



Clingendael

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Business Diplomacy

Shaping the firm's geopolitical risk environment

In the 21st century firms, large and small, increasingly have to operate in foreign markets. This process of internationalization opens them up to geopolitical and other non-commercial risks in an unstable and unpredictable international environment. Business Diplomacy (BD) seeks to adapt the skills and mind-set of the government diplomat to the needs of the firm. It facilitates the exchange of best practice in the analysis and management of geopolitical risk between government and the private sector. Business Diplomacy centers on the strategic use of coalitions of state and non-state actors to shape the firm's geopolitical risk environment. While larger firms should develop their own in-house BD capabilities, smaller firms will BD support from external consultancies or other institutions.

“All diplomacy is a continuation of business by other means”

– with apologies to Zhou Enlai

The globalization of markets since the 1980s has increasingly forced firms to operate internationally. This tendency has been reinforced in the west by the contraction of domestic markets provoked by the economic and financial crisis: the economic survival of many firms is predicated on their international activities. As a consequence firms must deal with foreign governments and publics. Their financial performance becomes vulnerable to international geopolitical risk. Operations abroad impact on their reputation at home. In a world of diminishing diplomatic budgets and fragmenting rule sets, they cannot always depend on the support of their governments and embassies nor rely on international law or institutions. Traditional business management and lobbying tools provide only

partial solutions, and can prove counter-productive. **Business Diplomacy (BD)** offers a new approach, which seeks to transfer and adapt the techniques and mind-set of the diplomat to the needs of the firm. It centres on the strategic use of coalitions of state and non-state actors to shape the firm's risk environment. Larger multinational firms need to develop their own diplomatic (BD) capabilities. Smaller firms need to buy them in, from consultancies, Chambers of Commerce or other institutions. These BD capabilities include:

- Analyze geopolitical risks to their operations at both global and market specific levels.
- Identify the governmental and non-governmental actors (“geopolitical stakeholders”) who shape those risks.

- Develop multi-level, heterogeneous networks of information and influence.
- Create coalitions among the geopolitical stakeholders based on shared interests to put pressure on reluctant collaborators and marginalise “problem actors”.
- Integrate these elements into a holistic, BD strategy to promote the firm’s objectives and manage geopolitical risk.

DOING BUSINESS IN A MESSY WORLD

Firms of all sizes increasingly have to operate internationally, whether in pursuit of low production costs or new markets. The international environment in which these firms must operate is ever less stable and predictable. As firms become actors in international relations, they also become targets of international discontents, whether expressed through governments or non-governmental organizations. As US hegemony weakens, a new multi-polar world increases uncertainties about international rules and regulations, while also increasing the instabilities between and within states. As the universality of international regulatory frameworks is questioned, many states opt for national legislation with extra-territorial impact. Firms must operate in an unpredictable geopolitical environment of enhanced volatility. Like diplomats themselves, firms find their comfort zone tested by Donald Rumsfeld’s “known and unknown unknowns”.

Many of the risks confronting firms arise from the nature of globalisation itself. These include the risk to firms’ operations and reputation from non-state actors, whose campaigns are enhanced by new ICT and social media. Their campaigns frequently focus on issues on the New International Security legislation in the commercial area. The implications of the US Corrupt Practices Act are still poorly understood in particular by those non-US firms subject to it. Agenda such as human rights, labour conditions, poverty, climate change or environmental degradation. Thus when Shell sought security for its installations and personnel in the Niger estuary, the consequent crackdown by the Nigeria military shredded Shell’s ethical

reputation in its home markets. Similarly, Western fashion houses scurried to rescue their reputations when the collapse of a building in Bangladesh revealed the appalling conditions their clothes were produced in. Other issues on the same agenda, such as terrorism, financial instability and organised crime, offer a more direct threat to the firm. Islamic State endangers the installations and personnel of foreign operators in Iraqi oil fields. More subtle, but no less deadly, are the challenges posed by international governance, and in particular the recent spread of national extra-territorial

However, the relative decline of US hegemony and the fragmentation of global rule sets have resurrected a more traditional geopolitical agenda. Older threats to firms, once thought long banished, have returned. Firms must now again confront the risks of expropriation, nationalization and political blackmail, as well as the direct physical and economic threats of civil war, ethnic conflict and inter-state war. As the international environment moves from a unipolar towards a multipolar system, firms will have to navigate between competing rules sets and value systems. Existing international law may no longer offer a reliable protection. Thus when the Argentine Government expropriated its subsidiary YPF, Spanish oil company Repsol received little support from its own government, which had to balance other interests, and even less from the European Commission (theoretically responsible for international trade policy in the EU). Recourse to international law offered limited solace. Meanwhile, concerned about possible Chinese expansion into the Argentine energy sector, the US effectively endorsed the expropriation by encouraging Chevron to sign a collaboration agreement with YPF. Eventually intermediaries, with their own agendas, negotiated an out of court settlement. Likewise, an Arbitration Tribunal in The Hague may have awarded former Yukos shareholders 50 billion dollars compensation for the company’s expropriation by the Russian Government, but the shareholders are unlikely to see any of it. Government responses to geopolitical instability and conflict pose their own problems, with Russian and Western commercial operations being damaged by the tit-for-tat sanctions over the Ukraine.

LIMITATIONS TO GOVERNMENT SUPPORT

The Repsol /YPF case shows that firms cannot always rely on their national governments or embassies. Governments have to balance a number of interests and priorities. These may not coincide with those of the firm in question (in the Repsol case other Spanish firms lobbied the government not to be too robust against Argentina). The firm may be operating in a country where its national embassy carries little weight, or is far away from the capital where the embassy is situated. The government, or national reputation, may be part of the problem – the firm may not wish to advertise its nationality. Major firms and corporations often have better access and influence than the national government. Many embassies, narrowly focused on commercial work, do not or cannot offer the geopolitical support firms need. With diplomatic services being cut as a result of the financial crisis, many firms are forced to operate where their national diplomatic service is not present. Firms increasingly have to find their own solutions to geopolitical risk.

TRADITIONAL APPROACHES

With the limitations that embassy support can offer, firms frequently turn to public affairs strategies, including government/political lobbying, to tackle the threats of geopolitical risk to their operations. But these are only partial solutions, and can prove counterproductive. Government/political lobbying is an activity aimed at influencing key stakeholders, including government, in a given country. Although some of the techniques may appear similar to those of diplomats, it tends to be more narrowly focused, both in time and thematically. The aggressive focus on bringing key people “on-side” can provoke resentment and rejection as frequently as success. The focus on a given country means that even when successful in its own terms, it risks provoking adverse reactions in other countries that can damage the firms operations elsewhere. Most successful in relatively open democracies, politically

lobbying risks descending into corruption in more authoritarian or poorer countries. A successful geopolitical risk management strategy must be able to function in all foreign markets in which the firm wishes to operate at the same time, understanding and taking advantage of cultural and political differences between them. It must also be conscious of the impact of messages and activities in one country on its reputation in another, including the home country.

Nor do Corporate Social Responsibility policies alone avoid geopolitical risk. While reputation risk is important, as shown by Shell’s problems in Nigeria, lavishing resources on local communities in social welfare projects can backfire if not integrated within a broader strategy. China Power contracted with the Government of Myanmar to construct the Myitsone hydroelectric dam. Conscious that the project would be sensitive with the local people, China Power invested considerable resources in local social and educational projects. Despite this expenditure, an NGO has successfully campaigned to persuade the new government to block the project. By not integrating the “CSR expenditure” in a broader strategy, China Power allowed the local people to pocket the investment without any corresponding commitment to support the project, or China Power (China Power’s problems also show the limitations of depending on government support: the Chinese government has broader strategic considerations in the region, including not upsetting the government of Myanmar).

MOVING TOWARDS BD

Firms increasingly need to adopt their own strategies and practices for the analysis and mitigation of the effects of geopolitical risk. These strategies and practices are familiar to students of diplomacy from their studies of both national foreign ministries and their diplomatic networks abroad. They include the identification of the geopolitical risk to the firm’s operations at a global level (“Geopolitical Risk Audit”) as well as the political economy analysis of the individual markets the firm is operating in. While the former should inform the

firm's broader strategic planning, the latter should serve as the basis for creating networks of influence and information among those actors, governmental and non-governmental, who shape and drive the political risk environment of the firm in that given market. For larger corporations these networks may need to include international as well as national actors, and the ability to link between different markets. These networks allow firms to form "coalitions of the willing", based on common interests rather than shared world-views, to secure their commercial objectives. Firms also need to develop contingency plans for coping with geopolitical and other national and international crises. Contingency planning extends beyond political work to consular-like activities, such as the evacuation of staff from crisis situations, and even to activities analogous to military action (e.g. a firm resorting to international legal action to block vital supplies to a country with which it is in dispute). In carrying out these activities, firms face many of the same problems faced by national diplomatic services: the exponential growth of non-state actors, with a corresponding rise of stakeholders who must be included both in cultivation networks and geopolitical strategies and risk analysis; implications of new ICT and social media; and the dangers of asymmetric resistance tactics.

BD AS GRAND STRATEGY FOR FIRMS

BD aims to help larger firms develop those diplomatic capabilities by transferring the techniques and "world view" of the diplomatic strategist to the needs of the firm. It develops the methodology that allows smaller firms to buy them in from consultancies or other institutions. Unlike CSR, it is not about the image or reputation of a firm, unless that is central to managing geopolitical risk. Unlike Public Affairs, BD understands that firms operate in a four-dimensional space across time and geographical extension. It develops a 4-D holistic vision that encompasses the history of the firm and its markets and forecasts of their future, as well as linking

the firm's operations across all its markets. In particular, it aims to avoid the "solution" to risk in one market provoking new problems in other markets or at home. BD recognises that the core objective of a firm is to make profit. The role of BD is to help ensure that the firm's ability to make profits at in foreign markets is not undermined by geopolitical risk. To do this, BD draws on both traditional diplomatic techniques and more innovative public diplomacy approaches to cultivate networks of influence and information. From these networks, BD creates "coalitions of the willing" built around shared interests rather than common world-views. These coalitions, which can include international institutions, national and sub-national governments, NGOs and other firms, serve as power and influence multipliers. They aim both to promote the firm's interests and mitigate geopolitical risk. The networks of information/influence and the coalitions are integrated within a BD strategy driven by both the firm's commercial objectives and the analysis of the geopolitical risks to those objectives. BD strategies aim to shape the firm's geopolitical risk environment in such a way as to prevent problems arising. Preventive BD, like all preventive diplomacy is not always visible. Its successes by definition are often defined by the lack of activity. However, just as good public diplomacy creates the environment in which policy objectives can be more easily secured, good long-term BD creates the environment in which commercial objectives and ambitions are more likely to be realised.

CRISIS BD

But even the best BD cannot always prevent problems arising. BD can be used to rescue firms suffering from geopolitical risks crises. Thus Repsol could have responded to the expropriation of YPF by developing a BD campaign to put pressure on the Argentine government. The Chinese Chamber of Commerce for Manufactured and Electrical Goods did respond to moves by the European Commission to impose quotas on Chinese solar panels by looking for allies in Europe. But as with ordinary Crisis Diplomacy, Crisis BD looks to pick up the pieces after the crash, rescuing what it

can from the mess. BD is more effective as a long-term approach which looks to anticipate and manage geopolitical risk in such a way that the crash does not occur. Even if a longer term BD strategy is unable to prevent geopolitical problems arising, its preparatory work will make Crisis BD more effective. Crisis BD also depends on key networks of influence/information, and interest-based coalitions to pressure key actors to change their behaviour. The Coalitions are much easier to generate if the key networks are already in place.

BD AS COUNTER-INSURGENCY (COIN) FOR FIRMS

Like governmental diplomacy, BD is not always soft. BD often aims to use coalitions to bring pressure onto governments or other key actors to change regulatory frameworks, change the law or modify their behaviour. Thus when the Bulgarian government insisted on regulating its mining industry in a way that discriminated against foreign firms, Canadian mining firms were able to create a coalition formed by their government, the European Commission and other mining firms to persuade the Bulgarian Government to amend the regulatory framework to allow foreign firms to compete for mining concessions.

But sometimes a key actor or stakeholder may not be amenable to pressure or influence. In some cases, a stakeholder may have decided to block or damage the firm's activities regardless of the arguments or actions of the firm. This appears to be what happened in Myanmar, when an NGO resolved to block the Myitsone dam project regardless of the arguments or actions (from which local people had benefited) of China Power. Such actors are analogous to extremist groups with which governments cannot negotiate, and the BD response is similar. BD strategies seek to build coalitions with those that can be convinced to isolate those that cannot. Instead of wasting time in negotiation with the "hold-outs", BD focuses on isolating and eventually marginalising them. As with government COIN (counter-insurgency) strategies, a key capability is

to identify at an early stage the shared interests which enable some stakeholders to be won over and drawn into coalitions, as well as identify those stakeholders with whom the firm has no shared interests and thus no prospect of convincing. Had China Power been able to develop a full BD strategy in Myanmar, it would have been able to isolate the NGO which has now blocked the project, and its argument that this NGO is in fact promoting the interests of a third country would have been more effective. Likewise, firms operating in regions with a terrorist or insurgency threat should look to build coalitions with local and regional actors that will offer protection from, or at the very least advance warning, of violence against their personnel or installations.

BUILDING THE BD STRATEGY

Geopolitical risk does not prevent firms from operating successfully in conflict zones. It is not the only, or even decisive, factor in their financial performance, or the performance of financial markets. It functions as one factor among many, but one of increasing importance and one that firms often have trouble integrating into wider management and commercial strategies. BD offers a way to manage and shape a firm's geopolitical environment so as to minimise the impact of geopolitical and other non-commercial risk on the bottom line. It does so by transferring to the firm not only the skill-set but also the mind-set of the diplomat. In doing so it focuses on:

- **Geopolitical Risk Audit:** analyzing the geopolitical threats to a firm's international operations in such a way that the analysis can be integrated into long term commercial strategies. In particular markets, it analyzes the key political, economic and legislative trends and threats to the firm's activities.
- **Geopolitical Stakeholder Audit:** identifying the key actors, governmental and non-governmental, who shape the firm's geopolitical risk profile in such a way as they can form the basis for national and (if necessary) global information and influence networks.

- Developing and managing effective **networks of information and influence** in the key foreign markets that enable the firm to both shape policy environments in their favour and to anticipate future problems.
- Drawing on this network, implementing **innovative public diplomacy strategies** that go beyond marketing and lobbying to engage with civil societies both abroad and at home.
- Developing a **BD Strategy** to generate **coalitions among key stakeholders** based on common interests both to promote the firm's "geopolitical objectives" and to isolate "problem actors".
- Creating networks within and without the firm to **manage knowledge and skills** in an uncertain world where firms cannot know what knowledge and skills they will need in 10 years.
- Developing **innovative training** to give executives both the knowledge and skills they need to carry out business diplomatic functions within the firm. By building such training around simulations, and by bringing state and non-state actors together in the training, it aims to transfer the mind-set as well as the skill-set of the diplomat.

Above all, BD aims to develop within the firm a **4D strategic vision**, which extends backwards and forwards through time and across geographical boundaries to include all countries where the firm operates, or which could affect the firm's operations. In a multi-polar world of fragmenting rule sets and regulatory frameworks and increasing open and latent conflict, BD, and the business diplomat, must function as the **geopolitical GPS** of the firm.

About Clingendael

Clingendael is the Netherlands Institute of International Relations. We operate as a think-tank, as well as a diplomatic academy, and always maintain a strong international perspective. Our objective is to explore the continuously changing global environment in order to identify and analyse emerging political and social developments for the benefit of government and the general public.

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