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Foreign Direct Investment in Conflict Locations: An Analysis of Firm Behaviour & Host Nation Development

Foreign Direct Investment (FDI) is defined by the UNCTAD as 'an investment made to acquire a lasting interest in enterprises operating outside of the economy of the investor' (UNCTAD, 2016). The advent of globalisation and the global value chain has elevated the prominence of FDI, both in academia and for business decision-making. Multinational corporations (MNCs) are increasingly engaged in FDI activities to non-traditional markets as a source of greater profitability. This research paper focuses on FDI activities to conflict locations that are characterised by a high degree of political and geopolitical instability. Specifically, this paper provides an investigation into the benefits accruing to MNCs engaging in FDI to conflict zones, the impacts of firm governance structures on the FDI decision, and the impacts of FDI for the host nation. This paper argues that FDI activities should ideally be mutually beneficial for MNCs and their stakeholders, and encourage further economic and social development in the host nation.

This paper extends the existing international business and economics literature and provides a greater understanding of the motivations and impacts of MNC FDI activities. It highlights that FDI decisions to conflict locations are often primarily driven by a firm's economic responsibilities and occur where corporate governance structures allows a firm to engage in unethical behaviour to exploit the weak institutional framework of the host nation. In contrast to this current behaviour, this paper argues that firms should adopt an integrated strategy framework and promote stronger corporate governance mechanisms in order to maximise their rewards from FDI whilst maintaining the social interests of all stakeholders and contributing to host nation development.

Keywords: conflict, Corporate Social Responsibility, Eclectic Paradigm, economic development, foreign direct investment, stakeholders

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Introduction

Foreign Direct Investment (FDI) is defined by the UNCTAD as 'an investment made to acquire a lasting interest in enterprises operating outside of the economy of the investor' (UNCTAD, 2016). As such, FDI requires a much larger commitment in terms of managerial time and organisational financing when compared with portfolio investment. Despite this commitment, FDI activities have grown significantly as a consequence of globalisation which has increased the interconnectedness of global markets and led to the creation of global value chains. Increasingly, multinational corporations (MNCs) are engaged in FDI to non-traditional markets as they seek to generate greater profitability offshore. This research paper considers such FDI activities to conflict locations which are characterised by a high degree of political and geopolitical instability. This paper provides an investigation into the benefits accruing to MNCs engaged in FDI to these locations, the impacts of firm governance structures on the FDI decision, and the impacts of FDI for the host nation. Ideally FDI activities should be mutually beneficial for MNCs and their stakeholders, and encourage further economic and social development in the host nation. Such a practice would enable firms to better satisfy their economic and moral responsibilities (Carroll, 1979, 1991).

However, building on the eclectic theory (Dunning, 1979, 2001) this paper shows that the market imperfections endemic in conflict zones, including corruption and weak formal institutional frameworks are a source of significant rewards for firms able to exploit these environments profitably. These rewards can be characterised as Ownership advantages for firms with past managerial experience of operating in turbulent environments, and Locational advantages including access to raw materials, and political connections (Driffield et al., 2013). Often FDI activities which exploit these rewards are viewed as unethical and subsequently firms with powerful stakeholders or which suffer from conservatism are limited in their ability to engage in FDI to conflict locations (Fama & Jensen, 1983; Mitchell, Agle & Wood, 1997).

This paper thus extends discussion to consider the impact of ownership, management, and corporate governance structures on an MNC's decision to invest in conflict zones. Concentrated ownership is argued to reduce the power and legitimacy of organisational stakeholders, enabling MNCs to more easily reach a consensus to engage in unethical behaviour and exploit the rewards from conflict zones (Mitchell et al., 1997). Hence, a lack of powerful stakeholders can lead firms to neglecting their moral responsibilities in their conduct of FDI to conflict locations (Carroll, 1979, 1991). Where this is the case, FDI activities can heighten existing instability in the host nation and thus lead to diminished levels of economic and social development.

Traditionally, literature has praised the economic and developmental benefits for the host nation of inward-FDI (Aitken & Harrison, 1993; Barro & Sala-i-Martin, 1995). These benefits stem from the spill-over of the firm's Ownership advantages, such as superior technology and managerial knowledge, to local firms and communities (Grossman & Helpman, 1990; Jovanovic & Rob, 1989; Nelson & Phelps, 1966; Segerstrom, 1991). This paper challenges that perspective and questions the extent to which the developmental benefits of FDI are actualised in host nations characterised by conflict. Inadequate absorptive capacities of the host country and domestic firms leads to significant rent capture by MNCs engaging in FDI to conflict zones. This is consistent with the literature on the 'resource curse' and with firms engaging in extractive or resource-seeking FDI (Sachs & Warner, 1999). In some cases, the FDI activities of MNCs are argued to generate heightened instability, potentially fuelling civil wars and the reversal of development.

Nature and Extent of Rewards from FDI

Nature of Rewards

Traditionally, internationalisation theory (Buckley & Casson, 1976; Rugman, 1980) and the eclectic paradigm (Dunning, 1979, 2001) have been employed to show how market imperfections give rise to significant rewards for MNCs as they engage in FDI. Internationalisation theory views these rewards as stemming from the firm's internalisation of markets and encompassing transaction cost savings and locational interdependencies (Buckley & Casson, 2009). Internationalisation gives rise to significant cost-savings, economies of scale and scope, and global synergy advantages for MNCs (Erdener & Shapiro, 2005; Tolentino, 2008). Dunning's (1979, 2001) eclectic paradigm extends this view of rewards and shows that in addition to Internalisation advantages, internationalisation requires firm-specific Ownership advantages – such as marketing and management capabilities, technology and experience – in addition to Location-specific advantages of the host nation (Anastassopoulos, 2003; Dunning, 1988). These Locational rewards, such as raw materials, a low-cost labour supply, and less stringent regulatory frameworks, are dynamic and often reflect the extent of market and government imperfections (Driffield & Love, 2007; Dunning, 1988).

Rewards from Investment in Conflict Environments

Market imperfections and weak institutions are typically viewed as a cause of additional transaction costs, and hence as a Locational-disincentive for MNC investment in conflict environments (Henisz, 2000; Meyer et al., 2009). This paper adopts an alternative perspective and argues that MNC investment in conflict zones may enable firms to exploit the greater market imperfections endemic in the host country and thereby generate greater rewards through first mover advantage and heightened market power.

Ownership Rewards: Managerial Experience

MNC investment in conflict locations can enable firms to leverage firm-specific Ownership advantages and thereby generate competitive advantage (Peteraf, 1993; Teece & Pisano, 1994). As illustrated by contemporary frameworks in Somalia and Nigeria, conflict zones are often characterised by weak formal institutions, including low levels of law and property right protection (Driffield et al., 2013; Rose-Ackerman, 2002, 2008). These weak institutions give rise to significant market imperfections, including corruption, which often deter MNC investment (Rose-Ackerman, 2002, 2008). However, these environments also confer an Ownership advantage to firms with previous operational experience in risky environments, enabling them to benefit from their managerial experience (Driffield et al., 2013; Peng et al., 2008). In the absence of strong market institutions, firm performance is more reliant on firm-specific and industry factors and this managerial experience can be utilised to generate profitability and to win market share in the host nation (Peng et al., 2008; Yang et al., 2012). For example, BP leverages its previous managerial experience in the Middle East as a springboard for successful expansion in Egypt and Iraq (BP, 2015). As highlighted by BP experience in the Middle East, past managerial experience enables MNCs to benefit from the market imperfections of the host nation (Eden & Miller, 2004; Yang et al., 2012).

Locational Rewards: Natural Resources

Investment in conflict environments can also be driven by the consideration of Locational rewards on offer. In accordance with Carroll's (1979, 1991) Economic Responsibilities, MNC investment to conflict locations is often driven by resource-seeking motives and the need to procure profitable natural resources and geographic assets. This is illustrated by South Sudan where over 80% of foreign direct investment is in petroleum extractives (Driffield et al., 2013; ERGO, 2011). As shown by the sequential expansion of Barrik Gold's mining operations in Tanzania, securing geographic assets is a first mover advantage that enables MNCs to generate long-term resource and rent extraction when peace and stability comes (Hansen, 2013; Resmini, 2000; Rivoli & Salorio, 1996). The market power of large MNCs also provides greater bargaining power over stakeholders, enabling MNCs to exploit turbulent markets and gain further access to resources (Caves, 1971; Driffield et al., 2013; Hymer, 1976). This is highlighted by the Angolan government which sold-off significant oil and diamond resources to MNCs to fund civil war in the 1990s (Addison & Murshed, 2001). Hence, markets characterised by high levels of instability confer significant opportunities and Locational advantages to MNCs willing to engage in FDI.

Locational Rewards: Political Relationships

Dunning's (1979, 2001) Locational advantages can be extend to incorporate corruption and political interference. In the literature, formal institutions are mostly viewed as providing Locational advantages by facilitating transactions and reducing risk whilst weak institutions are viewed as a source of increased transaction costs and hence as a Locational deterrent to investment (Bevan et al., 2004; Daude & Fratzscher, 2008; Javorcik & Wei, 2009; Peng et al., 2008).

However, this view neglects that market imperfections including corruption and a lack of formal institutions can confer significant rewards to MNCs that are able to engage successfully with corrupt officials and malleable institutions. Political resources can provide MNCs with significant first mover advantage in terms of spatial pre-emption, behavioural differentiation advantages, or through the government enacting formal entry barriers to prevent future rivals (Frynas et al., 2006; Kerin et al., 1992). These spatial rewards are illustrated by the Shell-BP joint venture in

Nigeria which used political connections to secure the majority of Nigerian oil licenses in the 1950s and which continues to profit from these licenses (Frynas et al., 2006). Political connections can also place first-moving MNCs on a path dependency of favour reciprocation (Frynas et al., 2006; Hadjikhani et al., 2008). As highlighted by the US government's partnership with Kellogg Brown and Root during the Iraq war, political reciprocation in turbulent environments can result in firms being rewarded with significant contracts and generating supernormal rents (Fifield, 2013). High levels of corruption also incentivise firms to pay bribes in return for favoured treatment on privatisation deals, concessions and contracts (Rose-Ackerman, 2002, 2008). In addition, political relationships and malleable institutions enable firms to favourably shape the rules of the game and thereby increase profitability (Peng et al., 2008; Ring et al., 2005).

Summary

MNCs engaging in FDI to conflict locations stand to benefit from market imperfections, including corruption and weak institutions, through first mover advantage and heightened market power. These factors give rise to significant Ownership and Locational advantages, including resources and political connections which can underpin long-term firm profitability. However, often rent-seeking FDI in extractives or FDI which exploits corruption is viewed as unethical. Thus, discussion now turns to the impact of governance structures on a MNC's decision to invest in conflict locations. Concentrated ownership, or a lack of powerful external organisational stakeholders, is argued to enable MNCs to more easily reach a consensus to engage in unethical behaviour and to exploit the rewards from conflict locations (Mitchell et al., 1997). This discussion is centred in agency theory which shows that principal-agent problems stemming from the separation of firm ownership and control can impact managerial risk-taking and, by extension, a firm's decision to invest into conflict locations (Fama & Jensen, 1983).

Impact of Firm Ownership, Management and Governance on the FDI Decision

Firm Ownership Concentration and Corporate Social Responsibility (CSR)

Firm ownership concentration is a significant determinant of corporate governance practices, and by extension a firm's decision to invest in conflict locations. In home countries characterised by weak institutions, concentrated ownership – which centralises power in the hands of a few shareholders – operates as a substitute for formal corporate governance which mitigates potential agency issues (Berglof & Pajuste, 2005; Fama & Jensen, 1983; Heugens et al., 2009). Subsequently, as is illustrated by family-owned firms in Asia, concentrated ownership facilitates outward FDI by reducing the level of scrutiny from external stakeholders and removing the need for voluntary information disclosure (Bhaumik et al., 2010; Chau & Gray, 2002). This lower level of transparency and scrutiny, coupled with the centralisation of decision-making power to a small group of controlling shareholders, weakens the power and legitimacy of the firm's other stakeholders (Rodriguez et al., 2006; Mitchell et al., 1997). Subsequently, firms with concentrated ownership are often less concerned about upholding CSR and their moral obligation to stakeholders

(Driffield et al., 2013; Gibson, 2000). This provides firms with a greater ability to exploit the Locational advantages of FDI to conflict locations, such as corruption and malleable institutions (Frynas et al., 2006; Kerin et al., 1992). Hence, firms with weak corporate governance or concentrated ownership are more likely to engage in FDI to conflict locations.

By contrast, widely dispersed ownership or formal corporate governance mechanisms often increases the need for management to voluntarily disclose information in order to mitigate potential agency issues (Fama & Jensen, 1983). This exposes the firm to external scrutiny from stakeholders, thereby placing an onus on the firm to uphold ethical and moral obligations to stakeholders and CSR (Carroll, 1991; Donaldson & Preston, 1995). As highlighted by Nike's exploitation of child labour in Asia, these factors reduce the ability of firms to reap the Locational advantages associated with FDI (Husted & Allen, 2006; Logsdon & Wood, 2005). Hence, firms with dispersed ownership or when complying with formal corporate governance mechanisms are less likely to engage in FDI to conflict locations.

Ownership Concentration and Decision-Making

Concentrated ownership also centralises decision-making power, limiting the potential interference from external stakeholders and making it easier to reach consensus (Driffield et al., 2013; Mitchell et al., 1997). Concentrated owners are typically more informed about the company's decisions and the risks involved with expansion (Connelly et al., 2010). Subsequently, firms with concentrated ownership may be more open to FDI in conflict zones where such investment serves to exploit Locational or Ownership advantages (Dunning, 1979). For example, this may be to exploit the firm's past managerial experiences of dealing with turbulent environments (Driffield et al., 2013). By contrast, widely dispersed ownership increases the number of stakeholders the firm must gain consensus from and this reduces the likelihood of outward-FDI.

Risk Preferences and Managerial Agency Issues

The decision to invest in conflict locations is also significantly influenced by the personal risk-tolerances of the firm's key stakeholders, such as managers and powerful shareholders (Filatotchev & Wright, 2011). Managers are traditionally viewed as risk-averse owing to the potential reputational and unemployment costs associated with failed corporate decision-making (Filatotchev et al., 2001; Zahra, 1996). Hence, weak corporate governance or high managerial ownership can lead to managerial-domination of the firm whereby managers exercise their power to avoid risky decisions, such as the decision to invest in conflict locations (Finkelstein & Hambrick, 1996; Luo, Courtenay & Hossain, 2006). This is highlighted by the findings of Filatotchev et al (2001) which showed that managerial ownership and board membership in Russia, Ukraine and Belarus led to lower levels of firm internationalisation. Consequently, strong corporate and board governance is required to mitigate this principal-agent problem, and to encourage the acceptance of risky projects and an entrepreneurial orientation (Naldi et al., 2007). An entrepreneurial orientation is fostered through inside directors who participate in strategic processes, contribute to the firm's culture, and are well-informed of the risks involved with company expansion (Baysinger & Hoskisson, 1990; Zahra, 1996). Similarly, an entrepreneurial orientation may be encouraged by concentrated ownership, or the appointment of outside directors, which provides a check on managerial power (Driffield et al., 2013). An entrepreneurial orientation improves the firm's ability to profit from volatile and uncertain business environments, hence increasing the likelihood of FDI to conflict locations (Zahra, 1993).

Ownership Concentration and Shareholder Entrenchment

On the contrary, it may equally be argued that firms with concentrated ownership are risk-averse and may experience less outward-FDI (Bhaumik et al., 2010; Garcia-Marco & Robles-Fernandez, 2008). Concentrated owners are typically under-diversified, and hence more risk-averse, and this may lead to shareholder entrenchment whereby controlling shareholders exercise their power to avoid risky firm decisions (Bergloff & Pajutse, 2005; Wei & Zhang, 2008). This is highlighted by family-owned firms in Asia, where high ownership concentration results in conservatism, strategic inertia, and risk-avoidance (Huybrechts et al., 2012; Short et al., 2009). In addition, ownership concentration inhibits the ability for the company to use equity funding for FDI since equity issuance would result in shareholder claim dilution and a loss of control (Bhaumik et al., 2010). The combination of these factors may render firms with concentrated ownership more risk-averse when it comes to project selection and thus less likely to invest in FDI to conflict locations. Hence by contrast, others argue that firms with widely dispersed ownership are more likely to invest in conflict locations owing to shareholder diversification and a subsequent greater level of risk tolerance.

Summary

The firm's ability to reap the benefits of FDI to conflict locations is significantly impacted by corporate governance, ownership and management structures. Firms with more concentrated ownership are likely to face weak external stakeholders and thus lower scrutiny over the ethical nature of their operations. In addition, concentrated ownership typically makes it easier for firms to reach a consensus when it comes to decision-making. Hence, these factors suggest that firms with highly concentrated ownership, or informal corporate governance structures, are more likely to successfully undertake FDI to conflict locations. However, agency issues including managerial power and shareholder entrenchment can induce conservatism and thus result in lower levels of FDI.

Given the consideration of firm-level advantages and the impacts of management and ownership on firm decision-making thus far provided, this paper now turns to an analysis of the benefits of FDI for the host nation. From the perspective of Carroll's (1979, 1991) ethical and philanthropic responsibilities, firms undertaking FDI should do so within a framework of decision-making and corporate governance that upholds the interests of their legitimate stakeholders and maximises the wellbeing of society. The next section of this research paper considers the positive economic and developmental impacts that FDI can have for the host nation, and questions to what extent these benefits are realised in conflict locations.

FDI and Development in Conflict Locations

Potential Developmental Benefits of FDI

The principle argument that FDI of MNCs contributes to the progress of conflict zones is centred in Dunning's (1979, 2001) finding that MNCs possess firm-specific ownership advantages, such as technology and managerial expertise, beyond those of domestic competitors (Driffield et al., 2013; Narula & Driffield, 2012; Nelson & Phelps, 1966). For conflict zones experiencing 'economic backwardness', FDI is argued to lead to economic development through the diffusion of superior technology and the transfer of knowledge and management capabilities from the MNC (Findlay, 1978; Gerschenkron, 1952; Narula & Dunning, 2000). FDI may also contribute to the development of human capital through labour training and skills acquisition (De Mello, 1999; Hansen & Rand, 2006). These spillovers stem from the MNC's backward and forward integration with domestic firms and the mobility of the labour force (Driffield & Love, 2007; Blomstrom & Kokko, 1998). In addition, FDI represents a significant inflow of capital and may be used to improve a nation's infrastructure (Afriyie, 1992). As highlighted by MTN Group's operations in Africa, this is particularly the case for telecommunications investment where infrastructure is a positive externality of the MNC's expansion (MTN Group, 2015). Hence, FDI is necessary in stimulating the development, building capacity and economic growth of recipient conflict zones (UN, 2009).

Extent of Benefits

Country-Level Absorptive Capacity

Whilst the potential developmental benefits of FDI for conflict zones are clear, the extent to which these benefits are realised is dependent on the absorptive capacity of the host nation and the extent of integration between the MNC and domestic firms (Omran & Bolbol, 2003; Hansen, 2013). Absorptive capacity refers to the ability of the host nation to integrate the MNC's existing and exploitable resources into the production chain. Whilst FDI may contribute to the development of a nation's absorptive capacity through spillovers and positive externalities, not all host nations have the capacity to exploit the ownership advantages of inward FDI (Narula & Driffield, 2012). Conflict nations are often characterised by poor macroeconomic management, inadequate infrastructure, insufficient human capital, and weak formal institutions (Omran & Bolbol, 2003). As illustrated by the failure of Somalia and Haiti to exploit the developmental benefits from FDI, these factors reflect an inadequate absorptive capacity (Driffield et al., 2013). For example, Somalia's weak formal institutions and inadequate contract enforcement provide an incentive for MNCs to internalise operations rather than integrating their value chains with local firms (Dunning, 1979; Li & Resnick, 2003). This limits the extent of knowledge and technological spillovers, and thereby reduces the developmental benefits of FDI.

Firm-Level Absorptive Capacity

A lack of absorptive capacity at a firm level in conflict nations can also lead to rent capture by the MNC and thereby also reduce the developmental benefits of FDI (Driffield et al., 2013; Narula & Driffield, 2012). Ideally, FDI should lead to a crowding-in of productive investment, with MNC investment spilling over to greater domestic production and productivity (Narula & Driffield, 2012). However, where the technological gap between MNCs and domestic firms is too great, integration may not occur and MNCs may capture rents and crowd out productive domestic investment (Driffield et al., 2013; Hansen, 2013). This is illustrated by extractive FDI in Tanzania's gold industry where the inadequate absorptive capacity of domestic firms prevents backward integration with MNCs (Hansen, 2013). In this case, FDI is argued to reduce the market share and profitability of domestic firms, reducing the host nation's economic progress and stability (Crotty et al., 1998; Garman et al., 2001).

Motivation behind the FDI Decision

In addition to the absorptive capacity of the host nation and domestic firms, the motivation of MNCs in undertaking FDI into conflict locations is often an important determinant of the developmental benefits accruing to the host nation. Specifically, the level of MNC integration with local firms, and by extension the developmental benefits of FDI, may be limited by the MNC's motivation. MNC investment to conflict zones is often extractive and driven by resource-seeking or geographic factors (Driffield et al., 2013; Hansen, 2013). For example, over 80% of South Sudan's inward FDI is in petroleum extractives (ERGO, 2011). This is in line with the primary economic responsibility of businesses, which recognises that MNCs are profit-driven and not the in the business of economic development (Carroll, 1979, 2001; Narula & Marin, 2003). Further, as is illustrated by Tanzania's FDI in extractives such as gold, resource-seeking MNCs may become enclaves in conflict nations with no interconnections or spillovers to domestic firms or the general economy (Hansen, 2013). This is also shown by FDI in Cameroon's oil industry in the 1980s, which led to 'Dutch disease', diverting resources away from other job-creating and poverty-alleviating industries (Benjamin et al., 1989). In these cases, FDI expropriates economic rents to the home nation and translates to higher inequality, social unrest and reversal of economic development for the host nation (Hansen, 2013).

Impact of FDI on Instability and Conflict

Multinational companies can also contribute to economic and political instability through their FDI activities, thereby diminishing the economic and social development of conflict locations (Driffield et al., 2013; Robertson & Watson, 2004). Conflict nations, as illustrated by Sudan and South Sudan, are often catalysed by high levels of political corruption which confers a significant Locational advantage to MNCs who are able to exploit these weak institutional frameworks to generate greater profits (Dunning, 1979). As highlighted by the experience of Ecuador in the early 2000s, such FDI further entrenches corruption and thereby heightens social and economic inequality in the host nation, contributing to underlying ethnic and sectarian tensions (Rose-Ackerman, 2002, 2008). This is particularly the case for natural-resource-rich countries which suffer from the resource curse (McNeish, 2011; Sachs & Warner, 2001). In these conflict zones, resource-seeking FDI is often exploited by political officials and religious militias as a source of geopolitical power which can be used to fund civil wars, and which increases the degree of corruption and general instability (Robertson & Watson, 2004; Ross, 2002). This is highlighted by the case of conflict diamonds and civil war in Sierra Leone in the early-2000s, and more recently in Iraq and Syria as Islamic State seeks to exploit geopolitical power from oilfield FDI (McNeish, 2011). In these cases, FDI in conflict zones can be a destabilising influence which reduces overall progress and development.

Summary

Whilst the potential benefits accruing to the host nation from FDI are clear, the realisation of these benefits is limited due to an inadequate absorptive capacity in the conflict location at both a country-level and a firm-level. In addition, much FDI to conflict locations is extractive and resource-seeking, meaning that integration between MNCs and domestic firms is limited and rents are captured by MNCs and home countries. This highlights that where FDI decisions are not undertaken within a utilitarian framework of decision-making, FDI to conflict locations can heighten existing instability and thus result in lower levels of host nation development.

Implications for Business and Government

Implications for Business Decision-Making

Ideally, FDI activities should be mutually beneficial for MNC investors and their stakeholders, and encourage further economic and social development in the host nation. As this paper has highlighted, FDI decisions to conflict locations are often primarily driven by a firm's economic responsibilities and occur where corporate governance allows a firm to engage in unethical behaviour (Carroll, 1979, 1991). In contrast to this current practice, MNCs investing in conflict locations should give greater consideration to the interests of their stakeholders and base their internationalisation decisions on an integrated strategy framework as outlined in Figure 1[1].

[1] Based on Baron, 1995.

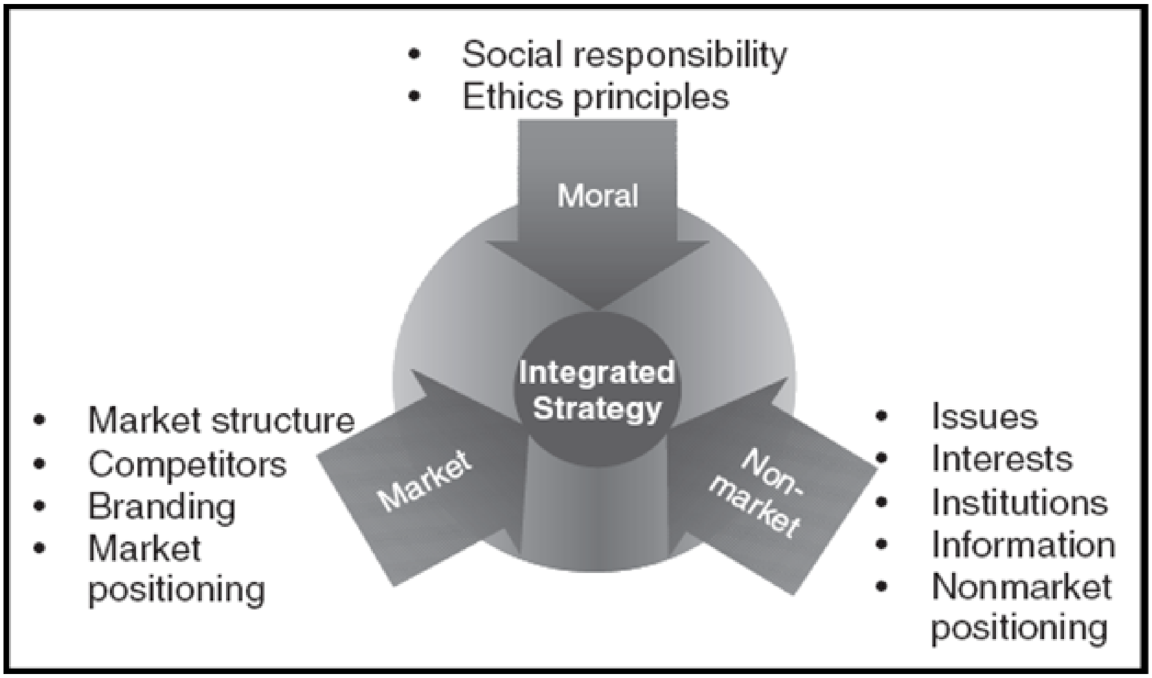

Figure 1: Integrated strategy framework.

Through adopting a proactive stance to CSR and upholding the moral and ethical demands of all stakeholders, MNCs can maintain their social contract to operate and thereby gain market access in turbulent environments (Donaldson & Dunfee, 1994; Donaldson & Preston, 1995). In addition, such an approach is likely to contribute to stability and peace in the host nation and enhance the ability for MNCs to exploit their Ownership advantages and to benefit from the Locational advantages offered by the host nation (Jamali & Mirshak, 2010). For example, MNCs should engage in public-private infrastructure projects with host governments and local businesses in order to fulfil both economic and moral responsibilities (Carroll, 1991; Custos & Reitz, 2010). In addition, where social needs are left unmet by host nation governments, MNCs should fill this void through the recruitment of local employees rather than expatriates (Bennett, 2002). This would promote the development of the host nation's human capital, thereby increasing absorptive capacity at a firm-level and hence at a country-level (Hansen, 2013). Through adopting an ethical standard, MNCs can also effect favourable institutional changes which translate to first mover advantage and yield a competitive advantage over other firms (Peng et al., 2008). By contrast, a failure by MNCs to consider the ethical demands of stakeholders is likely to increase international business risk and contribute to heightened instability in the host nation (Kolk & Lenfant, 2010). This represents a risk to the business's future profitability and reputation.

Moreover, in order to mitigate potential agency problems and thereby encourage outward-FDI within an integrated strategy framework, firms should increase their informational transparency and strengthen their corporate governance (Bushman & Smith, 2003). The presence of independent external board members would provide a check on the power of management and controlling shareholders, thereby enabling the firm to balance the competing needs for corporate entrepreneurship and ethical considerations (Filatotchev & Wright, 2011). Firms should also strengthen protection for minority shareholders, such that the decision to engage in FDI is based on a broader consideration of the firm's responsibilities as opposed to purely the interests of concentrated owners (Mitchell et al., 1997). In turn, this would limit the reputational risk of investment in conflict locations as such decisions would be based on generating both profitability and socially-desirable outcomes for all stakeholders (Driffield et al., 2013).

Implications for Host Nation Governments

In addition to informing business decision-making, this paper also offers insight for host nation governments seeking to attract the developmental benefits of FDI to conflict locations. Specifically, host nation governments are responsible for ensuring the development of an institutional framework conducive to ethically and socially responsible business (Peng et al., 2008). As this paper has argued, a high proportion of FDI to conflict locations is resource-seeking and extractive and this translates to rent capture by the MNC and few backward and forward linkages between the MNC and local firms. Strong institutions provide support for the enactment of contracts and thus contribute to making outsourcing of operations an attractive alternative to internationalisation (Dunning, 1979; Peng et al., 2008). In addition to fostering strong market-supporting institutions, host nation governments need to invest in their nation's absorptive capacity through initiatives such as skills training and higher education, or subsidisation for firms which adopt new technologies (Fu, 2008). Governments should also seek to cooperate with MNCs such as through public-private partnerships which encourage continued long-term investment in the host nation and subsequently mitigate the potential for rent extraction and exploitation (LaFrance & Lehman, 2005).

Conclusion

This paper has aimed to extend the existing international business and economics literature and provide a greater understanding of the motivations and impacts of MNC FDI activities. It highlights that FDI decisions to conflict locations are often primarily driven by a firm's economic responsibilities and occur where corporate governance structures allows a firm to engage in unethical behaviour to exploit the weak institutional framework of the host nation. In contrast to this current behaviour, this paper argues that firms should adopt an integrated strategy framework and promote stronger corporate governance mechanisms in order to maximise their rewards from FDI whilst maintaining the social interests of all stakeholders and contributing to host nation development. This would enable firms to satisfy the interests of all stakeholders, whilst simultaneously underpinning long-term profitability in conflict locations.

This paper is conceptual in scope and thus limited in its empirical investigation. Further research should be conducted to quantify the assertions of this paper and thus to more accurately inform firm decision-making and the policies of host nation governments seeking to benefit from inward-FDI.

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