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# INSTITUTIONAL DISTANCE: CONSTRUCT OF ISOMORPHISM RELEVANT TO MULTINATIONAL COMPANIES

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# Institutional distance

- defined as the relative difference in the quality of institutions of the country of origin and the host country (Gaur & Lu, 2007)
- The inefficiency or poorly established key institutions in the host country will negatively affect the operations of the subsidiaries operating under such local conditions
- poorly regulated political and legal institutions limits establishing quality business contracts, potentially leading to an inability to build stable and long-term relationships with local suppliers, which will impede the exchange and distribution of goods and services (Pattnaik, Choe & Singh, 2015).

# Institutional distance

- based on the institutional profile of the state, which consists of three dimensions: regulatory, cognitive and normative (Kostova, 1999)
- provides an explanation for the organizational behavior of multinational subsidiaries and monitors the operations of subsidiaries in two key aspects: (1) establishing legitimacy in the host country and (2) transferring strategic orientations and organizational practices from the parent company to foreign subsidiary (Kostova & Zaheer, 1999).

# Institutional distance and MNC

- Edwards and Kuruvilla (2005) imply that the institutional environment of the host country is complex and idiosyncratic and may be an obstacle to the successful transfer of business practices.
- Hall and Soskice (2001) focused on identifying specific attributes of the institutional setting at the country level, and used the results to explain variations in inter-institutional organizational behaviors and the degree of differences between institutional environments across countries
- Kostova (1999) finally systematized the institutional differences that multinational companies face as institutional distance; the greater the difference between the institutional environment of the host country and the country of origin, the more severe are the difficulties in transferring and establishing organizational business.

# Institutional distance and MNC

- Institutional infrastructure is often subject to layering processes (Mahoney & Thelen, 2010), that is, new institutions are added to existing previous institutions and can be potentially revived or used for new purposes.
- This conclusion offered a perspective on how institutional environments are characterized by a multitude of different institutional logics and interpretations of the environment (Thornton & Ocasio, 2008).
- When these logics coincide or are ambiguous they can create multinational enterprises a strategic opportunity and a solution for overcoming distances, creating patterns of behavior that have hitherto deviated from the host country's standard business practices (Jackson, 2010).

# Overview of the most significant research (1/7)

- Recent empirical research has conceptualized institutional distance as a multidimensional construct given the complexity of the institutional environment (Fortwenge, 2016)
- Researchers have shifted their interest towards defining the dimensions and attributes of the institutional environment that are critical to international business and the behavior of MNCs.

# Overview of the most significant research (2/7)

- The degree of institutional distance is usually calculated by summing the specific values of the cognitive, normative and regulatory dimensions that represent a particular institutional environment (Kostova, 1999): the greater the distance between the two countries, the greater and negative is the effect of the distance (Kostova & Roth, 2002).
- This perspective of institutional distance has proved significant as it explains the burning problems of international business such as why MNCs have difficulty transferring business practices to subsidiaries (Kostova & Roth, 2002), but does not provide explanation for how and why institutional distance between the two countries is so significant for transfer of practices.

# Overview of the most significant research (3/7)

- Jackson and Deeg (2008) conclude that institutional distance also affects the difference in terms of coordinating business activities in a particular institutional setting.
- Ahmadjian (2016) points out that the specifics of countries are characterized by a certain societal logic. Institutional distance is often shown only as the difference between the institutional infrastructures of the two countries. What this perspective lacks is a reflection on how institutions can weaken or more severely restrict organizational behavior, and that institutionalization must necessarily be scaled



# Overview of the most significant research (4/7)

- The Shirodkar and Konara (2017) study comprehensively analyzes the impact of formal institutional distance on the performance of multinational subsidiaries, and is driven by the increasing development and increasing influence that primarily formal institutions have on the institutional distance and multinational affiliate performance.

# Overview of the most significant research (5/7)

- They conclude that new markets create an environment where differences between the regulatory framework of the host country and the country of origin sublimate the characteristics of the foreigner. The results also confirm that new markets represent a unique context in which potential opportunities are arising from differences in institutions, as some authors have argued, are not directly linked to achieving competitive advantage.
- They conclude that the negative effect of formal institutional distance on subsidiary performance is stronger for wholly-owned subsidiaries, whereas for partially domestic-owned subsidiaries, this effect is not statistically significant, leading to diametrically opposite conclusions from those studies that use a (too) general context
- Third hypothesis assumes that the negative effect of formal institutional distance can be mitigated with greater experience of the subsidiary in the host country, and the results supported the hypothesis.

# Overview of the most significant research (6/7)

- Salomon and Wu (2012) argue that foreign companies from institutionally distant countries use experience to learn more about the institutional environment of the host country and, as a result, do not need to rely on imitation of the firm's domestic strategies in order to reduce foreigner characteristics; specifically they are interested in how two forms of experience, domestic competition and parent company experience, shape the impact of institutional distance on local isomorphism, and select U.S. bank branches from 1978 to 2006 as a sample.

# Overview of the most significant research (7/7)

- The research of Solomon and Wu (2012) is a multiple contributor to the institutional literature: the research proves that there is significant heterogeneity in isomorphic strategies, and the results suggest that local isomorphism strategies do not suit all firms equally; foreign companies from more remote institutional environments will find it useful to imitate local competitors. Furthermore, this research examines the impact of institutional distance on the specific operational decisions that companies make in the host country; research to date has examined the impact of institutional distance on site selection or market entry strategy, however, this is the first study to directly contrast institutional distance and local institutional isomorphism. Finally, with this research, institutional distance was analyzed as a multidimensional construct, while the research to date has largely examined one dimension: the cultural, economic or political dimension separately.

# Conclusion

- Institutional distance is a key concept in international business and research since it can be argued that international management is indeed distance management. The interest in institutional distance does not diminish despite sensitization and a stronger interest in managing sociocultural differences, which undoubtedly means that distance will continue to be an important construct when managing and studying multinational subsidiaries