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Navigating turbulent waters: the strategic role of embeddedness in location decisions

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Abstract

Purpose – This study aims to investigate how political and institutional embeddedness (PIE) operates as a strategic mechanism shaping multinational enterprises' (MNEs) location decisions in non-core regions in emerging economies.

Design/methodology/approach – Drawing on location theory and economic sociology, the analysis is based on semi-structured interviews with representatives from BMW, a German automaker that set up a production unit in Santa Catarina, a non-core Brazilian state.

Findings – Results reveal that MNEs develop PIE prior to foreign direct investment (FDI) as a strategic choice, influencing their location decisions. PIE moderates the effect of conventional determinants in non-core regions and mitigates the impact of host-country complexity, contributing to the creation and/or exploitation of ownership, location and internalization advantages.

Research limitations/implications – The findings indicate that MNEs strategically build PIE pre-FDI, which accelerates MNEs' learning about non-core locations and deepens the construction of social and political networks. Analysing the relative importance of firm characteristics and contextual factors is still necessary. The authors recomend investigating how resources generated from PIE impact perceived distance at the national level.

Practical implications – The results suggest that MNEs can strategically manage their pre-FDI choices through PIE, enabling diversification of subnational location strategies. The study also highlights elements that can inform public policies aimed at attracting and retaining FDI at the subnational level.

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Originality/value – The authors advance beyond conventional economic and institutional factors and analyze embeddedness pre-FDI. They integrate conventional determinants and PIE, examining their synergy and capturing their effects in isolation and interaction.

Keywords Determinants of FDI, Subnational location, Political and institutional embeddedness, Non-core regions, BMW

Paper type Research paper

Introduction

The importance of location decisions for a firm's competitiveness has been extensively researched, mostly using cross-country analyses. Although recent decades have brought greater attention to subnational variations (Hutzschenreuter, Matt, & Kleindienst, 2020), multinational enterprise (MNE) subsidiary location decisions are still studied mainly through conventional factors such as economic endowments, institutional quality, taxes and agglomerations, often centered on core regions (Dunning & Lundan, 2008; Kim & Aguilera, 2016; Nielsen, Asmussen, & Weatherall, 2017; McDonald, Buckley, Voss, Cross, & Chen, 2018).

While conventional determinants are important, they may not capture emerging economies' complexities and institutional dynamics, which lack the stability assumed by mainstream theories (Mbalyohere, Lawton, Boojihawon, & Viney, 2017). In an increasingly politicized international business (IB) landscape (Saittakari et al., 2023; Beugelsdijk & Luo, 2024), where subnational borders reshape business dynamics, accessing new knowledge sources is vital for MNE competitiveness and survival (Meyer, Mudambi, & Narula, 2011; Florida & Adler, 2022).

In uncertain contexts, MNEs rely on external learning through embeddedness. In IB literature, "embeddedness" describes the extent to which a subsidiary's local relationships (with companies, institutions, governments and actors) generate knowledge and enhance performance (Ratajczak-Mrozek, 2017; Florida & Adler, 2022).

While short-term immersion before entry may provide initial insights into a host country's investment climate (Harrison and Elaydi, 2014), embeddedness with institutions and governments is generally assumed to occur post-subsidiary establishment (Uzzi, 1997; Dacin, Ventresca & Beal, 1999; Hess, 2004; Heidenreich, 2012a; b; Mbalyohere et al., 2017; Röell, Arndt, & Kumar, 2022). There is a limited understanding of how pre-FDI (Foreign Direct Investment) political and institutional embeddedness (PIE) shapes MNEs' subnational location decisions, particularly in non-core regions.

This study examines the role of pre-FDI PIE in subnational location decisions within a non-core region of an emerging economy. We present a unique case study (Patton, 1990; Stake, 2005) of BMW, a German automobile company that, in 2012, established production in a Brazilian state previously overlooked by other global automakers.

Our contribution has two main aspects. First, we integrate a subnational perspective into the Eclectic Paradigm (Dunning, 1980; 1988), linking it to embeddedness to better conceptualize location complexity and determinants. This approach highlights how PIE facilitates institutional arbitration between national and local contexts (Donnelly and Manolova, 2020), enriching the location paradigm. Second, we emphasize the strategic role of embeddedness in the pre-FDI phase, showing how it can transform a non-core location into "a secure port amidst turbulent waters", enhancing and expanding ownership, location and internalization (OLI) advantages.

We provide practical insights for companies planning pre-FDI subnational strategies and for policymakers developing FDI attraction policies to enhance competitiveness in emerging markets.

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After presenting the theoretical framework, we discuss the methodology, empirical setting and case study. We then share findings and propositions, concluding with contributions to IB literature and practical insights for management.

Theoretical framework

Location and multinational enterprise strategy

Dunning (1980) first recognized the importance of location in IB, defining host country characteristics as critical to production internationalization. The eclectic paradigm, or OLI Model, analyzes MNEs' cross-border activities (Cantwell & Narula, 2001; Saittakari et al., 2023), focusing on ownership advantages (firm-specific strengths), location advantages (host market factors impacting performance) and internalization advantages (benefits of internalizing operations over outsourcing) (Dunning, 1998).

In IB literature, three main determinants define location advantages (Dunning & Lundan, 2008). First, "endowment effects," or economic factors affecting firm revenues and costs, include market size, labor availability, costs, skills, infrastructure and logistics. Second, "agglomeration effects" stem from specialized labor, access to inputs and knowledge spillovers (Nielsen et al., 2017). These are termed conventional economic determinants. Third, "policy-induced effects" relate to interventions improving economic appeal or reducing institutional distance, termed conventional institutional determinants, covering education, infrastructure, institutional quality and taxation (Dunning & Lundan, 2008; Kim & Aguilera, 2016). However, with its cross-country focus, the OLI model lacks a nonmarket strategy perspective (Mbalyohere et al., 2017).

National borders shape the nature of business (Beugelsdijk & Luo, 2024), but subnational borders also play a critical role in influencing politics, economic development, institutional environments and local actors (Florida & Adler, 2022). In the global economy, organizations must navigate diverse institutional contexts at both levels, each presenting unique opportunities and challenges. However, despite increasing studies on subnational dynamics, there is a lack of "research on the conceptual advancement of subnational level research" (Hutzschenreuter, Matt, and Kleindienst, 2020: 10).

Emerging markets lack the institutional stability assumed by the OLI model (Mbalyohere et al., 2017), exhibiting institutional voids (Khanna & Palepu, 1997) and internal differences that cross-country analyses often miss, causing contradictory findings on institutions' roles (Tomelin, Amal, Hein, & Dani, 2018). In such contexts, MNEs must demonstrate both business and institutional entrepreneurship to address these voids at national and subnational levels (Mbalyohere et al., 2017).

MNE environments are characterized by market imperfections, networks and institutions, often shaped by political factors (Saittakari et al., 2023). As MNEs operate across borders and are embedded in diverse national and subnational contexts, a deep understanding of these contexts is essential for meaningful analysis (Heidenreich, 2012a).

Research on FDI determinants and the influence of politics on location primarily emphasizes the advantages of core, metropolitan regions or global cities (Ma, Delios, & Lau, 2013; Goerzen, Asmussen, & Nielsen, 2013; McDonald et al., 2018; Saittakari et al., 2023). However, a comprehensive framework for analyzing subnational FDI determinants remains lacking, particularly in non-core regions (McDonald et al., 2018).

Non-core regions are typically seen as less favorable for FDI unless they are close to core regions (McDonald et al., 2018). However, their ability to attract or repel FDI depends on their political and institutional assets, and their interrelations with the broader national context (Goerzen et al., 2013; McDonald et al., 2018). Variations in subnational institutions

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can influence conventional determinants, mitigating or amplifying national-level challenges (Batschauer-da-Cruz, Eliete Floriani, & Amal, 2022).

The increasingly politicized IB landscape (Saittakari et al., 2023) involves a broader range of actors, including local governments, cities and NGOs, adding complexity to interactions (Florida and Adler, 2022). Political actors shape business networks, making political embeddedness vital. It entails building ties based on power, commitment and trust with institutions and actors (Granovetter, 1985; Halinen & Törnroos, 1998; Welch & Wilkinson, 2004).

Since the early 2000s, IB research has recognized that MNEs not only adapt to but also shape their environments (Cantwell, Dunning, & Lundan, 2010; Heidenreich, 2012b). To address frictions arising from diverse institutional contexts, MNEs must develop institutional strategies, with institutional embeddedness offering an effective approach (Röell et al., 2022).

Political and institutional embeddedness

Polanyi (1944) introduced the concept of embeddedness to describe how non-economic institutions influence economic activity. Granovetter (1985) expanded it, arguing that economic actions are embedded in social relations and should not be viewed independently. In IB literature, "embeddedness" refers to how a subsidiary's local relationships generate knowledge, enhance performance, reduce business costs and manage complexity (Ratajczak-Mrozek, 2017).

Several authors (Dicken and Thrift, 1992; Uzzi, 1997; Dacin et al., 1999; Hess, 2004; Sat, 2006; Meyer et al., 2011; Mbalyohere et al., 2017) have integrated the concept of embeddedness into organizational strategy research. Although while Harrison and Elaydi (2014) demonstrated that companies can engage in short-term pre-entry immersion to gather investment climate information, most studies assume embeddedness occurs after a subsidiary is established.

Yet negotiations and exchanges with institutions and governments often occur before FDI. The institutional characteristics of subnational regions and the roles of their representatives influence MNE decisions as regions compete to offer the best business environment (Monaghan, 2012). This highlights the need to explore the interplay between embeddedness and location advantages in the pre-FDI phase, where MNEs interact with various actors to determine the optimal subsidiary location. Therefore, distinguishing between pre-FDI and post-FDI embeddedness is essential.

The relationship between governments and MNEs involves mutual dependence, balancing tensions and shared goals. MNEs may adapt or influence, while governments can coerce or support (Hadjikhani & Ghauri, 2001). In unstable or developing nations, MNEs strategically use political embeddedness to mitigate market uncertainty and counteract the challenges of interventionist policies and regulatory frameworks (Welch & Wilkinson, 2004).

Political embeddedness has been studied in relation to firm strategy, internationalization, performance (Haveman et al., 2017; Michelson, 2007; Okhmatovskiy, 2010; Peng and Luo, 2000; Sun, Mellahi, & Thun, 2010; Talmud and Mesch, 1997) and business networks (Welch & Wilkinson, 2004). It refers to a portfolio of ties between companies and state institutions, involving power relations and enabling co-evolution (Granovetter, 1985; Halinen & Törnroos, 1998; Sun et al., 2010).

Studies on political embeddedness and FDI location focus on intergovernmental relationships, suggesting that bilateral relations (for instance, international friendship cities) boost cross-border and foreign investment (Zhang, Zhan, Xu, & Kumar, 2020;

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Hu, Natarajan, & Delios, 2021; Yao, Xie, Li, & Xu, 2023). However, they often overlook the subnational dimension and the role of embeddedness as a location determinant.

Institutional embeddedness describes the relationship between companies and their institutional environment (DiMaggio & Powell, 1983). MNEs both shape and are shaped by institutions in a co-evolution process (Cantwell et al., 2010; Heidenreich, 2012a, 2012b). Regional PIE, influenced by historical legal-political structures and power dynamics between local and central authorities, affects regional economic development (Zhang, 2013). Engagement with informal institutions and local nonmarket stakeholders enhances subnational institutional fit in new frontier developing economies (Mbalyohere & Lawton, 2022) and helps address friction from diverse institutional backgrounds (Röell et al., 2022). In order to examine these dynamics empirically, the next section outlines the methodology adopted in this study.

Methodological aspects

We conducted a single case study (Stake, 2005) of BMW, a German automobile company's entry into Santa Catarina state, a non-core region in Brazil, in 2012. The contextual richness provided by this case study enabled the identification of national and subnational political actors, processes and institutions often neglected by FDI location studies.

Empirical setting

Brazil is an ideal setting for this research. Its automotive industry began in the early 20th century in São Paulo State, home to most of the country's producers. As the world's fifth largest FDI recipient and leading economy in Latin America (U.S. Department of State, 2024), Brazil also ranked among the top ten investors in automotive R&D in 2015, a sector critical to its income and employment (ANFAVEA, 2021).

However, Brazil's market is highly complex, marked by the "Brazil Cost"—a combination of excessive red tape, intricate processes and high operational costs. Companies spend an average of 1,493 h annually on tax compliance, the highest globally (TMF Group, 2022; World Bank, 2021).

Income disparities in Brazil are significant, with the Southeast's per capita GDP nearly three times higher than the Northeast's (IBGE, 2019). São Paulo historically holds nearly 50% of FDI stocks (BCB, 2022). Companies must navigate municipal, state and federal tax regulations, with states offering financial benefits and ICMS incentives, fueling a "fiscal war." This underscores the importance of subnational institutions, which can create favorable local environments, even in non-core regions, to offset national-level complexities (Batschauer-da-Cruz et al., 2022).

Case selection and description

Our case study investigated how PIE in the pre-FDI phase shapes MNEs' subnational location decisions in non-core regions. After defining our research question, we selected the case and established the data collection instruments.

The case was selected to complement our theoretical framework (Eisenhardt, 1989) and the variables under study. We sought a foreign MNE in Brazil that chose a non-core state with less prominent economic and institutional conventional determinants, a small market size and limited FDI flows. The selected unique case (Patton, 1990) is a German company, Bayerische Motoren Werke (BMW), one of the world's top ten car manufacturers, producing three major luxury car brands. Operating more than 30 facilities across 14 countries and

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selling in 140 countries, the company chose an unexpected Brazilian location with no prior car manufacturers, diverging from the usual hubs in São Paulo, Rio de Janeiro and Minas Gerais.

Using primary and secondary data, such as the company's presence in Brazil, PIE development and the decision to establish a plant in a non-core region, we tracked over 17 years (1995–2012) of the company's history, including post-production insights. The case approach (Eisenhardt, 1989; Yin, 2009) provided the contextual depth needed to identify key actors and processes in the subnational location strategy.

In 1995, BMW partnered with a Brazilian company and acquired its authorized importer, establishing a national sales company. By 2009, it introduced another vehicle brand, achieving significant sales success and securing leadership in Brazil's premium segment. In 2011, with Brazil's economy growing 2.7% and the car market reaching 3.4 million units – an 11.91% increase compared to 2009 (G1, 2011) – BMW announced plans to establish a production plant in Latin America, in Brazil, Argentina or Mexico (B3).

In 2012, BMW announced plans for a new production unit in Brazil (BMW Group, 2012). At the time, automobile factories were predominantly concentrated in São Paulo, as well as in the states of Paraná, Goiás, Rio de Janeiro, Minas Gerais, Bahia, Rio Grande do Sul and Pernambuco (ANFAVEA, 2021). At the end of 2013, BMW began the construction of a plant in a small town in a non-core state, an area previously overlooked by other global automakers (BMW Group, 2013).

Data sources and collection

To mitigate potential biases, we used two primary evidence sources: (a) BMW informants involved in the decision-making process for the subsidiary installation in Brazil and (b) institutional actors directly involved in negotiations leading to its establishment in Santa Catarina (SC), a non-core state.

For data collection (Eisenhardt, 1989), we used a semi-structured interview script (average duration: one hour) to reconstruct BMW's international strategies. Seven interviews

Table 1. Informants

Interviewees	Identification	Relevance to the case
Interinstitutional relations manager	B1	Previously worked at the NC state government's international liaison secretariat
Senior quality control manager	B2	Responsible for verifying the operating conditions at the site against BMW's quality standards
Government affairs representative	B3	Responsible for negotiating following decisions taken at headquarters. Participated in negotiations with the federal government and several state governments
Environmental licensing manager	B4	Managed the environmental licensing process at three levels of government
Senior manager of technology and innovation	B5	Managed activities involving technology and innovation
Former state governor	B6	State governor at the time of installation. Directly involved in negotiations to attract the company
Former NC state secretary for economic development	B7	State government representative who led the negotiations and was in contact with the company to resolve all types of demands on both sides

Source(s): Table by the authors

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were conducted (three in person, four online), with consent recorded at the start of each session. Details of the informants are provided in Table 1.

The informants, who were actively involved in the subsidiary's establishment in Brazil, provided reliable insights. The interviews explored perceptions of key conventional determinants and the role of ties, capturing PIE aspects that influenced the location decision. Two researchers conducted the interviews, taking notes and recording them. Transcriptions were cross-checked to ensure accuracy. Additional interviews or email exchanges were conducted post-analysis to clarify findings and strengthen the emerging theorization (Welch, 2000).

To mitigate retrospective and interpretive biases (Jick, 1979; Eisenhardt, 1989), we used data triangulation with archival sources, including 15 newspaper articles, 12 company reports and 3 scientific articles. They complemented interview data, uncovering detailed accounts often lost to memory (Welch, 2000). Archival records aligned significantly with interviewee accounts, reinforcing the findings.

Triangulation with secondary data verified whether BMW's intended strategy aligned with actual location outcomes, which were documented in official reports. However, most insights emerged from interviews, driven by our research objective to understand BMW's location strategies, incorporating respondents' perceptions and intentions.

Data analysis

Data analysis (Miles, Huberman, & Saldaña, 2014) followed these steps: first, interview and archival data were synthesized into tables and case narratives, focusing on Brazil's internationalization process, conventional determinants and pre-FDI PIE development. Second, a case history was created to capture the timeline and context of location decisions. Third, interviews were individually coded and recoded using respondent phrases to develop primary categories. Preliminary analysis and open coding of transcripts and secondary materials occurred iteratively after each interview until data saturation was reached (Saldaña, 2021). Table 2 reports the codes, categories and examples from the data.

Fourth, we conducted content analysis, organizing citations by determinants and PIE elements and triangulation with secondary data to enhance reliability (Yin, 2009). Fifth, through iterative coding, we refined first-order categories, second-order themes and aggregate dimensions, establishing stable and theoretically significant codes (Gioia, Corley & Hamilton, 2013; Gioia, 2021; Locke, Feldman, & Golden-Biddle, 2022). This iterative process connected empirical data with literature to anchor emerging concepts (Miles et al., 2014). Finally, we defined two aggregate dimensions, forming the foundation of our emergent model, which illustrates the dynamics of PIE. Figure 1 presents the data structure.

Our analysis highlights conventional determinants while advancing to a perspective that integrates the PIE concept to explore interactions between local and national contexts, including ties with institutions, governments and local actors, to extend an understanding of MNEs' location choices in non-core areas of emerging economies.

Findings

Using primary and secondary data, we tracked BMW's journey from the announcement to factory establishment in Brazil, highlighting key actors and the decisive role of pre-FDI PIE in choosing a non-core region in an emerging market.

In response to the 2008–2009 crisis and rising Chinese imports, Brazil reduced the Tax on Manufactured Goods (IPI) to boost vehicle demand as part of the new automotive industrial policy launched in September of 2011 to limit import growth, called "Inovar-Auto".

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Table 2. Codes, categories and examples from data

Codes	Categories	Examples from data
Market attraction Agglomerations Main clients Logistic costs Logistic efficiency Ports Roads Labor availability Labor costs Labor skills	Economic determinants	"… according to income and population, this is where the main market is" (B1) "If you look at travel time, distance from the port of Santos to the city of São Paulo … we get from here to there faster than the customs clearance done by Santos" (B1) "[In Santa Catarina, workers proved to be] the quickest to learn. So the training here was theoretically the most efficient, of great comparison to the [sic] world" (B2)
Bureaucracy Complexity Corruption Transparency Licenses Environmental stringency Taxes Culture Quality of life	Institutional determinants	"Health care, security, etc., of the locality… find areas that were possible to implement or that followed all the sustainability criteria" (B1). "If the rules of the game are clear and transparent, … operations will be running very well [and]state dialogues have, let's say, less impact on business in the strategic sense" (B2)
FDI attraction policies Cooperation with local governments and institutions Institutional enhancements promoted by local government Facilitation of processes Support from local government De-bureaucratization initiatives Learning Ties (individual and/or institutional ties between the company and the constituent parts of the state)	Institutional embeddedness	"We have an exciting relationship with ACIJ, FIESC, ANFAVEA, the National Automotive Industry Association, AHK, the Brazil-Germany Chamber of Commerce, SESI, SENAI, and the industry federation in general. It has different associations… The port is also a partner" (B1)
Commitment and compliance (with what is agreed) Reciprocity Relationships Trust Imposed conditions	Political embeddedness	"Professionalism on both sides … There is much transparency here" (B1). "We have a history of fulfilling contracts" (B6) "[Santa Catarina was] a peculiar case, as BMW was the only one for which incentives generated an obligation. There were commitments on both sides" (B2)

Source(s): Table by the authors

By December 2012, manufacturers had to use at least 65% local or regional parts, invest in R&D and perform most production stages in Brazil to avoid a 30% IPI increase (Sarti & Borghi, 2017). "BMW decides on local production only if the market determines it" (B3). Initially, the plan was to assemble cars with a partner, but "[…] an additional 30% in IPI […] was going to increase the final price" (B3), making local production the solution.

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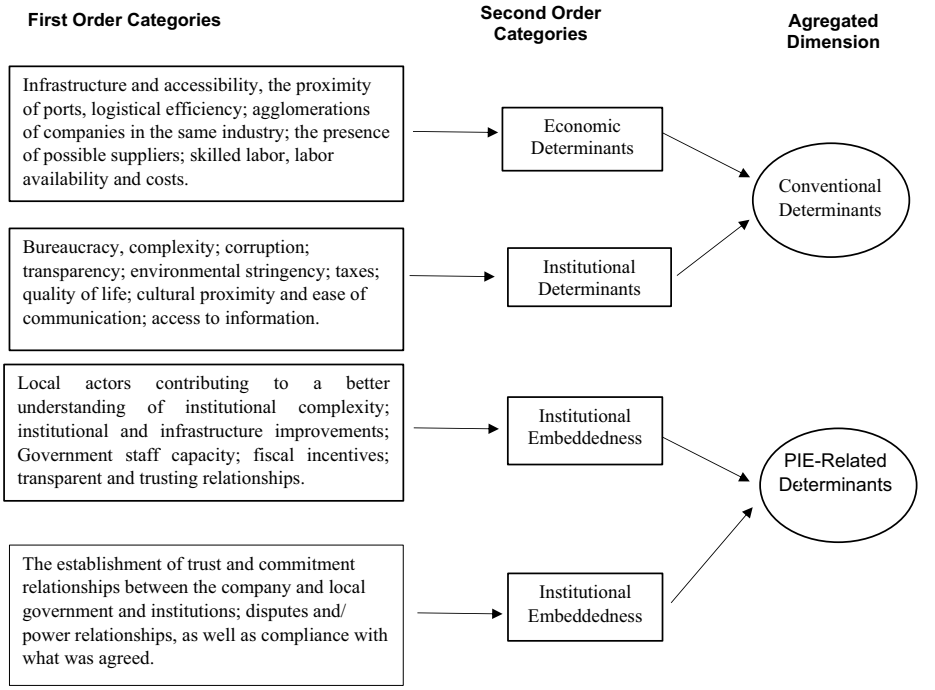

Figure 1. Data structure
Source: Figure by the authors

The changes in Brazil's institutional landscape forced BMW to adjust its strategy. Inexperienced, it hired consultants for government relations (Navarro, Dias, & Valle, 2013), though progress was slow and complex. BMW engaged with Brazil's Automotive Vehicle Importers Association, the SP Federation of Commerce and key government entities, including the Ministry of Development and the Ministry of Finance. "BMW provided high-level technical and benchmarking studies from other countries" (B3), helping the government recognize the premium segment niche.

Detailed regulations for the new regime were published only in 2012 (Presidency of the Republic, 2012), establishing more flexible rules for newly established companies in the Premium segment. Nonetheless, the efforts at the federal level were only the start of tackling the immense challenge of setting up a manufacturing plant in Brazil. BMW's project morphed from a simple assembly plant in partnership with a local company to "much more robust than necessary" (B3). The company faced the difficult and complex process of executing the project quickly enough to benefit from Inovar-Auto.

After announcing its intention to invest in Brazil in 2011, several states offered the company tax exemptions (Rolli, 2011). Initially, the focus was on "São Paulo [SP], Rio de Janeiro [RJ], and Minas Gerais [MG] states as possible sites for investment" (B1). "Since the volume was very low, the intention was […] to locate close to São Paulo, which is our biggest market and where other companies are located…" (B3).

At this point, Santa Catarina, as a non-core state, was not on BMW's radar. All previous attempts to attract a car factory to the state had failed. This time, the Santa Catarina

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Government took a proactive approach. “We got into a fight with giants, and we knew we needed to dare to compete with SP, RJ, and MG” (B7). While BMW waited three months for an unfulfilled meeting with a core state, “Santa Catarina made a powerful play to attract BMW; they even scheduled a meeting with our current CEO in Germany” (B3).

By the end of the analysis process, BMW had narrowed its options to four sites: two in São Paulo (SP) and two in Santa Catarina, a non-core state without any automotive manufacturers. In 2012, BMW chose the state of Santa Catarina as the location for its first premium car production subsidiary in Brazil. Construction began in 2013 in the small town of Araquari, near Joinville, the state’s largest city, with 400,000 inhabitants – relatively small by Brazilian standards – and production started in 2014.

Figure 2 shows a timeline illustrating the process of setting up BMW’s subsidiary in Brazil.

In October 2014, “the first car rolled off the assembly line at our new plant” in Brazil (BMW Group, 2014: 16). Brazil’s market size drove the country choice, but Santa Catarina represented only 1.1% of Brazil’s territory and 3.2% of its population (IBGE, 2019), lacking large urban centers. São Paulo, Minas Gerais and Rio de Janeiro host most automobile producers, skilled labor and specialized suppliers (Rolli, 2011). However, Santa Catarina offered available labor, a well-developed metal-mechanical sector that could be trained (SAI, 2021), and lower congestion costs: “We arrive faster [in São Paulo] from here than if we were there […] There is a lot of competition [in larger states], and the Southern market also has considerable potential” (B2).

Finding suppliers is complex in this segment “due to scale issues” (B1). However, “in SP we would be just another car producer. In Santa Catarina we were ‘THE’ [and only] car producer” (B3). Most direct suppliers are still in SP, “but this scenario tends to change” (B3). BMW recognized that “qualification issues and the search for professionals could be more complicated [out of SC]” (B2). In Santa Catarina, workers proved to be “among the fastest to learn […] training here was […] the most efficient of all overseas units” (B2).

Logistical costs are 12.2% of Brazilian GDP (ILOS – Instituto de Logística e Supply Chain. Custos logísticos, 2019). Transportation, inventory and storage spending can consume 7.6% (ILOS - Instituto de Logística e Supply Chain. Custos logísticos, 2019) to 12.37% (FDC, 2017; 2018) of company revenues. Logistical costs represent 12.2% of Brazil’s GDP (ILOS 2019), with transportation, inventory and storage consuming 7.6% (ILOS - Instituto de Logística e Supply Chain. Custos logísticos, 2019) to 12.37% (FDC, 2017; 2018) of company revenues. For BMW, “logistic saturation and distance to ports were very important” (B2). The factory needed to be within 200 kilometers of a port. While Santos

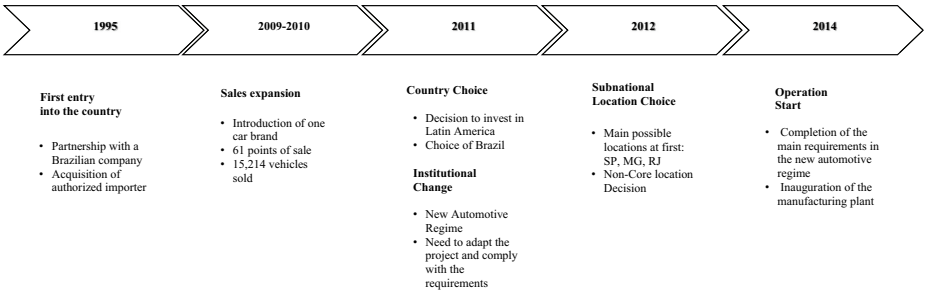

Figure 2. Timeline of the installation process
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in SP, the largest port in Latin America, is 70 km from the SP capital, "customs clearance at Santos is way more bureaucratic, complex and slower" (B2), and the port faces issues of congestion and corruption (Port Strategy, 2013).

Santa Catarina (SC) has five ports, including Brazil's second-largest by container volume. Unlike Santos, SC ports are more competitive, with less red tape and faster customs clearance, addressing one of Brazil's most complex logistical challenges (ILOS - Instituto de Logística e Supply Chain. Custos logísticos, 2019).

In addition, there was a strong synergy with several local actors: "We explain our objectives and what we want, and they are fulfilled […]. The port, industry associations, customs, I couldn't list them all" (B1). "It is an extensive cross-section … there is a search for interaction and contacts on both sides in the region." (B2). "The assistance and attention received from all institutions in Santa Catarina […] gave us serious and transparent support" (SAI, 2021).

Santa Catarina ranks second in the States' Competitiveness Ranking (CLP, 2022), with minimal red tape and corruption risks. "Professionalism on both sides… There is a lot of transparency here" (B1). The state "has a history of fulfilling contracts" (B6). Moreover, "German culture […] is rooted in Santa CAtarina" (B3), "we feel at home" (SAI, 2020). The "cultural issue weighed on our decision" (B2).

"Safety, health, bilingual schools… where expatriates could live, and their children could study, and overall quality of life" (B1) were key factors. Santa Catarina boasts a high Human Development Index, low crime rates and strong infrastructure, education and innovation levels (CLP, 2022).

In July 2011, a German delegate visited SC, initiating meetings where BMW outlined its conditions, including proximity to ports, infrastructure, quality of life, autonomy in site selection and direct negotiations with landowners and city governments. BMW also required that state investments not divert resources from education, health, or safety. Despite initial friction over these demands, the state government agreed to commit to infrastructure incentives without compromising resources from the mentioned areas.

The incentives offered by the local government were not tax-related. "*If the tate is going to invest, you're going to pay taxes* [ICMS] *because it is not our culture* [to grant tax exemptions]" (B7). Santa Catarina was considered a "*a peculiar case, as BMW was the only one for which incentives generated an obligation. There were commitments on both sides*" (B2) - including establishing a local R&D department as "*one of the company's contributions agreed with the government"* (B2).

To support BMW's compliance with federal regulations under Inovar-Auto, the state improved its experise and hired specialists, ensuring prompt project approval: "We managed to use the best project development methodologies" (B7). Rules were complex and subject to change at the federal level, and the company faced difficulties complying with them: "It is not an overnight learning process" (B1). It was important that this did not occur at the state level or "there would be dire consequences for our operations in Brazil […]. In Santa Catarina, the rules of the game are clear and steady" (B1). The Inovar-Auto policy was a major challenge and required lengthy negotiations between the federal government, BMW and the Santa Catarina state Government. Setting up the factory "involved Federal agencies; there were over 100 licenses before the factory opened. It was monstrously complex" (B7).

During the COVID-19 pandemic, BMW faced reduced sales and instability in Brazil, impacting automobile manufacturers. Ford, Brazil's first automaker, exited in 2021, citing unpredictable tax increases: "Taxes increased overnight and took everyone by surprise; there is no business plan that can adjust to this quickly" (Sutto & Fonseca, 2021). Despite challenges, BMW increased sales by 43% in 2020, maintaining its premium segment

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leadership (Rinaldi, 2021). By 2021, eight out of ten BMW cars sold in Brazil were made in Santa Catarina. "Brazil is the only place in the world where we have already grown more than in the pre-pandemic period", said BMW's CEO (CPG, 2021). That year, BMW launched a solar-powered charging station for electric cars, developed with a Santa Catarina university, which was recognized as one of the top five projects in BMW's global innovation and intrapreneurship program (UOL, 2021).

Discussion

Our study shows how the decision to invest in Brazil was partially influenced by conventional determinants, with PIE playing a decisive role in selecting a non-core region.

Santa Catarina offered high institutional quality, cultural proximity and logistical efficiency, with lower congestion costs typical of non-core regions (McDonald et al., 2018). These factors were crucial, as the location lacked conventional advantages such as market size, industry agglomeration or tax exemptions, key FDI determinants in IB literature (Kim & Aguilera, 2016; Nielsen et al., 2017; Hutzschenreuter et al., 2020). In this case, the negative effect of being a non-core region and lacking some conventional determinants would not be moderated by the proximity to the core regions (McDonald et al., 2018), as it was more distant from São Paulo than other states competing to have BMW in their territory. Santa Catarina state was not an obvious choice; its selection stemmed from the synergy between the local government, institutions and the company, making it an unconventional and unexpected decision. Thus, we present our first proposition:

P1. Political and institutional embeddedness during the pre-FDI phase has a moderating effect on location factors, reducing the weight of market size and agglomerations for multinationals when investing in non-core regions.

Ties of trust and commitment (Granovetter, 1985; Halinen & Törnroos, 1998) with state entities (Sun et al., 2010) and local actors (Florida and Adler, 2022) helped resolve frictions. Combined with existing conventional determinants, these ties facilitated faster learning and expanded BMW's options for selecting an appropriate subnational location.

The development of PIE enabled the company to identify a microenvironment distinct from the country's macroenvironment, effectively compensating for the absence of specific economic endowments. There was greater support, communication, commitment, and trust at the subnational level during the entire process.

The subnational business environment acted as a buffer, "a secure port amidst turbulent waters," mitigating the challenges of institutional change and Brazil's market complexity. By developing PIE in the non-core location, the MNE leveraged political and institutional assets in Santa Catarina to bridge national and subnational dynamics, making the investment viable. Based on this, we propose:

P2. During the pre-FDI phase, the constraints multinationals face in complex emerging markets are mitigated by the effect of PIE at the subnational level.

Although the company entered Brazil with clear ownership advantages (Dunning & Lundan, 2008), the complex emerging market posed challenges to exploiting them. The new institutional assets developed through PIE were crucial, reducing transaction costs, stabilizing operations and enabling BMW to navigate the national context more efficiently while achieving higher internalization than initially anticipated.

Our study distinguishes between maintaining and developing OLI advantages. In the short term, particularly during the pre-FDI phase, PIE was a strong mechanism that

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helped maintain OLI advantages, while in the long term, it facilitated the development of new ones to navigate a complex and evolving institutional environment. Thus, we propose:

P3a. PIE development at the subnational level preserves MNE´s OLI advantages when investing in complex emerging markets.

P3b. PIE at the subnational level facilitates the development of new OLI advantages in the post-FDI phase, enabling MNEs to navigate the complexities of emerging markets effectively.

Figure 3 presents a model showing PIE's role in choosing subnational, non-core locations in emerging markets.

The model illustrates the interaction between forces operating at the national and subnational levels. During the pre-FDI phase, when a company first approaches a market, traditional determinants such as market size and agglomeration effects are the primary factors influencing decision-making. However, as the MNC engages with subnational environments, PIE becomes increasingly critical.

Theoretical implications

Our model shows that conventional determinants are moderated by PIE, which can begin in the pre-FDI phase. Developing PIE allows firms to diversify subnational strategies, leveraging non-core regions to offset core region congestion costs. At the subnational level, PIE mitigates host-country complexity, enhancing MNE operations and enabling the sustained development of new OLI advantages.

This is crucial for the development of the location theory. In the eclectic paradigm, transactional ownership advantages arise as MNEs expand value-added activities across diverse markets and complex contexts. We extend this by exploring how these advantages can be created at the subnational level, especially when locating in non-core regions. Through PIE, MNEs acquire new assets to sustain market strategies

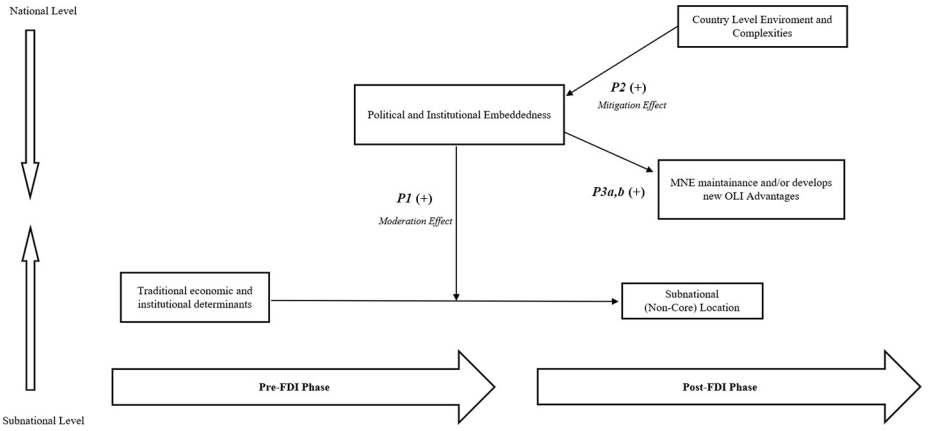

Figure 3. Theoretical model
Source: Figure by the authors

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nationwide, mitigating liabilities and additional transaction costs associated with operating far from core regions.

In summary, our study makes two key contributions. First, we integrate a subnational perspective into the eclectic paradigm, connecting it to embeddedness and deepening the understanding of location complexity, including the trade-offs between operating in core versus non-core regions. Second, we highlight the strategic management of embeddedness by MNEs during the pre-FDI phase at the subnational level.

Practical implications

We provide managers with elements to enhance subnational location strategies in the pre-FDI phase through PIE, accelerating learning about non-core locations and building institutional assets. Without PIE, firms risk poor location choices or additional local liabilities, impacting interactions with external actors.

We offer insights for regional policymakers: non-core areas can attract more FDI by promoting conventional determinants, fostering PIE development and creating location advantages to offset limited factor endowments.

Our case study focuses on PIE; future research could explore other aspects. We suggest studying the links between PIE and location advantages, co-evolution and their effects on speed, permanence and performance. Additionally, examining how PIE-generated resources affect perceived national-level distance and the role of firm characteristics relative to context would further advance this research.

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