Beyond Borders: Labor Governance and Firm Behavior in Global Production

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Abstract

While Western countries have strong domestic commitments to human rights, firms headquartered there may operate abroad under substantially different labor conditions. This raises questions about how differences in labor governance relate to firms' operating conditions and reported labor outcomes. This study examines how foreign ownership is associated with reported labor disputes and whether this relationship varies with host-country labor governance. Using firm-level World Bank Enterprise Survey data combined with labor-governance indicators from the International Labor Organization, I estimate the relationship between foreign ownership and labor disputes conditional on the strength of workers' rights. The results show that home–host labor-governance differences are associated with a variation in reported firm outcomes: the governance gap has a weak negative association with reported violations, while labor governance is more strongly related to reported disputes than inspections. Foreign ownership is consistently associated with reported labor disputes, while evidence that labor governance moderates this relationship is limited.

Introduction

Despite strong domestic commitments to workers' rights in Western countries, many of their firms operate abroad under labor conditions that would be unacceptable at home. In other words, firms' success is often built on exploitative labor conditions abroad. Companies have spent decades moving production overseas to avoid stricter domestic labor regulations and reduce labor costs. This strategy is known as 'offshoring.' [1 – 2].

There is much ethical debate about exploitative labor in global markets, but the continuation of such practices among firms originating from countries with substantially stronger labor standards raises important questions about how differences in national labor governance shape firms' international operations.

The question of this research is therefore:

How is the share of a firm's foreign ownership associated with firms' reported labor disputes and government labor inspections, and does this relationship vary with the stringency of the respective host-country labor governance?

The first part of this question asks whether differences in labor governance between firms' home and host countries are associated with differences in reported firm violations. This reveals the stringency of a country's 'labor governance.' With 'labor governance,' I am referring to the government environment in which a firm operates. Using these results, I then examine whether labor-governance conditions and foreign ownership are associated with reported labor disputes and government inspections. Analyzing these relationships answers A) whether home–host differences in labor governance are associated with differences in reported violations, and B) whether foreign ownership and labor-governance conditions are associated with differences in firms' reported labor disputes and government inspections.

The results of part A will tell us whether different degrees of government-environment gaps between a firm's home and host country tend to lead to certain firm behavior around labor practices via reported violations. This establishes whether differences in labor governance between firms' home and host countries can help explain the conditions under which such practices occur. We find that as the governance gap becomes more positive (indicating that home country has stronger worker-rights governance than the host), reported violations tend to decrease.

From this conclusion we examine through part B of this research whether domestic and multinational firms differ in their experiences and responses to labor-related disputes, where we find that find that foreign ownership is consistently associated with more reported labor disputes, while weaker labor-governance environments are associated with fewer reported disputes and are not significantly associated with government inspections. This study thereby considers the institutional conditions in which firms operate as well as whether firms operating across national borders apply different labor-related outcomes from firms that remain domestically oriented.

Literature Review

<u>Race to the Bottom</u>

The 'race to the bottom' debate addresses the relationship between multinational production and labor regulation. The 'race to the bottom' describes the reinforcing cycle in which developing countries attract multinational firms through relatively low labor costs, which are supported through weak labor protections. Governments seeking to attract foreign investments aim to maintain or further weaken labor regulations, reinforcing the low-cost conditions that initially attracted firms. This creates a 'race to the bottom' dynamic where governments continuously lower their labor standards in hopes to receive more foreign investments in return (Olney, 2013).

Establishing that firms may have incentives to locate production where labor is less regulated confirms that this problem between strong differences in labor standards exists, which is a foundational understanding I use.

However, the race-to-the-bottom literature generally examines whether weaker host-country regulation *attracts foreign investment*, rather than whether the *strength* of a firm's home-country labor governance *predicts* the size of the difference between its home and host environments and whether these institutional governance gaps are reflected in firms' labor practices. To address this, this study includes a firm-level dimension by using reported corporate violations as an outcome, allowing the relationship between differences in home- and host-country labor governance and firms' observed labor practices to be examined directly. A larger governance gap may provide multinational firms with greater scope to operate below the labor standards prevailing in their home countries, whereas firms operating within more similar regulatory environments face less institutional differences. Reported violations therefore provide a measure of whether these differences in institutional environments are reflected in firms' labor practices.

The Country-of-Origin Effect

The country-of-origin effect provides another critical theoretical foundation for this study by establishing that the institutional environment of a Multinational Corporation's (MNC) home country can shape its behavior internationally. The laws, political institutions, government policies, norms, and business practices they are exposed to at home shape their strategies, organizational practices, and decisions when operating in foreign countries. However, this does not mean that firms simply copy their home country's laws abroad. Rather, the home-country environment can leave an institutional imprint on the firm that influences its international behavior. Sethi and Elango (1999) deepen our understanding of the country-of-origin effect by demonstrating that MNCs originating from different countries exhibit systematic differences in their strategic choices and modes of operation.

Existing studies analyzing the country-of-origin effect for firms' international behavior establish that the home-country environment can remain relevant after firms cross national borders. However, they largely treat home-country institutions as an independent characteristic of the firm, rather than examining how those institutions compare with the regulatory environment of the countries in which the firm operates.

For example, studies have focused on wages, which represents an outcome of firm-level employment practices rather than a measure of the institutional environment itself, to explore whether multinational firms originating from countries with stronger labor institutions pay higher wages in host countries (Ali and Seric, 2014). Other studies have examined whether the institutional environment of an MNC's home country is associated with labor violations in its international operations (Babae, 2025), but such analysis does not treat the institutional environment of the host country as part of the central explanatory relationship.

Comparisons with Existing Research

Existing research also tends to emphasize the influence of the home- or host-country institution to be greater than the other. In this research, I instead compare the two to draw a combined governance gap, allowing the size of that gap to be compared across firms and examined as a predictor of reported violations.

Emphasizing both home- and host-country conditions is particularly important when considering multinational and domestic firms together. A domestic firm headquartered in a country with strong labor governance must comply with the regulatory environment of the country in which it operates. A multinational firm headquartered in the same country, however, may operate production in countries with substantially weaker labor governance, creating a larger home–host governance gap. Conversely, a firm headquartered in a country with weak labor governance may face less regulatory distance when operating in a country with similarly weak standards. These differences provide a theoretical basis for examining whether the size of the home–host governance gap is associated with differences in firms' labor practices, and whether these relationships vary according to foreign ownership.

Research such as Hu et al. (2024), for example, examines labor-standard compliance in overseas Chinese garment factories in relation to country-of-origin effects, host-country regulation, and private codes of conduct. Their findings show that multinational firms operate within overlapping institutional environments and that labor practices cannot necessarily be attributed to either home- or host-country institutions alone. This provides an important foundation for this study: The relevant question is not simply whether either country has strong or weak labor governance, but whether the difference between home- and host-country labor governance is associated with firms' reported labor outcomes. This study extends this perspective by examining both the home–host governance gap and the role of foreign ownership in reported labor disputes, government inspections, and violations.

Viewing this argument, that international production leads to worse labor practices, from the firms' perspective, Malesky and Mosley (2018) highlight that offshoring does not necessarily lower standards. Malensky and Mosley argue that even when firms operate in weaker regulatory environments, they may have incentives to maintain or improve labor practices because other factors like consumer perspectives, lead firms, shareholders, activists, etc. can impose pressure. Incentives to improve labor practices differ depending on the markets firms serve, the profitability of those markets, and the visibility of labor conditions. This perspective suggests that the labor practices of multinational firms cannot be explained solely by the regulatory environment of the host country, but can vary through reputational or commercial pressures which make poor labor practices costly.

Taking this perspective into account, this research carefully examines reported firm violations drawing from the observed differences between home- and host-country labor governance rather than assuming that multinational firms uniformly transfer their home-country labor practices abroad. Reported violations provide an outcome through which this relationship can be analyzed. Additionally, using the World Bank Enterprise Surveys, we have additional firm-level evidence on whether domestic and multinational firms differ in their experiences and responses to labor-related disputes. This study thereby considers the institutional conditions in which firms operate as well as whether firms operating across national borders apply systematically different labor-related outcomes from firms that remain domestically oriented.

Methods

The study develops a two-stage research strategy to examine how national labor-governance conditions and foreign ownership are associated with firm-level labor outcomes:

Part A: Preliminary Analysis— Examining Global Patterns

First, the study constructs a measure of the home–host Worker Rights Governance Gap, capturing the difference in labor-governance conditions between a firm's home country and the countries in which it operates. This measure is used to examine the relationship between the home-host governance gap and reported firm violations. 'Worker Rights' refers to national compliance with labor rights, freedom of association and collective bargaining, a variable provided by the International Labor Organization (ILO). Data from Violation Tracker Global prompts us to build these gaps, where the jurisdiction charging a firm for a violation represents that firm's host country, and their headquarters the home country. This provides an assessment of whether firms operating across larger differences in labor governance exhibit systematically different levels of reported violations. However, this analysis is descriptive and correlational and therefore does not explain whether the governance gap causes differences in firm behavior.

Part B: Main Analysis— Examining Firm-Level Behavior

Second, the study examines whether labor-governance conditions and foreign ownership are associated with reported labor disputes and government inspections. This is tested using a logistic regression model with reported labor disputes or government inspections as the binary dependent variable:

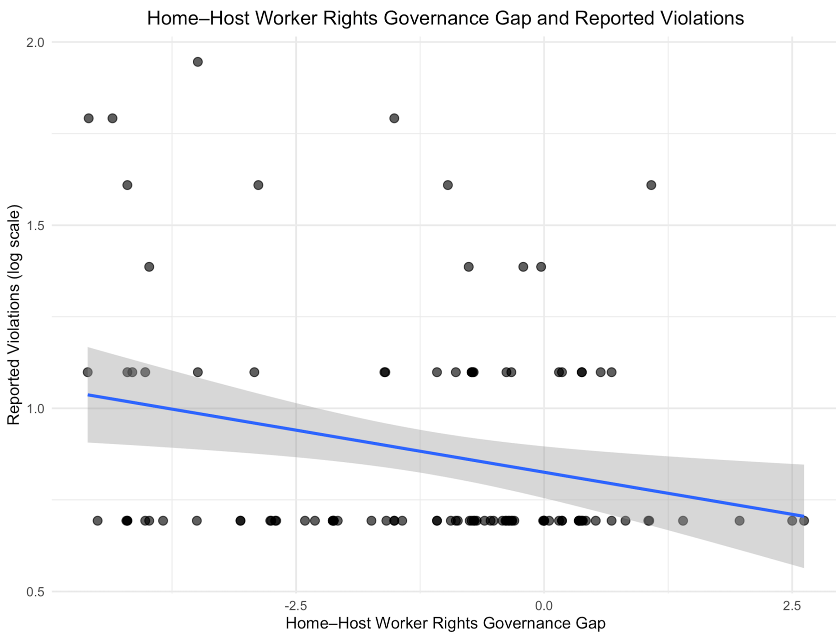
This model includes the Lack of Worker Rights (measured as (home-country Worker Rights) - (host-country Worker Rights)), foreign-ownership specifications (any (>0%), small (>0–25%), medium (>25–50%), and large (>50%)), and an interaction between the two to examine whether the relationship between labor governance and reported disputes/ government inspections differs according to foreign ownership. Controls for firm characteristics, sector, selling status, informal employment, and survey year are included. These firm-level outcomes and country-level labor governance patterns use data from the World Bank Enterprise Survey and the ILO.

Together, these analyses examine two related dimensions of firms' labor practices: reported violations and disputes, which capture firm-level labor outcomes, and government inspections, which capture interaction with the state's labor-regulatory system. The methodology therefore allows the study to assess whether differences in labor-governance environments are associated with differences in reported firm outcomes, and whether these relationships vary between foreign-owned and domestically owned firms. Because the analyses are observational, the results are interpreted as associations rather than causal effects.

Outputs

Part A: Preliminary Analysis

Plot 1: Home-Host Worker Rights Governance Gap & Reported Violations



Part B: Main Analysis

Table 2: Foreign Ownership, Worker Rights, and Labor Disputes

Foreign Ownership, Lack of Worker Rights, and Labor Disputes

	Dependent variable: Labor Disputes			
	Any Foreign	Small Foreign	Medium Foreign	Large Foreign
	(1)	(2)	(3)	(4)
Lack of Worker Rights	-0.063***	-0.056***	-0.055***	-0.053***
	(0.013)	(0.012)	(0.012)	(0.013)
Foreign Ownership	0.696***	0.856***	0.557***	0.602***
	(0.063)	(0.153)	(0.161)	(0.071)
Lack of Worker Rights x Foreign Ownership	0.018	0.058	0.122*	-0.013
	(0.023)	(0.064)	(0.068)	(0.026)
Lack of Worker Rights effect for foreign firms	-0.045*	0.002	0.068	-0.066***
	(0.023)	(0.064)	(0.068)	(0.025)
Informal Employment	-0.016***	-0.016***	-0.016***	-0.016***
	(0.001)	(0.001)	(0.001)	(0.001)
Survey Year FE	Yes	Yes	Yes	Yes
Sector FE	Yes	Yes	Yes	Yes
Firm Size Controls	Yes	Yes	Yes	Yes
Observations	47,337	47,337	47,337	47,337

Note: *p<0.1; **p<0.05; ***p<0.01

Table 3: Foreign Ownership, Worker Rights, and Government Inspections

Foreign Ownership, Lack of Worker Rights, and Government Inspections

	Dependent variable: Government Inspections			
	Any Foreign	Small Foreign	Medium Foreign	Large Foreign
	(1)	(2)	(3)	(4)
Lack of Worker Rights	0.008	0.009	0.010	0.009
	(0.007)	(0.007)	(0.007)	(0.007)
Foreign Ownership	0.154***	0.063	0.018	0.189***
	(0.047)	(0.124)	(0.117)	(0.054)
Lack of Worker Rights x Foreign Ownership	-0.003	0.028	-0.036	-0.005
	(0.016)	(0.047)	(0.041)	(0.018)
Lack of Worker Rights effect for foreign firms	0.005	0.038	-0.026	0.004
	(0.016)	(0.047)	(0.041)	(0.018)
Informal Employment	-0.003***	-0.003***	-0.003***	-0.003***
	(0.0004)	(0.0004)	(0.0004)	(0.0004)
Survey Year FE	Yes	Yes	Yes	Yes
Sector FE	Yes	Yes	Yes	Yes
Firm Size Controls	Yes	Yes	Yes	Yes
Observations	47,249	47,249	47,249	47,249

Note: *p<0.1; **p<0.05; ***p<0.01

Interpretation & Discussion

Part A: Plot 1

The scatter plot (Plot 1) shows a weak negative descriptive association between the home–host Worker Rights governance gap and reported corporate violations from the downward-sloping blue line. This establishes that firms operating across larger differences in worker protections between their home and host countries are associated with somewhat fewer reported violations. However, this relationship is weak and descriptive, so it does not necessarily prove that larger governance gaps reduce corporate violations.

This provides foundational evidence that differences in home–host labor governance are associated with variation in firm activity through reported firm violations.

Part B: Tables 2 & 3

Building on this, the main analysis uses firm-level data to examine whether labor-governance conditions and foreign ownership are associated with reported labor disputes and government inspections:

Looking at Table 2, we see that the Lack of Worker Rights (Lack of Worker Rights = Worker Rights x (-1)) is negatively and significantly associated with reported labor disputes across all four specifications (ranging from −0.053 to −0.063). This suggests that firms operating in environments with a greater Lack of Worker Rights have lower log-odds of reporting involvement in labor disputes. In other words, firms in countries with weaker labor-rights protections are less likely to report that they had been involved in a labor dispute.

Additionally, foreign ownership is consistently positively associated with reported labor disputes. That all the values are positive (any: 0.696, small: 0.856, medium: 0.557, and large: 0.602) indicates that the foreign-ownership indicator is associated with higher log-odds of reporting a labor dispute (when holding the other variables in the model constant). But considering Lack of Worker Rights with foreign ownership, the evidence for this moderation is limited. The only statistically significant interaction occurs for medium levels of foreign ownership (where $0.122 < 0.01$), where the negative association between Lack of Worker Rights and reported labor disputes is reduced. This limited moderation tells us that the statistical evidence that foreign ownership changes the relationship between Lack of Worker Rights and reported labor disputes is present only in the medium-foreign specification, and not in the other three specifications.

However, I would like to note that weaker labor rights necessarily cause fewer labor problems. The dependent variable is whether a firm reported being involved in a labor dispute, rather than whether labor conditions were objectively worse. Therefore, these outcomes could mean that stronger labor-rights environments may provide workers with greater institutional capacity to identify and report labor issues. Additionally, the measure captures whether firms *report* being involved in a dispute. Stronger labor-rights environments may instead provide greater opportunities and institutional capacity for workers to identify and report labor issues. Evidence that labor governance changes the foreign-ownership relationship is limited to the ‘medium-foreign’ specification.

Table 3 shows us that the national labor environment is not significantly associated with whether firms report being inspected by government labor authorities. We can draw this because all coefficients for ‘Lack of Worker Rights’ are positive (any: 0.008, small: 0.009, medium: 0.010, and large: 0.009), telling us that a one-unit increase in Lack of Worker Rights is associated with a 0.008 increase in the log-odds of reporting a government inspection when holding the other variables constant (in the case for firms with any share of foreign ownership). However, Lack of Worker Rights is not statistically significantly associated with reported government inspections across any of the four specifications because none of the coefficients reach even the $p<0.1$ threshold.

Moreover, we can read that foreign-owned firms are more likely to report government inspections in the ‘any-foreign’ and ‘majority-foreign’ specifications, while the ‘small-’ and ‘medium-foreign’ estimates are not statistically significant. We can read this off the ‘Foreign Ownership’ row: ‘any’ share foreign ownership (0.154) and a ‘large’ share in foreign ownership (0.189) are the only two coefficients which pass the $p<0.01$ threshold. This tells us that the association between foreign ownership and reported government inspections is concentrated in establishments with any or a majority of foreign ownership, although the analysis does not establish whether this reflects differences in regulatory exposure, firm characteristics, or other factors.

Comparing Tables 2 and 3, the results generally show stronger evidence of a relationship between the national labor-rights environment and reported labor disputes than between the labor-rights environment and government inspections. Lack of Worker Rights is negatively associated with reported labor disputes across all specifications, whereas its association with government inspections is small and statistically insignificant. Moreover, evidence that foreign ownership moderates the relationship between Lack of Worker Rights and labor disputes is limited to the medium-foreign specification, while no statistically significant moderation is observed for government inspections.

Conclusion

Overall, the results show that on a global level, the broader labor-governance environment appears more closely related to reported disputes than to state inspections. Specifying firms' activity, foreign ownership tends to be more consistently associated with firms' reported labor disputes than with their reported government inspections. In other words, where a firm operates and whether it is foreign-owned matter for how labor issues are reported, but the evidence is more limited on whether weaker national labor-governance systematically changes the behavior of foreign firms. The findings suggest that differences in governance around labor practices between a firm's home and host countries are relevant to firms' labor outcomes, although the lower incidence of reported disputes in weaker governance environments may reflect differences in workers' ability to report disputes rather than fewer underlying labor problems.

These outcomes provide a building block to better understand the relationship between who is offshoring and to what types of areas, and what this means for the labor conditions in their production. This research finds that firms operate across different labor-governance environments and examines how these differences are associated with firms' reported labor outcomes. However, further research is needed to better understand the relationship between home- and host-country governance and what these differences may mean for specific labor outcomes. I look forward to build on this work to determine whether specific regions or types of governance systems cause certain tendencies in firms' labor practices.

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