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RESEARCH ARTICLE

The Differential Effects of Minority State Ownership Types on the Internationalization of Emerging Market Multinationals from Democratic States

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Abstract We argue that governments use different types of minority state ownership in domestic multinationals to balance the provision of public and private goods and maximize political survival in emerging market democracies. Using a sample of Brazilian multinationals, we combine instrumental and fixed-effects regressions with an in-depth case study in order to measure and describe the effects of two types of ownership ties. We show that ownership through state-controlled institutional investors has a positive effect on the internationalization level of multinationals, whereas the ownership by state agencies and state-owned enterprises shows an opposite effect. By looking at these effects from the perspective of the political survival of democratic rulers, we contrast our results against the empirical research on multinationals from authoritarian states.

Keywords Political ties · Minority state ownership · Emerging market multinationals · Democratic states

1 Introduction

The relationship between businesses and the government has been a topic of interest in the International Business literature for many years (Boddewyn and Brewer 1994). A popular approach to this topic is to explain the effects of having a close proximity to the government by looking at these interactions as political

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ties, or “boundary-spanning personal and institutional linkages” (Sun et al. 2012, p. 68).

Political ties are more salient for firms doing business in and from emerging markets (Guillen and Garcia-Canal 2009; Peng et al. 2008). Emerging market multinationals (EMNEs) build political ties as a way to overcome institutional voids or to motivate state actors to provide them with resources and preferential treatment (Faccio et al. 2006; Khanna et al. 2005). Despite the fact that political ties are pervasive across all emerging economies, empirical research on their potential outcomes has mostly focused on the Chinese context (Sheng et al. 2011; Li et al. 2008, 2009; Shi et al. 2014). China has unique economic and political systems that diverge from the political economy of western democracies, which we consider, limits the external validity of the findings.

We explain this by pointing to the political economy literature on political survival (Bueno de Mesquita et al. 2003) which posits that representative democratic rulers from emerging economies make different decisions than authoritarian ones concerning the provision of public and private goods to their supporters. We draw from this literature to advance our hypotheses that democratic governments use different types of political ties arising from minority state ownership in domestic multinationals to balance the provision of these goods and maximize political survival. State ownership is theoretically and empirically relevant because it grants the firm access to government resources while allowing the government to gather information regarding the firm’s strategy and corporate governance (Wu et al. 2012). The phenomenon of minority state ownership is pervasive in emerging economies, representing 20–30% of all companies in which the state has equity (Musacchio and Lazzarini 2014).

We argue that minority state ownership has a dual purpose: It serves as a channel for the delivery of private goods, such as direct subsidies, preferential treatment and information to the elite group of multinationals, and it also serves as a grabbing hand to divert private investments to the provision of local public goods like jobs. While the former boosts international expansion, the latter hinders the internationalization of these firms. We investigate the differential effects of two types of minority state equity: Ownership by state institutional investors, which encompasses pension funds and development banks; and ownership by state agencies and state-owned enterprises (SOEs), such as the national treasury, government agencies, or state-owned enterprises under full control of the government. Because these two types of ownership have different governance profiles, we argue that governments use the former to boost the international expansion of their national champions, and the latter to hinder internationalization.

We test our hypotheses in the context of Brazil. The country provides a suitable context: It is a vibrant democracy with political party fragmentation, competitive elections and where the government uses equity ownership to implement a state-centric industrial policy (Pargendler 2015). We develop a multi-method research design. First, we estimate fixed-effect and instrumental-variable regression models to measure the hypothesized effect and, then, we unveil the underlying mechanisms in an in-depth case study. The qualitative analysis exposes the influence of state-ownership on the corporate governance of the firm and produces an effect on its internationalization.

We aim at delivering three contributions. First, we theorize about the effects of state ownership on the internationalization of domestic multinationals in democratic states using a theoretical framework that unifies existing empirical research in authoritarian and democratic states. Second, we show under which conditions minority state ownership ties have positive and negative effects on the internationalization of EMNEs. Finally, we unveil some of the mechanisms through which state actors, as minority shareholders, influence the governance of multinationals and affect their internationalization.

2 Research Background and Hypotheses

2.1 The Differential Effects of Political Ties

Research on political ties suggests that firms can gain political favors, special treatment and fiscal incentives as a result of their closeness to the state (Hillman 2005; Faccio et al. 2006). While research on these ties originally pointed to how they led to higher performance outcomes, recent studies posit that, under specific circumstances, they may actually lead to neutral or negative results (Sun et al. 2012). In the case of emerging economies, empirical research shows similar conclusions (Cheung et al. 2010; Sun et al. 2015). Zhu and Chung (2014) provide evidence on the negative effects of political ties associated with rival parties on unrelated diversification. Cheung et al. (2010) show the adverse effects of state-ownership concentration on excess returns to minority shareholders. Li et al. (2008) point to the efficiency level of ties, indicating the inverse U-shape effect of the interaction between foreign firms and political ties on performance.

There are different levels of analysis for studying political ties. Sun et al. (2012) catalogue these levels in four archetypes: Organizational linkages (established by structural links), interpersonal relationships (as those held between managers and politicians), and finally two types of personal-organizational linkages (either between political actors and key firms, or between managers and political institutions). For our study, we focus on one source of organizational linkages: The minority state-ownership as a political tie. Ownership ties yield direct access to the firm and therefore the possibility of a higher degree of direct influence by the state (Wu et al. 2012). Minority state ownership is a "new form of state involvement that does not entail majority state control" (Inoue et al. 2013, p. 1776). While minority state ownership is a key feature of emerging economies (Peng and Luo 2000; Inoue et al. 2013), equity holders are diverse and range from national development banks to fully state-owned firms (Bremmer 2009; Wu 2011).

2.2 Minority State Ownership and the Internationalization of EMNEs

The empirical literature on the effect of political ties through state ownership in EMNEs has recently seen an exponential growth due to the importance of Chinese multinationals in the world. Previous research on non-Chinese firms focused on the internationalization of SOEs from a resource-seeking perspective, that is, as vehicles for securing global cash flow (Choudhury and Khanna 2014) or for seeking resources needed locally, such as oil and minerals (Choudhury and Khanna 2014). The first empirical works on outward FDI of Chinese state-owned multinationals also focused on securing raw materials to be used back at home (Cai 1999). Later, Zhang and Van Den Bulcke (1996) modeled OFDI coming from China as an instrument to balance an entrepreneurial or profit driven orientation with the influence of the governmental bureaucracy. Nolan (2001) shows that the direct advantages received by the government, such as loans, procurement and protected markets, are the major reason for success of Chinese multinationals with large state ownership.

Recently, empirical studies build on the importance of the degree of state ownership as determinants of the outcome of the internationalization of the firm. Child and Rodrigues (2005) argue that the role of the state in Chinese firms will be distinctive when it retains "some (but not total) ownership in the companies" (p. 400). Buckley et al. (2007) argue that Chinese firms profit from their degree of state-ownership to access lower cost capital that allows them to undertake riskier projects. Pan et al. (2014) find supportive evidence on the positive effect of state ownership for reducing the effects of the heterogeneity of foreign institutional environments on subsidiary ownership. Some case studies illustrate the positive effect of minority ownership on FDI such as that of TCL, one of China's largest cellphone manufacturer (Deng 2009). Finally, Cui and Jiang (2012) show that firms having the state as owners increase their dependence on home country resources.

This previous empirical research indicates that the state ownership on EMNE serves the dual purpose of alleviating market failures and implementing public policies (Cuervo-Cazurra et al. 2014). While the existing research has added considerable knowledge about the relationship between state ownership and internationalization of EMNEs, we argue that focus on the Chinese context has prevented new discoveries. Because democratic governments face different constraints that those of authoritarian regimes, we hypothesize that state ownership heterogeneity produce differential outcomes on the internationalization of EMNEs from these countries.

2.3 Hypothesis Development

We develop hypotheses about the differential effects of minority state ownership on the internationalization of EMNEs from democratic states with free and competitive elections. We argue that because of the differences in political institutions, governments from these countries come to different decisions concerning how to use minority state ownership to affect the strategy of domestic multinationals. To derive our hypothesis, we first describe the reasons why democratic governments make particular decisions concerning the balance of public and private goods provision. Second, we detail why minority state ownership is a viable instrument for governments to implement public policy decisions. Finally, exploring the home country context of EMNEs, we present our predictions on the effects of different types of minority state ownership on the internationalization of these firms.

We begin by drawing from the political economy literature on the logic of political survival (Bueno de Mesquita et al. 2003). Rulers need to handle challengers in both democratic and authoritarian regimes. The political survival of a ruler is a function of how he or she gathers a winning coalition among the 'selectorate', i.e., individuals who have the influence and power to choose who the next ruler will be. Authoritarian rulers need to please a small number of elite members, or cronies, to remain in power and are therefore more concerned with the provision of private goods for the individuals of the wining coalition than with the provision of public goods for the population. In representative democracies, the number of constituents that effectively choose the next ruler in free and competitive elections is considerably larger than the selectorate of authoritarian regimes. The consequence of this difference in size for the democratic ruler is that the provision of private goods is more expensive than the provision of public goods for the supporting constituents (Bueno de Mesquita et al. 2003).

It is not only the size but also the composition of the winning coalition that affects the balance between the provision of private and public goods (Gallagher and Hanson 2013). This explains why authoritarian countries like China do invest is some public goods, such as education and economic growth, while holding the provision of protection of individual rights, of constitutional grounding for its judiciary system, and of political freedom and representation (Qian and Weingast 1996). For example, the decision to open the country to globalization was closely tied to the preferences of some top-ranked individuals from the Communist Party of China. This decision gave local leaders more leverage to negotiate with foreign multinationals, with the sole objective of achieving the desired performance goals of the country, established unilaterally (Weingast 1995; Breslin 2011). The opening also pushed the state to invest massively in Chinese multinationals in order to increase their political influence (Guo 2007). Interestingly, this policy was aimed at pleasing key supporters with private goods (local leaders and a burgeoning entrepreneurial class) but also had economic growth as an important by-product (Gallagher and Hanson 2013).

The size and preferences of these individuals also matter to determine the optimum offer of public and private goods. As the size of the winning coalition necessary to elect the ruler increases in a democracy with competitive elections, the threat of the challenger also increases, which leads the ruler to diversify public policies to include a larger number of constituencies (Milner and Kubota 2005). However, the power distribution in the selectorate is not homogenous, as some individuals are more influential than others because they provide the ruler with critical resources to win an election. As a consequence, the ruler has strong incentives to provide private goods to these highly influential individuals (Gallagher and Hanson 2013).

Therefore, in order to maximize political survival, representative rulers in a democracy with competitive elections need to create a more diverse set of public policies than authoritarian rulers do. This might explain why in democracies the distribution of public goods becomes more transparent and generalized amongst different stakeholders (Armijo and Kearney 2008). In addition, public leaders face more scrutiny from challengers as a way of swaying electoral outcomes (Lam 2000). These conditions will be further exacerbated in the presence of multi-party systems

(Block et al. 2003) as well as under fixed-timed elections (Kayser 2005). These theoretical predictions have straightforward implications to our hypotheses about the differential effects of types of minority state ownership.

We present three arguments that minority state ownership is an effective instrument to increase government discretion in implementing public policies about the provision of private and public goods. First, governments are particularly interested in the performance of large firms because these symbolize the state of the economy, which is a key strategy to secure voters (Frey and Schneider 1978). However, an uncontested state power in fully owned state companies SOEs makes these companies subject to special and restrictive legislation to curb possible abuse by the state (Pargendler 2015). As minority owners, on the other hand, the state does not need to fully disclose its activities, and the company remains private and outside the domain of restrictive legislations.

Second, even as minority shareholders, the state may uphold a privileged position of influence in several ways. The state can profit from the reciprocity expected from political activity to demand having a more influential voice than the one granted by its shares (Sun et al. 2012). The state can gain power above its voting rights by coercing the firm under the threat to alter the regulatory environment, increase competition or block access to capital in times of financial instability (Bremmer 2009; Musacchio and Lazzarini 2014). Finally, even if a board seat is not granted, the state is in a privileged position to negotiate favorable shareholder agreements in order to acquire more influence on the decision making of the company (Pargendler 2015).

Third, by securing influence in the corporate governance of the firms, the government can harness the entrepreneurial energy of the country and exercise direct influence and great discretion over economic outcomes in ways that could not be possible through the traditional means of the federal budget (Pargendler 2015). In a democratic state this is a cheap and viable alternative as ownership carries fewer costs to operationalize than other policy alternatives with more immediate results (Murtha and Lenway 1994).

Minority state ownership is therefore an attractive instrument to grant political survival. We predict that governments of democratic states will implement a more diverse set of state ownership positions in order to achieve the right balance between public and private goods provisioning and thus maximize their political survival. This leads to our hypotheses on the differential effects of types of minority state ownership. We argue that the effects of minority state ownership will differ depending upon the governance profile of the agent chosen by the government to hold the equity (Ryan and Schneider 2002; Inoue et al. 2013).

We model two distinct types of state ownership: State institutional investors and ownership by state agencies and SOEs. State institutional investment is the equity held by institutional investors that are controlled by the national government, such as the pension funds of SOEs or state-controlled development banks (Lazzarini and Musacchio 2010). State institutional investors are more likely to impose stricter governance practices and a long-term orientation of the expected returns (Pargendler 2015). For instance, state institutional investors are more likely than state agencies to conduct corporate governance practices, encouraging more transparency and reducing the risk of misrepresentation of voter rights (Chaganti and Damanpour 1991;

Connelly et al. 2010). State institutional investors are also more prone to undertaking capital-intensive projects that do not generate rents in the short term, a key feature of foreign direct investment (Inoue et al. 2013). These features change state institutional investors to be more accountable to markets, curbing the opportunistic rent-seeking behavior of political decision-makers (Bushee and Noe 2000).

Ownership through state-controlled institutional investors is the prototypical form of minority state ownership in the state capitalism version of industrial policy (Lazzarini et al. 2015; Pargendler 2015). These firms are essential for achieving industrial policy targets (Kee et al. 2013; Luong and Sierra 2015), often being referred to as 'national champions' (Soete 2007). This type of state ownership represents a direct transfer of private goods from the state to the chosen elite firms as they become recipients of subsidized finance and enjoy privileged information and preferential treatment by the regulators (Finchelstein 2017; Hennart et al. 2017). These firms are preferred over others not only because they possess the organizational capabilities needed to carried out industrial policies, but also because they signal their willingness to participate in the developmental agenda, especially through the financial support of political candidates and parties (Lazzarini et al. 2015). As a secondary effect, the state's presence in the design and deployment of such investments will provide some public goods as by-products of this development policy,[1] as these firms become exposed to a more competitive environment (Rasiah et al. 2010). The consequence will be reverse knowledge transfer in the form of new competences, processes, technology or innovations, inducing gains in productivity (Ambos et al. 2006).

Hence, we propose the following hypothesis:

Hypothesis 1: Political ties through ownership by state institutional investors will positively influence the internationalization level of EMNEs.

Representative rulers in democratic states cannot solely rely on the provision of private goods to a narrow group of influential firms and their by-product effects on industrial development. In order to maximize political survival, these rulers need to address a broader set of public goods (Bueno de Mesquita et al. 2003), especially those that make it costlier for challengers to sway voters in an election. Therefore, the minority state ownership aimed at increasing government discretion in the provision of these public goods will have a negative impact on the internationalization of EMNEs. This is because foreign direct investments can have a negative impact in job creation, lead to the circumvention of monetary policies, transfer capital abroad, reduce the taxes collected, decrease productivity gains, generate 'brain-drain' (due to the expatriation of personnel) and cause technology or national security information leakages (Wells 1971).

Ownership by state agencies and SOEs is preferred when the intention is to increase the short-term provision of public goods such as job creation and inflation control. This type of equity comprises all shares acquired by government

[1] Another consequence of the provision of these private goods is corruption. The illegal money collected by corrupt leaders can be used for personal enrichment, as well as to finance their political campaigns.

agencies, ministries, central banks as well as by majority state-owned companies. The particularity of this type of investment is the immediacy of communication and connection between the government actors and the parties they represent (Boubakri et al. 2009; Shleifer and Vishny 1994). This type of ownership has as a grabbing hand effect as it controls the rights or access to a resource (Bass and Chakrabarty 2014) and politically distorts private investment for electoral purposes (Pargendler 2012; Shleifer and Vishny 1994). It also produces an additional by-product: The provision of private goods for political allies. Because it is directly connected to the political nucleus of the government, ownership by state agencies and SOEs is less insulated against political pressures for rent distribution. This type of ownership serves as a direct channel for political decision-makers to use the firm to distribute rents, patronage, or to serve favoritism purposes (La Porta and Lopez-de-Silanes 1999).

Hence, we propose the following:

Hypothesis 2: Political ties through ownership by state agencies and SOEs will negatively influence the internationalization level of EMNEs.

3 Empirical Strategy

3.1 Research Setting

Our hypotheses explore the effect heterogeneity of political ties on the internationalization of emerging multinationals. We tested our model using data from Brazilian multinationals. The country offers a suitable setting for this research, as it provides the combination of strong state presence with free competitive elections. Brazil falls within the category of Newly Industrialized Countries (NICs), comprising Latin American and East Asian countries (Haggard 1990), which embraced government-led industrial policies to respond to pressures to globalization in the late 1980s and early 1990s. Despite the fact that the government led market reforms, the state remained an important player in the economy (Lazzarini et al. 2015). On the political side, Brazil is a vibrant democracy with free and competitive elections. The electoral system based on large district sizes and open lists make reelection too costly (Samuels 2002). As a result, politicians have strong incentives to secure political rents and to trade them for support by engaging in an individualistic relationship with businesses (Schneider 2004; Maxfield and Schneider 1997). As it is the case with many other newly industrialized economies, big businesses emphasize the importance of their political ties to as a survival tactic (Marquis and Raynard 2015; Schneider 2009).

3.2 Research Design

We developed a multi-method research design. We first estimate econometric models using a panel dataset of Brazilian multinational to test hypotheses H1 and H2.

Then, we show the findings of an in-depth case study to unveil the mechanisms through which minority state ownership affects the internationalization decisions.

3.2.1 Econometric Models

We restrict our sample to publicly traded Brazilian multinationals in order to alleviate some of the reliability issues frequently found in data from emerging economies (Hoskisson et al. 2000). We gathered data on internationalization levels, as well as on their financials and ownership structure to compose an unbalanced panel of multinationals ranging from 2006 to 2010. During this period, the country showed high levels of outward direct foreign direct investment coupled with an industrial policy that focus on state investments, particularly through the National Development Bank (BNDES). The final sample consists of 146 observations of 38 multinationals. These sampled firms are representative of the population of Brazilian multinationals. Appendix shows the names and industry of the sampled firms.

Dependent variable: In order to measure the level of internationalization, we used the transnationality index published by Valor, a major publisher in Latin America. This index follows a standard methodology to compute an average of the percentage of total assets, employees and revenues abroad. To increase reliability, we cross-matched the reports of Valor with the publications of Exame and America Economica, two other major Latin American publishers specialized in business (e.g., Guillen 2000; Khanna and Rivkin 2001). For robustness, we also tested our hypotheses using the individual components of the transnationality index as dependent variables.

State ownership: The ownership by state institutional investors aggregates voting shares owned by the pension funds of the state-owned bank Banco do Brasil and of the state-owned oil company Petrobras, and by the equity arm of the National Development Bank (BNDES). These state-controlled institutional investors are the most important institutional investors in Brazil (Pargendler 2015). The metric for the ownership by state agencies and SOEs aggregates voting shares owned by the federal, state, or municipal treasuries, or through enterprises in which the state has majority control or full ownership (SOEs). Figures for each multinational in a given year are the ratio of the sum of these shares to the total voting shares at the end of the year.

Control variables: Depending on model specification, we used foreign capital (the ratio of the equity hold by foreign investors to the total equity), firm size (the natural logarithm of total assets), a proxy for capital expenditure (the variation of investments in fixed assets relative to the previous year), operational profitability (the ratio of earnings before interest and tax to total assets), the founding year as a proxy for knowledge accumulation, whether the firm is affiliated to a business group, the non-voting counterparts of the two hypothesized types of minority state ownership, industry and firm fixed effects, and year dummies. For robustness, we also controlled for the interaction between the two types of ownership. This makes possible not only to control for any possible joint effect but also to isolate the main effect of one type of ownership for the particular case when the other type is absent. Finally, because the appearance in the transnationality index is not random, but self-reported by the multinationals, we control for possible sample selection bias. We estimated the inverse Mills ratio (IMR) using the sample of all listed Brazilian firms in the period. We added the IMR as a control variable in the final models.

Instrumental variable: While ownership by state agencies and SOEs are detrimental to internationalization, firms willing to boost internationalization would be prone to seek support from state institutional investors in the form of important private goods, such as direct subsidies, privileged treatment and information (Hennart et al. 2017). Capable firms or firms with internationalization projects already in place are more likely to be targets of state-controlled investors willing to invest in international expansion. These omitted variables make endogeneity a possible issue in modeling the effect of this ownership type on internationalization. Some of these omitted variables are time-variant and are not captured by firm-level fixed effects. We also estimated instrumental regression models to alleviate this problem. We built an instrument based on corporate campaign financing and exogenous electoral results. The rationale behind this instrument is that campaign financing is a way to pay for the private goods that come with minority state ownership by state-controlled institutional investors. Firms that signal their support to the government are more likely to be part of the elite group and become national champions, which are the preferential targets of state-controlled institutional investors (Pargendler 2015). Empirical research using data from Brazil has shown that firms donating to political campaigns have privileged access to equity and debt from the National Development Bank (Lazzarini et al. 2015) and show lower capital costs (Claessens et al. 2008). The Brazilian legislation allows for direct corporate political contribution to candidates and Brazil's electoral laws grant access to detailed information regarding donations made up to the candidate level. Using data from the Electoral Supreme Court (TSE). We were able to track not only the participation of the donating firms but also the number of winning and losing candidates among recipient candidates for each firm in a given election. Since the election results are not subject of firm decision, we used the difference between the number of winning and losing candidates to proxy for the firm's 'electoral performance'. We interacted this measure with the firm industry to build an exogenous instrument for the ownership by state institutional investors. The interaction with industry is important because some sectors are more attractive to the government as they are more important to implement the government agenda.

Equation 1 is the general model specification form. The dependent variable y is the internationalization level of firm i in year t. The variables x_1 and x_2 are the state ownership by institutional investors and the state ownership by government agencies and SOEs. The coefficient β_1 provides information for hypothesis 1, and the coefficient β_2, for hypothesis 2. The coefficient β_3 models the interaction between the two ownership types. The other elements are vectors representing the set of control variables (δ) and the error term (e).

$$y_{it} = \beta_0 + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_1 x_2 + \delta + e_{it}. \tag{1}$$

We estimated four models using these variables. Models 1 and 2 are fixed-effect OLS regressions and Models 3 and 4 are two-stage instrumental variable regressions.

3.2.2 In-depth Case Study

We conducted an in-depth case study to provide fine-grained evidence of how the government influences the internationalization of private firms through state ownership. More specifically, the case study complements the econometric estimation of how the ownership by state agencies and SOEs negatively affect the internationalization of the firm.

The case study follows Sugarcane Co., a fictitious name of a large Brazilian sugarcane and ethanol producer that became the target of state ownership in 2010. Sugarcane was partially acquired by the national oil company, Petrobras. We chose the ethanol market and the Sugarcane Co. for our analysis after thorough consideration of potential candidates who could fit the following criteria: (a) Be a multinational; (b) no prior state ownership; (c) operate in a competitive landscape with many

Table 1 Case study primary sources

Interviewee	Position	Job description	Date/duration
Interviewee A	Executive Director of Biofuels at Petrobras, Board Member at Sugarcane Co.	Executive Director of Biofuels at Petrobras with more than 12 years of experience in management positions for Petrobras. Representative for Petrobras at Sugarcane's Board	May 9, 2014/53 min
Interviewee B	Managing Director of Internal Communications at Sugarcane Co.	Manager responsible for all Internal Communications at Sugarcane Co. at the time of Petrobras' investment	November 11, 2014/45 min
Interviewee C	Public Relations Manager for Sugarcane Co.	Public Relations Manager who worked for the Foreign Mother Company during the acquisition of shares by Petrobras	December 3, 2014/1 h 55 min
Interviewee D	Strategy Manager at Petrobras	Responsible for strategy and project management with seven years of experience on the mechanisms of intervention of government agents into the investment and development decision making for Petrobras	March 25, 2014/32 min
Interviewee E	Executive Director of UNICA	Executive Manager of the UNICA, the largest Sugarcane Association in Brazil representing the interests of 50% of sugarcane producers and 60% of ethanol production in Brazil	November 14, 2013/55 min

equivalent prospects for receiving state ownership; and (d) operate in an attractive industry for the government.

We analyzed primary and secondary information gathered between September 2013 and July 2017. Our primary source of information were five interviews with employees at director level positions in Petrobras, Sugarcane Co., as well as in the business association UNICA (see Table 1 for a summary of primary sources). We designed the interviews to conceptualize specific events and detect their meaningful occurrences in a timeline (Langley 1999). We used a wide array of secondary sources to triangulate with the primary data. These sources included annual reports, financial and market reports, public interviews with the CEO's of Petrobras and the Sugarcane Co., reports from several business associations, industry reports, and government data on economic indices.

4 Results

4.1 Model Estimation

Table 2 reports descriptive statistics and the correlation matrix. The average value for the internationalization level suggests that the average of the assets, employees and revenues that are associated with foreign operations is around 16.93%. The value of this variable for the most internationalized firm is 68.40%. The state through its institutional investors holds on average 6.14% of total voting shares. The equity held directly by the state treasury or by fully owned SOEs is around 0.71% of the voting shares, on average, and 31%, the maximum value. The bivariate correlation coefficients between the two types of state ownership and the transnationality index shows the expected sign. Table 2 also shows the correlation coefficients between the instrumental variables (the interaction between political connection and firm industry) and the endogenous and exogenous covariates.

Table 3 presents the estimates for the econometric models of Eq. 1. Model 1 and Model 2 are firm-level fixed effect OLS estimates. Model 3 and Model 4 are instrumental variable (IV) regressions. We analyze the statistical properties of the instruments by the following tests. The Cragg–Donald Wald statistic rejects the hypothesis that the instruments are weakly correlated with the main endogenous variable (own. state institutional investor). The Wu–Hausman test is significant and suggests that the IV regression is consistent and preferable over the standard OLS. Finally, given that the model has more than one instrument, the Sargan test for over identification fails to reject the null hypothesis that all instruments are uncorrelated with the error term suggesting that the interaction between political connection and industry are valid exogenous instruments. Taken together, these tests suggest the Models 3 and 4 in Table 3 have statistically valid instruments.

In all four models in Table 3, the estimates for ownership by state institutional investors are positive and significant, ranging from 0.34 (Model 2, $\beta_1 = 0.34$, $p < 0.05$)

Table 2 Descriptive statistics and correlation matrix

	Mean	SD	Min	Max	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
1. Internationalization level	16.93	15.61	0.30	68.40																
2. State institutional investors (voting)	6.14	11.42	0.00	71.60	0.10															
3. State agencies and SOEs (voting)	0.71	3.88	0.00	31.00	−0.10	0.31														
4. State institutional investors (non-voting)	3.34	7.34	0.00	30.90	−0.21	−0.07	0.00													
5. State agencies and SOEs (non-voting)	0.23	1.80	0.00	19.40	−0.11	−0.07	0.70	0.06												
6. Foreign capital	6.37	16.57	0.00	74.00	0.19	0.10	−0.07	−0.06	−0.05											
7. Operational profitability	8.52	7.32	−6.20	38.57	−0.05	−0.11	−0.01	−0.13	−0.04	0.13										
8. Fixed-asset investment (var.)	0.20	0.23	−0.48	0.86	0.03	−0.03	−0.13	−0.04	−0.08	−0.06	−0.13									
9. Total assets (log)	14.70	1.59	11.20	18.67	0.40	0.00	0.02	0.01	0.11	0.31	0.08	0.13								

Table 2 (continued)

	Mean	SD	Min	Max	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
10. Founding year	1962.51	28.03	1899	2004	−0.11	−0.11	0.04	−0.26	0.18	0.26	−0.04	0.04	−0.10							
11. Group affiliate	0.81	0.40	0.00	1.00	0.14	0.05	0.09	0.22	0.06	0.13	0.09	0.01	0.58	−0.07						
12. Inst. transport	0.27	1.78	−4.00	10.00	0.11	0.14	−0.02	−0.09	−0.02	0.43	−0.11	−0.06	0.14	0.06	0.08					
13. Inst. manufacturing	0.53	2.21	−4.00	11.00	0.18	−0.06	0.09	−0.05	0.16	−0.10	−0.03	−0.09	0.09	−0.16	−0.17	−0.04				
14. Inst. extraction	1.90	7.48	−3.00	38.00	−0.15	−0.12	−0.05	0.36	−0.03	−0.07	−0.09	−0.04	0.16	−0.42	0.13	−0.04	−0.06			
15. Inst. food	0.88	4.21	−3.00	27.00	0.39	0.11	−0.04	−0.04	−0.03	−0.08	−0.12	0.18	0.19	−0.03	0.10	−0.03	−0.05	−0.05		
16. Inst. service	0.03	0.18	0.00	1.00	−0.14	−0.02	−0.03	−0.09	−0.02	−0.02	0.21	0.02	−0.18	0.04	−0.29	−0.03	−0.05	−0.05	−0.04	

$n = 146$. The means and standard deviations of continuous variables are in their original values

Table 3 Model estimates, internationalization of EMES

	(1)	(2)	(3)	(4)
Own. state institutional investors	0.38** (0.15)	0.34** (0.15)	1.58*** (0.39)	1.55*** (0.58)
Own. state agencies and SOEs	0.16 (0.15)	−23.35* (14.18)	−2.93*** (0.85)	5.46 (6.68)
Own. state institutional investors (non vot.)	−0.06 (0.05)	−0.05 (0.05)	−0.26 (0.20)	−0.24 (0.24)
Own. state agencies and SOEs (non vot.)	−0.50* (0.28)	41.28 (25.19)	2.68 (1.66)	−10.28 (10.38)
Foreign capital	−0.16* (0.09)	−0.08 (0.11)	−0.18* (0.09)	−0.20 (0.13)
Operational profitability	0.11 (0.11)	0.11 (0.11)	0.50** (0.19)	0.51* (0.31)
Fixed-asset invest (var.)	1.57 (2.20)	1.50 (2.19)	−3.80 (6.26)	−4.08 (8.45)
Total assets (log)	2.41 (3.54)	2.33 (3.51)	5.36*** (1.48)	5.64*** (1.53)
Founding year			0.02 (0.07)	0.03 (0.08)
Group affiliate			−8.62 (5.51)	−9.01 (5.55)
Own. state inst. investors × own. state ag. and SOEs		0.49* (0.29)		−0.17 (0.14)
Firm effects	Yes	Yes	No	No
Year dummies	Yes	Yes	Yes	Yes
Industry effects	No	No	Yes	Yes
Inv. Mills ratio	Yes	Yes	Yes	Yes
Observations	146	146	146	146
Adjusted R^2	0.88	0.88	−0.35	−0.31
Residual std. error	5.41 (df = 95)	5.42 (df = 94)	18.16 (df = 126)	17.90 (df = 125)
F statistic	22.30*** (df = 50; 95)	21.77*** (df = 51; 94)		
Wald stat.			7.87 ($p < 0.00$)	2.97 ($p < 0.00$)
Weak instrument			16.27 ($p < 0.00$)	1.82 ($p < 0.10$)
Wu–Hausman			18.45 ($p < 0.00$)	14.63 ($p < 0.00$)
Sargan			1.13 ($p < 0.89$)	1.25 ($p < 0.87$)

Model 1 and Model 2 are firm level fixed-effect regressions. Model 3 and Model 4 are instrumental variables regressions with own. state inst. investors as the endogenous regressor and the interaction between industry and the firm's electoral performance as instruments. The constant term in included in all models

*$p < 0.1$; ** $p < 0.05$; *** $p < 0.01$

to 1.58 (Model 3, $\beta_1 = 1.58,\ p < 0.01$). Looking at Model 3, each percent point in state ownership adds 1.58 percentage points to the transnationality index. This effect is almost a 10% increase based the sample average for the transnationality index. The effect of the ownership by state agencies and SOEs is significant and with the expected sign only in Model 2 ($\beta_2 = -\ 23.35,\ p < 0.10$) and Model 3 ($\beta_2 = -\ 2.93,\ p < 0.01$). These results lend reasonable support for Hypothesis 2.

The interaction term in Model 2 ($\beta_3 = 0.49,\ p < 0.10$) might explain the effect size differences of these two coefficients. It suggests that the effect size of the ownership by state agencies and SOEs is much greater when the firm has no ownership by state institutional investors. The positive sign of the interaction term suggests that the presence of this type of ownership counterbalance the negative effect of the ownership by state agencies and SOEs. Moreover, the relatively small interaction effect and the differences in the effect sizes of the two types of ownerships suggest that the government seems to be more aggressive in hindering internationalization to harness private investments than in relying on the by-product of the national champions' internationalization efforts to increase the provision of public goods. The case study analysis unveils the processes through which the detrimental effects of the ownership by state agencies and SOEs on the internationalization takes place.

4.2 Robustness Tests

We estimated Model 3 in Table 3 using the components of the transnationality index as dependent variables. Table 4 shows the model estimates for the percentage of firm's total assets, revenues, and jobs abroad.[2]

The effects of both types of ownership are significant and show the expected sign in all models. Both the positive and negative effects of minority state ownership on internationalization affect assets, revenues and job creation. The negative effect of ownership by state agencies and SOEs is stronger in reducing job creation abroad (Model 3, $\beta_2 = -\ 3.79, p < 0.01$) than in reducing the relative size of revenues or assets board. On the other hand, the effects of ownership by state institutional investors are stronger in increasing revenues abroad (Model 2, $\beta_2 = 1.98,\ p < 0.01$) than in increasing the relative size of assets and jobs. These results are in line with our theoretical reasoning. The creation of jobs locally is a valuable public good that has strong electoral appeal whereas increasing revenues abroad is an important by-product of the private good provision of subsidies to these elite firms since it contributes to the country's balance of payment.

[2] We also estimated Model 3 using the lagged (t − 1) values of the two types of state ownership for the transnationality index and each one of its components as dependent variables. The results did not change for any specification.

Table 4 IV regression estimates for the components of the transnationality index

	Internationalization of		
	Assets (1)	Revenue (2)	Jobs (3)
Own. state institutional investors	1.08** (0.46)	1.98*** (0.58)	1.89*** (0.43)
Own. state agencies and SOEs	−2.14** (0.94)	−3.27*** (1.18)	−3.79*** (0.97)
Own. state institutional investors (non vot.)	−0.58*** (0.19)	−0.15 (0.31)	0.002 (0.20)
Own. state agencies and SOEs (non vot.)	1.79 (1.77)	2.79 (2.18)	4.28** (1.89)
Foreign capital	0.13 (0.11)	−0.50*** (0.14)	−0.21** (0.11)
Operational profitability	0.28 (0.24)	0.49* (0.30)	0.98*** (0.26)
Fixed-asset invest (var.)	3.21 (7.66)	−17.26 (10.64)	3.87 (6.20)
Total assets (log)	4.12*** (1.48)	6.48*** (2.00)	5.85*** (1.67)
Founding year	−0.10 (0.08)	0.09 (0.09)	0.03 (0.09)
Group affiliate	−2.75 (5.39)	−9.94 (7.47)	−18.36** (7.65)
Firm effects	No	No	No
Year dummies	Yes	Yes	Yes
Industry effects	Yes	Yes	Yes
Inv. Mills ratio	Yes	Yes	Yes
Observations	145	146	146
Residual std. error	18.07 (df = 125)	25.48 (df = 126)	21.88 (df=126)
Wald stat.	9.84 (p < 0.00)	5.71 (p < 0.00)	5.82 (p < 0.00)
Weak instrument	15.71 (p<0.00)	16.27 (p < 0.00)	16.27 (p<0.00)
Wu–Hausman	7.11 (p < 0.01)	12.46 (p<0.00)	19.08 (p < 0.00)
Sargan	4.37 (p < 0.36)	2.68 (p < 0.61)	2.94 (p < 0.57)

All models are instrumental variables regressions with own. state inst. investors as the endogenous regressor and the interaction between industry and the firm's electoral performance as instruments. The constant term is included in all models

$^{*}p < 0.1$; $^{**}p < 0.05$; $^{***}p < 0.01$

4.3 Sugarcane Co.

The Sugarcane Co. was established in 1967 as a small alcohol production plant. The firm quickly grew to become market leader, by using some of the most modern processing features available in the sugarcane market. The following 20 years consolidated its position as a seller of liquid and processed sugar for the internal food processing industry as well as for the international market via exports. The firm quickly became a household name and was the first in the sector to perform a foreign direct investment by acquiring an international refinery. In 2001, an international group with large assets and operations in Europe, Africa, Asia and West Indies, acquired the firm aiming at tap the Brazilian market and increasing economies of scale and scope. The acquisition favored Sugarcane Co.'s consolidation and provided capital to pursue the purchase of other refineries.

Sugarcane Co. successfully launched an IPO into the Brazilian stock exchange in 2007. Although there was a positive outlook for the ethanol market at that time, government intervention on gasoline prices to control inflation severely reduced the sector margins. Gasoline prices has a major impact on voter perception and play a major role in Brazilian politics (Folha 2011). Although Brazil is one of the top ten producers of oil worldwide (EIA 2017) it is dependent on gasoline imports (ANP 2017). Therefore, gasoline prices and its impact on inflation makes it an important political issue before elections (Moita and Paiva 2013).

In this context, the Brazilian government decided to increase its intervention by direct investing in the ethanol sector through its state-owned oil company, Petrobras, by setting aside US$ 1.94 billion with the objective of quadruplicating its ethanol production (Folha 2013). For the selection of investment targets, Petrobras established a set of directives, giving priority to the fact that the firm was a national producer holding considerable assets, and that were located in the state of Sao Paulo, the largest sugarcane producer in Brazil and an electoral bastion with the largest population in the entire country. In April of 2010, Petrobras announced that it would acquire 26.3% of Sugarcane Co.'s capital for $393 million (Material Fact, March 28, 2010).

Although Petrobras was a minority shareholder, it negotiated several structural changes inside of Sugarcane Co., as part of the investment agreement. The first condition was delisting Sugarcane Co. and making it a private subsidiary to make the acquisition less troublesome (interviewee A). Additionally, Petrobras negotiated three seats in the new six-person board of directors and required that no independent members should be appointed. Petrobras also should appoint the Industrial Officer and the Investment and Portfolio Director, key management positions inside of Sugarcane Co. On top of that, the existing investor relations' team became fully dedicated to provide information to Petrobras. On the other hand, Petrobras committed to purchase a value worth of 2.2 billion liters of ethanol (over 1 billion dollars' value at the time) between 2010 and 2014.

The acquisition by Petrobras was detrimental to the internationalization of the Sugarcane Co. Although Sugarcane Co. was in a good position to profit from the Brazilian government plans to promote ethanol in Africa (Africatoday 2011), the discourse for such internationalization never led to any further internal changes that could commit time and resources for its development.

> *We shifted our focus 100% to the internal market. Currently, we have no intention of investing in any other country although many African countries have asked for it* (*Interviewer A*).

The drivers of such shift were neither related to Sugarcane Co.'s strategic plan nor to any change in the economic outlook, but they were essentially political. The government wanted to control the dependence on gasoline imports and curb inflation through price controls. For example, the inflation, under control until the end of 2010, started seeing a steep increase going beyond the highly communicated government targets. Meanwhile, gasoline imports saw also a rapid acceleration. Figure 1 summarizes the timeline of the case and its key events.

5 Discussion and Conclusion

Our paper contributes to research on political ties and their effects on the internationalization of EMNEs by advancing theoretical propositions about the effects of state ownership on internationalization of domestic multinationals in democratic states (Ramasamy et al. 2012). The theoretical framework we advance here, unifies existing empirical research in authoritarian and democratic states around the logic of political survival (Bueno de Mesquita et al. 2003). In authoritarian regimes like China, state ownership in multinationals serves the primarily the purpose of providing private goods to a narrow number of chosen firms and individuals loyal to the regime (Zhang and Van den Bulcke 1996), as well as some selected public goods to the general population (Gallagher and Hanson 2013). We argue that minority state ownership in emerging market democracies is a feasible way to provide primarily public goods to a larger winning collation, as well as some private goods to chosen national champions. We tested our hypotheses using a panel dataset from Brazilian multinationals.

Our results suggest that politically insulated, state-controlled institutional investors, are preferred by the government to boost the internationalization of elite firms. These investors are subject to larger transparency and performance orientation (Chaganti and Damanpour 1991). These features make the governments prefer this type of ownership to act as an industrial policy arm. By helping the elite firms become more competitive abroad, these may acquire new technologies, capabilities, and generate new sources of revenue for the country. We find that the larger positive effect of ownership by state institutional investors is in increasing the firm revenues abroad, which contributes to balance the payments accounts of the country when the company brings the profits back home.

Our results also suggest that state agencies and SOEs are more likely to respond to government pressures for providing local public goods by hindering internationalization. We found that the larger detrimental effect of the ownership from state agencies and SOEs is the reduction of jobs abroad, a very appealing public good. It is a way to extract rents and positively influence its constituent's perceptions, negatively affecting the internationalization chances of the firm. Our case study results show that the changes in the strategic plans for Sugarcane Co. were not made in response to the economic outlook, or the prospective margins for ethanol and its derivatives, but rather to control gasoline prices and inflation before the election.

The case study also reveals some of the mechanisms through which governments with minority ownership by state agencies and SOEs, can influence a firm's decision-making and lower the quality of governance practices. The devised mechanisms comprise the delisting of the firm, changes in the board composition and independence, decreased reporting and transparency, supply transactions and the participation of managers affiliated with the shareholders.

Public listed corporations, independent board members, external auditors and hiring of professional managers, are well accounted for in the literature as practices that help reduce conflicts between shareholders (Peng et al. 2008; Gilson 2006). In delisting the firm, Petrobras provided less information to markets and had less scrutiny

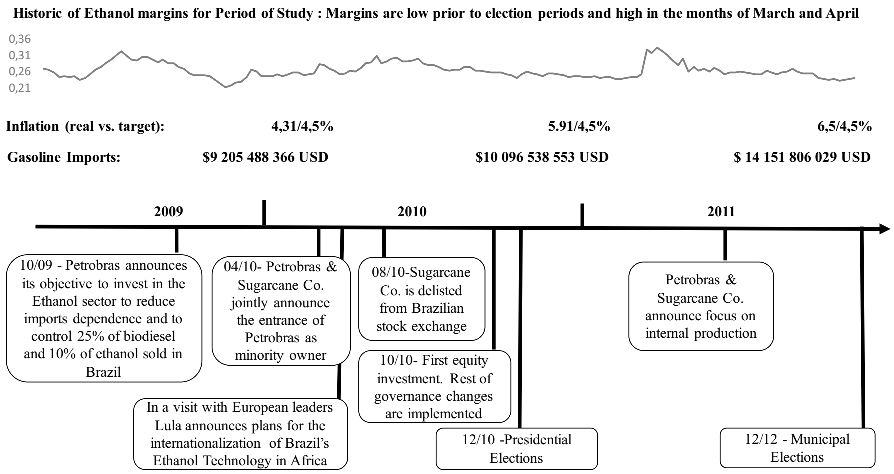

Fig. 1 Case study timeline

over its interference with the firm's choices in the public eye. The avoidance of supply transactions is also a way in which a firm reduces hidden interests and avoids giving preferential treatment to investors. The one-billion-dollar contract signed between Petrobras and Sugarcane Co., created additional dependence of Petrobras as a customer and provided Petrobras with private benefits of control (Gilson 2006). The participation of affiliated managers and executives inside of the firm left Petrobras with increased power and immediate access to information and decision-making. Finally, while it is not common to delist publicly traded firms in Brazil, there is evidence that Petrobras tends to favor the creation of separate business units when investing in firms, which somehow mimics the idea of reducing transparency and affecting the governance of the firm. For example, when investing in Sao Martinho, one of the largest sugar and ethanol groups in Brazil, Petrobras preferred, the incorporation of a new holding, requesting as well board seats (SEC 2010).

Finally, our study informs managers by showing that firms need to account for the type of minority state ownership and its interaction with a company's corporate governance and strategy. Firms should be aware of potential conflicts with their intended strategy and recognize the opportunities to take advantage of valuable country resources by selecting the right type of equity holders. We expect that a strong firm governance, portrayed by its transparency, affiliation to external governance boards, or participation in international governance organizations, may defer the state from undertaking such acquisition (Pargendler 2015). Managers should focus on enacting political capabilities that serve to bargain investments by state institutional investors, as this type of investment can allow a firm to profit from the investment to carry on international and long-term oriented projects (Inoue et al. 2013).

Multinationals in the sample

Firm	Industry
All America Latina	Transport
Ambev	Food
Aracruz	Extracting
Bematech	Manufacturing
Braskem	Manufacturing
BRF Foods	Food
Coteminas	Manufacturing
DHB	Transport
Duratex	Manufacturing
Embraer	Transport
Fibria	Extraction
Gerdau	Manufacturing
Gol	Transport
Industrias Romi	Manufacturing
Iochp-Maxion	Transport
Itautec	Manufacturing
JBS	Food
Klabin S/A	Extraction
Lupatech	Manufacturing
M. Diasbranco	Food
Marcopolo	Transport
Marfrig	Food
Marisol	Manufacturing
Metal Leve	Transport
Metalfrio	Manufacturing
Minerva	Food
Natura	Service
Portobello	Extraction
Randon Part	Transport
Sadia S/A	Food
Suzano Papel	Extraction
Tam S/A	Transport
Telemar	Service
Totvs	Service
Tupy	Transport
Ultrapar	Manufacturing
Vale	Extraction
Weg	Manufacturing

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