure and scope of city diplomacy, and its potential role in creating trade linkages across cities and city-regions, and in supporting a national innovation strategy. We emphasize that national economic diplomacy should encompass innovation, and this will require a better alignment with cities and city diplomacy. We further conclude that, while trade agreements can be important, the effects of physical and contextual distance make them a challenging policy tool for supporting geographically diversified trade and investment in goods and services. However, we do argue in support of extending and refocusing trade agreements towards those activities in the service sectors least subject to distance effects, namely digital and internet enabled services. Finally, we conclude that any shift toward city diplomacy may affect the nonmarket capabilities of MNEs, requiring them to adjust their own diplomatic and corporate networks (Li, Meyer, Zhang & Ding, 2018). We illustrate many of these ideas using the example of the Alphabet (Google) Sidewalk Labs project in Toronto, Canada.

2. A Two-Tier Framework of Economic Diplomacy

We first present a two-tier organizing framework of economic diplomacy.[3] Economic diplomacy refers to state actions that open markets to trade and investment, including multilateral treaties and various promotion activities that cross borders.[4] The framework is summarized in Figure 1.

Figure 1 About Here

In our framework, the first tier involves state actions, and the second tier involves interactions between the state (or subnational units) and firms. In the first tier, at the country level, we identify two forms of economic diplomacy: trade diplomacy, which includes treaty commitments by the state, both bilateral and multilateral, and commercial diplomacy, which involves each state establishing specific agencies to promote trade and investment (Lee & Hocking, 2010). We refer to the latter in the text as TIPAs (trade and investment agencies), but depending on the country, investment and export promotion can be separate, and each can encompass a wide range of activities from incentives to using trade and diplomatic missions (Moons & van Bergeijk, 2017). In Figure 1, we also distinguish agencies focused to investment promotion (IPAs) and to export promotion (EPA).

Therefore, as illustrated in Figure 1, in Tier 1 the state engages in trade diplomacy through trade and investment agreements that limit spatial transaction costs by lowering trade

[3] Some readers will recognize that our approach borrows from the early work of Ramamurti (2001) on two-tier bargaining models of FDI, and subsequent adaptations of his model in other contexts (Li, Newenham-Kahindi, Shapiro & Chen, 2013).

[4] There is debate over how to define economic diplomacy, largely between those in international relations who tend to reserve it for decision-making and negotiation at the state level, for example bilateral and multilateral trade negotiations, but do not include investment and trade promotion (Woolcock & Bayne, 2018), and those in international political economy who use the term to refer to promotion activities (van Bergeijk & Moons, 2018). We blend these two approaches, noting that opening trade and investment promotion offices abroad has been likened to signing a free trade agreement with that country (Cruz, Lederman & Zoratto, 2018).

barriers (tariff and non-tariff) and reduces political risk by offering protection against arbitrary state action. In addition, the state takes measures to promote trade and investment by creating agencies (TIPAs) to provide information, incentives and resources to address market failures associated with information asymmetries arising because potential investors and exporters lack specific information about the host market (Wells & Wint, 2000; OECD, 2018). At the firm level, in Tier 2, we find MNEs responding to these state actions by choosing the appropriate locations for trade and investment and by negotiating conditions for market entry, often involving their own corporate diplomacy initiatives.

We use this framework to consider the adequacy of policy tools to promote contemporary trade and investment, with a specific focus on trade and investment in services.

3. Trade in Services and Implications for Economic Diplomacy

Most of the empirical evidence on international trade and investment is derived from some version of the gravity model, which proposes that trade or FDI between countries is driven by the size (GDP) of the home economy, the size of the host economy and the distance between them (Anderson & van Wincoop, 2003; Baier & Bergstrand, 2009; Bloningen, 2005; Head & Meyer, 2014). Gravity models therefore suggest that it is not random with whom countries and firms trade or undertake FDI; economic size of either partner increases trade and FDI, while distance between them, capturing frictional factors and behind that transaction costs, reduces both. Moreover, the recent evidence suggests that, despite the significant decline in transport costs which are argued to be a major source of distance effects for exports, the impact of distance for trade in goods and FDI remains almost as important now as twenty or thirty years ago (Head & Meyer, 2014; Baier et al, 2018)[5]. Thus, trade and investment in goods remains an area where

[5] For example, PwC (2017) argues that gravity effects remain substantial because of regional supply chains and hub production sites of MNEs. Additionally, distance appears to play an even more marked

physical distance continues to matter and it is not surprising that recent evidence suggests that deepening trade relationships with near-partners may be more effective in expanding existing trade while trade agreements focused on goods with more distant partners may not be as effective (Baier et al, 2018; Freeman & Pienknagura, 2019).

However, there has been less analysis of trade and investment in the services industries, perhaps because it was widely believed that most services were not tradable (Gervais & Jensen, 2019). Certainly, accounting for trade and investment in services can be challenging as direct measures may not fully capture their importance. This is because services trade is often indirect and embedded in the export of final goods through increasingly disaggregated global value chains (Bohn, Brakman & Dietzenbacher, 2018). This also implies that higher trade in goods may also increase trade in services (Ceglowski, 2006). Finally, trade in services can occur in various ways, including the movement of information, capital and people. Figure 2 follows the World Trade Organization (WTO) classification of the four modes of supply by service industries, described in the notes to that Figure.

Figure 2 About Here

Consequently, the factors driving trade and investment in services are complex and might differ markedly from those for goods, implying the need for a more contingent policy framework. In particular, the provision of services, notably digital services, may not be impeded to the same extent by physical distance (mode 1). However, Figure 2 suggests that distance may still matter, for example for face-to-face meetings (mode 4). In fact, the empirical evidence on the importance of distance to trade in services is mixed. Some studies find that distance *per se* has not been found to be a significant factor in services trade (Kandilov & Grennes, 2012;

role for intermediate than final goods, because the former are an important component of supply chains (Freeman & Pienknagura, 2019; Ignatenko, Raei & Mircheva, 2019).

Walsh, 2008), particularly when the services are provided online (Alaveras & Martens, 2015; Lendle, Olarreaga, Schropp & Vézina, 2016). However, trade in information-based digital services may rely on countries being virtually rather than geographically proximate, especially trade in financial, communication and insurance services (Hellmanzik & Schmitz, 2015). Moreover, where services are traded through a commercial presence (mode 3), such as an R&D lab, and involve the international transfer, absorption and use of knowledge, their sensitivity to distance is significantly less than with manufacturing FDI (Castellani, Jimenez & Zanfei, 2013).

On the other hand, some studies find that physical distance is important for trade in services (Christen 2017), though the costs are declining over time (Christen, 2017; Head, Meyer & Ries, 2009), or are lower than for goods (Bohn et al, 2018; Eaton & Kortum, 2018).[6] Cultural and contextual distance has also been found to be a significant impediment to trade in services (Harms & Shuvalova, 2016; Nordås, 2018). Most recently, PwC (2019) estimated gravity models for UK trade in goods and services, and found that distance mattered approximately to the same degree for both, though the impact of distance on trade in services was sector-specific, with the largest impact being in industries like construction where the provision of services was linked to the provision of goods. It is also important to note that even when trade costs in services are high, there is only limited evidence that trade agreements in fact reduce such costs (Miroudot & Shepherd, 2014). Thus, on balance, there is no overwhelming evidence suggesting that distance matters less when establishing economic trade relations focused on services, although this is likely less true of those which rely on virtual connectedness between countries or the international transfer and absorption of information.

[6] However, the results may be sector dependent (Christen & Francois, 2017); for example, there is evidence that banking and financial services are distance dependent (Brei & von Peter, 2018).

In addition, economic diplomacy has proved problematic in the case of services. The very breadth of the nature of services outlined in Figure 2 creates regulatory and administrative complexity (OECD, 2019b); multiple opportunities for cost enhancing policies; and the possibility of lobbying by incumbents (Rodrik, 2018a). Trade costs in services can be much higher than in the goods sector because of the significant regulatory burdens facing trade in the services sector, which pertain even to the European Union single market (Miroudot, Sauvage & Shepherd, 2013). Thus, policy barriers or regulations, as measured by the OECD Services Trade Restrictiveness Indices (OECD, 2019a), remain high in many countries and have a negative and significant impact on total services trade (van der Marel & Shepherd, 2013). Service liberalisation agreements are therefore much harder to achieve when compared with trade in goods because the former are directly affected by domestic industry regulation in areas such as financial services, public sector procurement, public provision of services such as health or education, health and safety standards, transportation and communications (Crozet, Milet & Mirza, 2016). In addition, trade in services includes elements of foreign investment and movements of people (Sauvé & Roy, 2016). These factors tend to be politically sensitive and very difficult to achieve through trade agreements, and therefore restrictions on trade in services can be higher (PwC, 2019).

In summary, while geographic distance may at times matter less for trade in services, *contextual distance* matters a great deal. For example, the OECD (2019b) concludes that although digital transactions are increasing, so are the barriers to their provision. Behind the border, regulations and cultural differences create trading costs in services. Moreover, measures to address these costs are extremely difficult to build into trade agreements, so that economic diplomacy can be difficult. In addition, TIPAs do not usually have the power to change these

regulations. In fact, there is only mixed evidence about the effectiveness of TIPAs at the national level. One recent meta-analysis (Moons & van Bergeijk, 2017) finds little evidence that TIPAs are effective, although other recent surveys are more positive (Cruz et al, 2018; Paquin, Wooton, Roy, Eiser & Rious, 2018). Nevertheless, it is not clear that national commercial policies are effective, though to our knowledge there is no evidence specific to services.

Our analysis suggests that country-level economic diplomacy can be effective, but in limited areas. Trade and investment in goods remain constrained by distance and it is not clear that commercial diplomacy is broadly effective. Trade in services faces a variety of obstacles, including regulatory distance, that are difficult to overcome using national-level policy instruments relating to trade and commercial diplomacy.

4. Why Cities are Important

Thus far, we have approached the relevant policy questions through the lens of country-level economic diplomacy. It is now widely understood in the international business literature that countries are not always the appropriate unit of analysis (Mudambi et al, 2018a) and in this section we therefore explore the importance of cities by examining the interrelationships among multinational enterprises, global value chains and cities.[7]

4.1 The nature of global cities

We first discuss the emergence and nature of global cities, their link to knowledge creation and diffusion and how they have become attractive locations for the knowledge-based and professional services activities of the modern MNE. Cities and MNEs are connected through

[7] For the purposes of this paper we focus on countries and cities, but we acknowledge that subnational regions such as provinces or regions can be important (see Paquin et al., 2018). We also note that when discussing cities, one can "zoom in" to discuss specific clusters or "zoom out" to consider city-regions (Mudambi et al, 2018a).

changes in GVCs so high value-added knowledge-based services and activities such as R&D, marketing, legal, accounting and financial services agglomerate in a relatively small number of global cities, which act as both homes and hosts to MNEs (Mudambi et al, 2018a).

Cities, particularly global cities, provide access to a wide variety of complementary services, large pools of specialized labour, and a sophisticated transportation and communications infrastructure; agglomeration benefits that limit spatial transaction costs (Sassen, 2005; Davis & Dingel, 2019; Fujita, Krugman & Mori, 1999; Glaeser, 2008; Bryan et al, 2019). The agglomeration benefits of cities have meant that both world population and economic activity are increasingly concentrated in major cities and these cities represent important trade hubs (Berube & Parilla, 2012; Trujillo & Parilla, 2016). In some countries, this has also resulted in country GDP being concentrated in a relatively small number of cities[8].

Thus, large, global cities are not only critical to the world economy, but there is a symbiotic and co-dependent relationship between knowledge-based MNEs and global cities (Cano-Kollmann, Cantwell, Hannigan, Mudambi & Song, 2016) which has become a defining feature of the evolution of the global economy (McKinsey Global Institute, 2019; Trujillo & Parilla, 2016). The link between the location of higher value-added activities and cities occurs because cities can minimize the spatial transaction costs related to trade in knowledge-based services (Cano-Kollmann, et al, 2016; Cano-Kollmann, Hannigan, & Mudambi, 2018), and in particular those that are contextual in nature (Mudambi et al, 2018a).

MNEs are increasingly becoming knowledge-based firms that create and sell knowledge-based services and whose value depends on intangible capital (Haskel & Westlake, 2018;

[8] For example, London accounts for some 28% of UK GDP, while Toronto and Montreal together account for about the same percentage of Canadian GDP (Estrin, Shapiro, Cote, Meyer, Li & Borovinskaya, 2018). At the same time, cities account for some 64% of total British exports, and 77% of services exports, much of the latter coming from London (Whearty, 2019).

Mudambi, 2008). At the same time, the unbundling of activities along the GVC means that the different activities are performed in different locations and traded internationally (Gereffi, Humphrey & Sturgeon, 2005; Ignatenko et al, 2019). Thus, countries, and in the case of services and intangible goods, cities, tend to specialize in some specific segment of the GVC. The nature of the division of activities across countries (Gereffi & Fernandez-Stark, 2016) often suggests that higher value-added activities associated with R&D, design and business support services tend to be located in cities mostly, but not entirely, in developed countries.

However, while the emergence of global cities is about the location of high value elements of the value chain (which might favour developed countries in the case of locating research and innovation centres), it is also about the location of professional business service firms which locate around the globe and in the process help to create networks of connected cities. As we discuss below, these firms can and do locate in both developed and developing countries. Thus, global cities are also characterized by the broad presence of high value-added professional services firms, located in a large number of cities, including developing country cities. At the same time, some may also be home to more specialized innovation clusters. Importantly, firms that are not in the service industries often undertake these investments. One estimate suggests that in 2011, 35% of foreign investment projects by large MNEs (including those in non-service industries) were in support services, including marketing and sales, design, and R&D (Belderbos et al, 2016), up from 25% in 2003. These investments include units with coordination functions such as divisional or regional headquarters (HQ) or holding companies.

One important consequence of the unbundling of GVCs is that R&D and other innovative activities associated with MNEs are increasingly dispersed around the world, and then transferred internally. One example is provided by van den Buuse & Kolk (2019) who describe

how companies like Cisco, IBM and Accenture developed "smart city" technologies that they test in various locations but share the knowledge gained with other of their units. However, the decisions regarding the location of these activities are frequently based on city, not country, criteria. For example, Samsung's semiconductor business unit has R&D centres in 11 cities around the world. Belderbos et al (2016) conclude that some 40% of inbound Greenfield global cross-border R&D projects are directed towards 57 global cities and 40% is accounted for by large MNEs. Importantly, the 57 global cities also account for about 40% of outbound R&D projects. Global cities are therefore primary homes and hosts to knowledge-based investments in R&D and design, as well as other advanced business services. This suggests that cities should be seen as critical elements in the creation and global diffusion of knowledge, with MNEs acting as orchestrators and connectors of spatially dispersed knowledge sources (Cano-Kollmann et al, 2016).

Indeed, in the international business literature, the MNE is increasingly conceived as a global creator, organizer, and connector of knowledge networks and value-added activities across locations, rather than a simple vehicle for technology transfer between given locations (Beugelsdijk & Mudambi, 2013; Cantwell, 2017; Mudambi et al, 2018a). MNEs orchestrate global trade often through *internal* transfers of knowledge and services (Iammarino & McCann, 2013). Innovative and knowledge-based activities are therefore understood as a combination of firm- and location-specific advantages. Thus "the two processes of innovation and internationalization have become ever more interconnected as central drivers of development" (Cantwell, 2017: 41). The increased importance of knowledge-based activities to the MNE and the global sourcing of knowledge accompanying the emergence of global value chains have therefore "linked localized innovation systems to international business and to international

knowledge exchange" (Cantwell, 2017: 42)[9]. We submit that most of this linkage occurs within cities.

Thus, global cities both attract and create knowledge-based firms. Indeed, recent literature has focused on the role of cities as facilitators of entrepreneurship and new firm creation (Audretsch, Belitski & Desai, 2015; 2018), including those that are "born global" MNEs (Knight & Liesch, 2016). Many of these are likely to be based on digital platforms or knowledge platforms that result in firms selling services or locating abroad at an early stage (Autio, Szerb, Komlósi & Tiszberger, 2018).

4.2 Global cities and the location of business activity

Although the importance of cities has been studied by economic geographers, it has until recently been less prominent in the international business (IB) literature which has viewed these location issues from a country perspective (Iammarino, et al, 2018). However, there is now an increasing recognition by scholars of the role of cities as essential components of the process of knowledge creation and diffusion across borders (Cano-Kollmann et al, 2016; Mudambi et al, 2018b; Santangelo, 2018). A number of empirical studies confirm that global cities are preferred locations for MNEs (Asmussen, Nielsen, Goerzen, & Tegtmeier, 2018; Belderbos, Du & Goerzen, 2017; Belderbos et al, 2020; Blevins, Moschieri, Pinkham & Ragozzino, 2016; Goerzen, Asmussen & Nielsen, 2013)[10]. For example, Goerzen et al (2013) argue that global cities reduce various costs of distance, often referred to as the liability of foreignness, because they agglomerate advanced service providers, facilitate knowledge flows within and between

[9] "Localized innovation" could refer to a sub-national location, including a global city, or a specialized knowledge cluster within a global city, or a city-region (a region anchored by a global city such as the "golden horseshoe" in the Toronto area).

[10] There is also evidence that peripheral cities are preferred locations if they are proximate to a global city (McDonald, Buckley, Voss, Cross & Chen, 2018).

MNEs, and provide cosmopolitan environments that welcome the foreign presence. Global cities thus minimize contextual distance, and this is possibly more important when such distance is high at the country level (Belderbos et al, 2020). Moreover, as emphasized by Belderbos et al (2016), MNEs have begun to both internationalize their R&D activities, and to co-locate with other MNEs in specific city locations. Thus, global cities provide strong incentives for MNEs to locate in them, and these same incentives encourage co-location and co-evolution of firm and location.

Global cities are also preferred locations for HQ functions. For example, Belderbos et al (2017) find that connected global cities are favoured as locations for regional HQs. Asmussen et al (2018) find that global cities provide locational advantages for regional headquarters, which in turn serve as a "beachhead" investment. They provide as an example, the case of Schneider Electric SA, the French energy management and engineering MNE with operations in more than 100 countries. Schneider's main subsidiary in Denmark is Schneider Nordic Baltic A/S, located in central Copenhagen, listed by AT Kearney as a global city. However, Schneider Nordic Baltic A/S, owns other firms in Denmark, and thus operates as a regional investment platform from its base in Copenhagen. MNEs also prefer to locate R&D and design activities in global cities, as shown for example by Castellani & Lavoratori (2017). At the cluster level, Li & Bathelt (2018) find that knowledge intensive firms are more likely to locate in clusters, both at home and abroad. Thus, MNEs leverage local knowledge pools by strategically locating affiliates across clusters. In addition, there is evidence that internationally connected innovation clusters have performance advantages, supporting the idea that firms and locations co-evolve (Turkina & Van Assche, 2018).

Indeed, one prominent approach, taken by GaWC[11], to defining and ranking global cities (Beaverstock, Smith & Taylor, 1999; Taylor, 2004; Taylor, Ni, Derudder, Hoyler, Huang, Lu, Pain, Witlox, Yang, Bassens, & Shen, 2009) builds on Sassen (1991) and uses data on the presence of advanced producer services (MNEs in advertising, law, accounting, finance, and insurance) as the basis for ranking cities. Unlike other classifications largely based on the attributes of each city considered separately, GaWC ranks global cities based upon the magnitude of a city's business service connections to other major cities (https://www.lboro.ac.uk/gawc/world2018t.html). The ranking of global cities therefore incorporates their position in a global, interconnected network based on the shared presence of the service MNEs. Global cities are understood as key nodes in a global knowledge and trade network, rooted in the location decisions of a set of MNE service providers. It is important to note that the ranking method is based on global connectedness, but still allows for cities that house more specialized clusters. Thus, while New York and London are rated highest (alpha ++), Boston and Tel Aviv are ranked as beta +.

More recent versions (Taylor et al, 2009) allow individual cities to be ranked but also ranks the importance of city pairs in the network. We illustrate the relationships in Figure 3, in which the presence of 100 global service providers are measured in 315 cities in 2010 (Taylor et al, 2009; Taylor, Hoyler, Pain & Vinciguerra, 2014).[12] These data are used to both rank the cities and to establish connections between them. For our purposes, the point to note is that global cities are connected by the location decisions of MNEs to other cities that are distant from

[11] https://www.lboro.ac.uk/gawc/gawcworlds.html

[12] The number of MNEs and cities in the sample has increased over time and as of 2018 numbers 175 MNE business service providers located in 525 cities (https://www.lboro.ac.uk/gawc/rb/rb300.html)

them, with the implication that global cities both develop their own networks and minimize the spatial transaction costs associated with distance.

Another way to make the point is to consider whether distance matters in explaining these connections between cities. To explore this, we estimated a gravity model explaining the extent of inter-city bilateral connections in the GaWC dataset by the size (population) of each city and the distance between them for each year. The GaWC city classification for 2018 groups city pairs into ten categories by rank based upon the position of the city pair in the network based on service connections to 707 other major cities, using over 177 million measures of connections between pairs of cities. For example, New York-London are the highest rated city-pair (alpha++) and alone in their category. The next group (alpha+) comprises city pairs such as London-Hong Kong and New York-Paris. In total there are 10 such rankings.

We use ordinal regressions (with rank being assigned a number between 1 and 10) and in striking contrast to the standard gravity literature (e.g. Head & Meyer, 2014), we do not find any significant effect of geographic distance (kilometres) on the bilateral connectedness of the city pairs: the rank of the city pair is not statistically significantly related to distance between the cities, for 767 city pairs. Thus, these relationships between cities, including between MNEs in the service sector, are not affected by the traditional geographic (transactions cost) factors that have been established to limit trade in goods[13]. While not definitive, this evidence suggests that global cities help MNEs to offset the costs of distance, particularly in knowledge-intensive business services, by providing location-specific advantages that match the firm-specific needs of MNEs.

Figure 3 About Here

[13] The full results are available from the authors on request.

5. Introducing City Diplomacy: A Three-Tier Framework

Though, as we have seen, cities play a critical role in facilitating international trade and investment in services, they are very rarely part of the policy conversation, at least in the IB literature. We therefore propose to recognize the importance of this network of global cities by augmenting our previous framework with what we refer to as a Three-Tier Framework of Economic Diplomacy. The new framework explicitly accounts for cities and the locational preferences of services- and knowledge-based MNEs and is therefore more "place sensitive" (Iammarino et al, 2018). The framework is presented in Figure 4.

Figure 4 About Here

The international relations and urban studies literatures have recognised the role of cities as international actors (Acuto, 2016; Herrschel & Newman, 2017; Ljungkvist, 2016; Taylor, 2005). Their actions have been termed "city diplomacy" (Acuto, 2013), which involves the conduct of external relations by cities, including interactions with other cities, nation-states and corporations. Many global cities have an international strategy often represented by a dedicated international office, and participate in various international networks (Acuto, Decramer, Kerr, Klaus & Tabory, 2018). Thus, for example, the city of Los Angeles created an Office of International Affairs in 2017 to coordinate relations with institutions in some 100 countries (Hachigian, 2019), and the same is true of the City of New York, which has established the Mayor's Office for International Affairs. Thus, cities have become increasingly active in various types of international policy making and global governance including on climate change, terrorism, poverty, culture and (importantly as we write) pandemics (Ljungkvist, 2016). An example of cities taking autonomous policy action is the area of climate change where not only have cities taken coordinated policy actions (Bouteligier, 2013; Bulkeley, Carmin, Castán Broto,

Edwards & Fuller, 2013), but they have formed a multilateral group, C40, to coordinate their actions (C40 Cities, 2014).

Acuto & Rayner (2016) provide evidence suggesting that the number of formal city networks has increased rapidly and may now number some 200, the majority international. At the same time, cities engage in bilateral agreements with partner cities on specific issues (Jayne, Hubbard & Bell, 2011). Thus, while cities cannot sign treaties in the same way as nation states, they do engage in both bilateral and multilateral arrangements. Some of these arrangements have a commercial focus such as the publicly funded 'Sharing Cities' initiative (http://www.sharingcities.eu/) aimed at helping EU cities change attitudes and procedures to implement replicable smart cities solutions or the Asian Network of Major Cities 21 aimed at addressing common challenges such as industrial development. Other such initiatives are not specifically commercial in nature but create channels of information and cultural exchange that can result in locational advantages for member cities. For example, global cities utilize city networks to provide global public goods that reinforce their comparative locational advantages—cleaner air, sophisticated and cosmopolitan culture, transportation and health infrastructure (Goerzen et al, 2013; Pisani, Kolk, Ocelík & Wu, 2019).[14]

It is also important to recognize that although cities cannot necessary sign trade agreements, neither are they necessarily obliged to abide by them in all countries. As we have suggested above, trade agreements can be complicated by the existence of a variety of "behind the border" restrictions including for example government procurement provisions, and US cities can choose not to participate. Thus only 37 US states signed on to the WTO Agreement on Government Procurement (https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm), but

[14] As noted by a reviewer, there may be causality issues surrounding some city networks in that the network emerges from existing commercial relationships rather than the reverse.

even their commitments did not extend to their cities. Thus, the success of trade agreements depends in some measure on the participation and agreement of cities.

However, cities do not simply engage in broad diplomacy: they are increasingly involved in city-level commercial diplomacy (van Bergeijk & Moons, 2018). Thus, most global cities engage in investment and trade promotion activities paralleling those of national governments. Unlike the cooperative networks described above, these activities may be competitive (Gordon, 1999) for example by offering MNEs financial incentives and lower taxes (Becker, Egger & Merlo, 2012). Urban policy is therefore linked to national policies with the same goals of promoting international trade and investment, providing a possible link between national and city based commercial diplomacy, as suggested in Figure 4.

Commercial diplomacy applied to country-level organizations includes not only the use of trade and investment promotion agencies (, but a variety of other measures such as organized state visits and trade missions. These have been growing rapidly (OECD, 2018) and represent the area in which the policies of cities and nations most clearly intersect. Thus, both countries and the global cities within them are to various degrees engaged in trade and investment promotion (Harding & Javorcik, 2011; 2013; Sztajerowska, & Volpe Martincus, 2018). However, while there is a relatively substantial academic literature on the nature and effectiveness of TIPAs at the national level (see for example Moons & van Bergeijk, 2017; Cruz et al, 2018; OECD, 2018), there has been far less research on subnational entities (Paquin, et al, 2018), and almost none on cities (Ni, Todo & Inui, 2017), despite the hundreds of TIPAs that exist at the city level (Tavares-Lehmann & Tavares, 2017).

We conclude that global cities are deeply engaged in city economic diplomacy, both through the creation of city networks and through commercial diplomacy linked to the creation

of TIPAs. These activities appear to complement comparable policies at the national level, but the degree to which this is true, or the effectiveness of the policies is unclear.

The degree of complementarity will depend on the extent to which country-level economic diplomacy is consistent with city diplomacy. In general, countries may find it politically difficult to provide policies overly focused on cities. When eliminating regional disparities is a national goal, investment promotion activities may focus more on attracting investments to peripheral areas. Similarly, trade agreements with provisions designed to protect domestic manufacturing, often located outside of global cities, might conflict with the interests of cities. For example, the recently re-negotiated NAFTA (USMCA, CUSMA) contains provisions clearly designed to protect US manufacturing, particularly automobiles, in the form of country of origin and labour provisions, as well as provisions to promote the US dairy industry. At the same time, it contains provisions on intellectual property and digital rights to facilitate digital trade, which may benefit cities (see Table 1, below). These issues point to the continued need for coordination both among cities (which have a shared interest in these issues) and between cities and the national government.

6. Modifying Trade and Investment Policies in the Light of a Changing World

We have illustrated how the process of globalization is changing as economies transition toward knowledge-based services and as global cities become more important as preferred locations for existing MNEs, and potential homes to new ones. In consequence, country-level economic diplomacy must increasingly account for services, and city diplomacy should become an increasingly important policy tool for cities (and their countries) intent on attracting and creating knowledge-based companies. Thus, traditional economic diplomacy at the national level

needs to be augmented more fully to address issues raised by trade in services and to coordinate city-level and national-level economic diplomacy. Our discussion has highlighted two broad, non-mutually exclusive policy directions: the development of trade agreements between countries with deeper and broader trade in services provisions; and city-based trade and investment promotion. We discuss each in turn.

6.1 Trade diplomacy in services

As we have noted, trade in services is more complicated than trade in goods because it involves a heterogenous range of cross-border transactions, including movements of knowledge, people and capital. In addition, many of these service transactions are relation-specific, resulting in difficulties in negotiating contracts, and making it difficult to develop broad rules to protect them in a trade agreement. Thus, services agreements must include provisions on foreign ownership, cross-border movement of people, and protection of intellectual property as well as touching on new areas such as digital services and e-commerce. Negotiating trade in services agreements is therefore more complex than for goods and can be more politically sensitive.

Just as trade in services has increased at a rapid pace in the last few decades, so have the rules governing it. These have been negotiated at the regional or bilateral level as well as multilaterally at the WTO under GATS and the ongoing TISA. The WTO currently lists 302 active regional trade agreements, many negotiated during the period of rapid growth in the 1990s. The majority of these would have provisions dealing with trade in services, and yet there is limited evidence to suggest that they have been successful (Nordås, 2018). However, as we have suggested, the nature of global services activity has been changing. The way services flow across borders has been fundamentally altered by the fragmentation of production and the

associated emergence of GVCs, by the increased transfer of knowledge within MNEs and by the increased importance of intangible and digital assets.

In considering an effective set of policies aimed at facilitating trade in services, what lessons can we take from existing state-of-the-art trade agreements which address services, such as CETA, CPTPP and TISA, and to what extent have these instruments been rendered irrelevant by their inability to address changing service sector dynamics? New trade agreements and in particular CETA, which is considered the gold standard, have provisions aimed at liberalizing services through market access and non-discriminatory treatment for service providers. Sector-specific provisions deal directly with sectors such as financial services and telecommunications but also address new areas such as e-commerce and maritime transport services. Furthermore, CETA seeks to facilitate the provision of services once they cross the border through rules on domestic regulation as well as by tackling regulatory cooperation and coherence and addressing the mutual recognition of professional qualifications.

The problem is that CETA and other services agreements continue to provide for special treatment for countries' "sensitive sectors", allowing them to maintain market access restrictions that inhibit trade and investment flows[15]. Perhaps more importantly, existing rules have predominantly been designed to address the export of services as a final activity from a national firm and not as an intermediate input in the context of multiple suppliers and locations (Stephenson, 2016). The current trading rules for services found within even the latest regional agreements or at the WTO, are therefore being rendered irrelevant by the role played by services

[15] Canada, for example, has preserved costly restrictions in the transport, finance and telecoms sectors, including restrictions and regulatory barriers that hinder foreign market entry and competition (van der Marel, 2016).

within GVCs. Table 1 outlines the evolution in breadth and depth of key provisions addressing services trade in more recent trade treaties.

Table 1 About Here

Despite recent advances, trade agreements need to be further augmented to facilitate the rapid increase in trade in services. First, any new trade agreement must address services trade in greater breadth and depth than has traditionally been the case, reflecting and going beyond the more recent achievements under CETA and the CPTPP. The objective should be more comprehensive coverage of the new issues discussed above which recognise the role of services in global value chains, as well as that of technology and information flows in the provision of services. Moreover, it is essential that new areas such as e-commerce are covered alongside provisions on domestic regulation and commitments to achieve regulatory cooperation. It is important to note here that it has been especially difficult and slow to date to develop global agreements on data and digital governance (Burri, 2017; Ciuriak, 2018).

Second, as highlighted in Table 1, any trade agreement negotiated on services market access should be based on a negative list approach, covering all services unless explicitly indicated to afford greater depth of coverage Additionally, agreements must seek to allow for fewer exemptions and restrictions than for example under CETA, particularly in sectors where countries have a comparative advantage.

Third, because traditional trade rules do not fully recognise the reality of cross-border service activity, in which services act as intermediary inputs in GVCs, policy makers should consider additional complementary policy levers for reducing regulatory barriers to service market access. To this end, they should seek sectoral, regional and multilateral cooperation initiatives with the goal of achieving coherence in regulations and avoiding bottlenecks in GVCs.

Such cooperation initiatives might take the form of 'supply chain councils' (Hoekman, 2014) or regulatory councils modelled on CETA's Regulatory Cooperation Forum (van der Marel, 2016).

All of this suggests that the policy issues to be overcome in trade negotiations arise not only because contextual distance is so important in services, but also because the emergence of new knowledge-based services create new challenges for economic diplomacy. This complexity and uncertainty surrounding cross-border services provision also affects the work of trade and investment promotion agencies, especially at the national level.

6.2 Trade and Investment Promotion and (Global) Cities

A clear conclusion from our analysis is that policies which foster innovation and clusters in cities are critical because these investments can attract knowledge-based FDI, promote trade in knowledge-based services and can facilitate the creation of home-grown MNEs. This is a logical implication of our three-tier framework of economic diplomacy in Figure 4. Such policies should, therefore, be understood as the provision of trade- and investment-related infrastructure and should incorporate the specific nature of global cities, and the different roles each can play. In other words, we propose that domestic policies that strengthen global cities, global clusters or global city regions should be understood as part of a broader trade and investment promotion strategy.

Specifically, our policy proposal is that innovation strategies be explicitly linked to trade and investment promotion strategies, with a clear focus on cities. In fact, there is evidence of movement in this direction at the national level, but without a clear reference to cities. The OECD (2018, Fig. 1.8) reports that most national TIPAs have more than one mandate, and most often the related mandates are trade promotion and innovation. There is considerable support for the merging of trade and investment functions between the World Bank and the UN (see for

example ITC, 2014). It is argued that investment and trade promotion activities are complements in that promoting inbound FDI also improves export competitiveness. Many countries have adopted this approach, including the UK. Our analysis of services clearly points to the difficulty of separating trade and FDI, and the importance of not viewing them as alternative policy goals.

However, we are proposing that a further step be taken that would include innovation. The OECD reports that only 28% of investment promotion agencies (IPAs) perform both innovation and export promotion, and they suggest that this is "a judicious choice when IPAs seek to attract high-tech and R&D driven MNEs that can invest in high value-added activities" (2018: 26). We agree with this assessment and extend it by arguing that the extension of IPAs to include exports and innovation cannot be undertaken without the inclusion of cities. The inclusion of cities in turn will require a deeper understanding of the differences among cities in terms of global connectedness and specialized cluster development. Thus, a focus on innovation should include a well-defined cluster strategy for cities which includes support for investments in the infrastructure that connects cities with their peripheral areas. This may be understood as a specific example of the "zooming in" (clusters) and "zooming out" (city-regions) strategies discussed by Mudambi et al (2018a).

In summary we are suggesting that national policies on trade and investment cannot be divorced from innovation strategies, and innovation strategies cannot be divorced from cities. However, we have also emphasized that cities engage in their own form of economic diplomacy, and the nature of these activities remains under-studied and poorly understood.

While more research is required, there is some evidence that the scope of TIPA operations varies considerably across cities. For example, the Vancouver Economic Commission (VEC) "works to position Vancouver as globally recognized city for innovative, creative and

sustainable business" (http://www.vancouvereconomic.com/about/). This means that the VEC acts to both attract foreign investment and promote Canadian firms at home and abroad. It has followed a very targeted strategy in terms of sectors, focusing on high technology, digital entertainment, and green economy sectors, and the development of local clusters that support them. Thus, Vancouver offers a model of a TIPA that combines elements of investment, trade and innovation promotion. Although it has a global network, centred around cities, it has a particular focus on the Asia Pacific, and in that way works to diversity trade. Vancouver is therefore a global city, but in a very targeted way (a beta+ city in GaWC terms).

In contrast London and Partners is the Mayor of London's official promotion agency (https://www.londonandpartners.com/about-us). Like Vancouver, its scope includes both foreign and domestic investment promotion, but it considers a broader set of industries and activities. For example, it is responsible for conventions, travel and tourism, and overseas students. London and Partners explicitly supports innovation and cluster development in a range of knowledge-intensive sectors, and links them to both FDI and trade. Thus, London and Partners has also created a TIPA that combines innovation, trade and FDI promotion. It has 14 offices abroad, in 7 countries including offices in "distant" locations like San Francisco, Los Angeles, Toronto, Bangalore, Mumbai, Shenzhen, Shanghai and Beijing. London is an alpha++ city.

These are only examples that highlight how little we know about city level diplomacy. To begin to address the deficiency in our knowledge of city diplomacy, we went on to select a sample of cities from the GaWC database, all from the top three categories, and explored their investment promotion strategies. Our findings, derived from the websites of the various city-based TIPAs, are reported in Table 2.

Table 2 about here

We organized Table 2 around strategic elements common to many organizations: governance, horizontal scope, vertical scope and geographic scope. We summarize these results as follows:

1. We find that although most TIPAs are public agencies of the relevant city, in a few cities like London and Chicago, they are public-private partnerships, and some are separate non-profit entities (Toronto). This suggests that future research may focus on these governance choices and their implications.
2. The horizontal scope of activities varies from a relatively narrow focus on investment promotion (Sao Paulo) to investment promotion plus support (training, subsidies, consulting, as in Moscow and Tokyo) to extremely broad mandates that can include trade and tourism (London) and broad economic development (Chicago, New York). Most cities also have other related agencies to focus on trade (Hong Kong, Moscow), or innovation or entrepreneurship (Toronto, Singapore). Thus, from the perspective of horizontal scope, there is considerable diversity among the strategic choices made by TIPAs. In particular, some are responsible for broader economic development of their city, and some are not. These strategic choices have not been widely studied.
3. Vertical (sector) strategies are apparently more uniform. Consistent with the discussion in section 4, most TIPAs focus on knowledge- and technology-based sectors. However, a small number did list more traditional industries such as Milan (manufacturing) and Sao Paulo (aerospace), though both sectors might include high tech components. Our sample is limited, and it remains to be seen whether a broader sample would also suggest a strategic focus by cities on these same sectors. These

results are also not specific enough to understand whether and to what extent these vertical choices are defined by specific clusters.

4. The geographic scope of our sample exhibits considerable variation both in terms of number of countries in which they are represented, but also in terms of how they choose to be represented. Although most city TIPAs are represented abroad, the number of countries differs considerably as does the form of representation which ranges from having offices abroad (London), sending missions abroad (Chicago), partnering with other cities (Sydney), or sharing facilities with sister agencies with offices abroad (Beijing).

In sum, city level TIPAs exist in all major global cities in our sample and are active across a range of policy areas. The most striking thing about Table 2 is the scale, range and heterogeneity of their activity, suggesting the need for more careful and systematic analysis of the nature and impact of their strategic choices. An important outstanding policy question remains how the activities of these agencies can be understood as part of a national trade and investment strategy. However, the fact that most tend to focus on knowledge- and technology-based businesses suggests the importance of creating a well-defined city strategy that is differentiated both within and across countries.

We do have some general evidence that national investment promotion activities can be effective if they target sectors characterized by bureaucratic obstacles and information asymmetries (Harding & Javorcik, 2011). Whether this applies to cities, and to the knowledge-based and high-technology sectors many of them seek to attract, is certainly a question for future research. A related question is whether city diplomacy is more effective when cities simply promote existing clusters, or whether they are actively involved in developing and promoting

new clusters (horizontal scope). This question is related to the question of coordination across levels of government since the ability to create new localized clusters may depend on the actions of another level of government, for example in supporting universities or transportation and communications infrastructure.

Thus, our policy suggestion is that explicit attention be given to the coordination of national, regional and local objectives, particularly in the areas of knowledge- and technology-based activities. It is true that cities cannot fulfil their economic diplomacy objectives, particularly internationally, without the collaboration of the national government. Cities rely on trade commissioners, trade missions, and other services provided in various countries by the national government. What is not coordinated is the mandate and scope of operations of each city, and in particular a clear understanding of localized advantages of each city. Given the ambiguous evidence on the effectiveness of national trade and promotion activities, increased attention to how they can be better aligned with the activities of cities seems appropriate.

The OECD (2018) points to the variety of stakeholders with which a national TIPA interacts, and the coordination issues that result from these interactions. Although subnational units are one of the stakeholders noted, local governments are given little attention. We argue that cities must be seen as prominent stakeholders and their activities more explicitly coordinated within a national strategy, as suggested in Figure 4. This might not be simple because local agencies may be competing with each other for investment projects, and because the goals of national agencies may conflict with those of cities, as discussed in the previous section.

7. Further Discussion

Our analysis has focused on public policy as related to economic and city diplomacy. We note however that the transition to a more city-based diplomacy may have consequences for corporate diplomacy (Henisz, 2014; 2016). Corporate diplomacy involves building relationships with relevant external stakeholders and corporations can build strong capabilities in managing these relationship (Henisz, 2016). Firms are likely to have focused their corporate diplomacy on national or regional institutions and stakeholders. While this may continue to be important, it is also clear that the emergence of global cities may require MNEs to re-orient their strategies and capabilities to accommodate local politics.

We illustrate this using the case of Sidewalk Labs, a subsidiary of Alphabet (Google's parent), and their entry into the Toronto market in a public-private partnership to revitalize Toronto's waterfront by creating a technology-driven District (essentially a smart-city). Case details are outlined in Table 3. The essence of the matter is that the project involved a series of highly controversial issues ranging from data governance and privacy, to protection and use of intellectual property. For the most part, these issues are not covered by either local (Canadian) law or by treaty (including NAFTA). The resolution of these issues involved significant negotiation with three levels of government (Federal, Provincial, and the City of Toronto). However, local governments and communities created the major obstacles as strong concerns were expressed over broad issues of data governance. This suggests that the ability to manage relationships at the city level may require MNEs to develop or acquire rather different capabilities for stakeholder management than those for other levels of government. Moreover, city diplomacy has one important difference from national economic diplomacy and that difference has profound implications for firms and especially MNEs. City diplomacy does not and cannot involve treaty protection of the kind built into RTAs and IIAs through national

economic diplomacy. This is important because, in the absence of strong services provisions in RTAs, the MNE will be required to negotiate more outcomes with fewer frameworks, possibly with multiple levels of government. This is likely to be the case in the creation or provision of localized knowledge-based services, where that knowledge will be shared globally (Ciuriak, 2018). Thus, corporate diplomacy will be more complex, requiring the negotiation of transaction- or project-specific issues. The more localized is the issue (as would be the case with cities), the more likely the challenge of stakeholder management must focus on local communities (rather that government bodies). In the case of Sidewalk Labs, the end result was that after several years of negotiation, the proposed project was approved on October 31, 2019, but on a dramatically scaled back basis.

Table 3 about here

Finally, our analysis reinforces the emerging literature linking MNEs and global cities. Although we are concerned with policy, our approach is consistent with modern views of the MNE that take more nuanced views of space and place (Mudambi et al, 2018a) and regard them primarily as orchestrators of knowledge flows (Cano-Kollmann et al, 2016). However, future research may well expand on some of the themes raised here. For example, we have relied on the GaWC ranking of global cities to illustrate a number of points. This ranking is based on the location decisions of business service MNEs. Future research could well examine more carefully the role of these MNEs in fostering global connectivity among cities, and the location decisions of other MNEs, in particular those locating R&D and innovation activities. For example, Globerman, Shapiro & Vining (2005) find that the growth and survival of Canadian IT firms was higher when those firms were located within a narrowly defined postal code in Toronto, a postal code that included the major banks, law, and accounting firms, as well as the University of

Toronto. The issue is how to understand the co-evolution of cities housing a heterogeneous set of MNEs.

In a related way, the GaWC data suggests that developing and emerging market cities can be global. It is not clear whether this implies that over time these cities will compete for the location of knowledge-based activities. Rodrik (2018b) has argued that the rise of the knowledge economy may not favour developing countries in the future because their cost advantages in manufacturing become less relevant and the location of higher valued services will occur in developed countries. Whether this is true in the era of global cities remains an important question. Again, the question is how the location of advanced professional business MNEs is linked to the location of R&D and other innovative activities.

8. Conclusion

The transition to a more knowledge-based and services-based global economy, where these services are located in global cities and increasingly move across national borders, often within MNEs, provides a challenge to international trade and investment policy. This is especially the case for digital and data-based services, the location of which will require agreement of cities (and communities) affected because, as we saw in the Sidewalks Labs case, trade agreements have not yet addressed the relevant issues, and therefore direct negotiation between firms and city agencies occurs. We have argued that global cities are critical to this transition and must be incorporated into national economic strategies. This, we suggest, requires going much further than simply consulting cities on matters such as trade negotiations. It means creating and crafting policies that include cities as central players and expanding the range of policy options normally considered. While traditional national economic diplomacy tools like trade and investment treaties, and trade and investment promotion can still be relevant, they are challenged by the rise

of a knowledge-based and intangible-asset based service economy. Inclusion of these issues in trade and investment agreements has proved difficult, while at the same time cities have managed to create conditions that facilitate the growth of the global knowledge economy. Finally, multinational firms will need to augment their corporate diplomacy competences to include these more heterogeneous and complex policy frameworks.

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Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/index.aspx?lang=eng

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World Trade Organization Regional Trade Agreements. http://www.org/english/tratap-e/region-e.htm

The Authors

Christine Côté (PhD, LSE) is a Senior Lecturer in Practice in the Department of Management at the London School of Economics and Political Science. Her research and teaching have focused on international trade and investment policy and the internationalization strategies of MNEs, particularly in emerging markets. Prior to academia she worked as an international trade negotiator with the Department of Foreign Affairs and International Trade Canada where she represented Canada in negotiations at the WTO, the OECD and on bilateral trade and investment agreements. Her professional career also included time as a global strategy and policy consultant to governments in developed and emerging markets.

Saul Estrin (PhD, Sussex**)** is Professor of Managerial Economics and Strategy in the Department of Management at LSE. He has published widely, with 15 research monographs and edited volumes and more than 120 papers on privatisation, corporate governance and comparative/transition economics. He has publications in *Quarterly Journal of Economics; Journal of Economic Literature; Journal of Management Studies; Strategic Management Journal; Journal of International Business Studies and Journal of World Business*, He has worked in recent years on FDI entry mode; institutional theory, business groups, state ownership and governance.

Daniel M. Shapiro (PhD, Cornell) is Professor of Global Business Strategy and past Dean at the Beedie School of Business, Simon Fraser University. He has published five books and monographs and over 100 scholarly articles on international business and strategy, corporate ownership and governance, foreign investment and MNEs, industrial structure, and various aspects of public policy. His research has been published in *Strategic Management Journal, Journal of International Business Studies, Academy of Management Journal, Journal of Management Studies, Journal of World Business* and *International Journal of Industrial Organization*, among others.

Figure 1: Two-Tier Economic Diplomacy

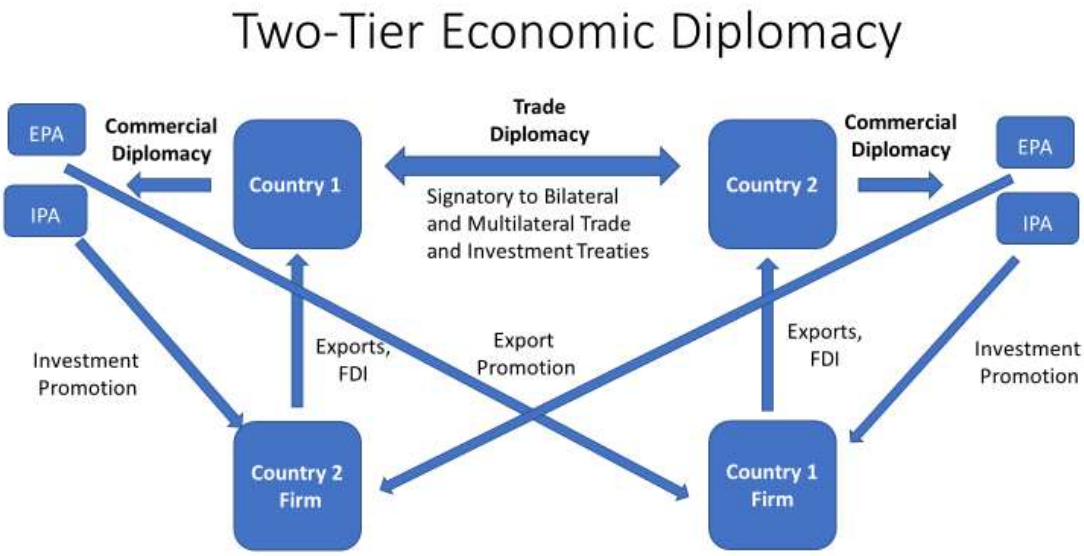
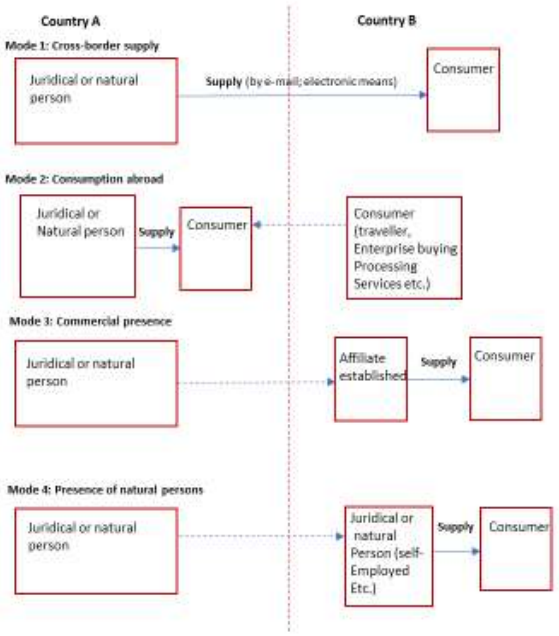


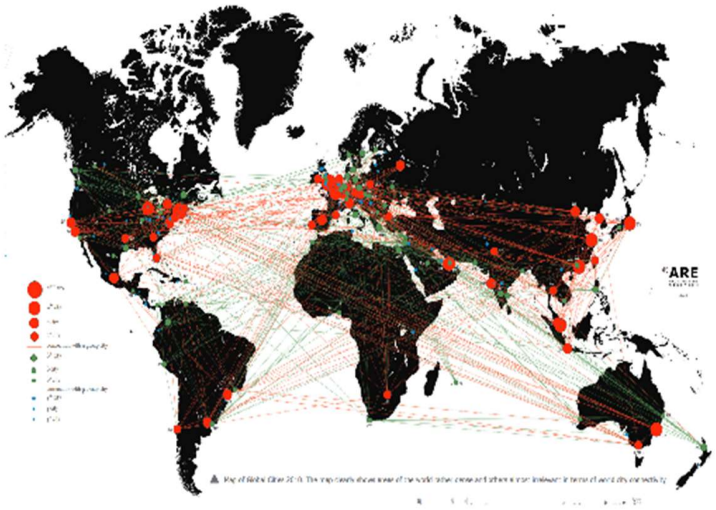
Figure 2: Under WTO GATS, services are supplied under four modes



Notes: Figure 2 indicates that trade in services occurs in different ways ranging from electronic transmission of data or information (mode 1); to the customer travelling to consume the service as in tourism (mode 2); to the establishment of an affiliate to provide the service as in some professional services (mode 3); to provide the service though provision by a person as in some consulting services (mode 4). Some services including professional services may involve all modes.

Source: Adapted by the authors from World Trade Organization General Agreement on Trade in Services (GATS), https://www.wto.org/english/tratop_e/serv_e/gatsqa_e.htm

Figure 3: The Global Networks of Cities, 2010



The classification is based upon the office networks of 100 advanced producer service firms in 315 cities. Cf. GaWC Research Bulletin 43. http:// www.lboro.ac.uk/gawc/world2000.html.

Figure 4: Three-Tier Economic Diplomacy

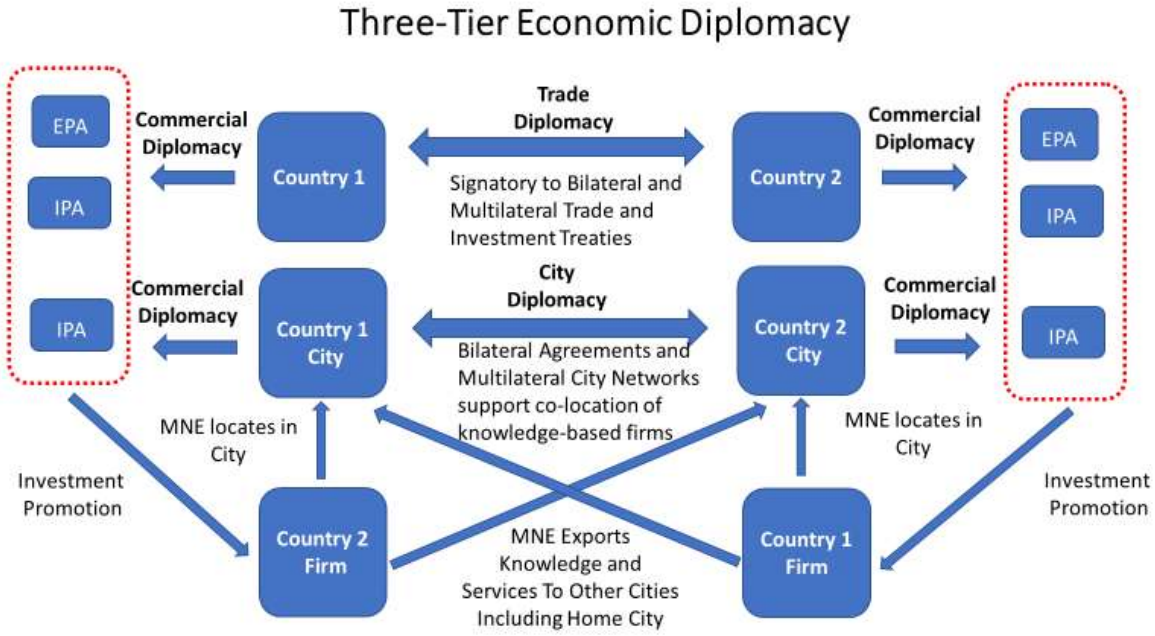


Table 1: Evolution in depth and breadth of services trade provisions

	CPTPP	CETA	TISA (under negotiation)	NAFTA (USMCA to replace)	WTO GATS
Breadth of Coverage					
Financial Services	Yes	Yes	Yes	Yes	Yes
Telecommunications	Yes	Yes	Yes	Yes	Yes
Maritime Transport Services	Yes	Yes	Yes	No (Yes under USMCA)	No
Digital Trade and E-Commerce	Yes	Yes	Yes	No (Yes under USMCA)	No
Investment protection/ ISDS	Yes (partial ISDS)	Yes	No	Yes (ISDS reduced under USMCA)	No
Depth of Coverage					
General Obligations (NT, MFN)	Yes	Yes	Yes	Yes	Yes
Positive or negative list approach[1]	Negative	Negative	Hybrid	Negative	Positive
Country exclusions for current & future non-conforming measures [2]	Yes	Yes	Yes	Yes	No
Regulatory Cooperation	Yes	Yes	Partial	Yes (USMCA strengthened)	Partial
Temporary entry business people (mode 4)	Yes	Yes	Yes	Yes	Yes (weak)
Mutual recognition professional qualifications	No	Yes	No	Yes	No

1 Under a positive list approach, countries have to explicitly list those sectors in which they will undertake commitment while under a negative list approach they do not list sectors for which commitments are taken, but only those which they want to exclude or limit through reservations or exclusions. A negative list approach tends to afford greater depth of coverage however this is also driven by the extent of the country specific exclusions.

2 Exclusions involve a list of non-conforming measures which are grandfathered at the prevailing level of non-conformity as well as sectors in which the Parties opt to retain the right to maintain or introduce new non-conforming measures. The greater this list the lower the depth of coverage of the agreement.

Compiled by the authors based on information from:

Comprehensive Economic and Trade Agreement (CETA) Between Canada and the European Union. https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/ceta-aecg/index.aspx?lang=eng
Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/index.aspx?lang=eng
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New NAFTA (USMCA); (https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cusma-aceum/index.aspx?lang=eng)

Table 2: Global City Strategic Promotion – Strategic Positions					
Global City Investment Promotion Strategic Positions					
Main City Agency (city rank)	**Other City Agencies**	**Ownership**	**Horizontal Scope**	**Vertical Scope**	**Geographic Scope**
London & Partners (alpha ++)	Innovation and Growth Directorate (domestic competitiveness)	Private-Public Partnership	Investment, trade, tourism	Financial services, high technology, creative, tourism	Offices in 14 countries; created entrepreneurship network with NY (CityLabs)
New York City Economic Development Corporation (NYCEDC) (alpha ++)	New York City Global Partners (focus on creating networks)	Public	Broad—economic growth	Tech, fashion, finance, health and bio tech, media	Partnership with Paris, Milan. Support for global innovation network (City Labs)
Invest HK (alpha +)	Hong Kong Exporters Association; Hong Kong Trade Development Council	Public	Investment promotion and support plus high tech development	Creative industries, business and professional service, ICT, finance and fintech	Offices in 30 countries
Open Beijing (alpha +)	Beijing Investment Promotion Service Centre	Public	Invest promotion plus cluster development and tourism	Media, technology, internet, professional services	Sister trade promotion agencies have 30 offices abroad
Singapore Economic Development Board (alpha +)	Enterprise Singapore (capacity)	Public	Investment promotion and support, talent development	Aerospace, resources + high tech	20 offices globally
Invest Shanghai (alpha +)	Shanghai Foreign Investment and Services Platform plus others	Public	Two-way Investment promotion and development	General	> 5 offices globally. Presumed access to sister agency offices
City of Sydney (alpha +)		Public	Very road mandate base on knowledge, services and creative sectors	Creative knowledge and digital industries	6 sister cities
Greater Paris Investment Agency and (alpha +)	Choose Paris Region, Paris Development Agency, Paris Region Planning and Development Agency (IAU Ile - de-France) – both economic development	Not for profit and Public	Investment promotion and support	Transport, Energy, Finance, Real Estate, Digital, Manufacturing, Education and Tourism	No offices abroad
Dubai FDI (alpha +)	Several supporting agencies focused on economic development/trade	Public	Investment promotion and support	Very broad.	No overseas offices; many overseas missions. Export agency has 7 offices abroad
Invest Tokyo (alpha +)	None found	Public	Investment promotion and support	None specified	4
Milan (alpha)	None found	Public	Investment promotion and broad economic development including startups	Manufacturing, agriculture, smart cities, culture	10 partner cities

World Business Chicago (alpha)	None found	Public Private Partnership	Investment and trade promotion; tourism	None specified	28 sister cities; gateway agreement with 8 Chinese cities;
Moscow City Investment Agency (alpha)	Moscow Export Center (trade)	Public	Investment promotion and support	Technology and innovation	None listed
Toronto Global (alpha)	StartUP HERE Toronto (entrepreneurship)	Not for profit	Investment promotion and support	Technology, Financial Services, Life Sciences, Food and Beverage, Advanced Manufacturing, Clean Technology	None listed
Investe Sao Paulo (alpha)	None found	Public-Private	Investment promotion	Aerospace and defense; Agribusiness; Automotive; Green Economy; IT and healthcare	Network of global partners; no offices abroad
Frankfurt Economic Development (alpha)	None found	Public	Broad business development	None listed	None listed
Los Angeles Mayor's Office of International Affairs (alpha)	Los Angeles Regional Export Council	Public not for profit	Broad business development and promotion	None listed	Multiple missions abroad; no offices
Madrid Investment Attraction (alpha)	None found	Public	Business development and tourism	Financial Services; Telecommunications, Software Development, IT, Freight and Logistics	Offices in Beijing, NY and London
Invest KL (alpha)	None found	Public	Broad business development and investment promotion	Oil, Gas & Energy; Engineering Services; Consumer Products; Technology; Healthcare; Industry 4.0; Supply Chain	None listed

Table 3: Sidewalk Labs-Waterfront Toronto Case Study[16]

Sidewalk Labs is a subsidiary of Alphabet Inc, parent of Google engaged in the design, development and building of innovative cities (smart cities). Waterfront Toronto is a public agency created by the Federal and Ontario governments, and the City of Toronto to oversee the transformation of the Toronto waterfront (some 190 acres). As part of that mandate, Waterfront Toronto issued an RFP seeking partners in that development, in essence the creation of a public-private partnership. The result was the creation of Sidewalk Toronto, a proposed partnership between Sidewalk Labs and Waterfront Toronto.

The public-private partnership between Waterfront Toronto and Sidewalk labs aimed to revitalize Toronto's waterfront by creating a technology-driven District. The project promised to stimulate technology and innovation and turn Toronto into the next high-tech and urban-tech leader. The two parties collaborate in research, idea generation, and public consultation. Sidewalk Labs faced concerns over digital governance as the smart city design envisioned extensive deployment of data sensors and surveillance cameras. Sidewalk Labs was tasked with establishing an oversight mechanism in the data collection, governance, and privacy process since there is currently no concept of urban data in the Canadian privacy law. Although the deal is between NAFTA partner countries, there are no relevant provisions in NAFTA that help resolve the issues. At the same Waterfront Toronto is developing its own Intelligent Communities Guidelines that will apply to all private companies using digitally-enabled services, including a variety of privacy issues.

Privacy and urban data use are therefore areas in which formal regulations are absent or emergent, and thus individual companies are often left to negotiate project-specific conditions. In the case of Sidewalk Labs, this included proposals on data governance (methods to prevent the sale of data), technology revenue sharing, and intellectual property sharing (providing access to Sidewalk Labs technology resulting from the project).

At every stage the project was confronted with issues surrounding data governance, intellectual property and privacy. Most came from local governments and communities. The project went through several rounds of negotiation, which ultimately resulted in a decision by Waterfront Toronto on October 31, 2019 to proceed but on a reduced scale, from a 190-acre 'Idea District' to 12-acre pilot project.

[16] All information in this case come from public sources:
https://www.sidewalklabs.com/
https://www.sidewalktoronto.ca/
https://medium.com/sidewalk-toronto/project-update-submitting-the-digital-innovation-appendix-9956d265419c
https://www.waterfrontoronto.ca/nbe/portal/waterfront/Home