

# The role of the state in shaping the internationalization of firms in the twenty-first century

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**Judit Ricz** 

Centre for Economic and Regional Studies HUN-REN, Corvinus University of Budapest, Budapest, Hungary

**Dorottya Sallai** 

Department of Management, London School of Economics and Political Science, London, UK

**Magdolna Sass** 

Centre for Economic and Regional Studies HUN-REN, Budapest Business University, Budapest, Hungary

## Abstract

The year 2020, with the outbreak of the COVID-19 pandemic and the subsequent crises, highlighted the significance of state intervention in shaping firm competitiveness. However, unprecedented government support for businesses has left us puzzled about the state's role in firm internationalization, especially in emerging markets and the Global South, where government involvement has been accompanied by democratic backsliding and rising authoritarianism. Our Special Issue moves the current debate forward by exploring how the state's changing role affects firm internationalization. The objective of this editorial is twofold: stimulating theory development by scrutinizing state intervention in emerging markets in recent decades and introducing the Special Issue articles. Contributions investigate how governments support the internationalization of their domestic businesses by focusing on firms' institutional embeddedness and the impact of institutions as both resources and constraints to their internationalization. By linking the discourse on state capitalism with business internationalization, our empirical studies advance research on political economy and the state's role in innovative ways, reflecting on recent geopolitical developments. Our introductory article situates the Special Issue papers in the state capitalism and firm internationalization literatures and discusses their implications for future research.

## Keywords

Firm internationalization, state capitalism, institutional embeddedness, emerging markets, central and eastern Europe

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### Corresponding author:

Dorottya Sallai, Department of Management, London School of Economics and Political Science, Houghton Street, London WC2A 2AE, UK.

Email: [d.sallai@lse.ac.uk](mailto:d.sallai@lse.ac.uk)

## Introduction

The last decade has brought about a sharp rise of state intervention in the economy and a general shift towards stronger states worldwide (Alami, 2023; Bremmer, 2008; Kurlantzick, 2016; Mazzucato, 2021). Academic literature has been addressing this phenomenon by either focusing on the transformative impacts of state intervention on the existing liberal economic world order (Kutlay, 2020; Öniş and Kutlay, 2017, 2021), or by highlighting how this trend enables states to effectively promote their own development and economic growth (Ricz, 2021). The focus of this special issue is related to this latter dimension. It aims to contribute to a better understanding of the link between growth models and types of state capitalism, with particular attention on how states promote the competitiveness and expansion of firms in domestic and/or international markets.

The COVID-19 pandemic has further complicated state capitalism, which manifests itself in various ways beyond direct, partial or even indirect ownership and influence (Dolfsma and Grosman, 2019; Szanyi, 2019). Researchers still lack conceptual tools to explain current changes in the economic role of the state, due to the variety of state-dominated economies, lack of analytical clarity and rather static approaches (Alami and Dixon, 2023; Sallai and Schnyder, 2021). However, governments across the globe are beginning to view transnational economic forces with scepticism as governments increasingly focus on long-term *national* economic development and national *control* over the economy (Colantone and Stanig, 2019).

## A critique of existing literature

The latest Comparative Capitalism research views the institutional configurations of capitalism as growth models (Nölke et al., 2019) and argues that the types of capitalism cannot be studied in isolation since the interaction between different growth models in the global or regional economy has crucial importance (Schedelik et al., 2021). Looking at the relationship between growth models and types of capitalism, studies in the Western context have established that coordinated market economies (CMEs) are primarily associated with export-led growth. In contrast, liberal market economies (LMEs) are generally consumption-led (Hope and Soskice, 2016). However, the growth model perspective and actual changes in growth models have rarely been explored in the emerging market context, presenting an 'exciting new avenue for research' (Schedelik et al., 2021: 4).

Although scholars have recently turned their attention to the growing role of the state by applying the comparative capitalism and Varieties of Capitalism (VoC) frameworks<sup>1</sup> to emerging markets and countries in Central and Eastern Europe (Alami and Dixon, 2020; Bizberg, 2019; Bohle and Greskovits, 2007, 2012; Burszt and Langbein, 2020; Carney et al., 2009; Hundt and Uttam, 2017; Mets et al., 2018; Nölke, 2014; Nölke et al., 2019; Petry, 2020; Ricz and Geröcs, 2023; Sauvart, 2008; Schedelik et al., 2021; Schneider, 2009), we still know little about how the various types of state capitalism and their different growth models influence the internationalization of firms and the flow of FDI across borders. Does the rise of state capitalism lead to economic nationalism and/or contribute to the growth of national champions on global markets? Is state capitalism associated with more internationalized firms in general or in certain sectors? How efficient are governments in promoting the internationalization of domestic firms? How do interventionist states affect domestic firms' growth and internationalization and global multinationals' investments in their economies? What are the implications of a country's integration in the global economy on its growth model and capitalist variety?

Critiques of the VoC framework highlight that capitalism is a historically specific system of production and that 'institutions are part of this system, not in some ill-defined external relationship

with it' (Bruff and Horn, 2012: 163). Indeed, recent studies show that the influence of the state on the internationalization of businesses is contingent upon the variety of capitalism in which the business is embedded (Mariotti and Marzano, 2019), though real-life case studies underline the complex and sometimes controversial relationship between state-business and VoC (Kinderman, 2017). However, existing studies only explore how the internationalization of state-owned enterprises is influenced by the state's involvement in ownership and the home country's institutional settings but do not tell us how other factors of state capitalism influence internationalization or how non-state-owned firms are affected.

The internationalization of companies is often viewed through an economic lens; however, since the rise of emerging market MNEs, there is a growing need to expand the international business theory to take greater account of the political and sociological factors that operate through a country's institutions (Child and Rodrigues, 2005). Latecomer companies from emerging and transition economies are typically characterized by active governmental involvement, either through ownership, regulation or both (Peng, 2000). Proactive and interventionist governments are mainly, but not exclusively, present in emerging economies, compared to developed economies (Gammeltoft and Cuervo-Cazurra, 2021) with an idiosyncratic set of supporting policies and measures (Whitley, 2014) to help the internationalization of firms.

The emergence of the so-called hybrid state-owned enterprises (SOEs) highlights the importance of the extent and quality of state ownership (Bruton et al., 2015). Different forms of state ownership (e.g., sovereign wealth funds) are also increasingly present (Alami and Dixon, 2022), making it more complicated to grasp, measure and compare state ownership. Furthermore, there is a looser correlation between the extent of state ownership and the extent of the state's actual control of the firm in question. Thus, ownership, the intention of the government (and changes over time within it), and other elements of the institutional and business environment matter. The co-evolution of emerging market MNEs – and among them SOEs – with their home and host country institutional environments is well documented in international business research (Hitt et al., 2016; Wright et al., 2021). Governments may affect the internationalization of firms through state ownership when they have governance control of the organization; or through government affiliation, whereby firms' internationalization trajectories are influenced through relationship building in the emerging economy (Wang et al., 2012). As Alami and Dixon (2023) put it, the state can be the owner, promoter and supervisor of capital at home and in its operation abroad.

Governments may be motivated by economic gains (Knoerich, 2017) and political motives (Cuervo-Cazurra et al., 2022) when helping or forcing domestic firms to internationalize, while in other cases, their impact on the internationalization process is unintentional. Hence, it is crucial to identify the various channels through which governments – intentionally or unintentionally – influence the internationalization of firms. Some see state capitalism as a multidimensional concept (Wright et al., 2021), distinguishing three types of government intervention: governance quality, state ownership and statism, and stating that different combinations of the three types may exist and ensure similar levels of government intervention in the economy.

Most recent scholarship on state capitalism urges us to take more explicit consideration of the political context as we explore how governments affect the impact of state ownership. Previous research found that changes in political institutions, political regimes and ideologies cause significant changes in the ownership structures of internationalizing enterprises (Wright et al., 2021). Corporate ownership goes through significant transformations in countries undergoing significant political changes, and the state gains a larger ownership stake in domestic and foreign businesses (Carney and Child, 2013). Incorporating these new approaches into studying state capitalism and firm internationalization may bring new results. Previous research has shown that emerging market

governments (such as India, Brazil, Turkey or certain Central and Eastern European countries) are just as much committed to pushing their national champions to compete on global markets (Götz and Jankowska, 2017; Nölke 2014; Sallai et al., 2023; Sauvart, 2008), as China (Szunomár, 2020), yet their strategies and achieved outcomes differ to a great extent.

We also see a variety in approaches in how emerging market governments approach inward FDI: while for Central and Eastern European economies, FDI is often a source of development strategy or the engine of their Dependent Market Economy (DME) (Nölke and Vliegthart, 2009) growth model, other emerging market economies such as China, India and Brazil have a more selective approach to foreign multinationals and national protection plays a more critical role in developing an alternative growth model to liberal capitalism (Nölke, 2017). Although some studies have looked at internationalization in the context of state capitalism, particularly that of state-owned firms (Cuervo-Cazurra and Cheng, 2022), existing literature has not thoroughly and systematically analysed state interventionism and its varieties. In this special issue, we offer an alternative to the conventional firm-centred and country-level approach of the traditional VoC framework by focusing on the role of the state and the interdependence between the export- and consumption-led models (Schedelik et al., 2021). The empirical studies in the special issue explore the changing role of the state and its interventions in firms' internationalization and investment strategies. The articles cover a broad geographical area and various state capitalist models, including Turkey, Hungary, Czechia, Latvia, Estonia, Argentina, Brazil, Kenya and Nigeria.

## Contributions

Each article in this special issue examines various levels of state interventionism in determining corporate internationalization and competitiveness and provides a novel angle for examining current iterations of state capitalism.

The first paper explores how key state agencies shape the internationalization path of the finance sector in the Baltic states. Edgars Eihmanis provides some clear answers in his reflections on the role of Central Banks (CB) as developmental actors when analysing the emergence of offshore finance in Europe's Eastern periphery. The article raises our attention to the need to embed the analysis of financial regulation and regulatory approaches into a broader institutional and political economy context. We need to look at small states in a globally interconnected world of big tech, banking and financial services and understand the role of specific niches that facilitate their competitiveness, even if this means servicing the needs of the global investment capital. Going beyond the classic cases of Ireland, Lichtenstein or Seychelles, Eihmanis explores the lesser-known cases of illicit financial flows in the Baltic countries, such as the emergence of domestically owned offshore banking in Latvia and the almost fully foreign-owned banking sector in Estonia, that 'have served not as "treasure islands" but as conduits of illicit wealth from Russia to the West' (Eihmanis, p: 1, this special issue). The comparative analysis of the Latvian and Estonian cases extends our understanding of state influence by investigating why the former developed a full-fledged domestic offshore sector while the latter did not. We gain novel insights into central banks' social and political embeddedness and how their historical linkages with and networks to different social and elite groups affect their policy approaches and lead to contrasting internationalization outcomes.

The second article, written by Magdolna Sass and Jana Vlčková, addresses how the state impacts the internationalization of post-socialist multinationals in the Czech Republic and Hungary. The paper raises our attention to differences in ownership structures and headquarter-location strategies between Czech and Hungarian multinationals while exploring the mechanisms through which the two governments – intentionally or unintentionally – initiated and accelerated in certain cases the

internationalization process of these firms. The idiosyncratic features of post-socialist multinationals are reflected in their characteristics. Most leading Czech multinationals are headquartered abroad, while in Hungary, despite the generally high foreign and low state ownership, indirect state control is more pronounced. In the post-socialist context, certain economic policies – especially around privatization, state ownership and tax policy – play a crucial role in directly or indirectly shaping the internationalization path of domestic multinationals. The contribution suggests that post-socialist multinationals substantially differ from their developed market counterparts in terms of what role the home country's government plays in their internationalization.

The third article widens the research perspective into under-researched terrains both in regional terms (beyond Europe) and thematic terms (by focusing on the fashion industry). Eka Ikpe, Lauren England and Roberta Comunian explore the nexus between state capitalism and firm internationalization by focusing on the creative economy in the context of the fashion industry in Sub-Saharan Africa. While recent literature has emphasized the role of entrepreneurialism and neoliberal values in relation to the development of contemporary fashion industries globally and in the African context, we still know little about the potential role and impact of state support in this sector. To fill this gap in the literature, Ikpe and her co-authors look at fashion designers in Lagos and Nairobi. Through the 'lead firms from below' concept, the paper explores how micro-level firms in the creative industries of the Global South – operating independently from international brands of the Global North – contribute to global markets while acting as local agents. The article's findings shed light on the significance of synergies between key areas of the operation of 'lead firms from below' and state capitalism's support for production, trade and finance.

By studying the under-researched sector of creative industries, the authors raise our attention to the challenges of state (in)action that must be addressed to enable or improve global competitiveness and enhance interactions with regional and continental markets towards greater internationalization. The study suggests that some mechanisms of state capitalism, such as state finance provision, spillovers from export-processing zones and domestic input provision, may provide advantages for fashion design firms in the African context. Nevertheless, these are often challenged by state interventions that might have adverse effects, such as financing structures that are inattentive to the capital intensity of the fashion industry, fiscal extraction from the digital subsector or poor trade facilitation narrowing down input options of local producers, among others.

Besides some of the positive impacts of state intervention in internationalization strategies discussed so far, the special issue also explores cases where the state goes beyond what markets appreciate. Mustafa Kutlay and Kerem Yıldırım explore Turkey's authoritarian turn and the government's increasing market capture through the analysis of public procurement. Recently Turkey became an outstanding example of the coinciding processes of new economic interventionism going hand in hand with authoritarian populist politics. This illiberal, authoritarian variety of contemporary state capitalism, where in weak(ening) institutional settings, state interventionism is susceptible to 'market capture', is often disguised by a developmental discourse. Kutlay and his co-author provide an original analysis of the Turkish case by collecting and analysing public procurement deals in the country between 2010 and 2019. Their results show that over a relatively short period of a decade, the level of competitiveness, as measured by the number of companies that receive public procurement, has decreased substantively. Accordingly, the subtle but decisive government interventions in Turkey tend to favour politically loyal private economic actors without abolishing the façade of the market economy. Accordingly, the most recent variety of Turkish state capitalism has led to growing market capture. It reveals strong political motives which cannot be understood without incorporating into the analysis the authoritarian changes in politics and the wider institutional context enabling these processes.

The last two papers in the special issue investigate the Latin American variety of state capitalism and internationalization. The case of Brazilian national champions' internationalization by Michael Schedelik and Judit Ricz provides rich insights into how Brazil became an example of the 'new generation' of state capitalism. The authors analyse the Workers' Party's 'national champions strategy' in the 2000s and extend our understanding of how the Brazilian National Development Bank (BNDES) became a key player in supporting the international expansion of Brazilian firms. The paper explores new ways of state ownership, state control and subsidies. The analysis contributes to the emerging debate about the viability of a 'National Champions' strategy as an industrial policy and sheds light on major achievements and inherent pitfalls of such a strategy within the weak(ening) institutional context of the Global South. While a range of globally competitive and internationalized Brazilian companies emerged within a few years due to the various forms of direct and indirect state support, this took place in those commodity and resource-intensive sectors which already featured strong comparative advantages before the recent state interventionist cycle. The study reveals a series of corruption scandals, predominately in sectors under the industrial policy, and especially those covered by the National Champions Strategy. The numerous bribery and kickback schemes and vast amounts of campaign donations cast doubt on the social benefits of this industrial policy for Brazilian society. The pervasiveness of corruption within the Brazilian political economy, as in other emerging economies, underscores the necessity of taking the broader institutional context of industrial policies into account.

Staying on the Latin American continent, but turning to Argentina, Christopher Wylde's article explores the active underbelly of new developmentalism while re-conceptualizing the state's power in the twenty-first century. The article analyses the Argentine development experience under the Kirchner's while developing a more sophisticated understanding of the state and associated concepts of capacity and autonomy. Wylde draws attention to the changing nature of industrial policy and how this is linked to changes in the state and its power relations by considering both pressures from below through the changing constellation of social forces and from above through the changing nature of global forces. Precisely the combination of these two forces led to the discrediting of the Kirchner project in Argentina and the subsequent election of Mauricio Macri in 2015. Consequently, this fleeting and temporary experiment with new industrial policy in Argentina can be seen as a cautionary tale for states in the Global East and South flirting with industrial policies in the twenty-first century. The main lesson to be learned from the Latin American experiences is that the success or failure of new industrial policies depends on both institutional and (global) political economy factors. As such, beyond the conventional state capacity and autonomy arguments, the power balance of domestic business and social coalitions, as well as the changes in international conditions (such as the commodity boom, or the end thereof) have to be taken into account.

Overall, the contributions present novel approaches in studying the role of the state in the economy and how it shapes the internationalization of firms. The articles illustrate the unique features of the diverse development trajectories of different national economies, while also highlighting their common characteristics. The studies offer original empirical evidence, fresh perspectives and nuanced insights that address and reflect the distinctive attributes of contemporary state-business relationships. By extending the current scholarship on political economy and the role of the state, the collection also sheds light on how the role of the state has changed in emerging markets and the Global South as a result of recent geopolitical developments.

## Conclusion and implication for future research

Articles in this collection highlight critical issues concerning the debate around state capitalism and firm internationalization. First of all, the findings of the special issue articles raise our attention to how the existing literature could benefit from the experience of the Global South, where state intervention in the form of ownership, state control and state subsidies have a determinant impact on firms' internationalization and growth. A common theme that emerges from the articles is the importance of institutional complexities, especially the embeddedness of institutions in the social and historical context. Findings that cut across the articles highlight the need to go beyond the Varieties of Capitalism (VoC) literature to understand the largely unexplored dynamics of state capitalism and internationalization of firms. The studies in this special issue suggest that specific dynamics of state-firm relations that affect internationalization through ownership structures (such as the contrasting case of the Czech and Hungarian multinationals), government subsidies (that might be politically motivated such as the case in Turkey) or the financial institutions' social and political links to different elite groups (such as in the Baltic states) affect firm internationalization in very different ways. Ignoring these dynamics is risky. Hall and Soskice's Varieties of Capitalism (2001) framework that places firms and not states into the centre of analysis limit the debate on firm internationalization. The VoC framework suggests, perhaps most prominently concerning the questions of this special issue, that greater international competition causes LME-CME differences to become more evident as firms focus more on economic activities and production profiles that fit with existing institutions (Blyth and Schwartz, 2022). Thus, the VoC typology suggests that governments should encourage growth and subsequent internationalization by implementing reforms that make their institutional frameworks more coherent, strengthening their institutional complementarities (Blyth and Schwartz, 2022). Subsequent studies criticizing the VoC framework – such as the emerging literature on Growth Models (GMs) (see Baccaro and Pontusson, 2016) – advocate a shift in focus to the demand drivers in the economy and its dominant growth coalition by exploring which sectors of a given economy generate value-added and which coalitions support these sectors' interests in public policy and politics (Blyth and Schwartz, 2022). Contributions in this volume move this debate forward and raise our attention to sectoral state interventions that have adverse effects (such as in the case of the Sub-Saharan African fashion industry) or the pitfalls of targeted government interventions such as the National Champions Strategy in Brazil, which brought into question the social benefits of this industrial policy for Brazilian society. Thus, the articles underline the importance of the context: space and time, against which various mixtures of state interventions must be assessed.

The articles in this special issue set the groundwork for future research in at least three crucial directions on contemporary state interventionism. First, different power constellations and shifts in the domestic and external institutional contexts might result in profoundly different outcomes of state interventions aimed at shaping firm internationalization and competitiveness than conventional theories based on core country experiences would imply. As the contributions to this special issue demonstrate, contemporary state capitalism has a multidimensional character with varieties and variations concerning their impact on the internationalization of firms. Instead of the broad-brush focus on state capitalism and its implications, future studies should explore more nuanced questions related to the complexities that stem from the impact of state capitalism, such as how specific types of state interventions, policy approaches, ownership structures or control mechanisms affect different firm types or industries and how the embeddedness of state institutions in the local and global economic networks might impact these dynamics. Moreover, future research could explore the same issues by focusing on how the changing global geopolitical context – such as the impact of the war

on Ukraine, of the US–China trade war, of membership in regional trade agreements such as the EU or USMCA or of state capitalist systems might determine internationalization outcomes. Hence, studies exploring these impacts cannot ignore the cross-disciplinary nature of the phenomenon. Future research should cross the boundaries of and combine the analytical perspectives of international business studies, comparative and international political economy approaches, institutional analysis and development studies when exploring the question of emerging markets firms' state-sponsored or state-promoted (or even state-hindered) internationalization.

Second, while we acknowledge that no grand theory can capture the multiplicity of factors, linkages and dynamics in contemporary state capitalism, new concepts focusing on the specificities of the Global East and South – such as the 'lead firms from below' concept introduced by Ikpe and co-authors in this volume – and more general themes such as how industrial policy targeting specific sectors, or groups of firms with specific ownership structures affect internationalization outcomes can help guide future studies. Questions include how different industrial policies targeting national champions affect internationalization outcomes or how state interventions with adverse social and economic impacts influence a firm's internationalization ability.

Third, a key focus of future research should be on variations and potential of new industrial policies that promote competitiveness and internationalization in weak(ening) institutional contexts prone to political or business capture, as shown in the Turkish, Brazilian and Argentine cases. Our special issue has highlighted these strategies' inherent risks and downsides in the emerging market context. Future research should explore mechanisms that prevent political or business capture in state capitalist business internationalization and the heterogeneity and variety of measures through which government intervention and state capture occur in volatile institutional contexts. A more systematic mapping of these measures is required for a complete understanding of the scope and characteristics of government intervention. Analysing their context-specificity impact is also one of the main tasks of future research. The multidisciplinary approach taken by the articles in this special issue is aimed to help move this discussion further.

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## ORCID iDs

Judit Riciz  <https://orcid.org/0000-0003-4371-142X>  
 Dorottya Sallai  <https://orcid.org/0000-0003-3411-4818>  
 Magdolna Sass  <https://orcid.org/0000-0002-6819-6041>

## Note

1. See the annual international conferences entitled The Role of the State in Varieties of Capitalism (SVOC) organized by the Institute of World Economics, Center for Economic and Regional Studies in cooperation with the Democracy Institute at the Central European University in Budapest, Hungary (<https://svoc-conference.webnode.hu/>).

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