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# Three Essays on the Influence of Political Connections on Firms International Expansion Strategy

Joao Eduardo Albino Pimentel

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Par

**M. João Eduardo ALBINO PIMENTEL**

Three Essays on the Influence of Political Connections on Firms International  
Expansion Strategy

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**Composition du Jury :**

M. Rodolphe DURAND  
M. Jean-Philippe BONARDI  
M. Myles SHAVER  
M. Pierre DUSSAUGE

Professeur, HEC Paris  
Professeur, Université de Lausanne  
Professeur, Université du Minnesota  
Professeur, HEC Paris

Président du jury  
Rapporteur  
Rapporteur  
Directeur de thèse

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## **ABSTRACT**

This dissertation is composed of three essays, each contributing to address part of the puzzle regarding how different types of political connections affect firms' international expansion strategies and performance. The first essay examines how political connections moderate the relationship between host country attributes and international strategy in a sample of greenfield investments in manufacturing during the 2003-2010 period. The second and third essays examine how political connections directly impact a firm's international expansion strategies and performance. The second essay investigates the role of different types of political connections on a firm's international investments amount and risk profile. Finally, the third essay analyzes the role of political connections as an explanatory factor of firms' ability to accelerate the provision of funding and development of their project finance-based investments. Both the latter two essays rely on an original dataset on various political connections enjoyed by the largest French firms during the 2003-2012 period.

**Keywords.** Political connections; international expansion strategy; non-market strategies; location choice; international investment treaties

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## TABLE OF CONTENTS

ABSTRACT.....	1
ACKNOWLEDGMENTS .....	2
TABLE OF CONTENTS.....	4
LIST OF TABLES .....	7
LIST OF FIGURES .....	8
CHAPTER 1: French Summary.....	9
Engagement politique, relation politique et stratégie de l’entreprise .....	12
Essai 1: relations politiques et choix d’emplacements .....	16
Essai 2: Types de relations politiques et le profil des Investissements internationaux des entreprises .....	18
Essai 3: Relations politiques et rapidité d’exécution .....	20
Conclusions.....	22
CHAPTER 2: Introduction .....	29
Political Engagement, Political Connections and Firm Strategy .....	33
Political Connections and Location Choice.....	36
Types of Political Connections and Firms’ Profile of International Investments.....	38
Political Connections and Speed Performance .....	40
Structure of the Dissertation .....	41
CHAPTER 3: The Influence of Foreign Affairs and Firm Political Influence on the Location Choice of International Investments .....	43
Abstract.....	44
Introduction.....	45
Theory and Hypotheses.....	49
The Effect of Bilateral Investment Treaties.....	52

The Effect of Firm’s Political Influence .....	54
Data and Methods .....	58
Dependent Variable .....	59
Independent Variable .....	59
Control Variables .....	60
Econometric Approach .....	64
Results.....	65
Robustness Tests.....	70
Discussion and Conclusion.....	72
 CHAPTER 4: A French Connection: The Influence of Political Connections on International	
Expansion Strategy .....	76
Abstract .....	77
Introduction.....	78
Theory and Hypotheses.....	81
Political Connections and Firms’ International Investments .....	82
Political Connections and Host Country Expropriation Risk .....	85
The Effect of a Favorable Political Change .....	87
Data and Methods .....	90
Business-Government Relationships in France .....	90
Setting and Sample .....	91
Dependent Variables.....	92
Independent Variables .....	93
Control Variables .....	95
Econometric approach .....	97
Results.....	100



Robustness Tests .....	106
Discussion and Conclusions .....	109
CHAPTER 5: Political Connections and Speed in Large Projects .....	115
Abstract .....	116
Introduction.....	117
Project Finance, Political Connections and Speed.....	121
Time and Project Finance-Based Investments .....	121
Political Connections and PF Investments Speed.....	122
Other Antecedents of PF Investments Speed.....	124
The Fuzzy Set Qualitative Comparative Analysis Approach .....	128
Outcomes and Causal Factors.....	129
Outcome conditions .....	133
Causal conditions .....	134
Other causal conditions.....	136
Results.....	140
Funding speed .....	142
Completion speed.....	148
Discussion and Concluding Remarks .....	154
CHAPTER 6: Conclusions .....	156
Overall Conclusion .....	157
Contributions.....	158
Limitations .....	163
Future Research .....	165
REFERENCES .....	168

## LIST OF TABLES

Table 1: Descriptive statistics and correlations .....	66
Table 2: Conditional logit models: H1 and H2.....	69
Table 3: Descriptive statistics and correlations .....	101
Table 4: Between-within analysis of international strategy.....	103
Table 5: Pre vs After Sarkozy’s election analysis .....	105
Table 6: Outcome and causal factors definitions and proposed effect on speed .....	127
Table 7: Projects distribution by year .....	131
Table 8: Projects distribution by sector .....	132
Table 9: Calibration of outcome and causal factors.....	139
Table 10: Descriptive statistics and correlations .....	141
Table 11: Pathway for high funding speed .....	144
Table 12: Pathways for low funding speed.....	147
Table 13: Pathways for high completion speed .....	150
Table 14: Pathways for low completion speed .....	153

## LIST OF FIGURES

Schéma 1: Résumé visuel de la thèse .....	28
Figure 1: Graphical representation of the dissertation model.....	31
Figure 2: Visual summary of the dissertation.....	42

## **CHAPTER 1: French Summary**

## **TROIS ESSAIS SUR L'INFLUENCE DES RELATIONS POLITIQUES SUR LA STRATEGIE D'EXPANSION INTERNATIONALE DES ENTREPRISES**

L'objectif principal de cette thèse était d'expliquer comment les capacités (capabilities) qui émanent des engagements hors marché des entreprises ont une influence sur leur stratégie et performance. Spécifiquement, j'avais pour but de révéler comment les relations politiques d'une entreprise, c'est-à-dire les relations hors marché qu'une entreprise entretient avec les autorités politiques et gouvernementales dans le pays d'origine de l'entreprise, ont un impact sur la stratégie et la performance de son expansion internationale. Je défends que les relations politiques sont le fondement même des capacités (capabilities) politiques des entreprises, qui en retour, ont une influence sur les mouvements stratégiques de l'entreprise, tels que l'expansion internationale. Lorsque les entreprises investissent à l'international, elles doivent prendre en considération des contextes politiques hétéroclites et doivent faire face à plus d'incertitude, notamment politique. En particulier, les entreprises deviennent sujettes à des difficultés liées à leur statut d'entreprise étrangère (liability of foreignness) (Hymer, 1976; Zaheer, 1995) du fait de leur manque de connaissance du marché étranger, des préférences des consommateurs pour les produits nationaux, et, notamment, des risques induits par les décisions des autres gouvernements. En conséquence, la stratégie d'expansion internationale de l'entreprise et sa performance ont tendance à véhiculer une profonde dimension politique ; ce qui donc constitue un terrain de recherche idéal pour étudier l'impact des relations politiques sur les stratégies menées par les entreprises.

Cette thèse est composée de 3 essais, chacun constituant une pièce du puzzle que constitue l'impact des relations politiques sur la stratégie d'expansion internationale de l'entreprise et sa performance. Dans le premier essai, j'examine le rôle des relations politiques comme effet modérateur de la relation entre les attributs du pays d'accueil et la stratégie internationale grâce à

un échantillon d'investissement entièrement nouveaux (greenfield investments) dans le secteur manufacturier, menés par des entreprises de 11 pays différents. Dans les essais 2 et 3, j'examine le rôle des relations politiques comme antécédents directs de la stratégie internationale et de sa performance. Dans ces deux derniers essais, je m'appuie sur un jeu de données original collecté par mes soins, qui inclue des informations sur différentes relations politiques dont profitent les plus grandes entreprises françaises. Dans le deuxième essai, j'étudie le rôle de différents types de relations politiques sur le volume des investissements internationaux d'une entreprise et sur son profil de risque. Enfin, dans le troisième essai, j'analyse comment les relations politiques influencent la vitesse avec laquelle les entreprises sécurisent un financement et achèvent le développement de leurs projets financiers, deux indicateurs de performance imprégnés de politique.

Cette thèse permet d'aider à la compréhension des courants de littérature relatifs aux stratégies hors marché des entreprises ainsi qu'au management international. Tout d'abord, je fais une distinction entre les différents types de relations politiques en prenant en considération si ces dernières s'inscrivent dans un contexte d'amitié, de parcours commun ou d'expériences communes. Cette démarche me permet d'obtenir une meilleure compréhension des mécanismes potentiels sous-jacents à l'influence des relations politiques sur la stratégie de l'entreprise et sa performance. Deuxièmement, j'analyse l'impact des relations politiques sur un type de stratégie qui est extrêmement imbriqué avec le politique, et pour qui l'effet des relations politiques devrait être plus visible et significatif, à savoir la stratégie d'expansion internationale de l'entreprise. En dernier lieu, j'examine l'impact des relations politiques sur un type de performance de qui colle au mieux avec la capacité des entreprises à obtenir des avantages de ses liens avec le gouvernement, à savoir la vitesse avec laquelle l'entreprise peut obtenir un financement et achever le développement de ses grands projets. Qui plus est, mes résultats s'appuient sur des données riches qui traitent de

nombreuses dimensions des relations politiques et des stratégies d'expansion internationale d'entreprises originaires de plusieurs pays. J'ai collecté et organisé avec soin ces données pour être en mesure d'avoir la compréhension la plus fine possible des relations que je cherche à révéler dans chaque essai. Avec cet objectif en tête, j'applique également des méthodes de recherche distinctes – le modèle de logit conditionnel (conditional logit), la différence-dans-la-différence (difference-in-differences) et l'analyse comparative et qualitative des ensembles flous (fuzzy set qualitative comparative analysis) – en fonction de la pertinence de la question de recherche de chaque essai.

Dans le reste de cette introduction, je présente dans un premier temps les arguments qui expliquent pourquoi examiner les fondements politiques des stratégies et de la performance des entreprises est important. Ensuite, j'apporte un résumé succinct de chaque essai et je montre comment elles permettent de contribuer à faire avancer notre compréhension académique de la relation entre relation politique et la stratégie d'expansion internationale/ performance de l'entreprise. Enfin, je présente la conclusion, qui inclue une discussion sur les limites de la thèse et ses principales contributions.

### **Engagement politique, relation politique et stratégie de l'entreprise**

Les entreprises et les gouvernements sont connectés de manière inextricable et, par voies de conséquences, s'influencent sur leurs décisions et performance réciproques. Quand le gouvernement met en œuvre, ou change, des politiques, des entreprises qui sont en activité sur un territoire, ou prévoient de s'y implanter, sont inévitablement touchées. Par exemple, les politiques relatives au marché du travail ou aux impôts ont un effet substantiel sur les coûts pour l'entreprise et sa profitabilité. Le gouvernement est aussi touché par les décisions faites par les entreprises, car ce dernier dépend aussi des emplois créés, des impôts collectés et autres effets induits générés par

l'activité des entreprises. Ainsi, les gouvernements font généralement en sorte d'attirer et de maintenir les investissements privés. Les littératures qui traitent des stratégies hors marché et des activités politiques des entreprises ont largement analysé comment la performance de l'entreprise est impactée par des activités comme les campagnes de donations ou de lobbying (De Figueiredo, 2009; Hillman, Keim, & Schuler, 2004) et par d'autres d'engagements politiques, comme l'embauche d'anciens politiciens ou fonctionnaires comme managers ou membres de comités de direction (Goldman, Rocholl, & So, 2009; Hillman, 2005; Lester, Hillman, Zardkoohi, & Cannella, 2008).

Pourtant, alors que le rôle de l'engagement politique des entreprises sur la performance a été analysé, un consensus sur le sens (négatif, neutre ou positif) de cette relation n'a pas encore été établi (Sun, Mellahi, & Wright, 2012). Certaines études ont trouvé que l'engagement politique a une influence positive sur la performance de l'entreprise (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001; Hillman, 2005). D'autres études ont trouvé un effet négatif ou neutre de l'engagement politique sur des indicateurs variés de la performance de l'entreprise (Aggarwal, Meschke, & Wang, 2012; Kramarz & Thesmar, 2013; Siegel, 2007). Trois éléments semblent avoir mené à ces résultats divers, constituant des zones d'ombres pertinentes à éclaircir.

En premier lieu est le fait que les entreprises varient dans leur capacité à utiliser l'engagement politique pour influencer les acteurs politiques et pour mobiliser les ressources des gouvernements. En d'autres termes, il existe une hétérogénéité possible des entreprises quant à leurs capacités à mobiliser leurs relations politiques, et cette hétérogénéité peut générer des résultats différents en termes de performance (Baron & Hall, 2003; Bonardi, 2011; Bonardi, Holburn, & Bergh, 2006). Le deuxième élément est que ce courant de recherche ne consacre toujours que peu d'attention au fait que différents types d'engagement politique – et différents



types de relations politiques – opèrent au travers de différents canaux et peuvent influencer les entreprises via des mécanismes distincts (Chung, Mahmood, & Mitchell, 2007; Hadani & Schuler, 2013). Le dernier élément est le fait qu'un engagement politique de l'entreprise peut avoir son effet le plus significatif sur la stratégie de l'entreprise et sa performance seulement de manière indirecte (Siegel, 2007; Zhu & Chung, 2014).

Je soutiens que le moyen de répondre à la première question est d'évaluer les capacités politiques d'une entreprise, ce qui devrait être plus stable dans le temps et refléter l'efficacité de l'entreprise à atteindre ses objectifs vis-à-vis du gouvernement. Je soutiens en outre que se concentrer sur les relations politiques, à savoir, les liens relationnels qu'une entreprise entretient avec les autorités dans l'environnement politique de son pays d'origine, est une approche appropriée pour évaluer les capacités politiques d'une entreprise. Par rapport aux relations politiques indirects ou transactionnels (Hillman et Hitt, 1999), qui sont générés par des actions telles que les dons de campagne et le lobbying, les relations politiques fondées sur les liens personnels sont plus stables dans le temps et sans doute plus efficaces pour générer des capacités politiques (Bonardi, 2011) : parce que les entreprises, dont les décideurs de haut niveau sont personnellement liés aux autorités gouvernementales, sont susceptibles d'être plus efficaces pour influencer ces acteurs politiques et dans la mobilisation des ressources gouvernementales. Néanmoins, de façon similaire à la littérature sur l'engagement politique en général, les études sur les effets des relations politiques sur les résultats au niveau de l'entreprise ont surtout mis l'accent sur leur impact sur la performance de l'entreprise (Amore & Bennedsen, 2013; Faccio, 2006; Goldman et al., 2009; Hillman, 2005), et ont, par conséquent, produit des éléments limités sur leur influence sur la stratégie de l'entreprise (Siegel, 2007; Zhu & Chung, 2014).

Pour répondre à la deuxième question, qui se fonde sur l'absence de consensus dans la littérature sur les effets de l'engagement politique, il est important de tenir compte des différents types de relations politiques et la façon dont elles peuvent fonctionner différemment (Sun et al., 2012). Des recherches antérieures ont élaboré, et ce de manière éparse, sur la pertinence de se documenter sur les nombreux types de relations politiques fondées sur les liens personnels. Les études précédentes ont montré qu'avoir une expérience professionnelle au sein d'un gouvernement, avoir un parcours commun et une amitié commune ou de liens familiaux sont particulièrement importants. Les relations politiques fondées sur une expérience gouvernementale sont créées lorsque les principaux décideurs d'une entreprise ont travaillé en politique ou en tant que hauts fonctionnaires du gouvernement, avant leur carrière professionnelle. Dans de tels cas, les décideurs de l'entreprise sont susceptibles d'avoir gardé des contacts au sein du gouvernement et d'avoir acquis les capacités de comprendre la façon dont le gouvernement fonctionne (Bertrand, Kramarz, Schoar, & Thesmar, 2006; Boddeyn, 1988; Kramarz & Thesmar 2013 ; Lester et al, 2008). Les relations politiques fondées sur un parcours commun sont établis lorsque les dirigeants d'entreprise et ceux du gouvernement ont le même niveau d'étude et ont étudié ensemble ou appartiennent à un réseau actif d'anciens qui compte (Kramarz et Thesmar, 2013; Siegel, 2007). Enfin, les relations politiques fondées sur l'amitié ou les liens familiaux sont créés lorsque les managers de haut niveau ont des amis personnels (Coulomb & Sangnier, 2014; Fisman, 2001) ou des membres de la famille (Amore & Bennedsen, 2013; Faccio, 2006; Fisman, 2001) avec des responsables importants au sein du gouvernement. Il est probable que ces relations politiques aient des influences différentes sur le comportement des entreprises et produisent des conséquences contrastées sur la performance de ces dernières.

Enfin, pour répondre à la troisième question, il est essentiel de comprendre si et comment les entreprises ayant des relations politiques opèrent des mouvements stratégiques distincts relativement aux entreprises sans relations politiques, car les écarts de performance évoqués peuvent découler de cette hétérogénéité. Quelques études récentes ont commencé à examiner l'influence des relations politiques sur plusieurs stratégies d'entreprises, telles que le financement (Leuz & Oberholzer-Gee, 2006), la diversification dans d'autres industries (Chung et al, 2007;. Zhu et Chung, 2014) et la capacité à prendre des risques (Boubakri, Mansi, & Saffar, 2013). Cependant, beaucoup reste à entreprendre pour mieux comprendre l'influence des relations politiques sur les stratégies des entreprises. En particulier, l'examen de l'influence des relations politiques sur les décisions politiquement très ancrées, où cette influence pourrait être plus facilement observable et plus significatif, peut énormément contribuer à l'avancement de la littérature. Ainsi, enquêter sur la stratégie d'expansion internationale, non seulement me permet d'observer un tel effet, comme il s'agit bien d'un type de stratégie avec un profond encastré politique, mais me permet aussi d'analyser si les bénéfices (ou les dettes) découlant des relations politiques sont limitées d'un point de vue géographique.

### **Essai 1: relations politiques et choix d'emplacements**

Une question centrale pour les entreprises qui envisagent des investissements internationaux est le risque que les décisions prises par les gouvernements étrangers pourraient avoir une implication négative sur la valeur de ces investissements et, dans les cas extrêmes, pourraient mener purement et simplement à exproprier l'investisseur étranger (Cuervo-Cazurra, 2008; Duanmu, 2014; Henisz, 2000; Holburn & Zelner, 2010; Kobrin, 1979, 1984; Ramamurti, 2001; Rodrik, 1991). En conséquence, les entreprises seront réticentes à investir dans des pays à risque (Delios & Henisz, 2003; Garcia-Canal & Guillén, 2008; Holburn & Zelner, 2010). Les pays

hôtes peuvent utiliser plusieurs mesures pour apaiser les inquiétudes des investisseurs concernant les risques d'expropriation, mais la plupart de ces mesures font peu de poids face à la souveraineté nationale, parce qu'une fois l'investissement effectué, le pays hôte peut être en mesure de modifier les règles du jeu au détriment de l'entreprise (Kobrin, 1987; Murtha, 1991; Vernon, 1980). Les Traités Bilatéraux d'Investissement (TBI), d'autre part, sont une mesure extraterritoriale qui permettent au pays d'accueil d'avoir un mécanisme qui produit un engagement crédible vis-à-vis des investisseurs étrangers (Kerner, 2009; Salacuse & Sullivan, 2005), et devraient, par conséquent, avoir un impact sur les décisions d'investissement des entreprises à l'étranger.

Dans le premier essai de la thèse, « L'influence des Affaires étrangères et l'influence politique de l'entreprise sur le choix d'emplacement des investissements internationaux », j'étudie le rôle des capacités politiques en tant que modérateur de la relation entre TIB, qui capture les liens entre pays d'origine-pays hôte, et le choix de localisation des investissements internationaux, un des types de stratégie d'expansion internationale. Dans la mesure où l'influence politique, reflétée d'une part par les relations politiques et d'autre part par la taille de l'entreprise, pourrait avoir un impact sur la capacité d'une entreprise à mobiliser le gouvernement du pays d'origine comme une ressource et, par conséquent, pourrait également avoir un impact sur la manière dont les entreprises répondent aux gages d'engagement émis par les pays hôte, par exemple via les TIB, je cherche à répondre à la question de recherche suivante: « Comment les capacités politiques modifient la sensibilité des entreprises à accueillir des engagements crédibles fondés sur la relation entre les pays ? ».

Dans un premier temps, je fais l'hypothèse que l'entreprise est plus susceptible d'investir dans un pays hôte lorsque le pays d'origine de l'entreprise dispose d'un TBI avec le pays hôte. Plus important encore, je prédis que les TBI sont plus fondamentaux pour les entreprises qui n'ont pas

la possibilité d'utiliser d'autres moyens pour protéger leurs investissements, en particulier les entreprises sans relations politiques dans leur pays d'origine et qui ne sont pas très grandes. En d'autres termes, je prédis que les entreprises qui sont politiquement connectées et qui sont grandes bénéficient d'un avantage concurrentiel en ce qui concerne leur capacité à investir dans des endroits où d'autres entreprises répugnent à investir.

J'ai utilisé des modèles de logit conditionnel (conditional logit) pour tester ces hypothèses sur un échantillon d'investissement entièrement nouveaux (greenfield investments) dans le secteur manufacturier, menés par des entreprises côtées de 11 pays hôtes entre 2003 et 2010. Dans l'ensemble, mes prédictions sont vérifiées. Les TIBs semblent fournir un mécanisme qui permet aux gouvernements de s'engager de manière crédible vis-à-vis des investisseurs étrangers, dans la mesure où l'existence d'un TIB ratifié entre les pays d'origine et d'accueil influe positivement sur la probabilité même de l'investissement. Plus important encore, cette mesure est particulièrement significative pour des entreprises qui ne disposent pas de solides relations politiques dans leur pays d'origine et qui ne sont pas très grandes. Autrement dit, les entreprises politiquement connectées et les très grandes entreprises choisissent l'emplacement de leurs investissements internationaux indépendamment de la présence des TIBs.

## **Essai 2: Types de relations politiques et le profil des Investissements internationaux des entreprises**

Dans le second essai, « Une connexion française: L'influence des relations politiques sur la stratégie d'expansion internationale », j'examine les effets des relations politiques sur la stratégie d'expansion internationale de manière plus détaillée. La principale question de recherche dans cet essai est la suivante: « Comment les différents types de relations politiques influencent la stratégie d'expansion internationale de l'entreprise ? » Pour répondre à cette question, j'analyse comment

trois types de relations politiques, à savoir (i) une expérience préalable dans un gouvernement, (ii) une formation initiale commune, et (iii) des relations politiques fondées sur l'amitié, influencent à la fois la quantité et le niveau d'exposition au risque d'expropriation des investissements internationaux de l'entreprise dans une période de temps donné.

Je propose trois façons par lesquelles les relations politiques devraient avoir un impact positif sur la stratégie d'expansion internationale de l'entreprise. Premièrement, les entreprises ayant des relations politiques savent comment traiter les gouvernements, ce qui leur permet d'avoir plus d'informations sur les changements et l'évolution des politiques grâce aux interactions qu'elles peuvent avoir avec les autorités gouvernementales. Deuxièmement, les relations politiques affectent la capacité réelle et perçue d'une entreprise à influencer le gouvernement du pays d'origine pour agir en vue de la protection des actifs de l'entreprise (Baron & Hall, 2003; Bonardi, 2011). Troisièmement, les relations politiques permettent aux entreprises d'obtenir des financements pour leurs investissements à moindre coût grâce à un accès privilégié aux diverses sources de financement et une valorisation sur le marché plus importante (Boubakri, Guedhami, Mishra, & Saffar, 2012; Claessens, Feijen, & Laeven, 2008; Faccio, Masulis, et McConnell, 2006). En outre, je soutiens que la valeur pour les entreprises des relations politiques fondées sur l'amitié est subordonnée au régime politique. Ces relations auront plus de valeur lorsque les décideurs de l'entreprise ont un ami personnel, ou un membre de la famille, qui bénéficie d'une fonction importante au sein du gouvernement du pays d'origine. En conséquence, si les relations politiques prennent plus de valeur pour l'entreprise, ces dernières devraient également intensifier leur influence sur la stratégie d'expansion internationale de l'entreprise.

J'utilise des données sur les investissements internationaux réalisés par les plus grandes sociétés cotées à la bourse française entre 2003 et 2012 pour tester empiriquement ces hypothèses. Mes

principales hypothèses sont vérifiées empiriquement. Les entreprises dotées de relations politiques se livrent à des stratégies d'expansion internationale distinctes de celles qui en sont dépourvues. Je trouve également que cette hétérogénéité est contingente au type de relations politiques : les relations politiques fondées sur des liens d'amitié et sur une formation initiale commune sont, respectivement, les plus significatives pour expliquer le montant et le niveau d'exposition au risque d'expropriation des investissements internationaux d'une entreprise. Enfin, je trouve que l'élection de Nicolas Sarkozy en tant que président de la République Française a eu des effets significatifs sur la stratégie des entreprises reliées à lui par des liens d'amitié. Plus précisément, les entreprises bénéficiant de liens d'amitié avec Sarkozy ont beaucoup plus investi, et ce de manière significative, à l'international après son élection de 2007.

### **Essai 3: Relations politiques et rapidité d'exécution**

Dans le troisième essai, "relations politiques et rapidité d'exécution dans les grands projets", je me concentre sur l'influence des relations politiques sur la performance des entreprises. En particulier, la question de recherche principale que je cherche à aborder dans cet essai est la suivante : « Comment les relations politiques ont une influence sur la rapidité d'exécution des investissements financiers des entreprises ?" En dépit de leur utilisation généralisée dans les grands projets d'infrastructure à l'échelle mondiale, il y a un manque frappant de recherche sur les projets d'investissement financier des entreprises (PF) (Esty, 2004; Vaaler, 2008), en particulier en ce qui concerne les capacités d'une entreprise à réaliser avec succès de tels investissements. La vitesse est un indicateur particulièrement pertinent de la performance du projet, dans la mesure où le temps nécessaire pour obtenir des fonds, et ensuite pour achever le développement du projet, entraîne des coûts importants pour les entreprises « sponsors » de ces investissements et pour les autres parties prenantes.

Comme la plupart des risques encourus lors du financement et développement des investissements financiers sont de nature politique (Esty, 2004; Sawant, 2010; Vaaler, James, et Aguilera, 2008), les relations politiques devraient être sensiblement importantes dans un tel contexte. En effet, les investissements financiers nécessitent généralement des « sponsors » pour collaborer étroitement avec les gouvernements afin d'obtenir différents types de licences et de permis, ou de s'allier avec les gouvernements au travers des « partenariats public-privé » (PPP), de négocier les taxes et les questions liées au code du travail, etc. Dans le même ordre, les prêteurs de capitaux peuvent juger différents sponsors comme plus ou moins susceptibles d'être renfloués par les gouvernements, en fonction des relations politiques de l'entreprise « sponsor ».

En conséquence, je revendique que les relations politiques permettent de réduire les risques liés aux investissements financiers et devraient, par conséquent, influencer positivement la vitesse d'exécution de ces projets d'investissement.

Cependant, les relations politiques devraient être pertinentes uniquement en combinaison avec d'autres dimensions, comme les autres projets en cours, l'entreprise « sponsor », et les emplacements géographiques qui déterminent au global le niveau de risque général d'un projet particulier. Je maintiens également que les relations politiques sont plus significatives lorsque le projet n'a pas d'autres caractéristiques qui pourraient aussi atténuer son risque. Les entreprises « sponsors » sans liens politiques, d'autre part, devraient être associées à une grande vitesse d'exécution des projets à la condition qu'elles annoncent des projets à faible risque. Enfin, je permets à différents types de relations politiques de s'associer à différents types de résultats.

J'utilise une méthode fondée sur les ensembles flous (fuzzy sets methods) pour étudier empiriquement ces propositions sur un échantillon d'investissements financiers « sponsorisés » par les plus grandes entreprises cotées à la Bourse de Paris et ce, au cours de la période 2003-2012.



L'échantillon comprend 95 projets, concentrés dans les industries d'infrastructure lourdes telles que la distribution d'énergie, le transport, le pétrole et le gaz, le traitement de l'eau et sa distribution ; projets « sponsorisés » par 17 entreprises de 31 pays d'accueil distincts. Mes résultats fournissent des indications intéressantes sur les différentes voies que les entreprises peuvent emprunter pour accélérer ou éviter des retards dans leurs investissements financiers.

### **Conclusions**

L'objectif principal de cette thèse était d'examiner comment les capacités provenant de l'engagement hors marché des entreprises influencent leur stratégie et leur performance. Bien que les recherches antérieures ont surtout porté sur l'étude des effets des relations politiques des entreprises sur les indicateurs de performance financière et comptable (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001; Goldman et al, 2009; Hillman, 2005), mes recherches explorent plus profondément la façon dont les relations politiques reflètent les capacités politiques d'une entreprise, et examinent leurs effets sur les décisions et les dimensions de la performance qui sont sensiblement ancrées dans des considérations politiques. Dans le premier essai, j'ai montré comment les relations politiques des entreprises ont un effet modérateur sur les liens pays d'origine-pays hôte et sur la stratégie internationale de l'entreprise. Dans le deuxième essai, j'ai montré comment les différents types de relations politiques influent sur le montant des investissements et le profil de risque, d'une entreprise internationale. Enfin, dans le troisième essai, j'ai montré comment les différents types de relations politiques influencent la vitesse d'exécution des investissements financiers. De façon générale, mes résultats suggèrent de nombreuses façons par lesquelles les relations politiques peuvent influencer la stratégie d'une entreprise et, en conséquence, la performance.

L'une des limites de cette thèse est que le rôle potentiel des relations politiques comme passif pour les entreprises (Aggarwal et al, 2012;. Kramarz et Thesmar, 2013; Siegel, 2007) n'a ni été largement discuté, ni empiriquement examiné au cours des trois essais. Bien que j'analyse l'impact des relations politiques sur la performance de l'entreprise dans le troisième essai, la thèse a principalement porté sur les implications stratégiques des relations politiques. Il est possible que dans certains cas, les relations politiques créent des pressions pour les entreprises qui les poussent à prendre des décisions qui s'alignent avec les intérêts du gouvernement du pays d'origine. Si ces intérêts ne sont pas en phase avec ceux l'entreprise, de telles décisions stratégiques pourraient éventuellement conduire à un impact négatif sur la performance de l'entreprise. En d'autres termes, il est possible que dans certains cas, l'entreprise ne fait pas des mouvements stratégiques distincts par rapport aux pairs qui n'ont pas de relations politiques car cette dernière a accès à un ensemble plus contraint d'options stratégiques, mais le contraire, à savoir l'entreprise pourrait suivre les recommandations gouvernementales sur comment et où investir à l'étranger. En outre, comme les relations politiques, telles que celles que nous avons mesurées, au cours des trois essais sont détenus par des individus et non par les entreprises, il est possible que ces individus utilisent leurs relations à des fins personnelles au détriment des intérêts à long terme de l'entreprise (Aggarwal et al., 2012 ). Les recherches futures se fondant sur des données supplémentaires pourraient explorer ces possibilités.

Premièrement, dans la mesure où les résultats de la performance de l'entreprise sont le résultat de mouvements stratégiques incités par des relations politiques, un modèle de médiation pourrait être développé dans lequel la stratégie et l'hétérogénéité des performances entre les entreprises seraient examinées simultanément. Deuxièmement, analyser la coévolution des investissements internationaux d'une entreprise et le modèle de relations politiques au sein du pays

d'origine en lien avec les pays étrangers pourrait contribuer à vérifier l'effet négatif potentiel des relations politiques. Si les entreprises qui ont des relations politiques ne changent pas leur choix d'emplacement d'investissements en fonction des changements au niveau des affaires étrangères dans le pays d'origine alors que d'autres entreprises le font, l'hypothèse de choix sans contrainte serait mieux soutenue. Si, au contraire, les entreprises qui ont des relations politiques changent leur comportement beaucoup plus que les autres, en alignant les investissements avec la politique internationale le gouvernement du pays d'origine politique le gouvernement, l'explication alternative de la pression gouvernementale serait plus pertinente.

En outre, les différentes mesures de relations politiques que j'ai utilisées dans les trois essais capturent différents niveaux de ces relations et sont hétérogènes et précises dans la représentation des capacités politiques d'une entreprise. Les recherches futures pourraient chercher à identifier des niveaux plus précis et dynamiques des relations politiques dans des échantillons transnationaux. En outre, bien que mes arguments, dans les trois essais, se réfèrent à des liens sociaux existant entre les décideurs de l'entreprise et ceux du gouvernement, ce qui implique qu'ils connaissent et échangent des informations et des faveurs les uns aux autres – et mes mesures développées au cours des trois essais essaient de capturer ces liens. Par exemple, certains diplômés de l'ENA ne se connaissent pas forcément ou ont des idéologies politiques opposées, ou encore des impératifs divergents, ce qui les empêcherait d'échanger des informations et des faveurs entre eux. Les recherches futures pourraient distinguer les individus en fonction de leur idéologie politique et de la durée de leur expérience professionnelle au sein du gouvernement afin d'obtenir des mesures plus précises des relations politiques. Enfin, mon analyse des liens politiques fondés sur l'amitié, dans le deuxième et troisième essai, nécessite également plus d'élaboration, car il se concentre sur un seul politicien. Bien que Sarkozy est un cas particulier, ce qui représente une rupture dans la

direction du gouvernement français, compte tenu de son orientation commerciale et de sa distance avec les élites politiques traditionnelles, d'autres recherches pourraient identifier les entreprises ayant des liens d'amitié avec d'autres politiciens de haut niveau.

Cette thèse apporte des contributions importantes à la littérature sur les stratégies globales et hors marché des entreprises. Tout d'abord, mes résultats viennent s'ajouter aux connaissances existantes qui portent sur la façon dont les entreprises peuvent tirer profit de leurs activités par rapport au gouvernement dans leur pays d'origine pour développer les capacités politiques qui deviennent utiles dans les pays étrangers, en particulier ceux qui sont caractérisés par un risque plus élevé d'expropriation (Cuervo- Cazorra & Genc, 2008; Garcia-Canal & Guillén, 2008; Holburn & Zelner, 2010). Bien que quelques études ont commencé à examiner le rôle joué par les relations politiques dans le pays d'origine sur certaines stratégies internationales des entreprises des pays émergents (Duanmu, 2014; leuz & Oberholzer-Gee, 2006; Wang, Hong, Kafouros, & Wright, 2012 ), le deuxième et troisième essai sont uniques dans la mesure où ils montrent que les relations politiques influencent les stratégies d'expansion internationale des entreprises qui ont été fondées et dont le siège se situe dans une économie avancée comme la France. En outre, mon analyse va au-delà de l'idée que des entreprises d'un même pays d'origine partagent un même niveau de capacités politiques (Cuervo-Cazorra & Genc, 2008; Holburn & Zelner, 2010), mais propose et, analyse empiriquement, l'effet de l'hétérogénéité des relations politiques entre les entreprises d'un même pays d'origine.

Je contribue également à la littérature sur les relations politiques, en comparant les effets de trois types de relations politiques sur la stratégie des entreprises. Alors que la plupart des recherches antérieures examinent l'effet d'un seul type de relation politique sur la valeur des entreprises (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001;. Goldman et al, 2009;

Hillman, 2005), mes recherches montrent que différents types de relations politiques ont des effets distincts sur la stratégie d'expansion internationale et la performance des entreprises.

En ce qui concerne les entreprises qui n'ont pas de relations politiques, ma recherche confirme les résultats antérieurs : les relations inter-gouvernementales sont des sources significatives de protection des investissements et donc contribuent à expliquer les stratégies d'expansion internationale des entreprises. Ainsi, j'ajoute une contribution au courant de recherche qui étudie les effets des liens inter-gouvernementaux sur les flux d'IDE (Alcacer & Ingram, 2013; Kerner, 2009; Li & Vashchilko, 2010; Salacuse & Sullivan, 2005; Yackee, 2008), grâce à l'analyse des données au niveau de l'entreprise et en se concentrant sur les traités bilatéraux sur les investissements (TBI).

Plus important encore, je montre que ces organisations, et les engagements crédibles et sous-jacents qu'ils permettent aux pays d'accueil de faire, ne sont que des antécédents significatifs de la stratégie internationale, pour les entreprises ne détenant pas les relations politiques avec les autorités gouvernementales dans le pays d'origine. Enfin, mes conclusions concernant l'effet de la taille de l'entreprise sur la relation entre les engagements crédibles effectués par les pays d'accueil et le choix de localisation des entreprises suggèrent que les entreprises peuvent remplacer les relations politiques avec d'autres sources d'influence politique. Il est à noter que seule la très grande taille, pour les entreprises, offre les mêmes avantages que les relations politiques. Ce résultat suggère que la taille des entreprises pourrait capturer d'autres corrélats importants de l'influence politique (Hillman et al., 2004), telles que les activités politiques et la visibilité.

En plus des contributions théoriques, au travers les trois essais, mes conclusions reposent sur des données extrêmement riches des différents types de relations politiques, des stratégies d'expansion internationale et de la performance des entreprises originaires de plusieurs pays. Les

méthodes utilisées dans les essais deux et trois sont relativement nouveaux dans la recherche en stratégie et la recherche sur les affaires internationales et pourraient être plus largement utilisées.

Dans le deuxième essai, j'ai utilisé une méthode qui permet l'identification d'effets intra-entreprises (within-firm) et inter-entreprises (between-firms) des relations politiques sur la stratégie d'expansion internationale des entreprises, et ce, dans la même spécification (Bartels, 2015; Bell & Jones, 2012; Mundlak, 1978). Cette méthode pourrait être utilisée pour examiner d'autres antécédents des décisions stratégiques des entreprises, contrastant leurs effets dans les entreprises et dans le temps, et ce, simultanément. Dans le troisième essai, j'ai utilisé une méthode fondée sur des ensembles flous qui permet l'identification des combinaisons de facteurs conduisant à un résultat tout en permettant « l'équifinalité », la complexité causale et des résultats asymétriques. De nombreux courants de recherche en stratégie et commerce international pourraient également bénéficier de l'utilisation de ce type de méthode.

Pour conclure, la figure 2 présente un résumé visuel de la thèse, y compris les principales questions de recherche, les méthodes et les résultats de chaque essai et les contributions générales de la thèse.

## Schéma 1: Résumé visuel de la thèse

<b>TROIS ESSAIS SUR L'INFLUENCE DES RELATIONS POLITIQUES SUR LA STRATEGIE D'EXPANSION INTERNATIONALE DES ENTREPRISES</b>			
<b>Question de recherche principale</b>	Comment les relations politiques influent sur la stratégie d'expansion internationale et la performance d'une entreprise?		
<b>Essais</b>	<i>L'influence des « Affaires étrangères » et influence politique de l'entreprise sur l'emplacement des investissements internationaux</i>	<i>Une connexion française : L'influence des relations politiques sur la stratégie d'expansion internationale</i>	<i>Connexions politiques et vitesse d'exécution dans les grands projets</i>
<b>Question spécifique de recherche</b>	Comment l'influence politique modifie la sensibilité des entreprises à recevoir des engagements crédibles de la part de pays tiers ?	Comment les différents types de relations politiques influencent la stratégie d'expansion internationale ?	Comment les relations politiques influencent la vitesse d'exécution des investissements financiers dans les grands projets ?
<b>Terrain</b>	Investissements entièrement nouveaux par les entreprises de onze pays d'origine développés au cours de la période 2003-2010	Les investissements internationaux des plus grandes entreprises françaises au cours de la période 2003-2012	Projets d'investissements financiers par les plus grandes entreprises françaises au cours de la période 2003-2012
<b>Méthode</b>	Logit conditionnel (conditional logit)	Adaptation de la spécification de Bartels des effets aléatoires de Mundlak	Analyse comparative et qualitative des ensembles flous (Fuzzy sets qualitative comparative analysis)
<b>Principaux résultats</b>	<ul style="list-style-type: none"> <li>- Les traités d'investissements bilatéraux (BIT) influencent positivement le choix d'emplacement de l'investissement international d'une entreprise</li> <li>- Les entreprises avec des relations politiques et les très grandes entreprises choisissent ces emplacements indépendamment de la présence d'un TIB</li> </ul>	<ul style="list-style-type: none"> <li>- Les entreprises avec des relations politiques fondées sur l'amitié, par le biais du conseil d'administration, font plus d'investissements internationaux que les autres entreprises</li> <li>- Les entreprises avec des relations politiques fondées sur l'amitié par le biais du-directeur général font des investissements moindres à l'international que les autres, mais leurs investissements augmentent après que les relations politiques deviennent plus importantes</li> <li>- Les entreprises avec des relations politiques fondées sur des études en commun, via le PDG, concentrent plus leurs investissements internationaux dans les pays les plus risqués</li> </ul>	<ul style="list-style-type: none"> <li>- Plusieurs combinaisons de facteurs conduisent à une augmentation du financement et la vitesse d'exécution</li> <li>- Le "chemin" pour la grande vitesse d'exécution est distinct de celui pour la faible vitesse d'exécution</li> <li>- Bien que pertinent, les relations politiques ne sont ni suffisantes ni nécessaires pour atteindre la haute vitesse d'exécution</li> <li>- Différents types de relations politiques se combinent avec différents facteurs pour déterminer la vitesse d'exécution</li> </ul>
<b>Contributions générales</b>	<ul style="list-style-type: none"> <li>- Les relations politiques sont les capacités qui aident les entreprises à réduire les risques dans les investissements internationaux</li> <li>- Les différents types de relations politiques affectent de manière hétérogène des dimensions distinctes de la stratégie et la performance international de l'entreprise</li> <li>- Les relations politiques ont des implications significatives pour les entreprises ayant leur siège dans une économie avancée</li> </ul>		

## **CHAPTER 2: Introduction**

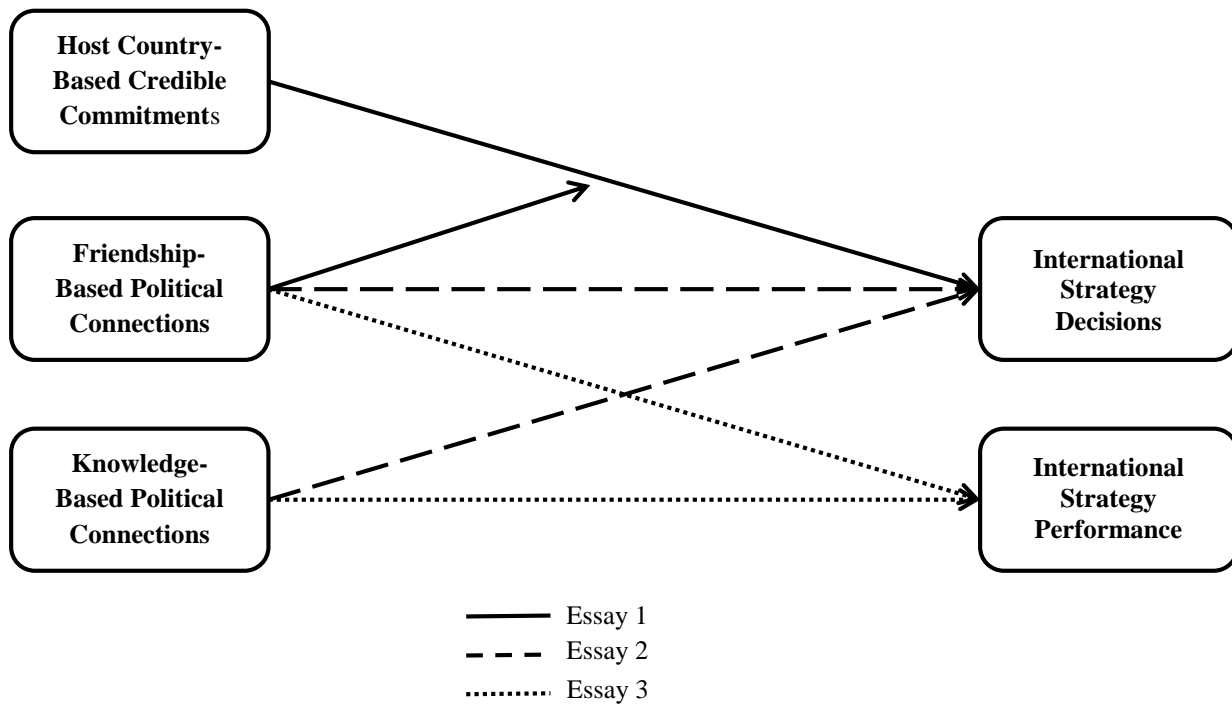


The main objective in this dissertation is to explain how capabilities stemming from a firm's non-market engagement influence that firm's strategy and performance. More specifically, in the chapters that follow, I aim to uncover how a firm's political connections, that is, the (non-market) relationships it holds with political and government authorities in its country of origin, impact its international expansion strategy and performance. I argue that political connections are the basis of political capabilities, which, in turn, influence a firm's strategic moves, such as international expansion. When investing internationally, firms have to deal with heterogeneous political contexts and face more uncertainty, including political uncertainty. In particular, firms become subject to liabilities of foreignness (Hymer, 1976; Zaheer, 1995) due to their lack of knowledge about a specific foreign market, from consumers' preference for domestic products, and, notably, from risks related to decisions made by foreign governments. As a consequence, international expansion strategy and performance tend to exhibit a deeply entrenched political nature and, therefore, constitute an ideal research setting to investigate the impact of political connections on firms' strategic moves.

The dissertation is composed of three essays, each contributing to address part of the puzzle regarding how political connections affect a firm's international expansion strategy and performance. Figure 2 shows a graphical representation of the overall model of the dissertation. In the first essay, I examine the role of political connections as a moderator of the relationship between home-host ties and international strategy in a sample of greenfield investments in manufacturing undertaken by firms from several home countries. In the second and third essays, I examine the role of political connections as direct antecedents of international strategy and performance. In these latter two essays, I rely on an original hand-collected dataset that includes data on various political connections enjoyed by the largest French firms. In the second essay, I

investigate the role of different types of political connections and of a favorable political change on a firm's international investments amount and risk profile. Finally, in the third essay, I analyze how political connections influence the speed with which firms secure funding and complete development of their project finance-based investments, two highly politically-entrenched performance indicators.

**Figure 2: Graphical representation of the dissertation model**



The dissertation helps advance non-market strategy and international business literatures by analyzing the impact of different types of political connections on firms' international expansion strategy and performance. First, I distinguish various types of political connections depending on whether they are rooted in friendship, educational background or professional experience. This allows me to obtain a better understanding of the potential mechanisms underlying the influence of political connections on firm strategy and performance. Second, I analyze the impact of political connections on a type of strategy that is highly entrenched in

politics – i.e. international expansion strategy – and in which the effect of such political connections should be more visible and meaningful. Finally, I examine the impact of political connections on a type of performance that more closely relates to a firm’s capacity to obtain advantages from the government than financial performance – i.e. the speed with which the firm can obtain funding and complete developing its large projects. Furthermore, my findings rely on extremely rich data about various types of political connections and international expansion strategies by firms originating in several countries. I carefully collected and organized these data to be able to obtain the most refined understanding of the relationships I aim to uncover in each study. With this objective, in each essay, I also applied distinct research methods – including conditional logit, panel data analysis, difference-in-differences and fuzzy set qualitative comparative analysis – depending on their appropriateness to the specific research question in each essay.

In the remainder of this introduction, I first provide arguments for why examining political foundations of firms’ strategy and performance is important. I start by briefly reviewing the literature in which I ground my argument that political connections are a relevant indicator of a firm’s political capabilities. I focus on showing how the dissertation helps address many of the issues and unanswered questions in that stream of research. I also emphasize the relevance of studying heterogeneity in strategic decisions stemming from political connections. Finally, I provide a brief summary of each essay and show how they, in combination, advance scholarly understanding of the relationship between political connections and firm international expansion strategy and performance.

### **Political Engagement, Political Connections and Firm Strategy**

Firms and governments are inextricably connected and, consequently, influence each other's decisions and performance. When the government implements or changes policies, firms operating or planning to start operating in its territory are inevitably affected. For instance, labor and tax policies have substantial effects on firms' costs and, as a consequence, profitability. The government is also affected by decisions made by firms, as it depends on jobs, taxes and other spillovers they generate. Thus, governments are usually interested in attracting and maintaining private investments. Present this interdependence between governments and firms, it is natural that firms engage in politics to obtain the best possible policies for their business interests. The literatures on non-market strategy and on corporate political activities have extensively analyzed how firm performance is affected by firm activities such as campaign donations and lobbying (De Figueiredo, 2009; Hillman, Keim, & Schuler, 2004) and by more relational forms of political engagement, such as hiring former politicians and government officials as managers or board members (Goldman, Rocholl, & So, 2009; Hillman, 2005; Lester, Hillman, Zardkoohi, & Cannella, 2008).

While the role of firms' political engagement on performance has been investigated, a consensus on the direction of the relationship has not been reached (Sun, Mellahi, & Wright, 2012). Some studies found that political engagement affects firm performance positively (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001; Hillman, 2005). Other studies found a negative or neutral effect of political engagement on various indicators of firm performance (Aggarwal, Meschke, & Wang, 2012; Kramarz & Thesmar, 2013; Siegel, 2007). Three issues appear to have driven the mixed results in the earlier work and constitute relevant gaps in the literature. The first one is that firms vary in their capability to use political engagement to

influence political actors and to mobilize government resources. In other words, firms are possibly heterogeneous with regards to their political capabilities and this heterogeneity may generate distinct performance outcomes (Baron & Hall, 2003; Bonardi, 2011; Bonardi, Holburn, & Bergh, 2006). The second issue is that this stream of research still devotes little attention to the fact that different types of political engagement – and different types of political connections – operate through different channels and may influence firms through distinct mechanisms (Chung, Mahmood, & Mitchell, 2007; Hadani & Schuler, 2013). The third issue is that a firm's political engagement may have its most meaningful effect on a firm's strategy, and only affect its performance indirectly (Siegel, 2007; Zhu & Chung, 2014).

I argue that a way to address the first issue is assessing a firm's political capabilities, which should reflect the firm's effectiveness in attaining its objectives from the government and be more stable over time. I further argue that focusing on political connections, i.e., relational ties a firm has with authorities in the political environment of its country of origin, is an appropriate approach to assess political capabilities. In comparison to indirect or transactional political relations (Hillman & Hitt, 1999), which are generated through actions such as campaign donations and lobbying, relational political connections are more permanent and arguably effective in generating political capabilities (Bonardi, 2011). This is because firms whose top decision makers are personally related to government authorities are likely to be more effective in influencing these political actors and in mobilizing government resources. Nonetheless, similarly to the literature on political engagement in general, studies on the effects of political connections on firm-level outcomes have primarily emphasized their impact on a firm performance (Amore & Bennedsen, 2013; Faccio, 2006; Goldman et al., 2009; Hillman, 2005),

and, thus, produced limited documentation of their influence on firm strategy (Siegel, 2007; Zhu & Chung, 2014).

To address the second issue underlying the lack of consensus in the literature on the effects of political engagement, it is important to account for the various types of political connections and how they may operate differently (Sun et al., 2012). Prior research has documented the relevance of numerous types of such relational political connections separately. Government experience, common educational background and friendship or family ties are particularly prominent in previous studies. Political connections based on government experience are created when a firm's top decision makers have worked in politics or as top government officials prior to their business career. In such cases, the firm's decision makers are likely to have kept contacts in the government and to have acquired capabilities related to understanding how the government operates (Bertrand, Kramarz, Schoar, & Thesmar, 2006; Boddewyn, 1988; Kramarz & Thesmar, 2013; Lester et al., 2008). Political connections based on common educational background are established when firm and government leaders share the same educational background and know each other from studying together at the same school or from belonging to a relevant and active alumni network (Kramarz & Thesmar, 2013; Siegel, 2007). Finally, political connections based on friendship or family ties are created when top business leaders have personal friends (Coulomb & Sangnier, 2014; Fisman, 2001) or family members (Amore & Bennedsen, 2013; Faccio, 2006; Fisman, 2001) at high-level positions in the government. These different types of political connections potentially operate differently in influencing a firm's behavior and may have contrasting performance implications.

Finally, to address the third issue, it is critical to understand whether and how firms with political connections are able and prone to make distinct strategic moves relative to firms without

political connections, because performance differentials may stem from this heterogeneity in strategy. A few recent studies have started to examine the influence of political connections on several firm strategies, such as financing (Leuz & Oberholzer-Gee, 2006), industry diversification (Chung et al., 2007; Zhu & Chung, 2014) and risk-taking (Boubakri, Mansi, & Saffar, 2013). However, much is yet to be understood regarding the influence of political connections on firm strategies. Particularly, examining the influence of political connections on highly politically-entrenched decisions, where this influence might be more easily observable and more meaningful, can contribute immensely in advancing the literature. Investigating international expansion strategy not only allows me to observe such an effect, as it is indeed a type of strategy with deep political entrenchment, but also allows me to analyze whether the benefits (or liabilities) stemming from political connections are geographically constrained.

Next, I briefly summarize the three essays composing the dissertation. Each essay helps solve the three issues described above and advance knowledge on the relationship between political connections and firm international expansion strategy and performance. First, I focus on political connections as indicators of political capabilities and argue that they enable firms to act in ways other firms cannot. Second, I examine the effect of three different types of connections across the essays. Finally, in two essays, the main dependent variables are firm international expansion strategies, and, in the third essay, the outcome is an indicator of performance for both domestic and international investments.

### **Political Connections and Location Choice**

A central issue for firms considering international investments is the risk that foreign government decisions might negatively affect the value of such investments and, in extreme cases, expropriate the foreign investor altogether (Cuervo-Cazurra, 2008; Duanmu, 2014;

Henisz, 2000; Holburn & Zelner, 2010; Kobrin, 1979, 1984; Ramamurti, 2001; Rodrik, 1991). As a consequence, firms will be reluctant to invest in risky countries (Delios & Henisz, 2003a; García-Canal & Guillén, 2008; Holburn & Zelner, 2010). Host countries can use several measures to assuage investors' concerns regarding expropriation risks, but most of those measures are trumped by national sovereignty, because, after an investment is made, the host nation might be able to modify the rules of the game in detriment of the firm (Kobrin, 1987; Murtha, 1991; Vernon, 1980). Bilateral Investment Treaties (BITs), on the other hand, are a specific extra-territorial institution centered on providing host countries with a mechanism to produce a credible commitment to foreign investors (Kerner, 2009; Salacuse & Sullivan, 2005), and should, therefore, impact firms' foreign investment decisions.

In the first essay of the dissertation, "*The Influence of Foreign Affairs and Firm Political Influence on the Location Choice of International Investments*", I investigate the role of political capabilities as modifiers of the relationship between BITs, a dimension of home-host ties, and the choice of location of international investments, one type of international expansion strategy. As political influence, reflected in both political connections and firm size, might influence a firm's ability to mobilize the home-country government as a resource and, hence, might also influence how firms respond to host country-based credible commitments, such as through BITs, I seek to address the following research question: "How do political capabilities alter firms' sensitivity to host country-based credible commitments?"

I hypothesize, first, that a firm is more likely to invest in a potential host nation when the firm's home country has a BIT with that potential host nation. More importantly, I predict that BITs are more meaningful for firms without the ability to use alternative means to protect their investments, particularly firms without political connections in their home country and not very



large firms. In other words, I predict that politically-connected and very large firms enjoy a competitive edge regarding their ability to invest in places where other firms shy away from investing into.

I use conditional logit models to test these hypotheses on a sample of international greenfield investments with manufacturing purposes undertaken by listed firms from eleven home countries between 2003 and 2010. Overall, I find support for my predictions. BITs appear to provide a mechanism that allows governments to credibly commit to foreign investors, as the existence of a ratified BIT between home and host countries positively affects the likelihood of investment. More importantly, this institution is especially meaningful for investing firms that do not have strong political connections in their home nation and that are not very large. Politically-connected and very large firms choose the location of their international investments independently of BITs.

### **Types of Political Connections and Firms' Profile of International Investments**

In the second essay, "*A French Connection: The Influence of Political Connections on International Expansion Strategy*", I examine the effects of political connections on international expansion strategy in more detail. The main research question in this essay is: "How do different types of political connections influence international expansion strategy?" To address this question, I analyze how three types of political connections, (i) government experience-based, (ii) common education-based, and (iii) friendship-based political connections, influence both the amount and the level of exposure to expropriation risk of the firm's international investments in a given period of time.

I propose three ways through which political connections should positively impact a firm's international expansion strategy. First, firms with political connections know how to deal

with governments and receive more and better information about changes in policies and other political trends through social interactions with government authorities. Second, political connections affect a firm's actual and perceived ability to influence the home country government to act aiming the protection of the firm's assets (Baron & Hall, 2003; Bonardi, 2011). Third, political connections enable firms to secure funds for investment at lower costs through privileged access to various funding sources and higher market valuation (Boubakri, Guedhami, Mishra, & Saffar, 2012; Claessens, Feijen, & Laeven, 2008; Faccio, Masulis, & McConnell, 2006). Furthermore, I submit that the value for firms of friendship-based political connections is contingent on the political regime. These connections will be more valuable when the firm's decision makers have a friend that enjoys more power in the home country's government. Accordingly, an increase in the value of those political connections should also intensify their influence on a firm's international expansion strategy.

I use data on the international investments made by the largest firms listed on the French stock exchange between 2003 and 2012 to empirically test these hypotheses. I find empirical support for the main predictions. Politically-connected firms engage in distinct international expansion strategy relative to non-politically-connected firms. I also find that this heterogeneity is contingent on the type of political connections, with political connections based on friendship ties and on common educational background being the most meaningful ones in explaining the amount and the level of exposure to expropriation risk of a firm's international investments, respectively. Finally, I find that the election of Nicolas Sarkozy as the president of France generated significant effects on the strategy of firms connected to him through friendship ties. Specifically, firms enjoying friendship ties with Sarkozy spent significantly more in their international investments after the 2007 election.

## **Political Connections and Speed Performance**

In the third essay, “*Political Connections and Speed in Large Projects*”, I move the focus to examining the influence of political connections on a firm’s performance. Particularly, the main research question I aim to address in this essay is “How do political connections influence speed in project finance-based investments?” Despite their widespread use in large infrastructure projects around the world, there is a stark dearth of research on project finance-based (PF) investments (Esty, 2004; Vaaler, 2008), especially regarding a firm’s capabilities to undertake successful PF investments. Speed is a notably relevant indicator of project performance, as the time required to obtain funding and then complete project development entails substantial costs for both sponsor firms and other stakeholders.

Because many of the risks faced in funding and developing PF investments are of political nature (Esty, 2004; Sawant, 2010a; Vaaler, James, & Aguilera, 2008), political connections should be substantially meaningful in this context. Indeed, PF investments typically require sponsors to closely deal with governments to obtain various types of licenses and permits, to ally with governments in public private partnerships (PPPs), to negotiate taxes and labor-related issues, etc. Relatedly, capital lenders may deem different sponsors as more or less likely of being bailed out by governments, depending on the sponsor’s political connections.

Accordingly, I advance that political connections operate as a mechanism to reduce PF investments risks and should, thus, positively influence PF investments speed. However, political connections should be relevant only when in combination with other project, sponsor, and location attributes that together determine the overall riskiness of a particular project. I further maintain that political connections are more meaningful when the project lacks other features that could also mitigate its riskiness. Sponsors without political connections, on the other hand,

should be associated with high speed only if they announce projects with low riskiness. Finally, I allow distinct types of political connections to associate with different outcomes.

I use fuzzy sets methods to empirically investigate these propositions on a sample of PF investments sponsored by the largest firms listed in the Paris stock exchange, during the 2003-2012 period. The sample includes 95 projects, concentrated in infrastructure industries such as power distribution, transportation, oil and gas, and water treatment and distribution, sponsored by 17 firms in 31 distinct host countries. My results provide interesting insights on the various paths firms can follow to speed up or to avoid delays in their PF investments.

### **Structure of the Dissertation**

Figure 3 presents a visual summary of the dissertation, including the main research question, methods and findings of each essay and the overall contributions of the dissertation. The remainder of the dissertation is organized as follows: chapters 2 through 4 are the three essays described before, and chapter 5 is a concluding chapter including the main contributions, limitations and avenues for future research derived from the dissertation.

**Figure 3: Visual summary of the dissertation**

<b>How do political connections impact a firm's international expansion strategy and performance?</b>			
<b>Essay</b>	<i>The Influence of Foreign Affairs and Firm Political Influence on the Location Choice of International Investments</i>	<i>A French Connection: The Influence of Political Connections on International Expansion Strategy</i>	<i>Political Connections and Speed in Large Projects</i>
<b>Research Question</b>	How does political influence alter firms' sensitivity to host country credible commitments?	How do different types of political connections influence international expansion strategy?	How do political connections influence speed in project finance-based investments?
<b>Setting</b>	Greenfield investments by firms from eleven advanced home countries during the 2003-2010 period	International investments by the largest French firms during the 2003-2012 period	Project finance-based investments by the largest French firms during the 2003-2012 period
<b>Method</b>	Conditional logit	Bartels's adaptation of Mundlak's random effects specification	Fuzzy sets qualitative comparative analysis
<b>Main Findings</b>	<ul style="list-style-type: none"> <li>-Bilateral investments treaties (BITs) positively influence a firm's choice of international investment location</li> <li>-Firms with political connections and very large firms choose investment locations independently of presence of a BIT</li> </ul>	<ul style="list-style-type: none"> <li>-Firms with friendship-based political connections through the board make more international investments than others</li> <li>-Firms with friendship-based political connections through the CEO make less international investments than others, but their investments increase after the political connections become more valuable</li> <li>-Firms with common education-based political connections through the CEO concentrate more their international investments in riskier countries</li> </ul>	<ul style="list-style-type: none"> <li>-Several combinations of factors lead to high funding and completion speed</li> <li>-The pathways for high speed are distinct from the pathways for low speed</li> <li>-Although relevant, political connections are neither sufficient nor necessary to achieve high speed</li> <li>-Different types of political connections combine with different factors to determine speed</li> </ul>
<b>Overall contributions</b>	<ul style="list-style-type: none"> <li>-Political connections are capabilities that help firms mitigate risks in international investments</li> <li>-Different types of political connections heterogeneously affect distinct dimensions of international strategy and performance</li> <li>-Political connections have meaningful implications for firms headquartered in an advanced economy</li> </ul>		

**CHAPTER 3: The Influence of Foreign Affairs and Firm Political Influence on the  
Location Choice of International Investments**

## **Abstract**

We investigate how Bilateral Investment Treaties (BITs) impact foreign investment decisions. Consistent with existing studies, we hypothesize that firms are more likely to invest in a nation when their home country has a BIT with that potential host nation. We advance the literature by proposing that BITs are less critical for firms that have the ability to use alternative means to protect their investments. Specifically, we argue that firms that are politically connected in their home country or are very large firms, rely less on BITs when choosing the location of their foreign investments. We test and find overall support for our hypotheses on a sample of international investments made by firms from eleven home countries between 2003 and 2010. By demonstrating firm heterogeneity in how they respond to BITs, we (a) provide better empirical tests of the mechanisms through which BITs affect investment; (b) reconcile research findings that suggest some firms do not consider BITs when investing abroad with findings that BITs do indeed affect foreign investment flows; and (c) highlight strategic considerations for when firms consider such extra-territorial institutions.

**Keywords:** Political connections; international investments; bilateral investment treaties; credible commitment.

## Introduction

A major concern for firms considering international investments is that future host government actions can negatively affect the value of their investments, after these investments have been made (Duanmu, 2014; Henisz, 2000; Holburn & Zelner, 2010; Kobrin, 1979; Ramamurti, 2001; Rodrik, 1991). In extreme cases, foreign investors may suffer outright expropriation (Holburn & Zelner, 2010; Kobrin, 1984). Wary of this, savvy investors are reluctant to invest in risky countries, all other things equal (Delios & Henisz, 2003a; García-Canal & Guillén, 2008; Holburn & Zelner, 2010). On the other hand, entering foreign countries in which competitors are reluctant to invest or entering earlier than others has been argued or shown to create a competitive advantage and enhance performance.

Because they might lose incoming foreign investment and the related spillovers to their economies, many host nations seek to assuage foreign investors' concerns by committing to protect their investments. One solution is to rely on supranational institutions, such as the World Bank, the International Monetary Fund (IMF), or the Organization for Economic Cooperation and Development (OECD), to make these assurances more credible (Alcacer & Ingram, 2013; Rangan & Sengul, 2009). However, the issue of nation-state sovereignty – which gives rise to the investors' underlying concern in the first place – also makes investors cautious about the credibility of such assurances (Murtha, 1991). Threats to foreign investors might arise from host country governments reneging on their promises or from government change in the host country. Similarly to any other commitments by a sovereign nation, assurances provided through supranational institutions can be upheld or undone, because most supranational institutions are trumped by national sovereignty and lack the power to enforce commitments (Cao, 2009; Ingram, Robinson, & Busch, 2005; Ramamurti, 2001).



We investigate how firms rely on the credible commitments potential host countries make to choose the location of their foreign investments and how some firms are able to forgo the safety provided by such commitments, thus benefiting from first mover advantages unavailable to most other firms. More specifically, we examine how Bilateral Investment Treaties (BITs), a specific extra-territorial institution centered on providing host countries with a mechanism to produce a credible commitment to foreign investors (Kerner, 2009; North, 1993; Salacuse & Sullivan, 2005), impact a firm's decision to invest in one country rather than another. We further examine how a firm's political influence allows it to choose the location of its foreign investments, even without benefiting from the protection provided by a BIT.

Based on external arbitration and the provision for affected investors to seize host government assets held outside the host country, a BIT provides a mechanism for countries to credibly commit to treat foreign investors fairly (Kerner, 2009; Yackee, 2008), thus mitigating foreign firms' concerns about expropriation. BITs have received relatively little attention in the strategy and international business literatures (Jandhyala & Weiner, 2014). In the political science and law literatures, the focus has been on country level exchange of FDI, and no consensus has emerged on whether and how BITs affect FDI (Berger, Busse, Nunnenkamp, & Roy, 2011; Busse, Königer, & Nunnenkamp, 2010; Haftel, 2010; Kerner, 2009; Salacuse & Sullivan, 2005). Most studies in this literature examine the influence of the number of BITs signed by a specific host country on its total FDI inflows (Busse et al., 2010; Neumayer & Spess, 2005). Such analyses overlook the fact that BITs are bilateral agreements that should primarily affect investment decisions by firms originating in one signatory country and investing in the other signatory country, but not firms originating in third countries.

Other studies in political science and law do examine the influence of a BIT between two countries on the FDI flows between these countries (Egger & Pfaffermayr, 2004; Kerner, 2009; Salacuse & Sullivan, 2005). However, firms may differ in how they deal with the risk associated with foreign investments, and in particular with the risk of expropriation, and may thus react differently to the existence of a BIT between their home country and potential host countries. More specifically, the effect of BITs may depend on what alternative means to protect its international investments a given firm is able to mobilize. In other words, despite the valuable insights provided by previous studies on the effect of BITs on FDI flows, we lack knowledge about how BITs affect firm level decisions concerning the location of international investments and about how different firms will react differently to the presence or absence of a BIT between their home country and a potential host country.

We hypothesize that, in general, a firm is more likely to invest in a nation when its home country has a BIT with that potential host nation. We argue that this is a more direct test of how BITs affect investment decisions than what exists in the current literature which deals with country-level FDI flows. Moreover, and more importantly, we propose that BITs are less critical for firms that have the ability to use alternative means to protect their investments. Specifically, we argue that firms that are politically connected in their home country, or are very large firms, rely less on BITs when choosing the location of their foreign investments because their connections or their significant size provide them with a means to influence either their home country government, the host country authorities, or both.

We use conditional logit models to test these hypotheses on a sample of international investments with manufacturing purposes undertaken by listed manufacturing firms from seven home countries in 119 host countries between 2003 and 2010. This approach provides several

research design advantages relative to previous work on the effect of BITs on FDI. First, we examine how BITs affect firm-level decisions, thus mitigating some of the potential endogeneity issues. Second, we introduce two firm-level factors, firm political connections and firm size, and evaluate how these factors make BITs more or less important for a firm deciding on the location of its international investments. Finally, based on recent findings showing that signed – but not ratified - BITs do not create a sufficiently credible commitment (Egger & Pfaffermayr, 2004; Haftel, 2010), we focus on BITs ratified by both signatory countries.

Overall, we find support for our predictions. BITs appear to provide a mechanism through which governments can credibly commit to foreign investors: a firm from a given home country is more likely to invest in a host country in the presence of a BIT between home and host country. With respect to firm level attributes, both political connections and firm size appear to provide alternative means to protect foreign investments, thus making BITs less important for both politically connected and very large firms deciding on the location of their international investments.

## **Theory and Hypotheses**

Prior literature has investigated multiple factors that explain where firms locate their international investments. Among these factors, host country characteristics have received the most attention because they can either attract – for instance, by providing a large market, cheap factor costs or low taxes – or repel international investments. One of the main hurdles firms may face when investing in foreign countries is the risk of expropriation. Although other types of obstacles to international investments, such as various forms of distance, can be alleviated through experience or organization design, expropriation risk is associated with potentially arbitrary decisions made by sovereign nations. This phenomenon has been extensively discussed through the lens of the obsolescing bargaining model (Kobrin, 1987; Ramamurti, 2001; Vernon, 1971), which describes the shift in bargaining power between multinational firm and foreign government, before and after an investment is made.

Although outright expropriation has become less frequent, it has been replaced by what has been termed ‘creeping expropriation’, a more subtle way for states to behave opportunistically (Henisz, 2000; Minor, 1994), gradually changing their policies in ways that detrimentally affect the foreign firm’s profitability prospects (Henisz, 2000; Holburn & Zelner, 2010). Naturally, multinational firms are highly concerned with expropriation risk, ranking these risks above other potential difficulties they face in foreign markets, such as access to finance and macroeconomic instability (Duanmu, 2014).

This discussion suggests that political factors are crucial in influencing firms’ decisions on where to locate their international investments. Existing studies have focused on three groups of host country political features that may affect international investment decisions: i) host country political attractiveness, ii) host country political distance relative to the home country,

and iii) host country political ties with the home country. Research on the first group of features has shown that firms prefer to invest in countries that are able to provide a favorable institutional environment in which their business is more likely to prosper (Blonigen, 2005; Henisz, 2000; Sauvart & Sachs, 2009). However, countries differ with respect to the institutional environment they provide to potential investors, and rarely offer an environment that optimally guarantees the protection of foreign investments. In order to mitigate the risks stemming from these differences, firms take into account the two latter groups of host country features – host country political distance relative to the home country, and host country political ties with the home country – when making their international investment decisions.

First, firms can rely on experiential knowledge (Delios & Henisz, 2003a), selecting locations that are closer to their home country with regards to expropriation risks (Cuervo-Cazurra & Genc, 2008; Holburn & Zelner, 2010). Second, firms can choose to invest in countries that are well connected globally (Büthe & Milner, 2008; Neumayer & Spess, 2005) and to their home country in particular (Alcacer & Ingram, 2013; Kerner, 2009; Li & Vashchilko, 2010). Thus, the first risk mitigating mechanism is the level of familiarity a firm perceives to have with the political environment of a particular host country. Greater familiarity increases the likelihood of choosing a particular host country as the location for international investment because the firm may have developed capabilities associated with how to deal with the type of political environment prevailing in that host country. Indeed, a few studies have examined the role of political distance as an obstacle for investment, showing that firms rely on their previous experience in other foreign countries when investing in locations that differ politically from their home country (Delios & Henisz, 2003a). Additionally, these studies show that firms seek locations that are politically closer to their home country (Holburn & Zelner, 2010).

The second mechanism to reduce the uncertainty associated with international investments is the political ties a firm's home country government maintains with foreign governments. Formal and informal ties between countries – such as diplomatic representation, treaties, co-membership in international organizations, military alliances, historical ties and trade – have a substantial effect on economic exchanges between them. For example, Makino and Tsang (2011) have shown that historical ties between home and host countries have affected the timing of firms' entry into Vietnam. Other studies that have analyzed this mechanism confirm that inter-governmental ties increase international capital flows. These studies have shown that countries that partake in preferential trade agreements and belong to multilateral trade organizations (Büthe & Milner, 2008), or that sign BITs with a greater number of foreign countries (Busse et al., 2010; Neumayer & Spess, 2005) receive more FDI. Several studies also suggest that political ties specific to a country pair affect firms' investment location decisions, as the bilateral flows of FDI seem to increase with the establishment of a BIT between two countries (Egger & Pfaffermayr, 2004; Kerner, 2009; Salacuse & Sullivan, 2005) and with the number of connections between them in the IGO network (Alcacer & Ingram, 2013). Other studies, however, find no effect, or even a negative effect of such formal inter-governmental ties on FDI exchange (Hallward-Driemeier, 2003; Yackee, 2008).

We posit that the issue of nation state sovereignty is central in investors' lack of confidence in inter-governmental ties as protection for their foreign investments, as these ties can be discontinued or, even if they are maintained, may not prevent a sovereign state from making decisions that are detrimental to the investors' interest, in extreme cases a decision to expropriate. In order to properly protect their international investments from the risk of expropriation, firms may seek some guarantee that the host state will not use its sovereign status

to confiscate value from the firm. As we will describe in the next section, states eager to receive foreign investment can offer such a guarantee to potential investors by credibly committing that they will not interfere detrimentally in the investor's business in their territory. Another way for firms to alleviate the expropriation risk they perceive is to rely on their own ability, and in particular on their political influence, to protect their international investments. We explore these possibilities in turn in the next sections.

### **The Effect of Bilateral Investment Treaties**

Although most prior research assumes that all inter-governmental ties promote international investments, not all such ties will capture the attention of investors in the same way and thus influence their foreign investment decisions identically. As we posited before, the considered ties must be recognized by investors as a reliable protection for their investments in the host country, if they are to influence location choice. In other words, to affect international investment decisions, inter-governmental ties should be associated with a credible commitment (North, 1993; Yackee, 2007) by the host country not to interfere detrimentally on a foreign firm's business in its territory.

Following a recent stream of studies in political science and law (Kerner, 2009; Yackee, 2008), we suggest that Bilateral Investment Treaties (BITs) are good examples of such strong, highly-visible and legally-binding inter-governmental ties that create a credible commitment by host countries vis-à-vis foreign investors. BITs are contracts signed by two countries with the objective of promoting and protecting investments by investors from one country in the other country (Dolzer & Stevens, 1995; Sauvant & Sachs, 2009; Vandevelde, 2005). In general, BITs include dispute settlement procedures that are accepted at the bilateral and international level (Kerner, 2009; Neumayer & Spess, 2005; Salacuse & Sullivan, 2005; Sauvant & Sachs, 2009;

Yackee, 2007) and which may partially overrule potential expropriation decisions by the host country (Büthe & Milner, 2009; Desai & Moel, 2008; Franck, 2007). Most BITs give access to international arbitration institutions (Desai & Moel, 2008; Salacuse & Sullivan, 2005; Yackee, 2007), such as the International Centre for Settlement of Investment Disputes (ICSID), an institution affiliated to the World Bank Group. In these institutions, a firm can initiate a process against a host country, and the dispute is resolved by a group of arbitrators agreed upon at the onset by both parts. Decisions are binding and may include the confiscation of assets in third countries as a guarantee. Before the creation of BITs, only countries could initiate lawsuits against other countries, making it necessary for firms to first convince their home country government to espouse their claim (Vandeveldt, 2005). Naturally, this was not an easy task, and even if the claims were espoused by the home country, the disputes could get resolved through an agreement at the country level, regardless of the firm's satisfaction with the settlement terms. The very first BIT was signed by Germany and Pakistan as far back as 1959, but this mechanism has been increasingly adopted during the 1990s and after 2000. By 2015, there were more than 2500 BITs signed between a large number of countries and, according to UNCTAD data, more than 500 processes involving BITs had been arbitrated, with no clear pattern as to whether host country or investors tend to win.

The establishment of a BIT typically receives wide media coverage in both signatory countries. In order to guarantee the protection of foreign investments, a BIT entails a partial loss of sovereignty by the signatory countries (Kerner, 2009). Because of this, there are substantial political costs in implementing these agreements. These costs signal that the involved countries are strongly committed to the BIT principles. As a consequence, a BIT can be seen as a credible



commitment in terms of investment protection which, in turn, should lead to more investments being exchanged between the signatory countries.

Finally, while most empirical evidence on the effect of BITs on FDI provides mixed results (Kerner, 2009; Sauvart & Sachs, 2009), more recent studies (Busse et al., 2010; Egger & Pfaffermayr, 2004; Kerner, 2009; Neumayer & Spess, 2005; Salacuse & Sullivan, 2005), analyzing a larger set of country pairs for a longer time period, find a positive and robust effect of BITs on the amount of FDI that a country receives. These studies also confirm that there is substantial variance regarding countries' use of BITs, both over time and across regions, suggesting that BITs are indeed a strong differentiating factor among potential host countries. On this basis, we advance that firms perceive BITs as reliable signals that their investments will be protected in a particular host country. Therefore, we put forth that:

*Hypothesis 1: The existence of a bilateral investment treaty between a firm's home country and a foreign country increases the likelihood of the firm investing in that foreign country.*

### **The Effect of Firm's Political Influence**

The above hypothesis presents BITs as a resource available to all firms originating in a given home country and seeking to invest abroad. However, firms may differ in terms of their capacity and willingness to leverage such treaties. Research on non-market strategies has long argued that firms are heterogeneous when it comes to political influence, that is, their ability to effectively achieve their objectives vis-à-vis governments (Baron & Hall, 2003; Bonardi et al., 2006). Research on corporate political capabilities and on political connections has also shown that firms differ in terms of the extent to which they engage in and influence politics (Faccio, 2006; Fisman, 2001; Hillman et al., 2004). Such differences in political influence might lead to

strategic choice and performance heterogeneity (Boubakri et al., 2013; Claessens et al., 2008; Faccio, 2006; Faccio et al., 2006; Leuz & Oberholzer-Gee, 2006). Persuading their home government to intervene in a foreign country or to appeal to multilateral arbitration to uphold a firm's interests, as well as deterring host governments from acting in a detrimental fashion, are non-market strategies. Accordingly, some firms are likely to be more effective than others at carrying out such non-market strategies.

Firms can derive their political influence from various sources: explicit political connections, lobbying, campaign donations or even bribery, the possession of strategic resources that are critical to the government, firm size, etc. Lobbying and campaign donations are only legal in a limited number of countries whereas bribery and the value different governments assign to various types of strategic resources are difficult to observe. Explicit political connections and firm size in turn are more prevalent sources of political influence in most countries in the world. We thus focus on explicit political connections and firm size as significant sources of political influence. Regarding political connections, we draw on prior research and consider that such connections are established through the ownership of a stake in the firm by current or former politicians from the firm's home country and by their associates (Faccio, 2006). We argue that such connections facilitate a firm's interaction with political authorities in its home country. They can help, for instance, in convincing the home country government to intervene in foreign countries on the firm's behalf. We, thus, propose that firms with political connections anticipate that they will be able to gain support from political authorities of their home country to protect their interests abroad, should this be necessary. In line with that, politically-connected firms may be better able to overcome the risks of investing abroad, even in host countries that are not related – or only weakly related – to their home

country. Thus, because they expect assistance from their home country authorities, irrespective of broad credible commitments by host countries, for example through BITs, firms with political connections may be more likely to invest in countries lacking a BIT with their home country than firms without such political connections.

Moreover, because turning to international arbitration institutions individually is costly (Franck, 2007), firms with political connections may prefer to avoid having to do so, thus ignoring BITs when making foreign investments. Relative to other firms, politically-connected firms feel more confident that they can rely on the assistance of their home country authorities to protect their interests. Not having to rely on formal mechanisms of investment protection may therefore provide politically-connected firms with an advantage, making it possible for them to invest in host countries their non-connected rivals shy away from. This reasoning is consistent with prior research that has shown that firms with political connections in their home country obtain first mover advantages in international business (Frynas, Mellahi, & Pigman, 2006), and are less sensitive to risks in their investments (Boubakri et al., 2013; Chen, Ding, & Kim, 2010). Such politically-connected firms may thus choose where to invest regardless of BITs, anticipating instead that, thanks to their political connections, they will be able to convince their home country authorities to act on their behalf, when needed, to protect their interests. In other words, politically-connected firms can rely on other sources of investment assurance, such as home-country intervention, and may therefore be less sensitive than their non-connected counterparts, or not sensitive at all, to the credible commitment created by BITs. For firms without political connections, on the other hand, given the lack of other safeguards for international investments, the credible commitment created by a BIT will often be a relevant factor when choosing the location of their international investments. Therefore, we put forth that:

*Hypothesis 2a: Politically connected firms rely less on bilateral investment treaties between their home country and foreign countries when deciding on the location of their international investments.*

We also argue that very large firms who, because of their sheer size, have enough clout to influence policies and decisions in both the home and host countries, and potentially at the international level, are less dependent on BITs when deciding on the location of international investments. Firm size has been shown to be one of the main antecedents of corporate political activity (Hillman et al., 2004). In parallel, large multinational firms have been argued to strongly influence local politics in countries in which they operate. For example, it has even been speculated that such firms as United Fruit in Central American countries or ITT in Chile have played a significant role in toppling governments whose policies were detrimental to their interests (Bucheli, 2008; Bucheli & Salvaj, 2013; Nye, 1974; Sampson, 1973). More recently, large firms have taken an active role in international organizations such as WTO, OECD or the World Economic Forum and have been able to influence policies, standards, norms and regulations that govern trade and other economic activity at an international level in their favor (Dunning & Lundan, 2008). On this basis, we formulate the following prediction:

*Hypothesis 2b: Very large firms rely less on bilateral investment treaties between their home country and foreign countries when deciding on the location of their international investments.*

## Data and Methods

We test our hypotheses on a sample of foreign investments made by listed firms from 2003 to 2010. The availability of data on firm political connections and on their foreign investments guided our choice of home countries. As in prior studies, we analyzed international greenfield investments by firms in manufacturing industries (SIC codes 20-39). We focus on greenfield investments because these decisions reveal information about location choice that is not confounded with other considerations as it would be in an acquisition (Alcacer & Chung, 2007; Chung & Alcácer, 2002; Shaver, 1998). We focus on manufacturing investments because many host countries are plausible locations for a given manufacturing investment. Other types of investments such as those in extractive industries (e.g., petroleum and minerals), distribution, or infrastructure are very location focused and reflect a different decision process.

Our primary data source is the Financial Times *fDiMarkets* database, which tracks greenfield investments around the globe (see Burger, van der Knaap, & Wall, 2013; Duanmu, 2014 for examples of studies using this data.). Due to the availability of political connections data, we restricted our sample to listed firms incorporated before 2001, and gathered data on investments made to establish or expand manufacturing activities. We verified that, for each home country, there were investments both by firms with political connections and by firms without political connections. This resulted in our sample including 1,073 firms originating from 11 home countries (France, Germany, Ireland, Italy, Japan, Malaysia, Philippines, Sweden, Thailand, United Kingdom and United States of America). We aggregated investments made by the same firm in the same host country in the same year, thus obtaining 5,001 unique firm-host-year observations.

### **Dependent Variable**

Our dependent variable,  $Investment_{ajt}$ , is binary and equal to 1 if firm  $a$  invested in host country  $j$  in year  $t$ , and 0 otherwise. We considered all countries on which we were able to gather data as potential targets for an investment. So, for each investment actually made, there were 123 potential alternative locations. That is, for each investment observation, we built a choice set of all countries in our dataset in which the focal firm did not make an investment, and assigned a value of zero for the dependent variable in these observations. Accordingly, our final sample for analysis comprises 618,350 data points.

### **Independent Variable**

We measured our independent variable with an indicator of the existence of a ratified BIT between home and host country. The variable  $BIT_{ijt-1}$  is a binary variable which received the value 1 if there existed a ratified BIT between home country  $i$  and host country  $j$  in year  $t-1$ . We relied on recent findings showing that signed – but not ratified - BITs do not create a sufficiently credible commitment (Egger & Pfaffermayr, 2004; Haftel, 2010) in choosing to focus on BITs ratified by both signatory countries. Such ratified BITs, as opposed to signed but not ratified BITs, should unquestionably reduce investment risk. We followed the literature and sourced these data from UNCTAD (Busse et al., 2010; Kerner, 2009; Neumayer & Spess, 2005; Salacuse & Sullivan, 2005; Yackee, 2008).

To test hypotheses 2a and 2b, which compare the impact of BITs on the decisions made by firms with distinct levels of political influence, we produced various groupings of investing firms. First, we split the sample depending on whether the investing firm was politically connected or not. We measured *political connections* $_a$  using a binary variable that is equal to 1 if firm  $a$  is politically-connected in its home country and 0 otherwise. We draw on Faccio's (2006)

work and considered a firm to be politically-connected if “at least one of its large shareholders (anyone controlling at least 10 percent of voting shares) or one of its top officers (CEO, president, vice-president, chairman, or secretary) is a member of parliament, a minister, or is closely related to a top politician or party” (Faccio, 2006: 369). We used inclusion in the list of politically-connected firms drawn up by Faccio as our measure of political connections (Boubakri et al., 2013; Chen et al., 2010; Faccio, 2006; Faccio et al., 2006). We then split our sample into investments by firms with political connections and investments (358 observations) by firms without political connections (4,643 observations). Second, based on information about each investing firm’s total assets, we generated the variable *very large firm<sub>ait</sub>*. This variable assigns the value 1 to the ten percent largest investing firms in terms of total assets in a given year *t*, and zero to all other firms. Data on total assets were obtained from the *Bureau van Dijk Osiris* database. We proceeded similarly to the previous variable and split our sample into two subsamples: investments by very large firms (1,723 observations) and investments by other firms (3,278 observations).

### **Control Variables**

We controlled for many other factors that could influence the relationship between the presence of a ratified BIT and the choice of a host country. We grouped these controls in three categories: i) cross-national distance, ii) inter-governmental relationships, and iii) host country attractiveness. When variables are time-variant, we used a one-year lag, unless otherwise stated.

Distance. We controlled for all dimensions of distance specified in the CAGE (Cultural, Administrative, Geographic, Economic) framework (Ghemawat, 2001, 2007). We used *colonial ties<sub>ij</sub>* – the existence of a colony-colonizer relationship (or vice-versa) between home country *i* and potential host country *j* at any time in the past – and *common official or spoken language<sub>ij</sub>* –

the existence of a shared official language or a shared spoken language by more than 10% of the population in each country – as indicators of cultural distance. We measured *geographic distance<sub>ij</sub>* as the great circle distance in kilometers between the largest city in home country *i* and the largest city in potential host country *j*. We also used the variable *common border<sub>ij</sub>* to indicate the degree of geographic distance and difficulty of transportation and access. Data for these four variables was obtained from the *Centre d'Etudes Prospectives et d'Informations Internationales* (CEPII). We measured administrative and economic distance by applying Kogut and Singh's (1988) formula – originally developed to calculate cultural distance – to indicators of institutional quality and economic performance. This index is calculated as the average of the ratio of the squared difference between home country *i* and host country *j* on a particular indicator and the global variance of that indicator. We used four components of governance quality from World Governance Indicators – voice and accountability, government effectiveness, regulatory quality, and rule of law (Kaufmann & Kraay, 2008; Kaufmann, Kraay, & Mastruzzi, 2011) – to calculate *institutional distance<sub>ijt-1</sub>*. Finally, to measure *economic distance<sub>ijt-1</sub>*, we applied the formula to GDP (in constant 2005 US\$), GDP per capita (in constant 2005 US\$) and GDP growth (annual %). This measure captures differences between home and host country in terms of economic size, wealth, and vigor. Data was obtained from the World Bank World Development Indicators (WDI) (World Bank, 2012).

Inter-governmental relationships. First, we included the variable *Interventionist IGO connections<sub>ijt10</sub>*, which was measured as a three-year moving average (between investment year minus 10 to minus eight) of the number of interventionist IGOs (Inter-Governmental Organizations) in which home country *i* and host country *j* were members at the same time (Cao, 2009; Ingram et al., 2005). Interventionist IGOs are international organizations that entail



coercion mechanisms, such as arbitration, mediation and adjudication means, to influence member countries to abide by their rules (Cao, 2009). Deviation from such rules is liable to substantial financial and reputational costs. Firms are, therefore, likely to perceive lower uncertainty in making investments in countries that belong to such types of organizations, jointly with their home country. The total number of interventionist IGOs in our sample is 48, including organizations such as the European Union, the International Monetary Fund, the World Trade Organization and the Organization for Economic Cooperation and Development. We follow prior literature in choosing a ten year lag to avoid concerns of simultaneity, to make sure that these interventionist IGO norms had been implemented by both countries at the time of the focal investment, and that the mutual membership was known by potential investors (Rangan & Sengul, 2009; Schrank, 2013). We follow prior research and use the data collected from Pevehouse, Nordstrom and Warnke (2004). Data on the classification of IGOs into interventionist and non-interventionist was kindly provided to us by Paul Ingram (Ingram et al., 2005). Second, we included the dummy variable *military alliance<sub>ijt-10</sub>*, which equals 1 if home and host country were in a military alliance ten years before the investment. Data for this variable was obtained from the Correlates of War project (Gibler & Press, 2009). Third, in line with prior literature, we measured the amount of international *trade<sub>ijt10</sub>* between home and host country, using the sum of exports and imports in dollars, as an indicator of a mutual dependence relationship between the two countries (Blonigen, 2005; Duanmu, 2014). We calculated this variable as a moving average of bilateral trade from year minus 10 to minus 8. Finally, we included the variable *political affinity<sub>ijt-1</sub>*, which measures the correlation of the votes of home country *i* and host country *j* at the United Nations General Assembly (Duanmu, 2014; Gartzke,

1998; Gartzke, Li, & Boehmer, 2001). For this, we used data provided by Mansfield and Milner (Mansfield & Milner, 2012).

Host country attractiveness. First, we included a dummy variable that indicates whether the head of the government in the host country is from the *military*<sub>*jt-1*</sub>, an indicator of political un-attractiveness of the host country. Data were obtained from the World Bank Database of Political Institutions (DPI) (Beck, Clarke, Groff, Keefer, & Walsh, 2001). Second, we included *population*<sub>*jt-1*</sub>, a measure of market size, *GDP per capita*<sub>*jt-1*</sub> (in constant 2005 US\$), a measure of market wealth, and *GDP growth*<sub>*jt-1*</sub> (% annual), an indicator of market expansion, to measure the economic attractiveness of the host country. Third, we included *inflation rate*<sub>*jt-1*</sub>, a sign of economic uncertainty in a potential location (Salacuse & Sullivan, 2005; Vaaler, 2008). Data for these variables were obtained from the World Bank WDI. We also included *policy uncertainty*<sub>*jt-1*</sub>, an indicator of the extent to which single political actors are unconstrained in their policy-changing intentions (Delios & Henisz, 2003a, 2003b; García-Canal & Guillén, 2008; Holburn & Zelner, 2010), which is measured with the “political constraints” indicator of the potential host countries, using data obtained from the POLCON V database (Henisz, 2002). Fourth, we added the variable *emerging country*<sub>*j*</sub>, an indicator of whether the potential host country is classified as an emerging country by the World Bank. Finally, we included the variable *prior investments in host country*<sub>*ajt*</sub>, which indicates whether a given firm had already invested in a given host country prior to the focal year. We measured this variable by assigning the value 0 to the first observed investment of a given firm in a given host country, and 1 for all subsequent potential investments decisions by the same firm in the same host country.

## **Econometric Approach**

We followed the literature and used conditional logit models (Alcacer & Chung, 2007; McFadden, 1974; Nachum, Zaheer, & Gross, 2008; Shaver & Flyer, 2000) to analyze the extent to which the existence of a BIT influenced the likelihood of a firm choosing a host country as a location for international investments. The conditional logit approach assumes that firms choose locations so as to maximize expected profit subject to some error. Expected profit is, in turn, determined by the host country attributes. Our unit of analysis is the firm-investment-year, so that each investment made by a firm in a given year is compared to all host country options that the firm could have chosen instead. The conditional logit model looks within this investment decision and uses variance across the potential choices in order to derive estimates. As such, it only makes it possible to include host country attributes as determinants of location choice, because it conditions out the investment (and firm) effects. In the results we present, we clustered standard errors by firm to recognize that investments made by the same firm may not be independent.

## Results

Table 1 presents descriptive statistics and correlations. There is substantial variance in our main variables of interest. A ratified *BIT* is present in 26.64% of the potential pairs of home and host countries. Other types of inter-governmental ties also exhibit substantial heterogeneity. For instance, the number of *interventionist IGO connections* between home and host country ranges from approximately 4 to 19, with an average of 8.34; 15.33% of the country pairs had a *military alliance* with one another; the level of *political affinity* varied from -0.48 to 1, with an average of 0.39. The variables measuring host country institutional characteristics also exhibit substantial variance: 11.79% of potential host countries have a military head of state; inflation ranges from 142.48% to -32.81%; population varies from 290 000 to 1.330 billion; 19.91% of the investments are made in emerging countries. Finally, firms with *political connections* account for 7.17% of the investment observations, a total of 358 observations. Investments by *very large* firms correspond to 34.50% of the observations. These investments are quite evenly distributed between home countries and years. Some of the independent and/or control variables are highly correlated. Unsurprisingly, countries tend to vote together in the UN if their economic situation is similar; bilateral trade, military alliances and interventionist IGO connections appear to follow similar patterns. Overall, variance inflation factors are all below 10, the accepted cutoff, with the average VIF at 1.82 and the maximum VIF at 4.15, suggesting multicollinearity is not a concern.

**Table 1: Descriptive statistics and correlations**

<b>Variable</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>	<b>12</b>	<b>13</b>	<b>14</b>	<b>15</b>	<b>16</b>	<b>17</b>	<b>18</b>	<b>19</b>	<b>20</b>	<b>21</b>	
1 Investment	1.00																					
2 BIT	0.01	1.00																				
3 Political connections	0.00	0.06	1.00																			
4 Very large firms	0.00	0.10	0.03	1.00																		
5 Geographic distance <sup>1</sup>	-0.03	-0.27	-0.09	-0.08	1.00																	
6 Common border	0.03	-0.05	0.00	0.04	-0.24	1.00																
7 Colonial ties	0.02	0.04	0.05	0.03	-0.10	0.03	1.00															
8 Common language	0.00	-0.07	0.02	0.03	-0.05	0.15	0.27	1.00														
9 Economic distance	-0.01	-0.05	-0.05	0.02	0.13	-0.03	-0.08	0.42	1.00													
10 Institutional distance	-0.03	0.11	0.01	0.04	0.07	-0.12	-0.02	0.01	0.13	1.00												
11 Interventionist IGO connections	0.05	-0.04	0.04	0.05	-0.35	0.35	0.08	0.11	-0.05	-0.48	1.00											
12 Home host military alliance	0.03	-0.10	0.01	0.05	-0.32	0.23	0.08	0.37	0.31	-0.21	0.55	1.00										
13 Bilateral trade	0.12	-0.06	-0.03	0.05	-0.20	0.24	0.12	0.21	0.13	-0.41	0.59	0.44	1.00									
14 Political affinity	-0.02	-0.02	0.01	-0.04	-0.15	0.06	-0.02	-0.44	-0.81	-0.24	0.18	-0.22	-0.16	1.00								
15 Military government	-0.02	0.01	0.00	0.00	0.04	-0.05	0.02	0.03	0.02	0.38	-0.19	-0.11	-0.18	-0.09	1.00							
16 Population <sup>2</sup>	0.19	0.04	0.00	0.00	-0.01	-0.01	0.01	0.01	-0.02	0.04	0.05	-0.01	0.28	-0.13	-0.02	1.00						
17 GDP per capita <sup>1</sup>	0.01	-0.22	0.00	0.00	-0.18	0.17	0.04	-0.04	-0.05	-0.56	0.54	0.30	0.46	0.17	-0.22	-0.10	1.00					
18 GDP growth	0.01	0.12	0.00	0.01	0.01	-0.07	-0.03	-0.04	0.04	0.20	-0.31	-0.16	-0.19	-0.04	0.06	0.12	-0.20	1.00				
19 Inflation	-0.02	0.02	0.00	0.00	0.07	-0.06	-0.04	-0.02	0.02	0.34	-0.23	-0.09	-0.18	-0.04	0.12	-0.03	-0.24	0.21	1.00			
20 Policy uncertainty	-0.01	0.06	0.00	0.00	0.13	-0.11	-0.04	0.00	0.04	0.61	-0.52	-0.25	-0.31	-0.22	0.32	0.05	-0.43	0.27	0.17	1.00		
21 Emerging country	0.08	0.14	0.00	0.00	0.02	0.01	-0.04	-0.03	-0.01	-0.11	0.08	0.01	0.26	-0.04	-0.02	0.34	-0.21	0.02	0.04	-0.12	1.00	
<b>Mean</b>	0.01	0.26	0.07	0.35	8.15	0.02	0.05	0.17	19.49	2.66	8.34	0.15	6.41	0.39	0.12	47.50	11.71	4.55	7.57	0.55	0.20	
<b>Std. Dev.</b>	0.09	0.44	0.26	0.48	3.97	0.13	0.21	0.37	20.48	2.39	2.31	0.36	2.47	0.39	0.32	157.00	16.01	4.67	9.98	0.30	0.40	
<b>Min</b>	0.00	0.00	0.00	0.00	0.17	0.00	0.00	0.00	0.00	0.00	3.67	0.00	-2.30	-0.48	0.00	0.29	0.12	-17.95	-32.81	0.11	0.00	
<b>Max</b>	1.00	1.00	1.00	1.00	19.71	1.00	1.00	1.00	66.06	12.99	19.33	1.00	12.85	1.00	1.00	1330.00	87.72	34.50	142.48	1.00	1.00	

N = 618,350.

<sup>1</sup> In thousands; <sup>2</sup> In millions.

Table 2 presents the conditional logit analyses. Model 1 contains only control variables. Model 2 introduces *BIT* to test hypothesis 1. Model 3 and Model 4 investigate the effect of BITs on politically-connected and nonpolitically-connected investing firms respectively, and are used to test hypothesis 2a. Similarly, Model 5 and Model 6 investigate the effect of BITs on very large and other investing firms respectively, and are used to test hypothesis 2b.

Model 2 confirms that the existence of a *BIT* between home and host country has a positive and significant effect on a firm's likelihood to choose a specific host country as the location for foreign investments ( $\beta=0.141$ ,  $p=0.004$ ). This result provides support for hypothesis 1. Regarding H2a, while the effect of a *BIT* between home and host country on the likelihood of host country choice is positive and significant in Model 4, i.e. for firms without political connections ( $\beta=0.133$ ,  $p=0.011$ ), the coefficient of *BIT* is not significant in Model 3, i.e. for politically-connected firms ( $\beta=0.170$ ,  $p=0.243$ ). Together, these results provide empirical support for hypothesis 2a. Finally, regarding H2b, the coefficient of *BIT* is positive and significant in Model 6, for all but the 10% largest investing firms ( $\beta=0.149$ ,  $p<0.016$ ), but not significant in Model 5, for very large firms ( $\beta=0.087$ ,  $p=0.262$ ). These results provide empirical support for hypothesis 2b.

We also found interesting patterns with regard to some control variables. Consistent with past research, *Geographic distance* and *institutional distance* have a consistently negative effect on a firm's likelihood to choose a specific host country. This confirms that firms prefer proximate locations in terms of both geography (Blonigen, 2005) and institutions (Cuervo-Cazurra & Genc, 2008; Holburn & Zelner, 2010) when choosing the location of international investments. Interestingly, *common border* and *common language* have a negative effect. We believe that these results may be specific to firms from the home countries in our sample, which

are mostly large and wealthy home countries. *Colony ties* and *economic distance*, on the other hand, positively influence location choice in most models. These results also make sense in light of previous literature. Firms prefer to invest in locations that share historical ties with their home country (Makino & Tsang, 2011). Because most firms in are data set originate in advanced countries, it is likely they are predominantly investing in less wealthy locations, notably to benefit from rapidly growing markets and lower costs of production (Blonigen, 2005). Regarding other measures of inter-governmental ties, *military alliance* has a consistently negative effect on the firm's choice of international investment location, after controlling for other forms of ties. These findings suggest that firms prefer not to mix business and military issues, avoiding investments in host countries with which these connections are stronger. These results contrast with analyses at the country level which have found a positive effect of military alliances on FDI exchange (Li & Vashchilko, 2010). Firms do, however, draw on trade relationships to choose the location of their investments, preferring countries with a higher level of *bilateral trade* with the home country, a finding that contributes to a better understanding of the effect of trade on FDI (Blonigen, 2005). As one would expect, *host country population* has an overall positive and significant effect on location choice. In contrast, *host country GDP per capita* has a consistently negative – though not significant in all models – effect. In line with this, we find that firms are more likely to invest in countries classified as *emerging*. Unsurprisingly, firms exhibit a preference for countries in which they have made a *prior investment*.

**Table 2: Conditional logit models: H1 and H2**

	(1)	(2)	(3)	(4)	(5)	(6)
	Controls	All firms	Politically-connected	Non-politically-connected	Very large	Other
<b>Distance</b>						
Geographic distance	-0.000 (0.000)	-0.000 (0.000)	-0.000 (0.007)	-0.000 (0.002)	-0.000 (0.742)	-0.000 (0.000)
Common border	-0.284 (0.000)	-0.281 (0.000)	-0.252 (0.463)	-0.288 (0.001)	-0.392 (0.001)	-0.176 (0.100)
Colony tie	0.378 (0.000)	0.372 (0.000)	0.364 (0.172)	0.388 (0.000)	0.451 (0.000)	0.344 (0.000)
Common language	-0.223 (0.000)	-0.219 (0.000)	-0.175 (0.382)	-0.212 (0.000)	-0.129 (0.109)	-0.299 (0.000)
Economic distance	0.020 (0.000)	0.020 (0.000)	0.016 (0.130)	0.021 (0.000)	0.010 (0.060)	0.025 (0.000)
Institutional distance	-0.151 (0.000)	-0.150 (0.000)	-0.086 (0.138)	-0.155 (0.000)	-0.028 (0.348)	-0.229 (0.000)
<b>Home-host country ties and affinity</b>						
Interventionist IGO connections	-0.044 (0.006)	-0.038 (0.019)	-0.104 (0.045)	-0.032 (0.057)	0.032 (0.234)	-0.074 (0.000)
Military alliance	-0.167 (0.005)	-0.179 (0.003)	-0.403 (0.043)	-0.161 (0.009)	-0.292 (0.003)	-0.097 (0.193)
Bilateral trade	0.577 (0.000)	0.584 (0.000)	0.545 (0.000)	0.588 (0.000)	0.465 (0.000)	0.638 (0.000)
Political affinity	0.059 (0.574)	0.026 (0.803)	0.617 (0.030)	0.012 (0.917)	-0.205 (0.286)	0.107 (0.392)
<b>Host country attractiveness</b>						
Military government	0.021 (0.793)	0.027 (0.730)	-0.235 (0.496)	0.050 (0.538)	-0.173 (0.168)	0.169 (0.103)
Population	0.000 (0.000)	0.000 (0.000)	0.000 (0.042)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
GDP per capita	-0.000 (0.000)	-0.000 (0.000)	-0.000 (0.432)	-0.000 (0.000)	-0.000 (0.423)	-0.000 (0.000)
GDP growth	-0.001 (0.844)	-0.003 (0.661)	0.023 (0.199)	-0.005 (0.416)	0.025 (0.014)	-0.023 (0.001)
Inflation	0.001 (0.728)	0.001 (0.755)	0.010 (0.008)	-0.001 (0.772)	0.008 (0.011)	-0.010 (0.026)
Policy uncertainty	-0.318 (0.000)	-0.322 (0.000)	-0.208 (0.426)	-0.310 (0.001)	-0.650 (0.000)	-0.165 (0.130)
Emerging country	0.590 (0.000)	0.580 (0.000)	0.774 (0.000)	0.564 (0.000)	0.553 (0.000)	0.589 (0.000)
Prior investments in host country	1.335 (0.000)	1.329 (0.000)	1.338 (0.000)	1.316 (0.000)	1.383 (0.000)	1.347 (0.000)
<b>Independent variable</b>						
BIT		0.141 (0.004)	0.170 (0.243)	0.133 (0.011)	0.087 (0.262)	0.149 (0.016)
N observations	618,350	618,350	44,325	574,025	213,341	405,009
N firms	1,073	1073	31	1042	93	1018
R-squared	0.285	0.286	0.226	0.292	0.224	0.327

P-values based on standard errors clustered by investing firm in parentheses.



## **Robustness Tests**

In order to evaluate the robustness of our findings, we carried out additional analyses. First, we tested the robustness of the measure of political connections. Because we used a list of politically-connected firms that was collected before the entire period of study, we also ran the analysis only considering those investments made between 2003 and 2005, a period which immediately follows the observation of the firms' links to their home country political authorities (Faccio, 2006). The main results remained unchanged, and, in particular, the presence of a BIT only influenced the choice of firms without political connections.

Second, we analyzed whether the effect of *BIT* varies depending on the predominance of distinct types of political engagement in distinct host countries. More specifically, firms in the United States may use other ways to connect with political authorities in the US, such as political donations and lobbying, whereas our measure of political connections might be more in line with political engagement in the other six home countries. To check for this, we split our sample into two subsamples: (i) investments by firms originating in the US, and (ii) investments by firms originating in the other six home countries. Results do not reveal any particular differences between these two subsamples and our findings remain substantially the same.

Third, we investigated the robustness of our findings to different definitions of host country choice sets. In our main models, we considered that a firm could have chosen any of the 124 countries on which we collected data as the location for an international investment. Such an assumption rarely corresponds to the actual choices a firm may consider for its international investments, which is probably more restrictive regarding the number of considered countries. To evaluate whether our use of 124 alternative choices impacts our findings, we also performed our analyses on two alternative definitions of choice sets. First, we only considered countries that

received at least one investment during our period of analysis rather than all countries on which we had data. This reduced the number of choices to 116. Second, for a given year we only considered countries that received at least one investment by a firm in our sample in that given year. This reduced the number of choices to between 60 and 69 depending on the year. Aligned with our expectations, given the assumption of independence of irrelevant alternatives (IIA) which underlies conditional logit analyses, all our results remained consistent across these alternative definitions of the choice sets.

While our statistical approach does not make it possible for us to explicitly control for endogeneity, we are confident our research design and some of our results mitigate such a concern. In past research examining the effect of BITs on FDI, the endogeneity concern was much more salient because bilateral FDI levels could credibly be speculated to influence governments' decisions to consolidate bilateral economic relations by providing a better protection to investors and thus setting up a BIT. In our study, it seems difficult to consider that an individual firm investing in a foreign country has enough influence to drive governments' decisions to enter a BIT. Additionally, were this the case, we would expect politically-connected and very large firms to be better able to achieve such an outcome. Indeed, our results show that foreign investment by politically-connected and very large firms are less associated with BITs than investments by other firms.

## Discussion and Conclusion

Consistent with prior research (Duanmu, 2014; Henisz, 2000; Holburn and Zelner, 2010; Kobrin, 1979; Ramamurti, 2001; Rodrik, 1991), we confirm that firms are concerned with risks stemming from nation-state sovereignty when investing abroad. More specifically, such sovereignty makes foreign investments vulnerable to policy changes that may be detrimental to foreign investors' interests, which in extreme cases can be manifest by outright expropriation. Within this broad context, Bilateral Investment Treaties appear to have a substantial impact on many firms' international investment location choices. These treaties aim to produce credible commitments that the host country will not interfere on investments made in its territory by firms from signatory countries. In line with our hypotheses – and while controlling for traditional determinants of foreign investment location choice – we indeed find that BITs have a significant influence in attracting foreign investments. By focusing on greenfield investments in manufacturing industries, our study is not marred by location choice constraints associated with the presence of natural resources or the availability of acquisition targets or joint venture partners in potential host countries.

Our results on the effect of firms' political influence suggest that firms with political connections in their home country or firms with enough clout do not rely as much on their home country's treaties with foreign countries when choosing the location of their international investments. These firms appear confident that they can protect their investments by acting in the political market, either by convincing their home country authorities to espouse their claims and bear the costs of dispute settlement or by deterring the implementation of detrimental actions by host governments. These firms are, therefore, able to invest in locations their competitors lacking such political influence tend to avoid, and could face lower levels of competition.

Our findings also suggest that institutions such as BITs can ‘democratize’ foreign investments. We show that smaller and non-politically connected firms are especially sensitive to the existence of these treaties. Therefore, BITs provide more equal footing between small or non-connected firms on the one hand and large or politically-connected firms on the other, when it comes to making foreign investments. We believe these insights are important contributions to the literature on corporate political strategies.

At first sight, one might find it intriguing that politically influential firms do not take advantage of existing BITs. Arguably, they could do so like any other firm, but they prefer instead to make an unconstrained choice of location, which may include both well-connected countries and less well-connected countries, where they enjoy competitive advantage and bet on their ability to obtain their home country’s assistance, should it be necessary. Although prior work suggests that FDI flows might drive the establishment of BITs between two countries, rather than the opposite, our results show that those firms most able to coerce the home and host governments into signing a BIT to protect their foreign investments actually appear not to be doing so, possibly to avoid attracting further competition into the host country.

Our results regarding firm size provide additional insights on how political influence is exercised and how it can affect foreign investment decisions. Contrary to political connections in the home country that lead a firm to exercise its influence primarily through its home country political authorities, firm size is highly visible by government authorities, both in the home and in the host country. This in turn allows very large firms to exercise their influence on the host country government both directly, and also indirectly through their home country authorities.

Our study has several limitations. First, our measure of political connections captures the existence of such connections towards the beginning of the period during which we observe foreign investment decisions. As a result, some of the political ties we take into account may have faded away over time. We run complementary analyses to deal with this issue, as described in the robustness tests section, and obtain similar results as in the main analysis. Furthermore, with our study potentially overestimating such political connections, our analysis provides a conservative test of our hypothesis 2a. Another limitation of our study is that the econometric approach we use does not make it possible for us to completely rule out the possibility that BITs are endogenous to foreign investments by specific firms. We believe, however, that our research design and our findings that politically influential firms do not rely on BITs when choosing the location of their foreign investments, alleviate such concerns. Finally, as we use conditional logit models, we cannot estimate the direct effect of firm attributes independent from a given host country on their foreign investment location choices.

We make three main contributions to the literature. First, we contribute to the stream of research on the effects of inter-governmental ties on FDI flows (Alcacer and Ingram, 2013; Kerner, 2009; Li and Vashchilko, 2010; Salacuse and Sullivan, 2005; Yackee, 2008), by analyzing firm-level data and focusing on BITs. We show that it is important that the ties between countries are strong enough to establish a credible commitment by the host country that it will not detrimentally interfere on investments on its territory made by firms from the partnering home country. Second, we contribute to the literature on international investment location choice, showing that some firms are able to leverage political resources (i.e., political influence) in order to overcome liabilities of foreignness (Hymer, 1976; Zaheer, 1995) and reduce the risks inherent in international business. We also advance the line of research that

focuses on the home country as a resource (Cuervo-Cazurra and Genc, 2008; Delios and Henisz, 2003a, 2003b; Wan and Hoskisson, 2003), by showing that some firms are better than others to get their home country authorities to act in their favor. In highlighting such firm heterogeneity, our study can help explain some of the equivocal results in the literature: namely, samples more heavily weighted to one type of firm or another could produce significantly different results. Third, we contribute to the literature on firm political strategies (Boubakri *et al.*, 2013; Chen *et al.*, 2010; Faccio, 2006; Faccio *et al.*, 2006; Leuz and Oberholzer-Gee, 2006), by showing that politically influential firms are able to choose from a broader set of potential host countries when investing abroad, thus improving the performance potential of their international investments.

Overall, we believe our study contributes to a better understanding of the impact of non-market strategies in international business. Our results show that, while supranational institutions are instrumental in fostering international investments, firms also take their political influence with their home country government into account when choosing the location of their foreign investments and suggest that their direct influence on host country authorities may also be an important factor in their decision. Future research could further examine this question and disentangle the impact of political influence in the home and host country respectively on a firm's decision to invest in one country or another.

**CHAPTER 4: A French Connection: The Influence of Political Connections on  
International Expansion Strategy**

## **Abstract**

We examine whether and how a firm's connections with political authorities in its home country influence its international expansion strategy. We argue that political connections are associated with a firm's ability to obtain better information regarding the home country's policies, to influence the home country's government and to obtain lower-cost capital for investments. Accordingly, we propose that political connections influence a firm's international expansion strategy. Analyzing international investments made by France's largest firms from 2003 to 2012, we find support for our predictions and obtain additional insights on the influence of political connections on firms' international expansion strategy. Distinct types of political connections seem to operate through different mechanisms in influencing the amount and the level of expropriation risk of a firm's overseas investments. Interestingly firms holding friendship ties with Nicolas Sarkozy, president of France between 2007 and 2012, invest significantly more internationally after his election. This result suggests that the effect of political connections is further influenced by contextual changes that alter the value of certain political connections.

**Keywords:** international expansion; political connections; French firms; political risk.



## Introduction

Political and institutional factors are critical for firms' international expansion strategy. Recent studies suggest that firms are distinct in their attitudes toward host country expropriation risk (Delios & Henisz, 2003a, 2003b; García-Canal & Guillén, 2008) and prefer to invest in countries with a similar political environment to the home country's (Cuervo-Cazurra & Genc, 2008; Holburn & Zelner, 2010). Yet, there is a dearth of research on the political foundations of firm international expansion strategy, particularly regarding a firm's ties with political authorities in its home country. Meanwhile, extant research on political connections has predominantly emphasized their direct effect on a firm value and performance (Amore & Bennedsen, 2013; Faccio, 2006; Goldman et al., 2009; Hillman, 2005) with limited documentation of the role of political connections as antecedents of firm strategy (Siegel, 2007; Zhu & Chung, 2014). Furthermore, little attention is paid to the potentially heterogeneous effects of different types of political connections on both firm value and strategy (Chung et al., 2007; Hadani & Schuler, 2013). In contrast, we provide arguments and empirical evidence for the role of different types of political connections as drivers of firms' international expansion strategy.

We broadly define political connections as various kinds of relationships between a firm and political authorities in its home country. Specifically, we consider political connections stemming from a firm's top decision makers having prior professional experience in the government (Bertrand et al., 2006; Kramarz & Thesmar, 2013; Lester et al., 2008), from a common educational background (Bertrand et al., 2006; Siegel, 2007) or from friendship ties (Coulomb & Sangnier, 2014; Fisman, 2001) between a firm's top decision makers and top government authorities. We conceptualize international expansion strategy as the patterns of

change in a firm's international presence, which are generated by the firm's international investments and divestments in a given period of time.

We examine how these different types of political connections influence two dimensions of a given firm's international expansion strategy: (i) the amount, and (ii) the level of expropriation risk exposure of the firm's international investments in a given period of time. We argue that, with globalization and competition from foreign firms, international expansion becomes crucial for firms to achieve competitive advantage. In such an environment, politically-connected firms will not only expand internationally, but they will use their political connections to better do so (Bonardi, 2004; García-Canal & Guillén, 2008). We propose three ways through which political connections positively impact a firm's international expansion strategy. First, firms with political connections know how to deal with governments, and political connections enable social interactions between business and government leaders in which politically-connected firms receive enhanced information about the home country's foreign policy and international interests. Second, political connections affect a firm's actual and perceived ability to influence the home country government to act on its behalf to protect its assets (Baron & Hall, 2003; Bonardi, 2011). Third, political connections enable firms to secure investment funds at lower capital costs through privileged access to various funding sources and higher market valuation (Boubakri et al., 2012; Claessens et al., 2008; Faccio et al., 2006).

Furthermore, we submit that the value for firms of friendship-based political connections is contingent on the political regime prevailing in the home country. These political connections will be more valuable when the firm's top decision makers have friends that enjoy more power in the home country's government. We, therefore, propose that changes within the political environment in the home country that alter the value of regime-specific political connections

moderate the balance between government and firm interests, thus also influencing firms' international expansion strategy. An increase in the value of those connections will intensify their influence on a firm's international expansion strategy.

We use data on the international investments of 103 of the largest firms listed on the French stock exchange during the period between 2003 and 2012 to empirically test these hypotheses. We find empirical support for our main predictions. Politically-connected firms engage in distinct international expansion strategies relative to non-politically-connected firms. We also find that this heterogeneity is contingent on the type of political connections, with political connections based on friendship ties and on common educational background being the most meaningful ones in explaining the amount and the level of expropriation risk exposure of a firm's international investments, respectively. Finally, we find that the election of Nicolas Sarkozy as the president of France generated significant effects on the strategy of firms connected to him through friendship ties. Specifically, firms with friendship ties with Sarkozy invested significantly more internationally after the 2007 election.

## **Theory and Hypotheses**

Prior research on political connections and corporate political activities shows that firms differ substantially in their political engagement (Faccio, 2006; Fisman, 2001; Hillman et al., 2004) and in the extent of their capabilities to achieve their goals vis-à-vis the government (Baron & Hall, 2003; Bonardi, 2011; Bonardi et al., 2006). Political engagement and capabilities may also be associated with heterogeneity in strategic choice. In effect, a few recent studies have started to document the influence of political connections on several firm strategies, such as financing (Leuz & Oberholzer-Gee, 2006), industry diversification (Chung et al., 2007; Zhu & Chung, 2014) and risk-taking (Boubakri et al., 2013).

This stream of research, however, devotes little attention to the fact that different types of political connections operate through different channels and may influence firm value and strategy through distinct mechanisms. We focus on direct or relational political connections, i.e. direct personal relationships between business and government leaders (Hillman & Hitt, 1999), because other political connections, indirect or transactional in nature, such as campaign donations and lobbying, might be less effective in generating political capabilities (Bonardi, 2011). Prior literature shows the relevance of several types of such relational political connections, of which three types provide particularly interesting contrast: (1) government experience, (2) common educational background and (3) friendship. The first two types operate independently of the regime in power and the third one is regime-specific.

Political connections based on government experience are created when a firm's top decision makers have worked in politics or as top government officials prior to their business career, in which case they likely keep contacts in the government and have acquired capabilities related to understanding how the government operates (Bertrand et al., 2006; Boddewyn, 1988;

Kramarz & Thesmar, 2013; Lester et al., 2008). Political connections based on common educational background are established when firm and government leaders share the same educational background and know each other from studying together at the same school or from belonging to a relevant and active alumni network (Kramarz & Thesmar, 2013; Siegel, 2007). Political connections based on friendship are created when a firm's top decision have personal friends at high-level positions in the government (Amore & Bennedsen, 2013; Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001).

Typically, firms with political connections in their home country might have an interest to focus their operations domestically in order to maximize the benefits from their special relationships with political authorities there. In recent years, however, firms face globalization and international competitive forces that encourage international expansion (Bonardi, 2004; García-Canal & Guillén, 2008). In addition, most large firms from developed and many firms from emerging countries are already operating internationally. We argue that, in such an environment, firms with political connections not only expand internationally, but they use their political connections to do so more freely.

### **Political Connections and Firms' International Investments**

Drawing from the literature on political markets and corporate political activities (Bonardi, Hillman, & Keim, 2005; Bonardi et al., 2005; Hillman et al., 2004), and particularly from the international non-market and political strategy (Boddeyn, 1988; Boddeyn & Brewer, 1994; Bonardi, 2004; Holburn & Zelner, 2010), we put forward three mechanisms through which political connections may impact firms' international expansion strategy: (1) information access and knowledge, (2) influence and (3) capital costs.

The *information access and knowledge* mechanism purports that politically-connected firms receive benefits, including more and better information, from the home country government and understand how governments work. First, we argue that, analogously to state-owned companies and firms operating in regulated industries (García-Canal & Guillén, 2008; Holburn & Zelner, 2010), politically-connected firms have political capabilities of understanding how governments operate. Politically-connected firms develop such capabilities through their experience dealing with government officials and politicians domestically. Second, we argue that political connections help firms obtain particularly distinctive information concerning the home country government's foreign policy and international interests, which may be useful for their international investment decisions. Furthermore, firms with political connections are arguably better equipped to understand such information and interpret political events and trends that may affect their activities. Finally, firms may also purposefully use their political connections to obtain information, for instance, by developing political intelligence and corporate diplomacy capabilities (Boddeyn, 1988; Boddeyn & Brewer, 1994; Jerke, 2010; Macnamara, 2012).

The *influence* mechanism is related to the literature suggesting that firms act in political markets and develop political capabilities to promote their interests to and achieve their objectives from the government (Baron & Hall, 2003; Bonardi, 2011; Bonardi et al., 2006). We argue that firms with political connections are more confident in their ability to influence the home country government actions to provide protection for their assets abroad, should it be necessary. First, due to their political capabilities, politically-connected firms may more confidently pursue good deals with a host country's political authorities. Second, since they are typically more successful in political markets, firms with political connections attend to and

interpret opportunities and risks in a different way, weighing difficulties intrinsic to doing business overseas less strongly.

Finally, the reduced *capital cost* mechanism implies that politically-connected firms can obtain capital for investments with a lower cost than firms without political connections (Boubakri et al., 2012). First, firms with political connections may have a facilitated access to funds tied to governmental sources, such as government-owned banks (Claessens et al., 2008; Inoue, Lazzarini, & Musacchio, 2013). Second, there is some evidence that the market assigns a positive value to political connections (Coulomb & Sangnier, 2014; Faccio et al., 2006; Goldman et al., 2009; Hillman, 2005). Accordingly, politically-connected firms should be able to obtain better funding to make investments, which, in turn, increases their openness to strategic experimentation.

These three mechanisms imply that firms with political connections face less uncertainty in making international investments than firms without political connections. Given the competitive pressures to internationalize (Bonardi, 2004), and that internationalization may itself be a source of competitive advantage (Hitt, Hoskisson, & Kim, 1997; Shaver, 2011), we propose that firms take advantage of their political connections to expand their international presence. These firms use political connections as a resource that helps them mitigate liabilities of foreignness (Hymer, 1976; Zaheer, 1995) and enables them to obtain value from internationalizing (Buckley, 1976; Morck & Yeung, 1992). In summary, political connections help firms obtain better information on potential locations to invest, to more successfully understand and deal with foreign governments, to influence the home country government to act on their behalf in case of need, and to obtain cheaper funding for investments. Accordingly, we propose that:

*Hypothesis 1: Firms with political connections invest more internationally than firms without political connections.*

### **Political Connections and Host Country Expropriation Risk**

Due to the *information access and knowledge* mechanism, the types of countries where firms with political connections choose to make most of their international investments could differ from those chosen by other firms. Following the arguments developed in the previous section, firms whose top decisions makers have prior professional experience in the home country government, share a common educational background or have friendship ties with top political authorities are likely to enjoy information advantages relative to other firms. These may include information on best investments opportunities in foreign countries as well as insights on countries that are more politically and economically aligned with the home country and where, therefore, an intervention of the home country government to protect the firm's interest would be more effective.

A first reason underlying the ability to obtain such advantages is that firm decision makers who have worked for the government prior to their business career understand how the government operates. They may also be better able to predict changes in the political environment in the places where they locate their investments. These arguments are consistent with the idea that firms from regulated industries develop better capabilities for dealing with governments (García-Canal & Guillén, 2008). They are also consistent with the idea that firms develop political capabilities simply as a result of being from a more politically-contentious country-of-origin (Holburn & Zelner, 2010), although we advance this idea by focusing on how political connections distinguish firms from the same home country in terms of their political capabilities.



A second reason is that firm top decision makers who have a common background or friendship ties with political authorities in the home country can obtain information through social interactions with the latter individuals. Such decision makers enjoy direct or indirect personal ties with current political authorities who have direct access to relevant information. Furthermore, through continuous social interactions with government leaders, firms develop political capabilities (García-Canal & Guillén, 2008; Holburn & Zelner, 2010) that might enable them to can extract more relevant information even from casual conversations with such individuals. Therefore, politically-connected firms, due to the information access and knowledge mechanism, will be less sensitive to host country institutional and political risk.

The other two mechanisms, *influence* and *capital cost*, may also impact the type of countries where firms choose to concentrate their international investments. Due to the influence mechanism, firms with political connections may tolerate or seek greater risk in their international expansion strategy. If a firm has political connections with top political authorities, the protection and privileges it receives from those authorities create an environment of less uncertainty in the home country. These firms can also rely on obtaining capital at lower costs, even for investments in riskier locations. Indeed, prior research has shown that politically-connected firms rely less strongly on international sources of funding (Leuz & Oberholzer-Gee, 2006) and obtain better access to loans from governmental banks (Claessens et al., 2008) than non-politically-connected firms.

As a result, firms with political connections are at more liberty to engage in risky strategy outside the home country than firms without political connections. For example, firms with political connections may perceive weak formal protection of property rights or pervasive corruption in the host country as less of a threat to their business prospects than firms without

ties to political authorities in the home country. As a matter of fact, prior evidence suggests that firms in regulated industries invest more in countries with high political risk, where they feel better able to deploy their political capabilities regarding how to interact with government officials and get better investment agreements (García-Canal & Guillén, 2008). Analogously, political connections also imply that the firm has a capability to deal with political authorities to achieve their goals, and, thus, a higher tolerance to risk than firms without political connections. I, hence, propose that:

*Hypothesis 2: Firms with political connections invest relatively more in host countries characterized by greater expropriation risk than firms without political connections.*

### **The Effect of a Favorable Political Change**

Thus far, we have described the general effects of political connections on firms' international strategy. However, the three types of political connections examined in this paper – government experience, common educational background and friendship – are distinct in terms of their specificity to the person in power in the home country's government. Government experience and common education political connections are sources of general skills and give access to broad networks that, on average, may not necessarily depend on political cycles. This is particularly so in countries with a well-developed civil service system that is not largely affected by changes in political power. Indeed, as we described before, government experience refers to the development of capabilities of understanding how the government operates and interpreting signs of change. Such capabilities are developed regardless of an individual's party affiliation. Similarly, common education political connections indicate that firm decision makers

belong to a broad network of individuals who may share information and favors through their social interactions, despite being affiliated to distinct parties.

The effect of friendship political connections, on the other hand, is more specific to whom exactly the firm is connected to and how much political power that individual holds in the home country's government. Hence, changes in the political environment, such as a friend of one of the firm's top decision makers being elected president in the home country, may affect the relationship between friendship political connections and international expansion strategy.

As firms with political connections are more likely to take political factors into account in their decisions, they may also respond more strongly to changes in the political environment, particularly if such changes alter the value of their political connections (Cho & Hambrick, 2006; Siegel, 2007). When one of the firm's top decision makers has a friend competing for a top position in the home country's government, that friendship tie implies a more positive prior attitude to the eventual change in the political environment, leading the firm to focus on the opportunities it presents (Barreto & Patient, 2013). That is, a potential favorable change in the political environment in the home country leads to a broader set of opportunities and strategic choices for firms with friendship political connections. These opportunities may be seized through an increase in the firm's international investments and set of potential locations for investments, which may include countries previously avoided due to high risk of expropriation.

Consistently, prior research suggests that firms with political connections in the home country obtain first-mover advantages in international business (Frynas et al., 2006) and that political connections allow firms to take more risk in their investment decisions (Boubakri et al., 2013; Chen et al., 2010). These effects are likely to be more pronounced when the political connection is based on social relationships that entail obligations of favor exchange and

reciprocation, such as friendship ties (Blau, 1964), and when the politician to whom the firm is connected is in a sufficiently high power position. Although political connections already imply a stronger likelihood of protection from the home country government through the influence mechanism, firms will be even more confident that they will successfully obtain this protection if the politician to whom they are connected occupies a relatively stronger political position.

We, thus, predict two effects of an increase in value of a firm's friendship political connections. First, the friendship tie will enable the firm to anticipate success in convincing political authorities to use their power vis-à-vis foreign governments, should it be necessary. Second, the friendship tie will also enable the firm to expect the home country government to more effectively shield the firm against potential detrimental actions from host countries. Firms with these friendship ties will respond even less stringently to the lack of investment protection, or to other features of a detrimental institutional environment in the host country, than before the political change. Hence, we propose that:

*Hypothesis 3: After a favorable political change, the effect of friendship political connections on a firm's international investments is strengthened.*

*Hypothesis 4: After a favorable political change, the effect of friendship political connections on a firm's investments in host countries characterized by greater expropriation risk is strengthened.*

## **Data and Methods**

### **Business-Government Relationships in France**

The business environment in France has traditionally been characterized by strong relationships between firms and the government (Kadushin, 1995; Schmidt, 1996), a feature related to France's patterns of elite education and business careers (Kramarz & Thesmar, 2013). These patterns of education and professional careers create an environment in which business and political leaders are likely to know each other personally. This promotes the alignment of business and government actors' mindsets and interests, and may also create an environment conducive to exchanging information and favors.

The system of higher education in France comprises public universities, which are almost free of charge and have thousands of students, and a few highly competitive and selective specialized schools, including Ecole Polytechnique, HEC Paris and ENA. These latter schools accept only a limited number of students, with a prevalence of members of the nation's elite, most of which are successful in obtaining high-level positions in the French government and private sector upon graduation. Given such an educational system, it is reasonable to expect a prevalence of social ties between individuals in power positions both in business and in the government. Indeed, ENA, a school with an annual intake of about 100 students, has been traditionally responsible for educating the highest-level government officials in France. More recently, an increasing number of the school's graduates are switching to the private sector, typically starting at top positions in major firms. While the demand for ENA graduates in top positions at firms is diminishing, they still represent a high proportion of the current CEOs and board directors among the largest French firms (Kramarz & Thesmar, 2013; Schmidt, 1996).

With respect to the patterns of executive careers in France, some evidence suggests that having experience working at high-level government jobs is beneficial for career advancement in the private sector. According to Kramarz and Thesmar (2013), in the 1990s, CEOs who were former government officials controlled the majority of the assets listed on the French stock market. This type of trajectory is still common among current CEOs and board members, as we will show in the data description section.

Moreover, during the 2000s, France witnessed important political changes. Nicolas Sarkozy, the president in office from 2007 to 2012, had a particularly business-oriented approach and numerous personal friends in decision making positions at top firms (Chemin & Perrignon, 2007; Coulomb & Sangnier, 2014; Dély & Hassoux, 2008). Studying friendship ties between Sarkozy and top business leaders allows us to evaluate the effects of a change in the value of these ties on a firm's international expansion strategy. As Sarkozy was already a top politician prior to being elected president, his friendship ties with top leaders in firms should affect those firms' international investments even before his rise to power. After his election, which we treat as a favorable political change for firms holding friendship ties with him, the value of these ties increases, thus affecting international expansion strategy. Furthermore, prior research uncovers a positive relationship between having friendship ties with Sarkozy and a firm's value after his election (Coulomb & Sangnier, 2014).

### **Setting and Sample**

Accordingly, French firms are an ideal context to examine the hypotheses raised in the previous section. Our setting comprises firms in the SBF120, an index of the 120 most actively-traded firms in the French stock exchange. After excluding banks, due to difficult comparability of financial and accounting data, and firms with systematic missing data, the final sample

comprised 103 firms, for which we used annual data from 2003 to 2012. The sample is, thus, an unbalanced panel of 103 firms over 10 years, comprising a total of 990 observations.

This setting is appropriate for this study for many reasons. First, the largest French firms have global interests and make substantial international investments during the analyzed period. Furthermore, while French firms are among the largest firms in the world, and despite their strong international presence, prior research has not given enough attention to their international strategy. Second, in France, most individuals holding ties with political authorities are associated with the largest firms. Third, political connections are quite widespread and heterogeneous in French firms. Analyzing these firms allowed us to compare the effect of all three types of political connections on firms' international expansion strategy. Fourth, since changes are rare within the firms' leadership and the friendship ties we identified between firm leaders and Nicolas Sarkozy date further back in time than 2003, these relationships are arguably exogenous to firms' international expansion strategy during the period we analyzed. Finally, the analyzed period allowed us to compare the effect of the political connections based on firms' friendship ties with Nicolas Sarkozy before and during his tenure as the president of France.

### **Dependent Variables**

We measured international expansion strategy based on two components of a firm's international investments: amount and level of exposure to expropriation risk. The variable *FDI amount* measures the net amount of foreign direct investments a firm makes in a given year. It is equal to the sum of total investments in greenfield projects and total investments in acquisitions minus total value of divestments. Data on greenfield investments, comprising 3949 specific investments, were obtained from the Financial Times *fDiMarkets*, a database that tracks firm-level greenfield investments around the globe (see Burger et al., 2013; Duanmu, 2014, for

examples of empirical studies using this data). Data on acquisitions (692 in total) were obtained from Thomson Reuters *SDC Platinum*, a database widely used in M&A research (see Capron & Guillén, 2009; Capron & Shen, 2007). In line with usual definition of FDI, we considered an acquisition investment when one of the firms in the sample acquired more than 10% of the shares of a foreign firm. Data on divestments (922 in total) were also collected from *SDC Platinum*. We considered a divestiture when a firm in the sample was the parent of a target firm in an acquisition and retained less than 10% of the target's shares after the deal. All amounts are in millions of 2005 US dollars. This variable is used to test hypothesis 1 and hypothesis 3.

The variable *FDI riskiness* measures the level of expropriation risk associated with a firm's FDI in a given year. We calculated this variable in three steps. First, we weighted each investment a firm made in foreign countries in a given year by multiplying the amount invested by the host country level of expropriation risk. Host country expropriation risk was measured with an indicator of weakness of property rights (Duanmu, 2014), extracted from the Heritage Foundation Economic Freedom indicators (Kane, Holmes, & O'Grady, 2007). Second, we aggregated the weighted investment amounts at the firm-year level. Third, we divided that figure by the firm's total investments in that year. We, therefore, obtained a measure that varies from 0 to 1, with higher values indicating a greater concentration of investments in countries characterized by higher expropriation risk. This variable was used to test hypothesis 2 and hypothesis 4.

### **Independent Variables**

We used six measures to assess a firm's political connections (PC), two for each type of political connection, depending on whether the channel of the connection was the firm's board of directors or the firm's CEO (see Amore & Bennedsen, 2013; and Goldman et al., 2009 for a



similar approach). The first two variables refer to government experience political connections: (1) *Board government experience PC* is the proportion of board directors who have worked for the government as top officials. We calculated this variable by dividing the number of directors with government experience in a given firm in a given year by the firm's board size. (2) *CEO government experience PC* is an indicator variable that equals 1 if the CEO has worked as a top government official, and zero otherwise. We assumed that prior experience in the government helps individuals to develop capabilities with respect to understanding how the government and the public policy process operate. As in previous research using similar measurements, we only considered top positions in the French government, such as minister assistant, president advisor and high-level executive functions in ministries (Bertrand et al., 2006; Kramarz & Thesmar, 2013). We relied on information contained on each CEO and directors' biographies in the firms' annual reports to code this variable. When biographies were not available in the annual report, we used alternative sources, such as company websites, Who's who in France, Business Week Executive biographies and news articles.

The second pair of variables refers to common educational background political connections: (3) *Board common education PC* is the proportion of board directors who are ENA graduates in a firm's board in a given year. We calculated this variable analogously to *board government experience PC*, but using information on the directors' educational background. (4) *CEO education background PC* is an indicator variable that equals 1 if the CEO graduated from ENA, and zero otherwise. Following prior research, we assumed that ENA graduates share a common educational background with individuals in high-level political and governmental positions (Bertrand et al., 2006; Kramarz & Thesmar, 2013). We coded whether CEOs or directors are ENA graduates in two steps. First, we relied on the biographies of CEOs and

directors available at each firm's annual report, identifying individuals whose educational background included ENA. Then, we checked each CEO and director on the ENA's Graduates Yearbook.

The third group of variables assesses friendship political connections: (5) *Board Sarkozy friendship PC* is the proportion of board directors who are personal friends of Nicolas Sarkozy. (6) *CEO Sarkozy friendship PC* is an indicator variable that equals 1 if the CEO is one of Sarkozy's personal friends, and zero otherwise. We draw on Coulomb and Sangnier (2014) and followed similar procedures to construct these variables. First, we used a list of businessmen reported as personal friends of Sarkozy in biographical books (Chemin and Perrignon, 2007; Dély and Hassoux, 2008; Hamel, 2011; Pinçon and Pinçon-Charlot, 2010). The books and popular press have extensive coverage of some of these relationships. Also, most of the individuals on the list were invited by Sarkozy and his then-wife for a dinner on the day of the election in 2007 and before Sarkozy even addressed the French population. More importantly, most of the friendship ties were formed long before 2003. Finally, prior research has shown that the presence of these individuals among owners and top managers of French firms led to a 3% increase of the firms' value after Sarkozy's election (Coulomb & Sangnier, 2014). It is important to note that Sarkozy was already in a top political position before being elected president of France; so, while a friendship political connection was already in place, such connection became more valuable for firms with Sarkozy's election in 2007.

### **Control Variables**

We included several control variables that could influence a firm's international expansion strategy and their relationship with political connections. First, we controlled for *firm size*, as larger firms may also be more inclined and have more resources to invest abroad, even in

riskier countries. Larger firms are also more likely to have political connections (Hillman et al., 2004). We measured firm size with the natural logarithm of a firm's total assets in a given year. Second, we controlled for the *firm total investments*, since these may also include international investments. We measured total investments with the firm's capital expenditures in a given year. Third, we controlled for *firm performance*. On the one hand, more profitable firms have more resources to invest, even in less familiar or riskier locations. On the other hand, high profitability may also create inertia and the tendency to keep investing in more familiar locations. We measured firm profitability with the firm's return on assets (ROA) in a given year. Fourth, we controlled for two types of firm intangible resources, as it has been shown that such resources influence a firm's international expansion decisions (Buckley, 1976; Morck & Yeung, 1992). The first one is the total *R&D expenses* of a firm in a given year, and the second one is *firm innovation*, the number of patents a firm produced in a given year, both proxies of the firm's technological capabilities. Fifth, we controlled for *firm debt*, because firms with more debt may face additional hurdles in obtaining funds to invest abroad. Also, this variable may affect politically-connected firms less strongly than other firms. Finally, we controlled for *firm multinationality*, measured as the number of countries in which a firm had operations in a given year. Firms with a higher level of multinationality are likely to invest more internationally and to respond differently to host country risk and political alignment due to prior international experience. In addition to these control variables, we included *year* dummies to account for the effect of time trends, and *industry* dummies to account for the effect of a firm's industry affiliation. Data for these control variables were gathered from various sources, including the Bureau van Dijk's Osiris and Diane databases, annual reports and Patstat. All right-hand side variables are one-year-lagged.

### **Econometric approach**

While we have panel data, the focal relationship we want to identify is cross-sectional, as hypotheses 1 and 2 are concerned with differences between firms with political connections and firms without political connections. Thus, fixed effects models would not be appropriate as an identification strategy, because they would capture the effect of changes in a firm's political connections over time on its international strategy. In line with this, Hausman tests indicated the adequacy of a random effects approach in most specifications. However, in some cases, despite the low and rare changes in firms' political connections over time, fixed effect models were suggested. This is probably related to unobservable firm-level attributes that influence a firm's tendencies regarding international expansion strategy and political connections.

We address this issue by estimating both within-firm and between-firms effects in the same specification (Bartels, 2015; Bell & Jones, 2012; Mundlak, 1978; Wooldridge, 2010). We use an estimation technique based on the approach introduced in the literature by Mundlak (1978), which consists in estimating a random effects model while simultaneously controlling for time invariant firm-level attributes. Only recently this technique has been suggested as an appropriate way of estimating the within and between-cluster effects in the same equation (Bartels, 2015; Bell & Jones, 2012) and applied to management research (Ceccagnoli and Jiang, 2013; Choi, Jia, and Lu, 2014). Bartels's (2015) approach includes two transformations of each predictor in a random effects specification: (1) the first one is the firm-specific mean over time ( $\bar{x}_i$ ) for each variable, which captures between-firms effects; and (2) the second one is a yearly deviation from the firm-specific mean over time ( $x_{it} - \bar{x}_i$ ) of each right-hand side variable, which captures within-firm effects.

This specification has two main advantages. First, it produces statistically efficient coefficients for predictors that display limited longitudinal variance, while fixed effects models do not perform well with this type of data (Wooldridge, 2010). Second, through the inclusion of the within-firm version of predictors, it guarantees that the independent variables are uncorrelated with the between-firm random effects, thus removing the main potential source of bias in the random-effects approach (Bartels, 2015).

We defined the following statistical model to test hypotheses 1 and 2:

$$(1) FDI_{kit} = \alpha_{00} + \sum_j \beta_j PC_{jit}^B + \sum_l \beta_l Control_{lit}^B + \\ + \sum_j \gamma_j PC_{jit}^W + \sum_l \gamma_l Control_{lit}^W + \tau_t + \omega_m + u_{i0} + \varepsilon_{it}$$

In Equation (1), the dependent variable  $FDI_{kit}$  is the international expansion strategy  $k$  reflected in the FDI by firm  $i$  in year  $t$ . Criterion  $k$  indicates either *FDI amount* or *FDI riskiness*, depending on the hypothesis being tested. The right-hand side of the equation contains a constant  $\alpha_{00}$ , two versions of each independent and control variable, year dummies  $\tau_t$ , industry dummies  $\omega_m$ , the firm-specific error term  $u_{i0}$ , and the event-specific error term  $\varepsilon_{it}$ . The first version of each independent variable  $PC_{jit}^B$  corresponds to the indicator of between-firms effects of each type  $j$  of political connection. The second version  $PC_{jit}^W$  corresponds to the indicator of within-firm effect over time of each type of political connection. The only independent variable included in the raw form is *CEO friendship PC*, because it has minimal within-firm variance (only three firms have experienced changes in this variable over the period under analysis). Correspondingly, each control variable also has a version for between-firms and a version for within-firm effects.

To test hypotheses 3 and 4, we used an adaptation of the differences-in-differences approach, according to the following specification:

$$(2) FDI_{kit} = \alpha_{00} + \sum_j \beta_j PC_{jit}^B + \sum_j \delta_j PC_{jit}^B * T + \sum_l \beta_l Control_{lit}^B +$$

$$\sum_j \gamma_j PC_{jit}^W + \sum_j \lambda_j PC_{jit}^W * T + \sum_l \gamma_l Control_{lit}^W + \varphi T + \tau_t + \omega_m + u_{i0} + \varepsilon_{it}$$

Our main interest is in comparing how firms with different portfolios of friendship political connections change their international expansion strategy in the aftermath of a political change that increases the value of their friendship connections. In addition to the variables in equation (1), we included the interaction between the measurements of political connections and an indicator variable, T, for whether the observation is post-Sarkozy's election (2008-2012). These interactions  $\delta_j$  and  $\lambda_j$  identify the extent to which changes in international strategy by firms with friendship political connections differ from changes in international strategy by firms without friendship political connections. Although we only claim that friendship political connections are affected by political changes, we also included interactions with the other two types of political connections to verify this assumption and to test the consistency of our findings. In all specifications, the standard errors are clustered by firm, thus accounting for potential non-independence between observations of international expansion strategy of the same firm over time.

## Results

Table 3 shows descriptive statistics and correlations. Firms in the sample have made substantial investments abroad, as shown in the average *FDI amount* of 539.78 million dollars. Some firms had negative net *FDI amount*. Overall, firms do not concentrate their investments in risky countries, but the maximum *FDI riskiness* attains the value 0.9. *FDI amount* and *FDI riskiness* are not highly correlated with each other, but clearly reflect different dimensions of a firm's international expansion strategy.

With respect to friendship political connections, the proportion of Sarkozy's friends on firms' boards of directors ranges from 0 to 0.29 and in 25.86% of the cases firms have at least one friend of Sarkozy on their board. Also, 5% of the CEOs belong to Sarkozy's friendship network. As for *common education PC*, the variable concerning the board varies from 0 to 75%; that is, some firms have most of their board directors belonging to the ENA network. Also, 11% of the CEOs graduated from ENA. Finally, *board government experience PC* varies from 0 to 71%, and 18% of the CEOs have experience working for the government. Interestingly, the measures related to CEOs and those related to the board of directors are not highly correlated. Different types of political connections do not show remarkably high correlations between one another, except for *board common education PC* and *board government experience PC*.

**Table 3: Descriptive statistics and correlations**

<b>Variable</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>	<b>12</b>	<b>13</b>	<b>14</b>	<b>15</b>
1 FDI amount	1.00														
2 FDI riskiness	0.15	1.00													
3 CEO friendship PC	-0.02	0.17	1.00												
4 Board friendship PC	0.23	0.20	0.16	1.00											
5 CEO common education PC	0.12	0.10	-0.08	0.07	1.00										
6 Board common education PC	0.11	0.14	0.08	0.14	0.31	1.00									
7 CEO government experience PC	0.03	0.10	0.00	0.07	0.41	0.07	1.00								
8 Board government experience PC	0.18	0.15	0.06	0.17	0.33	0.77	0.25	1.00							
9 Firm size	0.32	0.48	0.25	0.36	0.22	0.37	0.26	0.42	1.00						
10 Firm total investments	0.27	0.14	0.23	0.25	0.09	0.19	0.09	0.18	0.40	1.00					
11 Firm performance	0.05	0.00	-0.06	0.05	-0.04	-0.01	-0.06	-0.02	-0.02	-0.05	1.00				
12 Firm R&D	0.21	0.23	-0.02	0.16	0.01	0.06	0.05	0.09	0.41	0.20	-0.06	1.00			
13 Firm innovation	0.08	0.22	0.00	0.02	-0.02	0.06	0.04	0.05	0.25	0.06	-0.12	0.51	1.00		
14 Firm debt	0.29	0.28	0.15	0.15	0.10	0.28	0.12	0.32	0.60	0.38	-0.08	0.17	-0.03	1.00	
15 Firm multinationality	0.21	0.40	0.15	0.26	0.05	0.16	-0.08	0.16	0.47	0.09	0.04	0.24	0.16	0.17	1.00
<b>Mean</b>	539.78	0.20	0.05	0.03	0.11	0.11	0.18	0.16	9.90	1546.16	3.76	803.82	32.94	11980.42	22.43
<b>S.D.</b>	2230.17	0.23	0.23	0.06	0.31	0.12	0.39	0.15	1.63	5919.13	7.28	2250.59	96.58	25410.42	17.17
<b>Min</b>	-13953.72	0.00	0.00	0.00	0.00	0.00	0.00	0.00	5.19	-0.51	-59.77	0.00	0.00	-24578.38	0.00
<b>Max</b>	22779.08	0.90	1.00	0.29	1.00	0.75	1.00	0.71	13.77	69207.25	45.60	22378.68	756.00	218778.20	80.00



Table 4 presents the analyses testing hypotheses 1 and 2. The indicators for within-firm and between-firms effects have distinct impacts on international expansion strategy. Model 1 presents results for the analysis of *FDI amount* to test hypothesis 1, which predicts a positive effect of political connections on a firm's total overseas investments. We find that *board friendship PC (between indicator)* ( $\beta=6,606.810$ ;  $p<0.05$ ) has a positive and significant effect on *FDI amount*. This result suggests that, *ceteris paribus*, firms with a higher (longitudinal) average proportion of Sarkozy's friends on their boards invest more internationally than firms with a lower average proportion of Sarkozy's friends on their boards. This finding is consistent with our predictions in hypothesis 1.

On the other hand, depending on the type and channel of political connections, the coefficients yielded in our estimations are negative. Specifically, *CEO friendship PC* ( $\beta=-1,211.461$ ;  $p<0.05$ ) has a negative and significant effect on *FDI amount*, which is the opposite of our predictions. Other types of political connections, particularly within-firm indicators, do not affect *FDI amount* significantly. We, hence, find mixed support to hypothesis 1, depending on both the type and the channel of political connections.

Model 2 shows results testing hypothesis 2. We find that *CEO common education PC (between)* is positive and significant ( $\beta=0.098$ ;  $p<0.05$ ). This result suggests that firms with more political connections (higher longitudinal average proportion of ENA graduates on the board of directors) are associated with greater concentration of investments in countries with higher expropriation risk. Other types and channels of political connections, particularly their within-firm indicators, do not appear to significantly affect this dimension of firms' international expansion strategy. Therefore, the effect of political connections on FDI riskiness is corroborated regarding common education political connections, which provides support to hypothesis 2.

**Table 4: Between-within analysis of international strategy**

Variables	(1)		(2)	
	FDI amount		FDI riskiness	
	Between	Within	Between	Within
CEO friendship PC	-1,211.461* (597.592)		0.056 (0.040)	
Board friendship PC	6,606.810* (3,170.727)	8,776.353 (5,028.966)	0.306 (0.246)	-0.082 (0.267)
CEO common education PC	810.318 (468.843)	1,019.001 (552.309)	0.098* (0.042)	-0.044 (0.036)
Board common education PC	-2,774.601 (1,417.772)	-2,140.524 (1,756.121)	-0.118 (0.142)	0.057 (0.120)
CEO government experience PC	-485.368 (301.931)	-1,113.602 (642.955)	-0.017 (0.040)	0.032 (0.042)
Board government experience PC	1,989.321 (1,153.698)	610.004 (1,162.162)	-0.159 (0.131)	-0.059 (0.115)
Firm size	-9.016 (128.717)	170.198 (165.351)	0.046** (0.015)	0.028 (0.021)
Firm total investments	0.017 (0.028)	0.047* (0.023)	-0.000 (0.000)	0.000 (0.000)
Firm performance	23.283 (15.532)	12.293 (10.165)	-0.000 (0.002)	0.002 (0.001)
Firm R&D	0.061 (0.058)	-0.014 (0.104)	-0.000 (0.000)	-0.000 (0.000)
Firm innovation	1.618 (1.352)	0.173 (1.209)	0.000*** (0.000)	-0.000 (0.000)
Firm debt	0.032** (0.010)	-0.017 (0.024)	0.000 (0.000)	-0.000 (0.000)
Firm multinationality	18.968** (6.409)	-24.826 (40.380)	0.002 (0.001)	0.001 (0.002)
Constant	35.409 (1,156.830)		-0.293* (0.135)	
Industry FE	YES		YES	
Year FE	YES		YES	
<b>Number of observations</b>	990		990	
<b>Number of firms</b>	103		103	
<b>Wald <math>\chi^2</math> test</b>	15119 (p<0.000)		2362 (p<0.000)	
<b>P</b>	0.0591		0.283	
<b>R<sup>2</sup> between</b>	0.714		0.632	
<b>R<sup>2</sup> within</b>	0.056		0.022	
<b>R<sup>2</sup> overall</b>	0.280		0.337	

Robust standard errors clustered by firm in parentheses

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

Finally, Table 5 presents the results of our adapted difference-in-differences analysis testing hypotheses 3 and 4. Although the effect of *CEO friendship PC* remains negative in Model 3, its interaction with the period indicator is positive and significant ( $\delta=1517.304$ ;  $p<0.05$ ), which is consistent with hypothesis 3. That is, after the election of Sarkozy, firms with friendship political connections through the CEO increase the amount of their international investments relative to before his election. These results support hypothesis 3.

Concerning hypothesis 4, interactions between measures of friendship political connections and the post-election period marker in model 4 are not significant. Thus, our analysis does not provide support for hypothesis 4. Interestingly, model 4 shows that firms with a former government official as the CEO for longer periods of time (greater *CEO government experience (between)*) decrease their *FDI riskiness* in the period post-Sarkozy's election ( $\delta=-0.076$ ;  $p<0.05$ ). It appears that the election of Sarkozy as the president of France affected not only firms connected with him through his personal friends, but also firms that hold other types of political connections.

The control variables behave similarly with and without the interactions of political connections and the post-election period marker. Between-firms heterogeneity in *firm debt* and *firm multinationality* and within-firm changes in *firm total investments* affect *FDI amount*. Between-firms heterogeneity in *firm size* and in *firm innovation* have a positive effect on *FDI riskiness*. As I suspected, most of the relevant determinants of firm international expansion strategy in this setting are between-firms effects.

**Table 5: Pre vs After Sarkozy's election analysis**

Variables	(3)		(4)	
	FDI amount		FDI riskiness	
	Between	Within	Between	Within
CEO friendship PC	-1,921.526**		0.042	
	(706.539)		(0.045)	
CEO friendship PC*Post-election period	1,517.304*		0.033	
	(658.513)		(0.028)	
Board friendship PC	7,269.572*	3,165.174	0.393	-0.218
	(3,552.096)	(3,864.554)	(0.274)	(0.447)
Board friendship PC*Post-election period	-1,246.153	12,408.537	-0.170	0.140
	(2,171.875)	(7,358.797)	(0.182)	(0.702)
CEO common education PC	-432.611	-125.125	0.072	0.001
	(261.924)	(500.035)	(0.051)	(0.045)
CEO common education PC*Post-election period	1,931.559**	2,264.734	0.062	-0.109
	(747.345)	(1,203.969)	(0.045)	(0.066)
Board common education PC	-271.472	-1,421.554	0.019	0.103
	(1,163.857)	(1,807.993)	(0.188)	(0.183)
Board common education PC*Post-election period	-3,170.427	-3,253.706	-0.277	-0.190
	(2,159.069)	(3,036.453)	(0.197)	(0.323)
CEO government experience PC	-286.674	72.573	0.021	0.026
	(320.338)	(850.189)	(0.049)	(0.051)
CEO government experience PC*Post-election period	-100.741	-2,420.381	-0.076*	0.040
	(393.272)	(1,627.513)	(0.037)	(0.070)
Board government experience PC	705.193	-325.719	-0.196	-0.143
	(964.929)	(1,376.762)	(0.179)	(0.155)
Board government experience PC*Post-election period	1,285.190	2,576.947	0.080	0.223
	(1,443.730)	(2,102.581)	(0.187)	(0.263)
Firm size	28.967	159.018	0.044**	0.022
	(113.538)	(192.844)	(0.015)	(0.022)
Firm total investments	0.008	0.039	-0.000	0.000
	(0.026)	(0.022)	(0.000)	(0.000)
Firm performance	23.741	3.180	-0.000	0.002
	(15.934)	(10.012)	(0.002)	(0.001)
Firm R&D	0.050	-0.016	-0.000	-0.000
	(0.064)	(0.105)	(0.000)	(0.000)
Firm innovation	1.395	-0.099	0.000***	-0.000
	(1.361)	(1.262)	(0.000)	(0.000)
Firm debt	0.027*	-0.018	0.000	-0.000
	(0.011)	(0.025)	(0.000)	(0.000)
Firm multinationality	19.712**	-30.543	0.002	0.002
	(6.017)	(34.528)	(0.001)	(0.002)
Post-election period	-108.048		0.056	
	(217.551)		(0.035)	
Constant	-400.919		-0.296*	
	(1,061.841)		(0.137)	
Industry FE	YES		YES	
Year FE	YES		YES	
<b>Number of observations</b>	990		990	
<b>Number of firms</b>	103		103	
<b>Wald <math>\chi^2</math> test</b>	14349 (p<0.000)		2851 (p<0.000)	
<b><math>\rho</math></b>	0.000		0.262	
<b>R<sup>2</sup> between</b>	0.748		0.636	
<b>R<sup>2</sup> within</b>	0.075		0.031	
<b>R<sup>2</sup> overall</b>	0.305		0.343	

Robust standard errors clustered by firm in parentheses

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

## **Robustness Tests**

We also implemented robustness tests to check the sensitivity of our results to alternative econometric approaches and to different sets of independent variables. Although Bartels's approach is the most appropriate for this study, we checked whether results would hold using four alternative specifications.

First, as our main interest is on differences across firms on the relationship between political connections and international expansion strategy, we used a pooled OLS specification, with standard errors clustered by firm. All results remain qualitatively similar and, additionally, *CEO friendship PC* appears to also affect *FDI riskiness* positively.

Second, we performed standard random effects models, but not separating between-firms from within-firm effects. Again, results are consistent in terms of sign and significance, but reveal less information than Bartels's (2015) specification. For instance, none of the measures of political connections significantly affect *FDI riskiness*. This could lead us to believe that political connections have no effect on a firm's degree of concentration of overseas investments in countries with greater risk of expropriation. However, such result is due to confounding between-firms and within-firm effects of *CEO common education PC*.

Third, although the independent variables rarely change over time, we performed a fixed-effects analysis. The results are similar to the within-firm effects in the main analysis, that is, political connections seem not to affect international expansion strategy. Additionally, the variance explained with this analysis is substantially lower than the variance explained with Bartels's or random effects specifications.

Fourth, as *FDI riskiness* is a fractional variable, ranging from 0 to 1, results could be biased. Using a generalized linear model with a logistic link function has been suggested in the

literature as a solution (Papke & Wooldridge, 1996). Applying this methodology yields similar results, but only friendship political connections have a significant effect on international expansion strategy.

With regards to the independent variables, we performed four robustness analyses. First, regardless of the proportion of board members with a specific type of political connection, the actual number of individuals with a political tie to authorities in the home-country government may be meaningful. We therefore replaced the measures referring to the board with the number of board members who are ENA graduates, the number of directors who worked for the government, and the number of directors who are Sarkozy's friends. Results remained qualitatively unchanged.

Second, because *common education PC* and *government experience PC* are highly correlated and because, in many instances, board members and CEOs are both ENA graduates and former government officials, there could be imprecision in the estimation of these indicators in the same model. I, therefore, performed regressions excluding the measures of *government experience PC*. Most results remained unchanged.

Third, while we control for time-invariant unobservable factors with the within-firm indicators, there could be other time-variant firm characteristics that affect the relationships we tested. For instance, firm past international strategy could contain relevant information to determine a firm's current international strategy. I, therefore, ran alternative models controlling for lagged dependent variables. Despite all the specification problems inherent in using lagged dependent variables, the results of this analyses did not differ qualitatively from our main specification. Interestingly, the lagged dependent variable is significant and positive in the *FDI riskiness* equation and non-significant in the *FDI amount* equation.

Finally, the extent to which a firm takes more risk in its international strategy could depend on the overall amount of investments it makes in a given point in time. I, therefore, reran the models testing hypotheses 2 and 4 while controlling for *FDI amount*. These alternative specifications yielded results qualitatively similar to the main ones.

## **Discussion and Conclusions**

This paper examines how different types of political connections influence a firm's international expansion strategy. We argued that a firm's political connections in the home country influence positively the amount and degree of expropriation risk of international investments that a firm makes in a given period of time. We empirically analyzed our predictions on a setting of the international expansion strategy of the largest French firms during the period 2003-2012. The analyzed firms invested actively outside of France during that period, and their investments were largely heterogeneous regarding the commitment of resources in host countries with distinct levels of expropriation risk. Firms also exhibited substantial variance in terms of the types and levels of their political connections. Furthermore, the inclusion in the analysis of a period before and a period after the election of Nicolas Sarkozy as the president of France allowed us to evaluate the effects of this major political change that altered the value of our indicators of friendship political connections. The empirical analysis provided corroboration to our broad predictions. That is, politically-connected firms make distinct international expansion strategy relative to non-politically-connected firms, with such heterogeneity being contingent on the type of political connections.

Turning to the specific results, our findings indicate that different components of a firm's international expansion strategy are sensitive to distinct types of political connections. Firms in our setting appear to use their friendship political connections as levers to make decisions regarding the amount (but not regarding the level of expropriation risk) of their international investments in a given period of time. Additionally, friendship political connections have a contingent effect on the amount of international investments a firm makes. Before Sarkozy is elected president of France, but acts as a minister and leader to a faction opposing then-president



Jacques Chirac, firms whose CEO is a friend of Sarkozy invest significantly less overseas. A possible explanation is that, because before 2007 Sarkozy did not have the necessary power to trigger the benefits underlying the three mechanisms we offered here, these firms interpret the benefits of their political connections as being bounded to the home country. Indeed, the negative effect of having a friend of Sarkozy as CEO on the amount of international investments is reduced after Sarkozy rises to office, probably because his political power becomes both broader – as it reaches all levels of the French political system, including foreign affairs – and deeper – as Sarkozy becomes the most important political figure in France. Facing such a change of context, CEOs who have a friendship connection with Sarkozy may have reconsidered their focus on domestic business and undertaken more international investments as the marginal benefits of this type of investment increases.

Nonetheless, friendship political connections do not seem to impact the level of expropriation risk of firms' overseas investments. What firms do leverage to invest in riskier countries are political connections related to a common education background between the firms' decision makers and government authorities. Firms in which the CEO is usually a graduate from ENA, therefore belonging to a large network of powerful individuals in the French business and government scene, exhibit a greater concentration of their international investments in countries with higher risk of expropriation. A CEO enjoying such powerful connections in the French government is likely to benefit from a greater perceived influence over governmental decisions, particularly concerning protection of private assets in foreign countries. Also, these CEOs' connections could improve the firm's access to capital, allowing it to boost its investments, even in riskier countries, at a lower cost. These results are consistent with the idea of firms benefiting from their activities towards the government in the home country to develop political capabilities

that become useful in countries with higher risk of expropriation (García-Canal & Guillén, 2008).

Political connections based on previous experience in the government do not affect international expansion strategy significantly, though. Even when we separately examine the effect of government experience and common educational background political connections, government experience does not yield significant results. Collectively, these results seem to indicate that individuals who hold friendship ties or who studied together and belong to the same broad network (the community of ENA graduates), with strong roots in both the business and the political world, may provide each other with relevant resources to do business abroad. To benefit from these resources, individuals need to be deeply connected to one another. Simply having worked for the government in the past may not give individuals the same access to top government officials as common-education and friendship bonds would. Accordingly, we find no evidence that having worked for the government generates capabilities of how to deal with governments that could be replicated in foreign countries.

This study is not without limitations. First, several reasons could explain the lack of significance of government experience political connections. Many of the directors who were government officials in the past are also ENA graduates. Accordingly, the effects of government experience and common education political connections could confound each other, with some of the effect of government experience political connections being captured by the measures of common education. However, as we explained in the robustness tests, removing the measures of government experience political connections does not change the results. Another possibility is that government experience does indeed create capabilities of knowing how the government operates, but that these capabilities are circumscribed to doing business in France. Future

research could analyze domestic and international investments jointly to investigate in what circumstances each type of political connection is more relevant. Given the results obtained in our analysis of international investments exclusively, we suspect that government experience political connections would have an asymmetric influence on domestic relative to international investments.

Second, although the hypotheses refer to social ties between decisions makers in the firm and at the government, implying that they know each other and exchange information and favors with one another, our measurements are proxies of such ties. For example, some ENA graduates may not know each other or have opposite political ideologies and agendas relative to one another, which would prevent them from exchanging information and favors. Future research could distinguish individuals by political ideology and potentially by the period of their professional experience in the government or studies at ENA to obtain more refined measures of political connections.

Finally, our analysis of friendship political connections also requires more elaboration, as it focuses on only one politician. Although Sarkozy is a special case, as he represents a disruption in the command of the French government, given his business orientation and non-alignment with traditional political elites, future research could identify firms holding friendship ties with other top politicians. Assessing friendship connections between top business leaders and politicians such as Ségolène Royal (Sarkozy's opponent in the 2007 election and ex-wife of François Hollande, Sarkozy's successor) and Jacques Chirac (the president of France before Sarkozy) could be particularly helpful to better capture the effects of this type of political connections.

We make several contributions to the literature with this study. First, we contribute to the literature on global strategy. Although a few studies investigate the role of political connections in the home country on particular international strategies of emerging-country firms (Duanmu, 2014; Leuz & Oberholzer-Gee, 2006; Wang, Hong, Kafouros, & Wright, 2012), this study is unique in showing that political connections influence international expansion strategy of firms founded and headquartered in an advanced economy. Additionally, our study goes beyond the idea of firms from a same home country sharing the same level of political capabilities (Cuervo-Cazurra & Genc, 2008; Holburn & Zelner, 2010), but proposes and empirically analyze the effect of heterogeneity in political connections among firms from a same home country. Also, our study adds knowledge to the stream of research that investigates how firms respond to international investment risk (García-Canal & Guillén, 2008), by showing the importance of political connections in these responses.

We also add to the literature on political connections, identifying one way in which political connections create value for firms (Siegel, 2007; Zhu & Chung, 2014), that is, by providing them with better conditions to manage their international expansion. Additionally, we contribute to studies on political connections by comparing the effects of three types of political connections on firms' strategy. While most prior research examines the effect of only one type of political connection on firms' value, this paper shows that different types of political connections have distinct effects on international expansion strategy.

Finally, we used a method that is relatively new in management research and that allows the identification of within-firm and between-firms effects of political connections on firms' international expansion strategy in the same specification (Bartels, 2015; Bell & Jones, 2012; Mundlak, 1978). This method could be used to examine other antecedents of firm strategic

decisions, contrasting their effects across firms and over time simultaneously. The method could also be applied to better understand the performance implications of such decisions, comparing both firms' long-term performance persistence and short-term changes in performance due to strategic actions.

## **CHAPTER 5: Political Connections and Speed in Large Projects**

## **Abstract**

We investigate the role of firm-specific political connections on the speed with which project finance-based investments obtain funding and start operations. We argue that political connections operate as a mechanism to mitigate risks of project finance-based investments, particularly when projects lack other features that could alleviate the risks perceived by potential lenders and other stakeholders. We further argue that firms without political connections get projects financed and start operating faster only if they announce low risk projects. We also propose that political connections based on interpersonal relationships and political connections based on government experience have contrasting effects on the speed of project finance-based investments. Finally, we propose that high-speed projects are not simply the mirror image of low-speed projects, but that these two categories of projects are characterized by different features. We use fuzzy sets qualitative comparative analysis to empirically investigate these predictions. We analyzed a sample of 95 project finance investments sponsored by the largest French firms in 31 countries and identified the circumstances leading to high speed in project finance-based investments.

**Keywords:** project finance; political connections; French firms; political risk; project funding; fuzzy set QCA

## Introduction

Investments in infrastructure are crucial for sustainable development and inclusive growth, particularly in emerging and frontier markets. According to recent estimates, the required amount of investments to reach an optimal level of infrastructure worldwide until 2030 surpasses four trillion dollars (World Economic Forum, 2015). Given the economic and political risks and the public utility of the outcome generated by these investments, typical mechanisms for investment governance and funding through corporate finance are usually unreasonable. Alternative governance structures in which governments and private firms agree on the liability claims to the investment risks are typically required. In this context, project finance emerges as one of the most common and advisable ways to fund large infrastructure investments (Esty, 2004; Sawant, 2010a).

Project finance-based (PF) investments usually encompass one or a group of sponsors – firms, governments or other organizations – that incorporate a new firm with project-specific purposes (Esty, 2004; Kleimeier & Megginson, 2000). Funding is determined according to the project's predicted cash flows rather than the sponsors' financial resources. Some features of PF investments, such as high leverage, separate incorporation from sponsors, and concentrated equity and debt, help solve problems related to the risks involved in large infrastructure investments (Esty, 2004; Sawant, 2010a; Vaaler et al., 2008) and make PF investments funding distinct from more commonly studied corporate finance funding (Kleimeier & Megginson, 2000; Vaaler, 2008). Indeed, PF investments are frequent in industries characterized by long-term commitments, large investments, problems related to obsolescing bargaining power (Vernon, 1980), and in countries where creeping expropriation may become an issue during the investment life cycle (Kleimeier & Megginson, 2000; Sawant, 2010a).



Firms have been extensively using PF investments since the 1970s. The amount invested through this mode has grown substantially during the 1990s, and surpassed \$100 billion dollars annually during most of the 2000s. Notwithstanding its widespread use by firms and governments, its differences relative to traditional corporate finance funding, and its potential to become a source for important theoretical and practical insights, there is a stark dearth of research on PF investments (Esty, 2004; Vaaler, 2008). In management, particularly, only a handful of studies have investigated this mode of investments (Doh, Teegen, & Mudambi, 2004; Ramamurti, 2003; Sawant, 2010a; Vaaler, 2008; Vaaler et al., 2008). On top of that, the existing studies only tackle more straightforward questions, such as how PF investments use capital structure to manage host country risk or the antecedents of firms' propensity to use project finance rather than corporate finance for investments. Less is known on firms' capabilities to undertake successful PF investments. Particularly, there is a lack of knowledge on how fast an announced PF investment is actually funded and put in operation. Speed is, nonetheless, a relevant indicator of project performance. Given the high leverage and liabilities based on project cash flows of PF investments, the time required to obtain funding and then from funding through operations start involves substantial costs for both sponsors and other stakeholders involved in the project.

We investigate the role of sponsor-specific political connections on patterns of PF investments speed. We analyze how a project sponsor's political connections in its home nation influence its speed to obtain funding and to start operations of its PF investments. We also analyze how these relationships vary depending on the location of the investment and on other factors that shape the level of the project risk for sponsors and for lenders. As many of the risks faced in funding and developing PF investments are of political nature, political connections

should be substantially important in this context. Indeed, PF investments typically require sponsors to closely deal with governments to obtain various types of licenses and permits, to ally with governments in public private partnerships (PPPs), to negotiate taxes and labor-related issues, among others. Additionally, lenders of capital may deem different sponsors as more or less likely of being bailed out by governments, depending on the sponsor's political connections.

Accordingly, we advance that political connections may operate as a mechanism to reduce PF investments risks and, thus, positively influence a project speed. However, we consider that the effect of political connections on a sponsor's PF investments speed may only operate when in combination with other project, sponsor, and location attributes that together determine the level of risk for a particular project. Specifically, we maintain that political connections will be associated with sponsors being able to obtain funding and start operations in a relatively quicker way than sponsors without political connections. We further maintain that political connections will be more meaningful when the project lacks other features that could mitigate its risk. Sponsors without political connections, on the other hand, will be associated with high speed only if they announce low risk projects. Finally, we allow distinct types of political connections to associate with different outcomes.

We use fuzzy sets qualitative comparative analysis (fs/QCA) to empirically investigate these propositions on a sample of PF investments sponsored by at least one of the largest firms listed in the Paris stock exchange, during the period from 2003 through 2012. The sample includes 95 projects sponsored by 17 firms in 31 distinct host countries. These investments are concentrated in infrastructure industries such as power distribution, transportation, oil and gas, and water treatment and distribution.

Our contributions to literature and practice are threefold. First, we contribute to the literature on political connections, revealing the relationship between political connections and firms' strategies and performance (Fisman, 2001; Zhu & Chung, 2014). Particularly, we show how political connections affect firms' performance regarding the speed to obtain funding for and to start operating their PF investments. Second, by introducing the project location in our analysis, we contribute to international business literature, showing that projects in the home country and projects in foreign countries differ in their risk profiles and on the sponsor's ability to use political connections to alleviate risks. Finally, we contribute to the understanding of how PF investments can be better used to meet the increasing global needs for infrastructure investments (Esty, 2004; World Economic Forum, 2015).

## **Project Finance, Political Connections and Speed**

Additional explanation of the project finance-based (PF) investments context provides the necessary background for our theoretical framework and choice of empirical method. We rely on studies in management (Sawant, 2010a, 2010b; Vaaler, 2008; Vaaler et al., 2008) and finance (Esty, 2004) to further describe PF investments. PF investments are large, stand-alone, single business organizations costing hundreds of millions of dollars to construct and operate, most often in infrastructure industries such as power generation, water- and sewage-related services, telecommunications, transportation, and mining and energy exploration and refining. Typically, one to four sponsors, often well-known MNEs, own a PF investments, with the lead sponsor holding the largest equity share and having the greatest involvement in the PF investment structure and supervision. The majority of PF investment capital for construction and operations does not come from sponsor equity, but from debt, usually in the form of large loans made by commercial banks. Most importantly, only cash flows from the project itself can service these loans, and only the PF investment assets can serve as loan collateral. That is, creditors do not have recourse to other sponsor assets.

### **Time and Project Finance-Based Investments**

Time is one of the most valuable resources for firms. Even the most resourceful firms may lose competitive advantage if they do not take the right decisions in the right time or if they take too long to execute a decision. Prior research has emphasized the analysis of the conditions under which firms may attain first- or late-mover advantages (Frynas et al., 2006; Hawk, Pacheco-De-Almeida, & Yeung, 2013; Lieberman & Montgomery, 1988), and firms' speed capabilities (Pacheco-de-Almeida & Zemsky, 2003; Salomon & Martin, 2008), which are related

to how much time they need from the moment a decision to implement new businesses, facilities or technologies is made until operations actually start.

We focus on speed because this can be of extreme importance in PF investments. Specifically, there are two crucial stages in which speed is relevant for PF investment performance: the funding provision stage and the project development stage (Finnerty, 2013). Estimated transactions costs in PF investments are around 10-15% larger than in similar investments funded through more traditional mechanisms (Esty, 2004; Kleimeier & Megginson, 2000). Given the difficulties related to their large size and often uncertain future cash flows generation, PF investments typically take a long time to receive funding and to develop. Nonetheless, several factors explain the superiority of project finance as a way to deal with the risks of large infrastructure investments (Sawant, 2010a) and may explain their extensive use despite the larger transaction costs. Particularly, prior research has analyzed several project and host country factors that may help mitigating risks involved in PF investments. We describe these factors and their proposed relationship with PF investments speed in the next paragraphs.

### **Political Connections and PF Investments Speed**

One of the major sources of difficulties, and therefore costs, in PF investments is obtaining government authorizations to start and develop a project (Esty, 2004). A sponsor that can demonstrate a capability to interact successfully with governments to procure such authorizations is likely to be positively evaluated by potential lenders. Also, such an ability has an intrinsic bearing on the firms' probability of rapidly developing the project to start operating it. Prior research on political connections and corporate political activities suggests that firms differ substantially in their political engagement (Faccio, 2006; Fisman, 2001; Hillman et al., 2004) and in the extent of their capabilities in the political market (Bonardi et al., 2006). These

capabilities may help sponsors to accelerate lenders' decision process regarding the provision of funding for their PF investments. Additionally, having the support from the government increases the likelihood that funding will be provided by institutions linked to the government. Finally, political connections may also help accelerating the project development, as such connections reflect superior capabilities to deal with political stakeholders that control several of the licenses and permits required to start operations.

We propose that two types of political connections are particularly significant for PF investments: government experience-based political connections and interpersonal relationships-based political connections. Political connections stemming from government experience are created when business leaders have worked in politics or as top government officials prior to their business career. Such leaders are likely to have kept contacts in the government and to have learned how the government and the public policy formulation works (Bertrand et al., 2006; Kramarz & Thesmar, 2013; Lester et al., 2008). Evidently, these capabilities can be extremely useful when the firm has to deal with political actors in order to make its investments operational. Interpersonal relationships-based political connections, on the other hand, are created when top business leaders have personal friends or family members at high-level positions in the government (Coulomb & Sangnier, 2014; Fisman, 2001). Such interpersonal relationships may help sponsors to influence government-related lenders and other stakeholders to facilitate funding provision and project development.

Each type of political connections may play a distinct role in defining how potential lenders perceive the sponsors' capacity to enable their projects to generate the necessary cash flows to meet debt obligations, and how the sponsor can manage multiple stakeholders to accelerate project development. Government experience-based political connections should

operate by increasing the sponsor's capability to obtain authorizations and sponsorship from the government, as sponsors with such political connections are better in dealing with government officials. In contrast, interpersonal relationships with politicians should help sponsors obtain assistance from their home-country governments' in case of problems. However, political connections are probably only one of several mechanisms that can reduce the level of risk in PF investments, and may only operate when in combination with other factors (Esty, 2004).

### **Other Antecedents of PF Investments Speed**

Another enhancer of PF investments speed is the sponsor's prior experience with PF investments. First, from the lenders' point of view, more experience signals that there is a higher likelihood that a potential project will generate enough cash flows to meet debt obligations. Such experience is positively seen by potential lenders, influencing their propensity to more rapidly provide sponsors with funding (Vaaler et al., 2008). Second, more experience is associated with a superior ability to handle the process of project development for operations. This is because an experienced sponsor may know how to deal with the various stakeholders that affect its ability to start operating. Therefore, the more a firm relies on PF investments and the more the projects that it previously sponsored were successful, the higher the likelihood that the firm's future projects attain high speed.

The investment location is also crucial for funding evaluations and project development. Lenders will probably feel more assured when the project is in the same country as the sponsor's home country, as such project avoids liabilities of foreignness (Zaheer, 1995) that could increase its risk. Regarding the sponsor's ability to start the project operations, location may also have a meaningful role, as liabilities of foreignness and difficulties related to political and economic risks may affect the firm's interactions with suppliers, governments and other stakeholders

involved in the project development. Presumably, firms are better able to deal with such stakeholders in their home country (or in countries similar to the home country) than in foreign host countries, where practices may substantially differ (Delios & Henisz, 2003a; Holburn & Zelner, 2010).

Some organizational characteristics of the project also matter in determining its speed. First the project size in terms of the required financial investment is important. Naturally, larger projects are more difficult to fund and may require more time for lenders to evaluate funding applications. Also, larger projects are likely more challenging to develop and may, thus, be characterized by a lower speed of development.

PF investment capital structure at the time of initial announcement may also affect the project speed. The debt-to-equity ratio of a PF investment offers a potentially unbiased, forward-looking indicator of investment risk. As Esty (2002) and others (e.g., Vaaler et al., 2008) have documented in prior studies of PF investments capital structure and risk, more debt (equity) financing of a PF investment indicates lower (higher) investment risk. As a higher level of debt suggests lower project risk in the future, thus, guaranteeing the funding for a project with higher debt-to-equity ratio is likely to be less challenging than for projects with higher risk. Also, projects based on more debt may take less time to construct, given the lower risks. Therefore, higher levels of debt at announcement should lead to a higher speed of funding and of development.

Finally, the timing of the project announcement may also affect its speed to obtain funding and to start operations. When it comes to political connections, timing relative to political cycles are particularly important. The higher the political leverage of a firm within the government, the more effective are the political connections. Thus, projects announced when the



sponsor's contacts in the government enjoy more political power may be helpful in enhancing the project's speed. Table 6 presents a summary of all these factors that should impact PF investments speed and their potential impact on speed when observed in isolation.

Most of these attributes that shape PF investments risk are interdependent and possibly endogenously determined (Esty, 2004). Accordingly, we propose that, given such interdependence, it is unlikely that any of the attributes described in the previous paragraphs, including political connections, is sufficient to guarantee that a project obtains funding and starts operations more rapidly. In contrast, we propose that these aspects combine with each other in determining the speed of a particular PF investment. We further propose that sponsors with political connections may be able to reach high project speed even if they provide fewer insurances of low risk. Finally, we propose that the combinations of attributes that lead to high speed are not symmetrical to combinations of attributes that lead to low speed.

**Table 6: Outcome and causal factors definitions and proposed effect on speed**

<b>Variable</b>	<b>Definition</b>	<b>Impact on funding speed</b>	<b>Impact on completion speed</b>
Funding speed	Speed with which a sponsor is able to obtain funding for a PF investment	...	...
Completion speed	Speed with which a sponsor is able to complete the construction of a PF investment and start operating it	...	...
Interpersonal relationships-based political connections	Presence of friendship ties between top decision-makers in a sponsor firm and top politicians in the sponsor firm's home country	+	+
Government experience-based political connections	Presence of top decision makers in a sponsor firm who have prior experience working for the government or who are graduates from schools specialized in educating government officials	+	+
Sponsor PF investment experience	Sponsor firm has previously invested using PF financing	+	+
Domestic investment	The PF investment is located in the sponsor firm's home country	+	+
Project size	Project capital value	-	-
Ratio of debt	Ratio of debt to equity of a PF investment capital structure	+	+
Post-2007	The project is announced between 2008 and 2012	...	...

The proposed impacts refer to the direct effect of a causal condition on the two outcomes. Naturally, when in combination with various levels of other outcomes, these isolated impacts might be of a different sign or neutral.

## **The Fuzzy Set Qualitative Comparative Analysis Approach**

Our propositions are aligned with prior research suggesting that most attributes that contribute to reduce PF investments risk are interdependent and possibly endogenously determined (Esty, 2004). Therefore, it would not be accurate to analyze the effect of each attribute of PF investments on the project's overall risk and performance separately.

Accordingly, econometric analyses that treat each attribute as separate predictors of performance would yield incomplete and biased results. One way to address this issue could be to use a system of equations (Esty, 2004). However, this approach is still based on several limiting assumptions regarding the statistical distributions of the factors entered into the model. An alternative way to address the issue of interdependence is to adopt a configurational approach that facilitates the identification of sets of attributes that jointly determine distinct levels of performance.

We take the second approach and use fuzzy set qualitative comparative analysis (fs/QCA) to empirically evaluate our propositions. Fuzzy set QCA is appropriate to investigate complex models in which several causal conditions, spanning different levels of analysis, may combine with each other in multiple ways leading to either high or low levels of an outcome (Fiss, 2007; Ragin, 2000). A fuzzy set analysis has many advantages relative to correlational approaches, particularly in the case of moderately large samples. First, by not focusing on variables but on sets of cases grouped according to their association with different causal conditions, the method allows the researcher to go beyond the identification of net effects of single factors and actually compare real cases according to complex combinations of conditions. Second, the method does not simply categorizes cases into sets, but, through the calibration process in fuzzy sets, it allows partial membership in different sets (Fiss, 2007; Ragin, 2008).

Third, as the method is based on set theory, it is consistent with the possibility of equifinality and non-linearity of combinations of causal conditions (Fiss, 2007, 2011; Ragin, 2008). That is, distinct combinations of causal conditions may lead to the same outcome, and opposite combinations may not lead to opposite outcomes. Finally, the use of fs/QCA is flourishing in social sciences in the last decade, with several examples in strategy and management (Bell, Filatotchev, & Aguilera, 2013; Fiss, 2011) and international business (Crilly, 2011; Schneider, Schulze-Bentrop, & Paunescu, 2010).

We used two outcome factors: (i) the speed with which a sponsor obtains funding for an announced PF investment, and (ii) the speed in which the project starts operating. Naturally, speedier projects are those for which we identify a shorter period between announcement and funding and between announcement and operations commencement. Each of the mechanisms that help firms to mitigate the risks in PF investments is included as a separate causal condition, but the main emphasis is placed in understanding the role of political connections. We expect that these causal factors will combine in several different ways yielding alternative configurations of mechanisms that, to a large extent, help firms to reduce the time necessary to obtain funding for and complete their PF investments. Finally, given the fuzzy sets reasoning, we do not expect the projects with low speed to be characterized by opposite conditions as the projects with high speed. Indeed, we expect factors that lead to each of these outcomes to be asymmetric (Fiss, 2007; Ragin, 2008).

### **Outcomes and Causal Factors**

Drawing on prior research on speed capabilities and on PF investments, we designed an empirical study to investigate why and how some firms are able to obtain funding for and start operations of the PF investments they sponsor in a faster way. As we attempted to demonstrate

earlier, the factors that may determine PF investments speed cross many levels of analysis, being sponsor-specific, project-specific, host-country-specific, etc. Additionally, the presence of some factors may eliminate the need for other factors to be present, or even require the absence of some other factors in order for the desirable outcome to be attained.

We used data on a sample of PF investments whose sponsors include at least one of the largest firms listed in the Paris stock exchange, during the period from 2003 through 2012. We first identified all firms in the SBF120, an index that comprises the 120 most traded firms in France. Then we searched for PF investments in which one of these firms were among the sponsors during the 2003-2012 period. We were able to identify 95 projects with full information, including date of funding and date in which operations started. These projects were sponsored by 17 firms<sup>1</sup> in 31 distinct host countries.<sup>2</sup> These investments are concentrated in infrastructure industries such as power distribution, transportation, oil and gas, and water treatment and distribution. Table 7 and Table 8 depict the distribution of projects over time and across industries. Table 7 reveals that the largest number of projects was announced between 2006 and 2010. In Table 8, it is possible to see that Power & Energy, Social Projects, and Transportation account for most of the investments.

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<sup>1</sup> The firms include Alstom, AXA, BNP Paribas, Groupe Bourbon, Bouygues, EDF, Eiffage, GDF, Maurel et Proms, Societe Generale, Sodexo, Suez, Theolia, Total, Veolia, Vinci and Vivendi.

<sup>2</sup> The host countries include Australia, Bahrain, Belgium, Brazil, Canada, Chile, China, Colombia, France, Gabon, Germany, Ghana, Hungary, India, Ireland, Italy, Jordan, Netherlands, Oman, Portugal, Qatar, Russia, Saudi Arabia, Singapore, Slovak Republic, South Africa, South Korea, Thailand, United Kingdom, United States and United Arab Emirates.

**Table 7: Projects distribution by year**

<b>Year</b>	<b>Number</b>	<b>Percentage</b>
2003	6	6.32
2004	8	8.42
2005	6	6.32
2006	13	13.68
2007	13	13.68
2008	20	21.05
2009	10	10.53
2010	10	10.53
2011	5	5.26
2012	4	4.21
<b>Total</b>	<b>95</b>	<b>100.00</b>

**Table 8: Projects distribution by sector**

<b>Project sector</b>	<b>Number</b>	<b>Percentage</b>
Oil and Gas	6	6.32
Power & Energy	41	43.16
Social projects	21	22.11
Telecommunication	2	2.11
Transportation	19	20.00
Water	6	6.32
<b>Total</b>	<b>95</b>	<b>100.00</b>

To perform fs/QCA, all the causal factors need to be calibrated into (fuzzy) sets with basis in theory and deep knowledge of the empirical field of analysis. We based most of our calibration decisions on data about all funded PF investments made worldwide by any sponsors from 2003 to 2012, which includes information on 3,854 projects in 119 host countries. Each project in our sample of French projects is classified into fuzzy membership levels in each set according to how they compare to benchmark thresholds derived from the overall data. For some causal factors, we also relied on prior literature and on attributes of our sample of French projects to determine set membership benchmarks.

### **Outcome conditions**

We analyzed two outcome conditions in this paper. The first one is the speed with which a sponsor obtains funding for an announced PF investment. We used the number of days between the announcement date and the date in which funding is provided to measure funding speed. The shorter the duration between announcement and funding, the faster the sponsor's procurement of funding. To calculate the funding speed, we first counted the number of days between the date a project is announced and the date it obtains funding for all 3854 projects announced between 2003 and 2012. Second, as that count assigns greater values to projects that take more time to obtain funding, we subtracted the number of days from the sample maximum, which was 4017 days, so that larger values represent higher funding speed. Finally, we subtracted the average funding speed of projects in the same sector as a focal project from that focal project's funding speed, thus obtaining a measure that compares a PF investment funding speed with other projects in the same sector. To calibrate this indicator into fuzzy sets, we defined four benchmarks. The benchmark for *fully out* the set of high funding speed was the 25<sup>th</sup> percentile of the distribution of speed for all 3854 projects, in this case -61.81. The benchmark for *more out than in* was the



sample mean, in this case 0. The benchmark for *more in than out* was the median, a value of 207.19. Finally the benchmark for *fully in* was the sample's 75<sup>th</sup> percentile, a value of 266.63.

Regarding completion speed, we proceeded similarly. However, because data on the date of operations commencement was collected manually only for the projects in our sample, we used exclusively information on our sample of French projects. Again, we built a measure that compares the completion speed of a focal project with the average speed of projects in the same sector. We defined four benchmarks to calibrate this indicator into fuzzy sets. The benchmark for *fully out* the set of high completion speed was the 25<sup>th</sup> percentile of the sample, in this case - 345.42. The benchmark for *more out than in* was the sample mean, in this case 0. The benchmark for *more in than out* was the median, a value of 225.76. Finally the benchmark for *fully in* was the sample 75<sup>th</sup> percentile, a value of 411.58.

### **Causal conditions**

As we discussed before, our main causal condition are political connections. We evaluate two types of political connections: interpersonal relationships-based political connections and government experience-based political connections. Interpersonal relationships-based political connections are created when top business leaders have personal friends at high-level positions in the government (Coulomb & Sangnier, 2014; Fisman, 2001). These ties would potentially lead the firm to obtain advantages from the home country government. They could also be positively perceived by lenders in determining funding and by other stakeholder in facilitating the process of project development. We used an indicator of whether the sponsor firm's *CEO is Sarkozy's friend* to classify firms. We drew on Coulomb and Sangnier (2014) and followed similar procedures to create this measure. We used a list of businessmen cited as personal friends of Sarkozy's in two books about Sarkozy's personal and professional life (Chemin & Perrignon,

2007; Dély & Hassoux, 2008). Most of the individuals in the list were invited by Sarkozy and his wife for a dinner at the day of the election in 2007, before Sarkozy even addressed the French population. More importantly, most of those friendship ties were formed before 2007, some when Sarkozy was not yet a politician. Also, prior research has shown that the presence of these individuals among shareholders and top managers of French firms led to a 3% increase of the firms' value after Sarkozy's election (Coulomb & Sangnier, 2014), indicating that these connections are visible to the market. I, then, assigned a value 1 to cases in which the firm's CEO was one of Sarkozy's friends when the project was announced, a value 0, otherwise.

The second type of political connections, based on government experience, are created when business leaders have worked as top government officials prior to their business career, in which case they likely keep contacts in the government and acquire capabilities of understanding how the government operates (Bertrand et al., 2006; Kramarz & Thesmar, 2013; Lester et al., 2008). We used an indicator of whether the sponsor's *CEO is a former official* to assess these connections. Cases were assigned the value 1 if the CEO is a graduate from ENA, a school that traditionally educates top government leaders in France, or has worked as a top government official, and 0, otherwise. We assumed that prior experience in the government and membership to the ENA alumni network helps individuals to develop capabilities with respect to understanding how the government and the public policy process works (Bertrand et al., 2006; Kramarz & Thesmar, 2013; Lester et al., 2008). We relied on information contained on each CEO and directors' biographies in the sponsors' annual reports to code this variable. When biographies were not available in the annual report, we used alternative sources, such as company websites, Who's who in France, Business Week Executive biographies, and news articles.

We used these indicators to build two crisp sets. In the first one, a project is assigned as *fully in* the set of projects sponsored by firms with interpersonal relationships-based political connections if the CEO is Sarkozy's friend, and *fully out*, otherwise. In the second set, analogously, a project is *fully in* the set of projects sponsored by firms with government experience-based political connections if the CEO is a former government official, and *fully out*, otherwise. These two crisp sets are the focus of our analysis, as our predictions refer to the circumstances in which the presence (absence) of political connections may help sponsors obtain faster funding for and start operating their PF investments more quickly.

### **Other causal conditions**

Many other conditions may complement or substitute the effect of political connections in determining the speed of PF investments. Most of these factors are indicators of the amount of risk a lender would experience if providing funding for the project. They also reflect the difficulties a sponsor would face in order to effectively start operating the project. We assumed that the higher the risk, the larger the amount of time required by lenders to evaluate a project and provide funding and the larger the amount of time a sponsor would need to develop a project and start operating it.

The first condition we considered is sponsor-specific and refers to the extent of the sponsor's *prior experience* investing through PF. Lenders will probably evaluate such experience positively, as the sponsor signals its capability to make the project go through. Projects whose sponsors have more experience will, in turn, probably reach higher funding and completion speed. In order to build the fuzzy sets of PF investments experience, we first assigned values to a sponsor's experience depending on the number of prior years, within 2003-2012, in which a sponsor announced PF investments. The value ranged from 0 to 9. We built the fuzzy set by

assigning the following benchmarks: the 75<sup>th</sup> percentile for *fully in*, the median for *neither in nor out* and the 25<sup>th</sup> percentile for *fully out*.

The next condition, whether the *investment is in France* or abroad, refers to the location of the investment. Investments in France probably signal lower risk to potential lenders, favoring a facilitated provision of funding. Also, sponsors are probably more accustomed with home-country-based lenders that can better evaluate projects located in the home country. Finally, firms investing in the home country face no liabilities of foreignness which could delay the commencement of a project's operations. We measured this attribute with a binary indicator which is equal to one when the investment is made in France. We considered projects as *fully in* the crisp set of investments in France if this indicator is equal to 1, and as *fully out*, otherwise.

The third group of conditions is project-specific, as they refer to project features that may also affect the level of risk perceived by lenders and other stakeholders, and, therefore, project speed. The first of these features is the *project value*. The larger the project, the more risks are involved and the more commitments have to be made by sponsors to obtain funding and develop the project. We used information on all funded PF investments in the globe between 2003 and 2012 to define the following benchmarks to assign projects to the project size fuzzy set: the 90<sup>th</sup> percentile (\$991 million) for *fully in* the set of big projects, the mean (\$475.19 million) for *more in than out*, the 75<sup>th</sup> percentile (\$403 million) for *more out than in*, and the median (\$154 million) for *fully out*.

The second condition is the project's *debt to equity ratio* at the announcement date. This ratio indicates the level of risk entailed by a project, as the riskier the project, the less its capital structure at announcement date is based on debt rather than equity. PF investments usually have a high debt to equity ratio, of around 70%. We determined the following benchmarks for

assignment of projects to the high debt ratio fuzzy set based on the global sample of projects: the 75<sup>th</sup> percentile (100% debt ratio) for *fully in*, the mean (87.73% debt ratio) for *more in than out*, the 25<sup>th</sup> percentile (76.4% debt ratio) for *more out than in*, and the 10<sup>th</sup> percentile (66% debt ratio) for *fully out*.

Finally, the last condition refers to the project time of announcement and differentiates projects announced before from projects announced after 2007. We chose 2007 as the milestone because this year marks the election of Nicolas Sarkozy as president of France. We assigned projects to the crisp set post-2007 as *fully in* if the project was announced between 2008 and 2012 and as *fully out* if the project was announced between 2003 and 2007. Table 9 summarizes the factors used in our analyses and their calibration benchmarks.

**Table 9: Calibration of outcome and causal factors**

<b>Variable</b>	<b>Operationalization</b>	<b>Calibration Base</b>	<b>Calibration Benchmarks</b>
Funding speed	Time length between announcement date and funding date adjusted by the project sector	All 3854 PF investments announced worldwide during 2003-2012	Fully out: 25 <sup>th</sup> percentile More out than in: mean More in than out: median Fully in: 75 <sup>th</sup> percentile
Completion speed	Time length between announcement date and date of construction finalization or operations initialization adjusted by the project sector	Sample of 95 PF investments by French sponsors	Fully out: 25 <sup>th</sup> percentile More out than in: mean More in than out: median Fully in: 75 <sup>th</sup> percentile
Interpersonal relationships-based political connections	Sponsor firm CEO is a personal friend of Nicolas Sarkozy	Crisp set	Fully in: 1 Fully out: 0
Government experience-based political connections	Sponsor firm CEO has prior professional experience in a top position in the French government or is a graduate from ENA	Crisp set	Fully in: 1 Fully out: 0
Sponsor PF investment experience	Number of years in which the sponsor firm has undertaken PF investments previously	Sample of 95 PF investments by French sponsors	Fully out: 25 <sup>th</sup> percentile Neither in nor out: median Fully in: 75 <sup>th</sup> percentile
Domestic investment	Whether the investment is located in France or not	Crisp set	Fully in: 1 Fully out: 0
Project size	Project value in millions of dollars	All 3854 PF investments announced worldwide during 2003-2012	Fully out: median More out than in: 75 <sup>th</sup> percentile More in than out: mean Fully in: 90 <sup>th</sup> percentile
Ratio of debt	Ratio of debt to equity at announcement date	All 3854 PF investments announced worldwide during 2003-2012	Fully out: 10 <sup>th</sup> percentile More out than in: 25 <sup>th</sup> percentile More in than out: mean Fully in: 75 <sup>th</sup> percentile
Post-2007	Whether the project is announced between 2008 and 2012	Crisp set	Fully in: 1 Fully out: 0

## Results

Table 10 shows descriptive statistics and correlations between the raw measures – before set calibration – of our outcome and causal conditions. Most conditions are characterized by substantial variance. After centering speed by sector mean, funding speed varies from -2708.69 to 379.50, with an average of -246.69. That is, the projects in our sample are on average slower in obtaining funding than the average project in the same sector. We also observe substantial variance regarding completion speed, which varies from -5876.24 to 1456.76, with a standard deviation of 928.69. Regarding political connections, 32% of the projects are sponsored by firms whose CEO is a personal friend of Sarkozy and 40% by sponsors whose CEO is a former government official or an ENA graduate. These two measures are negatively correlated and most politically-connected CEOs are either a friend of Sarkozy or a former government official, but not both. Other conditions also show substantial heterogeneity. For instance, 31% of the projects in our sample are located in France, the average debt ratio is 82.63%, and 65% of the projects are announced between 2008 and 2012.

**Table 10: Descriptive statistics and correlations**

<b>Variable</b>	<b>Mean</b>	<b>S. D.</b>	<b>Min</b>	<b>Max</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>
1 Funding speed	-246.69	512.12	-2708.69	379.50	1.00							
2 Completion speed	0.00	928.69	-5876.24	1456.76	0.37	1.00						
3 Interpersonal relationships-based political connections	0.32	0.47	0.00	1.00	-0.05	0.09	1.00					
4 Government experience-based political connections	0.40	0.49	0.00	1.00	0.21	-0.10	-0.37	1.00				
5 Sponsor PF investment experience	3.72	2.60	0.00	9.00	0.32	0.13	0.07	-0.03	1.00			
6 Domestic investment	0.31	0.46	0.00	1.00	0.23	-0.01	0.04	-0.17	0.19	1.00		
7 Project size	910.57	1627.01	10.70	12000.00	-0.44	-0.08	-0.10	-0.03	-0.23	-0.23	1.00	
8 Ratio of debt	82.63	17.94	0.60	100.00	0.16	0.05	0.02	-0.09	0.17	0.37	-0.24	1.00
9 Post-2007	0.65	0.48	0.00	1.00	0.40	0.04	-0.12	0.10	0.61	0.10	-0.17	0.15

N=95 projects, 2003-2012, 31 host countries, 17 sponsors.



## **Funding speed**

Moving to the discussion of the fs/QCA results, we decided to define a minimum consistency threshold of 0.80 and a minimum number of cases in a solution as 3. In other words, in our final solutions, each combination leading to either high funding speed or high completion speed should include at least three projects in which the combination of causal conditions is present. Additionally, when the combination is present in the sample, high speed should be obtained in at least 80% of the cases.

In light of these requirements, we obtained a solution composed of only one combination of causal conditions that is associated with high membership of projects in the set of high funding speed. Table 11 provides a graphical representation (Fiss, 2011) of this solution. Black circles represent causal conditions that should be present and white circles represent those that should be absent to obtain the outcome. Larger circles represent core conditions stemming from the parsimonious solution of the fuzzy set analysis, and smaller circles stem from the intermediate solution, thus only including easy counterfactuals (Fiss, 2007, 2011; Ragin, 2008). This solution has a consistency of 0.81 and covers 14% of our sample projects, that is, it explains with 81% of consistency 13 projects that attained high funding speed relative to other projects in the same sector.

To obtain funding rapidly, projects should be characterized by two core conditions: they should be sponsored by firms with government experience-based political connections and they should be located in France. This result suggests that firms use their capabilities of knowing how the government works to assuage lenders' concerns regarding the project prospects. Additionally, these capabilities are probably more effective for projects in the home country, where the firm's CEO has acquired government experience. Also, as we mentioned before,

projects in the home-country are probably seen as less risky by lenders, which may contribute to making faster decisions regarding PF investment funding.

In addition to the two core conditions, all other causal factors contribute to the solution as peripheral conditions. In line with our predictions concerning the level of risk of a given project, to attain high funding speed, a project should be sponsored by a firm with strong experience with PF investments, the project should be small and with a high debt-to-equity ratio, all attributes of low-risk projects. Finally, projects should be sponsored by firms without friendship-based political connections and should be announced after 2007. In other words, projects that quickly obtain funding are substantially standard: they have both experience with PF investments and with dealing with the government, they announce a small project in the home country, and with the typical high debt-to-equity ratio.

**Table 11: Pathway for high funding speed**

	<b>1</b>
<b>Political Connections</b>	
Interpersonal relationships-based political connections	○
Government experience-based political connections	●
<b>Sponsor</b>	
Sponsor PF investment experience	●
<b>Host country</b>	
Domestic investment	●
<b>Project</b>	
Project size	○
Ratio of debt	●
<b>Time</b>	
Post-2007	●
<b>Overall Solution Consistency</b>	<b>0.81</b>
<b>Overall Solution Coverage</b>	<b>0.14</b>

This combination is a complete explanation for cases that belong to the set of high funding speed. Large circles represent core conditions; small circles represent peripheral conditions. White circles represent absence of a condition; black circles represent presence of a condition.

In contrast with the solution for high funding speed, in which only one path was observed in our analysis, Table 12 shows that there are five alternative paths to fail in obtaining funding quickly, or rather to obtain funding with a substantial delay compared to projects that were speedily invested in. Each column in the table represents an alternative pathway to high non-membership in the set of projects characterized by high funding speed. This solution has an overall consistency of 0.94 and covers 33% of the cases, that is, it explains 31 projects that obtained funding in a substantially slow way. The first three pathways for failure in obtaining fast funding are characterized by one core condition: the project is located in a foreign country. As we predicted, projects located outside of France may be subject to liabilities of foreignness that increase the risk perceived by lenders and, thus, slow down decisions concerning funding provision. Combination 2 indeed includes relatively risky projects. The peripheral conditions in this pathway are the absence of government experience-based political connections, absence of experience with PF investments and high project value. The only low risk attribute of these projects is the high debt-to-equity ratio. Finally, these projects should be announced before 2007.

Combination 3 and Combination 4, on the other hand, are not systematically characterized by high risk attributes. These pathways for failure in obtaining high funding speed require sponsors with government experience-based political connections and with experience investing through PF. Another major difference relative to Combination 2 is that, in Combination 3 and Combination 4, projects should be announced after 2007. The difference between Combination 3 and Combination 4 is that the former is characterized by low project value, another low risk feature, and the latter has an additional core condition, which is low membership in the high debt-to-equity ratio set, therefore a high risk feature.

Together, these three combinations seem to indicate two main interesting results. First, announcing projects outside of the firms' home country may involve delays in obtaining funding. Second, after 2007, lenders seem less sensitive to the various risk insurances sponsors can provide for their projects. Although projects meeting the attributes in Combination 3 and Combination 4 should be considered low-risk, they still fail in reaching high funding speed, whereas projects in Combination 2 are more logically prone to take more time to obtain funding, as they have many high-risk attributes. One possible explanation is that lenders became more cautious in providing funding after the financial crisis and penalize even projects with low-risk profile if they are not located in the sponsor's home country.

Combination 5 and Combination 6 are both characterized by one core condition: low membership in the high debt-to-equity ratio set. Thus, these should be quite risky projects for lenders. Additionally, projects in these two combinations are characterized by the sponsor's experience with PF investments and low project value, both of which should decrease the project risk. However, these projects are announced after 2007, which as we discussed before, may be related to lower effectiveness of low risk insurance mechanisms. The sponsors also lack government experience-based political connections, which indicates a lower capability to accelerate funding decisions by lenders. Projects in these two combinations differ in their location and on the presence of interpersonal relationships-based political connections. It seems that these two attributes substitute one another in determining a project failure to achieve high funding speed. Projects located in France should be sponsored by firms without friendship ties with Nicolas Sarkozy to attain slow speed of funding. On the other hand, projects located outside of France should be sponsored by firms with friendship ties to Sarkozy to fail achieving high funding speed.

**Table 12: Pathways for low funding speed**

	2	3	4	5	6
<b>Political Connections</b>					
Interpersonal relationships-based political connections		○	○	○	●
Government experience-based political connections	○	●	●	○	○
<b>Sponsor</b>					
Sponsor PF investment experience	○	●	●	●	●
<b>Host country</b>					
Domestic investment	○	○	○	●	○
<b>Project</b>					
Project size	●	○		○	○
Ratio of debt	●		○	○	○
<b>Time</b>					
Post-2007	○	●	●	●	●
Consistency	0.99	0.85	0.95	0.91	1.00
Raw Coverage	0.07	0.09	0.14	0.04	0.06
Unique Coverage	0.07	0.03	0.08	0.04	0.06
<b>Overall Solution Consistency</b>					<b>0.94</b>
<b>Overall Solution Coverage</b>					<b>0.33</b>

Each combination is a complete explanation for cases that belong to the set of low funding speed. Large circles represent core conditions; small circles represent peripheral conditions. White circles represent absence of a condition; black circles represent presence of a condition.

## **Completion speed**

Moving on to the results regarding completion speed, Table 13 shows the solution for projects that were very rapidly developed. This solution is composed of three different pathways that lead to high completion speed. The solution has an overall consistency of 0.94 and covers 18% of the cases, that is, 17 projects that go very rapidly from their announcement date to operations commencement.

Combination 7 is characterized by the following core conditions: the sponsor should not have political connections of any type, the project should be located in France and with low membership in the set of projects with high debt-to-equity ratio. That is, the low risk stemming from having a project in the sponsor's home country mitigates the lack of political connections and the low level of debt. The low debt may also stimulate the sponsor to accelerate construction and rapidly start generating cash flows. As peripheral conditions, this combination is characterized by high membership in the set of sponsors with experience in PF investments and low project value, which both reduce the project risk and facilitate construction. Finally, these projects are announced after 2007.

Combination 8 is characterized by six core conditions. As we predicted, it seems that political connections provide the conditions for projects to attain high speed even without an absolutely good risk profile. In this combination, the sponsor firm should have friendship-based political connections and the project should have high debt-to-equity ratio. However, the sponsor firm should have no experience with PF investments, the project should be located outside of France and should be characterized by a high value. Finally, the project should have been announced before 2007, which seems to indicate that friendship ties with Nicolas Sarkozy are

particularly useful to develop projects rapidly in foreign countries before Sarkozy's election as the president of France.

Finally, Combination 9 requires two core conditions: that the sponsor has government-experience political connections and that the project is located in France. This pathway suggests that the sponsor's capabilities to deal with the government are useful to accelerate the development of projects located in the home country, where the political connections were formed. Additionally, as peripheral conditions, the sponsor firm should have high experience with PF investments, the project should have a high debt-to-equity ratio and the project should be small, which characterizes low-risk projects. The project should be announced after 2007; thus, similarly to the results for funding speed, it seems that projects announced after 2007 are only capable of rapidly starting to operate if they meet several criteria of low risk simultaneously.



**Table 13: Pathways for high completion speed**

	7	8	9
<b>Political Connections</b>			
Interpersonal relationships-based political connections	○	●	○
Government experience-based political connections	○	○	●
<b>Sponsor</b>			
Sponsor PF investment experience	●	○	●
<b>Host country</b>			
Domestic investment	●	○	●
<b>Project</b>			
Project size	○	●	○
Ratio of debt	○	●	●
<b>Time</b>			
Post-2007	●	○	●
Consistency	0.85	0.99	0.97
Raw Coverage	0.06	0.06	0.07
Unique Coverage	0.06	0.06	0.07
<b>Overall Solution Consistency</b>			<b>0.94</b>
<b>Overall Solution Coverage</b>			<b>0.18</b>

Each combination is a complete explanation for cases that belong to the set of high completion speed. Large circles represent core conditions; small circles represent peripheral conditions. White circles represent absence of a condition; black circles represent presence of a condition.

Finally, Table 14 shows the solution for projects that do not achieve high membership in the set of high completion speed. The solution is composed of three separate pathways for low speed, which together have a consistency level of 0.87 and cover 24% of the cases. Projects in Combination 10 meet two core conditions: sponsors lack friendship-based political connections and the project is large. Both these core conditions and some peripheral conditions – lack of government experience-based political connection, lack of experience with PF investments, and location outside of France – are typically associated with high-risk projects which we predict to take more time to develop. The only low risk feature is the high debt-to-equity ratio. Finally, these projects are also announced before 2007.

Projects in Combination 11 are characterized by seven core conditions. Some increase the project risk: lack of government experience-based political connections, location in a foreign country and low debt-to-equity ratio. Others are presumably associated with low project risk: interpersonal relationships-based political connections, experience with PF investments and low value. Interestingly, these projects are announced after 2007. Again, similarly to the analysis of funding speed, it seems that projects announced after 2007 need to meet more low risk insurances in order to attain high completion speed. It also seems that the combination of friendship ties with Sarkozy after his election did not help sponsors to accelerate the development of their announced projects outside of France.

Finally, Combination 12 is characterized by projects meeting two core conditions: sponsors without friendship-based political connections and large projects. Both conditions seem consistent with low completion speed. Additionally, the project should be located outside of France and should have low debt-to-equity ratio. However, these projects should have government experience-based political connections and a sponsor with experience with PF

investments. In any case, these projects are also announced after 2007, which is apparently consistent with projects being unable to attain high speed even with a low risk profile.

**Table 14: Pathways for low completion speed**

	10	11	12
<b>Political Connections</b>			
Interpersonal relationships-based political connections	○	●	○
Government experience-based political connections	○	○	●
<b>Sponsor</b>			
Sponsor PF investment experience	○	●	●
<b>Host country</b>			
Domestic investment	○	○	○
<b>Project</b>			
Project size	●	○	●
Ratio of debt	●	○	○
<b>Time</b>			
Post-2007	○	●	●
Consistency	0.93	0.82	0.87
Raw Coverage	0.05	0.07	0.12
Unique Coverage	0.05	0.07	0.12
<b>Overall Solution Consistency</b>			<b>0.87</b>
<b>Overall Solution Coverage</b>			<b>0.24</b>

Each combination is a complete explanation for cases belong to the set of low speed to start operations. Large circles represent core conditions; small circles represent peripheral conditions. White circles represent absence of a condition; black circles represent presence of a condition.

## **Discussion and Concluding Remarks**

We investigated how sponsor-specific political connections influence the patterns of funding and completion speed of PF investments. We used fuzzy set qualitative comparative analysis to empirically analyze data from a sample of 95 PF investments whose sponsors include at least one of the largest firms listed in the Paris stock exchange, during the period between 2003 and 2012. We found that funding speed is contingent on the sponsor's political connections, on the sponsor's experience with PF, on other factors determining the project riskiness, and on whether the project is in the sponsor's home country or abroad. Moreover, apparently, firms without political connections must ensure more low-project-riskiness factors than firms with political connections in order to achieve high PF investments funding and completion speed.

One limitation of this paper is that it draws conclusions from an analysis based on PF investments by sponsors from a single country. Additionally, all sponsors belong to the list of large public firms in France and the sample is limited to the 2003-2012 period. All these features may reduce the generalizability of our findings. However, after comparing the projects sponsored by these firms to the full population of PF investments in the period, we are confident that French projects are substantially appropriate for an analysis of PF investments in general.

We make several contributions to the literature with this paper. First, we contribute to the literature on political connections by showing its relations to firms' strategies of using PF mode of investments and to their performance in obtaining funding for and developing these investments faster (Fisman, 2001; Zhu & Chung, 2014). Second, we contribute to the literature in international business, particularly the studies devoted to understanding how firms deal with economic and political risks in foreign countries (Delios & Henisz, 2003a; Frynas et al., 2006;

Vernon, 1980). Finally, we advance the understanding of how PF investments can be used to increase the chances of meeting the global needs for infrastructure investments (Esty, 2004; World Economic Forum, 2015).

## **CHAPTER 6: Conclusions**

## Overall Conclusion

The main objective in this dissertation was to examine how capabilities stemming from a firm's non-market engagement influence that firm's strategy and performance. While prior research has largely focused on investigating the effects of firms' political connections on financial and accounting performance indicators (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001; Goldman et al., 2009; Hillman, 2005), my research more deeply explores how political connections reflect a firm's political capabilities, and examines their effect on decisions and performance dimensions that are substantially entrenched in political considerations. More specifically, in the three essays constituting the core of this dissertation, I examined the impact of a firm's political connections on its international expansion strategy and performance. In the first essay, I have shown how firms' political connections modify the relationship between home-host ties and international strategy. In the second essay, I have shown how different types of political connections impact a firm's international investments amount and risk profile. Finally, in the third essay, I have shown how different types of political connections influence speed in project finance-based investments.

Overall, the three essays generated interesting insights to address the research question I sought to answer in the dissertation, "*How do political connections impact a firm's international expansion strategy and performance?*" Broadly, my findings suggest that political connections impact firms' strategies regarding the choice of location and the overall amount of their international investments, as well as how such investments are distributed across foreign countries with varying levels of expropriation risk. I also found that different types of political connections affect the speed with which firms succeed in obtaining funding and completing the



development of their large investments. These findings suggest numerous ways through which political connections may influence a firm's strategies and, ultimately, performance.

### **Contributions**

In combination, the three essays presented before help advance non-market strategy and international business literatures by addressing the issues, and underlying gaps, I have identified in these literatures in Chapter 1. In addressing these gaps, I have also made contributions to other streams of literature, as I explain in the following paragraphs.

Regarding the lack of studies on the influence of political connections on firm strategy, rather than simply examining the effect of political connections on a firm's financial performance, I analyzed their impact on a type of strategy that is highly entrenched in politics – i.e. international expansion strategy – and in which the effect of such political connections should be more visible and meaningful. The first and the second essays have shown that one of the main mechanisms through which political connections affect a firm's strategy is political influence. Politically-connected firms appear to be less affected by the presence of BIT-based credible commitments provided by potential host countries in choosing the location of their international investments. Also, politically-connected firms invest more internationally and concentrate their investments in riskier countries than their nonpolitically-connected peers. More interestingly, firms that are politically connected through friendship ties with governmental authorities increase their investments when such authorities become more powerful. Finally, in the third essay, I examined the impact of political connections on a type of performance that more closely relates to a firm's capacity to obtain advantages from the government than financial performance – i.e. the speed with which the firm can obtain funding and complete developing its large projects in infrastructure. Together, these results strongly suggest that firms perceive their

political connections as a “safety net” that enables them to make risky strategy moves, even in foreign locations. These firms are thus able to invest in locations that their nonpolitically-connected counterparts tend to avoid, and can benefit from first-mover advantages or face lower levels of competition.

This is an important contribution to the literature on political connections. While most prior studies stress the influence of political connections on firm performance and value, very little is known on how they influence firm strategies (Bertrand et al., 2006; Zhu & Chung, 2014). My finding that politically-connected firms are able to - and do - bypass formal inter-governmental ties when investing abroad advances the understanding of how politically-connected firms make distinct decisions relative to firms without these connections.

I also make contributions to strategy and international business literatures, particularly to studies regarding firms’ international investment location choice, by showing that firms are able to leverage political resources (i.e., political connections) built in their home country in order to overcome liabilities of foreignness (Hymer, 1976; Zaheer, 1995) and reduce the risks inherent in international business. Furthermore, I also advance the line of research that focuses on the home country as a resource (Cuervo-Cazurra & Genc, 2008; Delios & Henisz, 2003a, 2003b; Wan & Hoskisson, 2003), by showing that the effectiveness of such a resource depends on a firm’s need and ability to leverage it when doing business abroad. Overall, the first and second essays thus contribute to a better understanding of the impact of non-market strategies in international expansion strategies.

Finally, regarding the lack of studies on the differences between various types of political connections, I did not consider all political connections as identical, but have rather distinguished various types of political connections depending on whether they were rooted in friendship,

educational background or professional experience. Distinguishing different types of political connections allowed me to obtain a better understanding of the potential mechanisms underlying the impact of political connections on firm strategy and performance. Accordingly, in addition to showing the overall impact of political connections on firms' strategies, my findings indicate that distinct types of political connections affect different dimensions of a firm's international expansion strategy and performance differently. Firms seem to use their friendship-based political connections as levers to make decisions regarding the amount – but not regarding the level of expropriation risk – of their international investments. More interestingly, as the value of a firm's friendship-based political connections increases, the marginal benefits of international investment increases, encouraging firms to reconsider their focus on domestic business. Nonetheless, friendship-based political connections do not seem to impact the level of expropriation risk of firms' overseas investments. Instead, to invest in riskier countries, firms leverage political connections based on a common education background between the firms' top decision makers and government authorities.

In combination, these analyses allow me to make substantial contributions to the literature. First, I contribute to the global strategy literature. My results add knowledge to studies investigating how firms can benefit from their activities vis-à-vis the government in the home country to develop political capabilities that become useful in foreign countries with higher risk of expropriation (Cuervo-Cazurra & Genc, 2008; García-Canal & Guillén, 2008; Holburn & Zelner, 2010). Although a few studies have started to consider the role played by political connections in the home country on particular international strategies of emerging-country firms (Duanmu, 2014; Leuz & Oberholzer-Gee, 2006; Wang et al., 2012), the second and third essays in this dissertation are unique in showing that political connections influence international

expansion strategy of firms founded and headquartered in an advanced economy such as France. Additionally, my analysis goes beyond the idea of firms from a same home country sharing the same level of political capabilities (Cuervo-Cazurra & Genc, 2008; Holburn & Zelner, 2010), but proposes and empirically analyzes the effect of heterogeneity in political connections among firms from a same home country.

I also add to the literature on political connections, by comparing the effects of three types of political connections on firms' strategy. While most prior research examines the effect of only one type of political connection on firms' value (Coulomb & Sangnier, 2014; Faccio, 2006; Fisman, 2001; Goldman et al., 2009; Hillman, 2005), my research shows that different types of political connections have distinct effects on international expansion strategy and performance.

Regarding nonpolitically-connected firms, my research confirms prior results suggesting that inter-governmental ties are meaningful sources of investment protection and therefore explain international expansion strategies. I thus make a contribution to the stream of research on the effects of inter-governmental ties on FDI flows (Alcacer & Ingram, 2013; Kerner, 2009; Li & Vashchilko, 2010; Salacuse & Sullivan, 2005; Yackee, 2008), by analyzing firm-level data and focusing on BITs. I show that these organizations, and the underlying credible commitments they allow host countries to make, are only meaningful antecedents of international strategy for firms not holding political relationships with government authorities in the home country. Finally, my findings regarding the effect of firm size on the relationship between host country-based credible commitments and firm location choice suggest that firms may substitute political connections with other sources of political influence. It is notable that only very large size provides the same

benefits as political connections. This finding suggests that firm size proxies for other important correlates of political influence (Hillman et al., 2004), such as political activities and visibility.

In addition to the contributions to theory, across the three essays, my findings rely on extremely rich data about various types of political connections and international expansion strategies and performance by firms originating in several countries. The methods used in the second and third essays are relatively new in strategy and international business research and could be more extensively used. In the second essay, I used a method that allows the identification of within-firm and between-firms effects of political connections on firms' international expansion strategy in the same specification (Bartels, 2015; Bell & Jones, 2012; Mundlak, 1978). This method could be used to examine other antecedents of firm strategic decisions, contrasting their effects across firms and over time simultaneously. The method could also be applied to better understand the performance implications of such decisions, comparing both firms' long-term performance persistence and short-term changes in performance due to strategic actions. In the third essay, I used a fuzzy sets-based method that permits the identification of combinations of factors leading to an outcome while allowing for equifinality, causal complexity and asymmetric results.

To sum up, the dissertation helps advance non-market strategy and international business literatures by analyzing the impact of different types of political connections on firms' international expansion strategy and performance. First, I analyzed the impact of political connections on a type of strategy that is highly entrenched in politics – i.e. international expansion strategy. Second, I distinguished various types of political connections, being thus able to obtain a better understanding of the potential mechanisms underlying the influence of political connections on firm strategy and performance. Finally, I examined the impact of

political connections on a type of performance that more closely relates to a firm's capacity to obtain advantages from the government than financial performance.

### **Limitations**

Naturally, the dissertation has several limitations. One of the most important limitations is that the potential role of political connections as liabilities for firms (Aggarwal et al., 2012; Kramarz & Thesmar, 2013; Siegel, 2007) has neither been extensively discussed nor empirically examined over the three essays. Although I do analyze the impact of political connections on firm performance in the third essay, the dissertation has been mainly focused on the strategic implications of political connections. It is possible that in some cases political connections create pressures for firms to make decisions that align with the home country government's interests. If such interests are misaligned with the best interests of the firm, such a strategic move could eventually lead to poor performance. In other words, it is possible that in some cases the firm is not making distinct strategic moves relative to nonpolitically-connected peers because it has access to a more unconstrained set of strategic options, but the very opposite, i.e. the firm could be following governmental guidelines in how and where to invest abroad. Also, as political connections such as those we measured over the three essays are held by individuals and not by firms, it is possible that these individuals use their connections for private benefit in detriment of the firm's long term interests (Aggarwal et al., 2012). Future research relying on additional data could explore these possibilities. First, as performance results from strategic moves incited by political connections, a mediation model could be developed in which strategy and performance heterogeneity across firms is simultaneously examined. Second, analyzing the coevolution of a firm's international investments and the home country government's pattern of political connectedness with particular foreign countries could help verifying the potential negative effect

of political connections. If connected firms do not change their pattern of location choice according to changes in the home country foreign affairs while other firms do, the unconstrained choice hypothesis would be better supported. If, instead, politically-connected firms change their behavior significantly more than other firms, aligning investments with home country government foreign policy, then the government pressure alternative explanation would be more relevant.

Also, the various measures of political connections that I have used across the three essays capture different strengths of connections and are heterogeneously accurate in representing a firm's political capabilities. The measure I used in the first essay, in particular, captures the existence of political ties between firms and their government authorities towards the beginning of the period during which I observe foreign investment decisions. As a result, some of the political ties I have taken into account may have faded over time. I did run complementary analyses to deal with this issue, as described in the essay, but future research could seek to identify more accurate and dynamic levels of political connections in cross-national samples. Furthermore, although my arguments in all three essays refer to social ties existing between decisions makers in the firm and at the government, implying that they know each other and exchange information and favors with one another, my measurements are proxies of such ties. For example, some ENA graduates may not know each other or have opposite political ideologies and agendas relative to one another, which would prevent them from exchanging information and favors. Future research could distinguish individuals according to their political ideology and to the period of their professional experience in the government to obtain more refined measures of political connections. Finally, my analysis of friendship political connections in the second and third essays also requires more elaboration, as it focuses on only

one politician. Although Sarkozy is a special case, as he represents a disruption in the command of the French government, given his business orientation and non-alignment with traditional political elites, future research could identify firms holding friendship ties with other top politicians.

### **Future Research**

This dissertation represents the beginning of a research program that I plan to pursue in the future as an assistant professor. While my main priority is to improve the three dissertation essays and publish them in academic journals, I have also been working on several other projects. These projects aim to advance knowledge in the fields of non-market and international expansion strategies. In the following paragraphs, I provide a brief summary of a selection of projects that I consider extremely relevant to expand what I did in the dissertation.

First, regarding the origins of political connections, I have started a project in which I examine the patterns of generation of political connections by firms as a two-sided matching process. Specifically, I examine the recruitment and retention of politically-connected members in French firms' boards of directors as a result of a process in which firms and board members select one another according to their specific interests. In order to empirically investigate this process, I use an expanded version of the political connections data deployed in the second essay.

Second, I have a few projects investigating the strategic implications of political connections. In a paper with Pierre Dussauge and Rahul Anand, we explore the role of political connections on firms' corporate reconfiguration. Specifically, we examine how firms' political connections at the board level and political connections at the top management team level differentially affect their acquisition strategies, both domestically and internationally. We use



data on political connections enjoyed by all French firms listed in the French stock exchange to empirically test our hypotheses. In another project, I investigate how firms use their political assets and capabilities to mitigate problems they may face in countries characterized either by suboptimal intellectual property protection or by high distance from knowledge resources. I will use data on the innovative activities of the largest French firms to analyze these phenomena.

Third, I have some projects exploring the effects of institutions and international relations on firm strategy. In a paper co-authored with Denisa Mindruta and Glenn Hoetker, we examine the impact of the macro-institutional environment on exploitation-exploration innovation. Our analysis of all patented firm inventions in 22 countries during 1985 to 2008 demonstrates the role of institutions regulating the education, labor, finance, and corporate control markets in explaining cross-country and cross-temporal variation in the level of exploitative and exploratory innovation. In another working paper, I examine, with Panikos Georgallis, the impact of public policies in attracting foreign investments in the solar electricity industry in Europe. Finally, in a paper co-authored with Paul Vaaler, we investigate strategic issues related to large projects worldwide. Specifically, we examine whether and when international, publicly-legislated and privately-contracted dispute resolution mechanisms reduce risk for foreign investing firms. We developed hypotheses and found evidence of substitution relationships between these various forms of dispute resolution mechanisms.

In the longer run, I plan on continuing to do research in the area of non-market and global strategy. Some of the projects I have been working on will generate follow-up papers. For instance, the paper with Denisa Mindruta and Glenn Hoetker suggests some interesting unaddressed questions concerning how macro-institutions influence firms' choices regarding the level of exploration and exploitation they pursue. These questions will generate interesting new

research endeavors. Also, the study of the impact of supranational institutions on firm strategies is also a relatively overlooked area of research. For instance, little is known about the heterogeneity between international treaties and the patterns of their actual deployment by firms in order to access international arbitration, a topic that I would really enjoy to investigate. Finally, there are many interesting research opportunities concerning cross-national comparison of the effects and origins of political connections, particularly in emerging countries such as Brazil, Russia, India and China.

All in all, I aspire that my research will contribute to provide a better understanding of how non-market and market strategies are integrated by firms and on the resulting theoretical, managerial and policy implications of such integration. I believe this research can have significant effects on the fields of strategy and international business.

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**Titre :** Trois Essais sur l'Influence des Relations Politiques sur la Stratégie d'Expansion Internationale des Entreprises

**Mots clés :** Relations politiques; stratégies d'expansion internationale; stratégies politiques; stratégies de localisation; traités internationaux d'investissement.

**Résumé :** Cette thèse est composée de trois essais, chacun contribuant à mieux comprendre la façon dont différents types de relations politiques affectent les stratégies d'expansion internationale et la performance des entreprises. Le premier essai examine le rôle des relations politiques comme modérateur de la relation entre les attributs du pays hôte et le choix d'investir dans ce pays par des entreprises. Nous examinons le cas des premiers investissements dans les pays concernés par des entreprises du secteur manufacturier au cours de la période 2003-2010. Les autres essais examinent le rôle des relations politiques comme antécédents directs des décisions et des performances des stratégies d'expansion internationale des entreprises. Le deuxième essai étudie l'influence des différents types de relations politiques dans l'ampleur et le profil de risque des investissements internationaux des entreprises. Enfin, le troisième essai analyse le rôle des connexions politiques en tant que facteur explicatif de la capacité des entreprises à accélérer le financement et le développement de leurs projets. Les deux derniers essais sont testés sur une base de données originale recensant les relations politiques dont bénéficient les plus grandes entreprises françaises au cours de la période 2003-2012.

**Title :** Three Essays on the Influence of Political Connections on Firms International Expansion Strategy

**Keywords:** Political connections; international expansion strategy; nonmarket strategies; location choice; international investment treaties.

**Abstract:** This dissertation is composed of three essays, each contributing to address part of the puzzle regarding how different types of political connections affect firms' international expansion strategies and performance. The first essay examines how political connections moderate the relationship between host country attributes and international strategy in a sample of greenfield investments in manufacturing during the 2003-2010 period. The second and third essays examine how political connections directly impact a firm's international expansion strategies and performance. The second essay investigates the role of different types of political connections on a firm's international investments amount and risk profile. Finally, the third essay analyzes the role of political connections as an explanatory factor of firms' ability to accelerate the provision of funding and development of their project finance-based investments. Both the latter two essays rely on an original dataset on various political connections enjoyed by the largest French firms during the 2003-2012 period.