

# Introduction: Bringing Institutions Back in the Study of Global Value Chains

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## Abstract

This article introduces and summarizes the key questions and findings of this special issue of *Global Policy* on the role of domestic and international institutions in the study of global value chains (GVCs). The article starts by briefly introducing the concept of GVCs and the state-of-the-art of the existing literature focusing on the political implications of these landmark changes in the global economy. Then, we make a case for grounding this emerging literature more strongly into an 'institutionalist' perspective. More specifically, we argue that while a great deal of attention has been paid to intra-chain governance modes – that is, the different ways in which firms organize their cross-border production arrangements – the role external institutional forces play in structuring chain dynamics remains surprisingly under-researched. These observations invite an analytical perspective that brings institutions back into the study of GVCs. The contributions to the special issue focus on multiple causal pathways linking GVCs and various types of domestic- and international institutions. Altogether, these contributions underscore that the politics engendered by GVCs, as well as how they evolve, can only be fully understood by paying attention to the external institutional context in which they are embedded.

## Policy implications

- Political decisions about domestic and international institutions—be it their creation, strengthening or weakening – have crucial implications for how firms organize production and distribution within GVCs. The stakeholders involved in policy debates about the reversal of regional trade integration in the EU (Brexit) and North America (renegotiating NAFTA), should pay greater attention to these long-term dynamics.
- Particular configurations of domestic institutions can enable countries to maintain and even expand output and employment in the manufacturing sector, even when these firms are highly integrated in GVCs. Policy debates about the reform of domestic systems of interest-intermediation or labor market institutions cannot neglect the systematic effects these factors have on firms' foreign investment choices, and on the resulting effects on patterns of domestic production and employment.
- While private standards and codes of conduct are often hailed as potential ways to govern GVCs, they either play a minor role or prove ineffective in many instances because of the lack of the necessary support of public actors. GVC-related standard-setting initiatives are more likely to be effective when devised through multi-stakeholders processes envisaging an active role for both private and public actors.
- GVCs can activate relevant societal actors (i.e. Multinational Corporations) that have an interest fostering greater global economic integration and in upholding the international institutions that support it (i.e. the World Trade Organization), even in the face of reluctance from their own political leaders and rising popular protectionist sentiments. Policy debates about the appropriate degree of global economic integration in the coming years are likely to define by a confrontation between coalitions of actors operating within or outside GVCs.

The globalization of trade, production and distribution systems stands out as one of the most important developments in the contemporary international economy (Antràs, 2010). Until the 1990s, most retailers and producers in advanced capitalist economies bought or produced the bulk of their products and inputs domestically. However, the growth of the industrial capabilities of a number of important developing countries

enabled such producers to cut costs and streamline production by outsourcing their labor-intensive, less value-added operations to low(er) income countries while at the same time retaining core competencies such as innovation and product strategy, marketing and the highest value-added segments of manufacturing and services (Elms and Low 2013; Lanz and Miroudot, 2011; OECD et al. 2013).

These transformations have contributed to changing the nature of international economic exchanges. Today, trade in intermediates accounts for over two-thirds of total imports for the majority of OECD countries (Johnson and Noguera, 2012). Moreover, it is estimated that more than 80 per cent of merchandise exports and imports of pivotal international economic players now takes place within global networks of production and distribution (see Bernard et al., 2009 for data on the USA). As a result, many goods (and increasingly also services) are no longer being produced in a certain country, but are 'made in the world' and it is now widely accepted that these changing patterns of trade, production and distribution crucially affect countries at all income and development levels (Taglioni and Winkler, 2014). Unsurprisingly, shedding light on the political economy that drives, and is engendered by these transformations has been identified as one of the key challenges for scholars in the field of International Political Economy (IPE) (Neilson et al., 2014).

The global value chains (GVCs) framework has emerged in recent years as a promising conceptual tool around which systematic thinking on these phenomena can be developed, capturing the interconnectedness of such increasingly geographically dispersed patterns of trade and production across the globe (De Backer and Miroudot, 2014; Gereffi and Fernandez-Stark, 2011; Gereffi et al., 2005; Neilson et al., 2014). Since the term GVCs was first coined, a promising research program has developed. For one, the GVCs framework spurred a wide array of large-scale data gathering and analysis projects, often initiated by international organizations, aimed at: (1) capturing the interconnectedness of economies and shifting patterns of trade and production across the globe (see e.g., OECD and WTO, 2015; Timmer et al., 2015); and (2) studying the economic impact of GVCs (Saito et al., 2013; Taglioni and Winkler, 2014). In addition, the GVCs framework triggered much work by economists, who have gone a long way in describing the phenomenon of GVCs and its implications for the dynamics of global economic competition and, in particular, which firms control and coordinate production and trade activities in the world economy (Gereffi, 1999; Humphrey and Schmitz, 2002; Sturgeon et al., 2008). Over time, scholars working in this field have also drawn attention to the social, cultural and political dimensions of these transformations (Levy, 2008). While also focusing on ongoing changes in the material economic processes of production, distribution and consumption, this body of scholarly work devotes ample attention to the role of non-chain factors and to how power relations among different sets of actors shape the structure and organization of global production (Coe et al., 2008: 280).<sup>1</sup>

Altogether, these works have gone a long way in developing the appropriate analytical tools to capture and explain ongoing changes in the global economy centered on industrial transformations constructed within system-wide dynamics of coordination and control by economic and non-economic actors (Neilson et al., 2014). And, perhaps most importantly, this body of work has been able to shed

light on these transformations' far-reaching implications, both for foreign economic policymaking and for the international economic system at large. For instance, studies focusing on these changing patterns of production and distribution have shown how they contribute to systematically decreasing demands for protectionist policies (Baccini et al., 2017; Osgood, 2017), including during economic crises (Baccini and Kim, 2012; Gawande et al., 2015), thereby reducing political support for the imposition of anti-dumping measures (Eckhardt, 2015; Jensen et al., 2015), and promoting support for trade liberalization through Preferential Trade Agreements (PTAs) (Antràs and Staiger, 2012; Baldwin, 2011; Chase, 2003; Manger, 2009). In addition, these works have shed light on the new challenges and opportunities that firms and governments in developing countries face in this new global political economy (Barrientos et al., 2011; Gereffi and Frederick, 2010; Henderson et al., 2002; Phillips and Sakamoto, 2012).

Notwithstanding the relevance and quality of these contributions, our understanding of GVCs remains far from comprehensive. In particular, strikingly little attention has been paid to systematic theorizing about- and presenting comprehensive empirical evidence on the multiple causal mechanisms connecting (national, regional and international) institutions and GVCs. This is surprising, as early work on global commodity chains (GCCs), as GVCs were first called, focused mainly on the role of (state) institutions in shaping global production. For instance, in their seminal contributions, Hopkins and Wallerstein's (1977, 1986) show how states can exercise power within GCCs in large part in the form of tariffs and rules of origin. In Gereffi's revision (1994, pp. 100–101) of the GCC concept, attention shifted to firm strategies and actions, yet he too emphasized the pivotal role of 'state policies in global commodity chains'. In his framework, Gereffi (1994) laid out four key structures that shape GCCs: input-output, geographic, (firm-level) governance, and institutional. However, of these four structures, firm level *governance* has received by far the most attention in the GVC research agenda that has developed since then, while institutions have disappeared somewhat of the scholarly radar screen. In short, GVC scholars have focused primarily on conceptualizing and accounting for different *inter-firm* governance patterns (Gereffi et al., 2005; Nadvi, 2008), treating institutions as an external 'context' within which firms actions take place.

While recent works have paid more attention to how (state) institutions constitute and are constituted by GVCs, the central focus of this research agenda has also been almost exclusively on existing political dynamics, interactions and power relations *within* value chains. As nicely argued in a recent contribution by Neilson et al. (2014), while the conceptual prisms of GVCs have long prefigured central questions about the role of state institutions, within this literature state institutions are rarely placed in the foreground, and even more rarely given due theoretical consideration. And this line of reasoning could be easily extended to the role of regional and international institutions. Few

would doubt that the emergence and increasing importance of multiple layers of governance 'above' the state, more or less formalized, has become a central feature of contemporary international relations (Mattli and Woods, 2009). Yet, systematic research on the causal links connecting GVCs with such various types of regional and international institutions is largely missing.

To be fair, recently the literature has slowly started to move in this direction. Some recent contributions focus on the role of state institutions, analyzing, for instance, whether GVCs reduce or increase the scope for state action in the domestic economy, and what strategies states can devise to support and to capture a better slice of GVCs (Curran, 2015; Lee et al., 2014; Mayer et al., 2017; Ravenhill, 2014; Yeung, 2014). Others have explicitly adopted a GVC framework to account for otherwise surprising support for trade liberalization, through Preferential Trade Agreements (PTAs) (Eckhardt and Poletti, 2016). While the former set of works shows that domestic institutions can play a role in determining where GVC production processes 'land' in the world economy, the latter suggests that GVCs may directly bear relevant actors' propensity to create international institutions. Other authors have also started to shed light on how various types of global governance mechanisms affect intra-value chain dynamics (Nadvi, 2008; Posthuma and Rossi, 2017). These important works draw attention to the need to think much more systematically about the causal mechanisms that connect GVCs and the "external" institutional context within which they are embedded.

## Institutions and GVCs

The contributions to this Special Issue systematically address the question how institutions are affected by and shape an international political economy increasingly organized around GVCs. To paraphrase a leading scholar in this field of inquiry: our aim is to bring institutions back in the study of GVCs (Sturgeon, 2009). We define institutions very broadly as sets of formal and informal humanly devised constraints that structure economic political and social interactions (North, 1990). This definition encompasses different types of institutions. On one side of the spectrum, we think of institutions as laws, policies, decision-making rules, bureaucratic institutions and governmental agencies with a more or less significant organizational standing. On the other side, we think of institutions as sets of values, beliefs, norms and shared meanings that are embedded in particular societies. In between these two extremes, we think of institutions as stable patterns, more or less formalized, of interactions between societal actors and public officials that structure the ways in which societal interests come to be aggregated and channeled in public policy-making and may even be instrumental to setting and implementing standards for production based on voluntary adherence to common rules, reciprocity and trust (Abbott and Snidal, 2009).

While GVCs can, and should, themselves be thought of as institutions, we consider them as two analytically distinct categories. Sturgeon (2009) identifies three pillars of GVCs

analysis: (1) the characters of governance modes of chains, that is, with the variation in the ways in which firms organize their cross-border production arrangements; (2) how power is distributed and exerted among firms and other actors in the chain; and (3) the role external institutional forces play in structuring chain dynamics. The analytical distinction between institutions that are internal to the chain and those that are external to it is therefore critical to enable disentangling the causal mechanisms that exist between GVCs and the external institutional context in which these institutionalized forms of inter-firm relations and power struggles are embedded.

The contributions to the special issue focus on both sides of the causal relationship connecting institutions and GVCs. One set of contributions concentrates on the dynamics of causation that go from institutions to GVCs. These contributions conceive of the organizational and spatial features, as well as the dynamics of power distribution and domination within GVCs as, at least partly, endogenous to the external institutional environment. These works thus shed light on how external institutional forces constrain or enable particular sets of organizational arrangements and power struggles within a value chain, but also on how they affect relations between actors located within and outside these GVCs. A second set of contributions focuses on the causal mechanisms to go from GVCs to institutions. This second set of contributions aims to shed light on how external institutions themselves are affected by particular governance configurations and power dynamics within GVCs. These works thus analyze instances in which the creation, design and evolution of the external institutional environment can be traced back to the influence of GVCs. The contributions to the special issue investigate these causal channels connecting GVCs and institutions located at the national and international levels. As mentioned above, we consider institutions of various kinds, ranging from formal institutions in which public actors play a dominant role, to less formalized arrangements entailing various configurations of public and private actors' interactions. Against this background, and relying on the distinction between domestic and international institutions, we briefly introduce the key questions and findings of this special issue.

## Domestic institutions and GVCs

The question how domestic institutions affect the responses of states to the incentives and constraints brought about the dynamics of international economic exchange have always been central in comparative political economy debates (Gourevitch, 2002). While there is no space here to do justice to richness and quality of this literature, broadly speaking these studies have concentrated on how a number of different institutional factors – that is, types of political systems, electoral institutions, and configurations of state-society relations – affect how preferences of societal actors are aggregated to produce particular outcomes in domestic policymaking, as well as the extent to which states develop particular domestic institutional settings with a view to

effectively extract resources to provide regulatory and redistributive public goods in the face of competitive pressures brought about globalization (Hall and Soskice, 2001; Katzenstein, 1985; Milner and Kubota, 2005; Rogowski, 1987). The centrality acquired by GVCs in the contemporary world economy opens up new opportunities for developing linkages between comparative political economy and international economics, with a view to advancing our understanding of how domestic institutions filter pressures emanating from GVCs and vice versa.

De Ville's (2018) contribution to this Special Issue sheds light on this important debate by integrating insights from the GVC literature and the so-called varieties of capitalism (VoC) literature. Starting from the observation that the domestic institutional arrangements allowing firms to deal with their coordination problems vary across countries, the VoC literature contends that these different types of domestic "institutional complementarities" – the two ideal types being coordinated market economies (CMEs) and liberal market economies (LMEs) – critically affect how states respond to the incentives and constraints generated by an increasingly globalized economy. Against this background, De Ville (2018) investigates whether these domestic institutional factors affects the strategies pursued by firms that operate in GVCs. He hypothesizes that for firms in CMEs the gains of offshoring are lower while the costs are higher than for firms in LMEs and that this will, in turn, result in a different geography of GVCs. De Ville (2018) shows the plausibility of this argument by focusing on Germany – with data for the UK and the USA as benchmarks – and convincingly shows that, although German firms are intensively integrated in GVCs, its core sectors have made relatively more use of 'nearshoring', allowing firms to retain comparative institutional advantages. As a result, Germany has managed to maintain and even expand output and employment in its core industries.

Another key debate in the IPE literature concerns the increasingly important role of governance arrangements on setting and implementing standards for (global) production in the fields of labor and human rights, as well as sustainability and the environment (Abbott and Snidal, 2009; O'Rourke, 2003). Standards are mechanisms by which public or private authorities can regulate and govern production and, as such, we see them as another set of institutional arrangements that should be included in our discussion on GVCs. Standards can take several forms: self-regulatory codes by companies and/or their trade associations; non governmental organizations (NGOs) promoting standards for voluntary adoption by companies; or multi-stakeholder organizations in which various combinations of firms, NGOs and state actors promote and implement codes of conduct for member and non-member firms (Abbott and Snidal, 2009). Until recently, there was no explicit dialogue between the literature on standards and the GVC literature. Although this is changing (Nadvi, 2008), the focus of the literature on standards and GVC has mainly focused on the role of, and implications for industry actors in setting and adopting private standards (Lee et al., 2012; Manning et al., 2012).

Two of the contributions to this special issue aim to move the debate on GVCs and standards away from a focus on *within* value chain dynamics and power relations by looking at a broader set of actors and wider political struggles around standards. Both contributions do so by focusing primarily on domestic standards.

Dermawan and Hospes (2018) highlight the growing importance of standards, as domestic private governance initiatives, within GVCs and the resulting power dynamics between state and non-state actors, through an in-depth analysis of the rise and fall of the Indonesian Palm Oil Pledge (IPOP). IPOP was a domestic institutional arrangement of the largest Indonesian palm oil producers aimed at zero-deforestation by 2020. At its initiation in 2014, IPOP was lauded as a turning point in curbing the negative impact of palm oil expansion on deforestation, yet the Indonesian Government dissolved IPOP in 2016. The authors convincingly show that the Indonesian Government decided to put an end to the IPOP, less than 2 years after it was launched, because this private business initiative was perceived as a potential threat to its sovereignty. The Government successfully framed IPOP as a threat to smallholder development, the state's rulemaking authority, and presented the IPOP as an illegal cartel. The authors argue that there is a need to bring domestic state institutions back into GVC analysis, as the state is bringing itself back into GVC governance because it experiences that firm-driven governance of GVCs affects their sovereignty over territory, rule-making, producers and economic organization.

Heron et al. (2018) on their part also look at domestic private standards as an institutional arrangement through which GVCs are governed and regulated. In their contribution, the authors aim to overcome the 'firm centricity' of existing scholarship, which has looked mainly at how private standards are used by powerful retailers to control supply chains, by looking at the role of both state and non-state actors in the rise of such standards and the broader (domestic) institutional context in which they emerge. To this end, Heron et al. (2018) carry out in-depth analysis of the GVC governance of soy in general and private standards schemes linked to the soy GVC in particular. The authors trace the actors that have shaped private certification initiatives related to GMO-free soy and deforestation in Brazil and conclude that private standards have played a relatively minor (and largely ineffective) role in the governance of soy. They describe one Brazilian initiative that has been successful: the 'Soy Moratorium'. This voluntary initiative, commits the soy industry to avoid buying soy grown on deforested lands and the authors show that the initiative's success is attributable to the ability of a few relevant actors to exert control on the process, the simplicity of the compliance requirements, and the active support of the Brazilian government.

### International institutions and GVCs

The remaining contributions of the Special Issue highlight various causal mechanisms linking GVCs and institutions located 'above' states. Economic policy-making increasingly

takes place within a complex, multilateral context, consisting of bilateral, regional and global institutions, which vary widely both in terms of their degree of bindingness and with respect to their composition. The literatures on 'legalization' (Abbott et al., 2000) or on the rational design of institutions (Koremenos et al., 2001) have widely investigated the first dimension, while studies on the emergence of complex and hybrid forms of governance encompassing different configurations of public-private actors' relations have shed light on the second (Eberlein et al., 2014; Mattli and Woods 2009). The contributions to this special issue seek to advance the debate by investigating the causal links connecting GVCs and international institutions varying along the three dimensions of geographical scope, degree of legalization and type of governance.

Looking at the causal dynamics going from GVCs to international institutions, one contribution focuses on how GVCs affect the performance of a global, and highly legalized institutions such as the World Trade Organization (WTO). The WTO stands out as a prime example of strong legalization and delegation of authority in international politics (De Bièvre et al., 2014). The functioning of a governance system which regulates over €23 trillion in trade in goods and services on a yearly basis, ultimately depends on its judicial arm's ability to prevent opportunistic behavior by its members, and on its ability to restore compliance when these are found to violate WTO rules. Unsurprisingly, the politics of WTO compliance has attracted a great deal of attention (for a review of this literature see Poletti and De Bièvre, 2016). However, and quite surprisingly, we know very little about how the performance of the crucial institutional of the post-WWII liberal international order is affected by GVCs.

The contribution by Yildirim et al. (2018) helps filling this gap by showing that decision-makers are more likely to try and eliminate barriers to cross-border trade by tabling WTO complaints when facing pressures by firms and sectors highly integrated into GVCs. In particular, the contribution shows that whenever a potential WTO dispute touches upon the interests of Multinational Corporations, policymakers in complainant countries can expect these firms' affiliates in defendant WTO members to contribute to a political climate that is more conducive to compliance. This finding has important implications for the current debate about the continued centrality of the WTO, particularly in light of anti-WTO rhetoric of the current US administration, as well as its blatant attempts to undermine its functioning and legitimacy. Indeed, this analysis suggests that GVCs activate relevant societal actors (i.e. MNCs) that have an interest to uphold existing multilateral trade commitments even in the face of reluctance from their own political leaders.

Two additional contributions look into the causal mechanisms linking GVCs and bilateral or regional international institutions such as PTAs. GVCs have been widely shown to stimulate PTAs. For one, firms integrated in GVCs are increasingly reliant on imports of intermediate inputs. This changes the balance of domestic trade-related interests by increasing the domestic coalition of firms favoring trade liberalization. While traditionally seen as a battle between firms

exporting in foreign markets, that is, firms in export oriented sectors, and firms fearing competition from foreign producers, that is, firms in import-competing sectors, GVCs make import-dependent firms more important in the domestic political economy and thus stimulate support for PTAs (Eckhardt and Poletti, 2016; Manger, 2009). In addition, GVCs create incentives for greater regulatory harmonization, generating a demand for PTAs that are broader in scope (Baldwin, 2011).

Baccini and Dür (2018) contribute to this debate by showing for the first time how GVCs interact with intra-industry trade (IIT) to produce particular preferences and outcomes with regards to PTAs. More specifically, contrary to the shared view that GVCs should always make trade liberalization easier, this contribution demonstrates that GVCs, namely, trade in intermediate goods, in the presence of IIT, that is, trade in differentiated products make trade liberalization less appealing and, therefore less likely. Baccini and Dür (2018) empirically corroborate this argument by showing that the combination of GVCs and IIT incentivizes firms to lobby alone rather than via encompassing trade organizations, and leads to lower tariff cuts in PTAs. This finding has important implications because it casts doubts on the widely held view that GVCs should always give rise to deep and ambitious trade agreements. As the paper shows, the combination of GVCs and IIT may actually decrease the depth of institutionalized international cooperative arrangements, *in casu* PTAs.

Finally, Eckhardt and Lee (2018) contribute in another important way to this debate through an in-depth case study on the preferences and political strategies of tobacco firms in the context of NAFTA negotiations. This contribution shows that while highly productive firms integrated in GVCs are generally supportive of PTAs, their preferences over the design of these institutions may vary considerably depending on the organization of their value chains at the time of the PTA negotiations. More specifically, Eckhardt and Lee (2018) convincingly demonstrate that firms sourcing the bulk of their inputs from within the PTA area have a strong preference for stringent rules of origin (RoOs), while firms depending on offshore procurement from outside the PTA area are in favor of more lenient RoOs to accommodate their foreign sourcing of inputs. This finding has important implications because it underscores that even the most productive firms may have divergent preferences over important design features of PTAs.

## Conclusions

The contributions to this Special Issue contribute to shed light on the multiple causal pathways linking institutions and GVCs. As far as the domestic side of this institutional story is concerned, the findings of the special issue suggest that the domestic institutional complementarities that characterize various types of political economies, concerns about state sovereignty, and the domestic institutional arrangements for standard setting all play a critical role in shaping how particular states respond to the incentives and

constraints brought about by GVCs. Similarly, the contributions focusing on the international institutional dimension also suggest that GVCs are a key factor influencing the politics underlying the functioning of a multilateral institution such as the WTO, as well as of PTAs. Altogether, these contributions highlight that both the globalization of production has far-reaching implications for how domestic and international institutional setups evolve and perform their functions, and that global production patterns are themselves crucially affected by such national and international institutional incentives and constraints.

## Note

1. This latter body of work employs and different conceptual terminology, the so-called Global Production Networks (GPN) framework. While acknowledging that the GVCs and GPNs frameworks draw attention on different elements they are both fundamentally concerned with the political-economic transformations brought about by the globalization of trade, production and distribution systems. For avoiding conceptual complexity in this context, we only use the concept of GVCs in this special issue to characterize works that focus on these economic transformations.

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