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Three Essays On Institutional Sensemaking Of Political Connectedness

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THREE ESSAYS ON INSTITUTIONAL SENSEMAKING OF POLITICAL CONNECTEDNESS

by

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DEDICATION

I dedicate this dissertation to my parents, Yılmaz and Güzin Ulusemre, who have always loved and sacrificed for me, and to my uncle, Doğan Ulusemre, who have always loved and supported his only nephew. I would not be where I am today without them.

I also dedicate this dissertation to my wife, Xiaolei, who have encouraged me throughout my PhD, and to my children, Ayhan and Deniz, who are the joy of my life.

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ABSTRACT

Through a collection of three integrated essays, this dissertation investigates how institutional logics shape the way firms and their decision makers perceive, interpret, and respond to political connectedness. More specifically, it elaborates on the cognitive mechanisms through which institutional logics affect responses to political connectedness. Essay 1 provides a fresh perspective to studying political connectedness by showing how the differences in the interplay between multiple institutional logics generate opposing logics – bureaucratic logic in developed countries vs. patrimonial logic in emerging countries –, which lead to two dissimilar forms of firm-government interaction across countries. Essay 2 proposes a new conceptual framework, *institutional sensemaking*, which I develop by building on the institutional logics and sensemaking literatures. This framework is used to investigate how bureaucratic logic and patrimonial logic differently shape the way the expatriate managers make sense of and respond to political connectedness in China. Essay 3 examines how managerial sensemaking affects firms' responses to dissimilar logics of firm-government interaction by looking at the relationship between managers' attention focus and their internationalization choices regarding whether to expand into developed countries – where bureaucratic logic prevails – or into emerging countries – where patrimonial logic prevails.

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CHAPTER 1

OVERVIEW

My dissertation is organized as a collection of three integrated essays. Each of the three essays has been developed to make contributions both to the institutional frameworks used in international business and to our understanding of the international business phenomena in emerging countries. Essay 1 is a perspective paper that proposes a new lens to study political connectedness by drawing on the institutional logics perspective. Essay 2 is a qualitative paper that develops the theory of institutional sensemaking of political connectedness by integrating the institutional logics framework and the tripartite sensemaking framework with the insights that I gained into the political connectedness phenomenon during my field research in China. Essay 3 is an empirical paper that examines the relationship between managerial sensemaking and firm's strategic responses to political connectedness through an analysis of panel data. Overall, my dissertation comprises a new theoretical framework and two unique datasets: one longitudinal and one cross-sectional obtained through interviews. Both of these datasets have great potential to be used in numerous future studies.

1.1 Essay 1

In the first essay, entitled, *What is the logic behind political connectedness?*, I explore the political connectedness phenomena in emerging countries by reviewing the

concerning international business research from an institutional logics perspective, by which I identify the prevailing logics that shape firm-government interaction in developed and emerging countries. In line with the extant international business research, I conclude that prevailing logics in emerging countries and those in developed countries are not different in degree, but rather different in kind (Jackson & Deeg, 2008). Then I build on the institutional logics perspective to provide a new perspective to studying differences in firm-government interaction across countries. In this regard, I argue that patrimonial logic is generated when weak logics of the market and the state blend with the strong logics of the family and the community, which results in the prevalence of patronage ties between firms and governments. Such patrimonial logic and the consequent patronage ties exist in emerging countries to various extents. In developed countries, on the other hand, market logic and state logic dominate the institutional system, "insulating" the domain of firm-government relations against the logics of the family and the community. This results in bureaucratic logic, which leads to the prevalence of rule-based, impersonal exchanges between firms and governments. This essay contributes to the international business literature on corruption, a deconstruction of which in the essay reveals that our knowledge of firm-government interaction is to a large extent shaped by Western bureaucratic logic, and hence fails to explain such a non-Western phenomenon as political connectedness (Tsui, 2007).

1.2 Essay 2

In the second essay, entitled, *Making sense of political connectedness: Corruption or strategy?*, I examine how institutional logics draw the boundary that separates

legitimate exchanges between firms and governments from illegitimate ones. More specifically, the essay shows how different institutional logics differently shape the way managers make sense of and respond to political connectedness by integrating the institutional logics framework and the tripartite sensemaking framework with the insights gained into the political connectedness phenomenon in China through field research. In this regard, I argue that under bureaucratic logic, managerial attention will be directed to the legal and moral aspects of political connectedness. As a result, political connectedness will be framed in negative terms, and managers will try to avoid political connectedness. Under patrimonial logic, on the other hand, managerial attention will be directed to the economic and relational aspects of political connectedness. As a result, political connectedness will be framed in positive terms, and managers will try to increase political connectedness.

Further, my field research in China shows that some expatriate managers have actually been able to navigate in the Chinese institutional system by developing cognitive complexity, which enables them not only to learn the patrimonial logic prevalent in their host country, but also to blend it with the bureaucratic logic prevalent in their home country. The consequent hybrid logic directs these managers' attention to both legal and moral aspects of political connectedness. As a result, they frame political connectedness both in positive and in negative terms. In other words, those expatriate managers make sense of political connectedness as a double-edged sword. In this regard, they find political connectedness to be essential in order to operate in the Chinese institutional system, and they do not think of it necessarily as corruption. However, they believe it can turn into corruption depending on the nature of the political ties and on the way these ties

are utilized. Therefore, although these managers essentially seek to increase political connectedness to gain economic benefits in China, they avoid engaging in practices that are blatantly illegal and blatantly immoral in their home country. In other words, although they do not want to commit to the white area, at the same time they want to avoid the black area. Thus, they end up navigating in the Chinese institutional system by operating in the gray area, in which they find a balance between the two dissimilar logics.

1.2.1 Methodology

In the field research, I conducted interviews on expatriate managers in China, who were all from countries in which bureaucratic logic is prevalent. In order to prompt participants to talk such a sensitive topic as and political connectedness, I use a scenario in the interviews as a stimulus material. The scenario is based on the corruption scandals of JPMorgan, which routinely hired sons and daughters of government officials to win government contracts (New York Times, 2013). By evaluating the behavior described in the scenario, the participants reveal 1) what aspects of political connectedness they focus their attention on (legal/moral aspects vs. economic/relational aspects), 2) how they frame political connectedness (threat vs. opportunity), and finally 3) how their framings influence their responses, including their likelihood to engage in political connectedness, the solutions they propose, and their perceptions of the causes of political connectedness. The interview data was analyzed by using *NVivo* software. The theory and the findings of this research contribute to the institutional logics literature by elaborating on the cognitive mechanisms by which logics affect firm’s responses. It also contributes to the sensemaking literature by showing that the entire sensemaking process does not occur at

the managerial level and independent of the environment, but is rather embedded in institutions.

1.3 Essay 3

In the final essay, entitled, *Institutional logics, managerial sensemaking, and internationalization strategy*, I examine how managerial sensemaking shapes firm's responses to dissimilar logics of firm-government interaction by looking at the relationship between managerial attention to firm's external environment and firm's internationalization strategies.

Drawing on the managerial sensemaking literature (Daft et al., 1988; Nadkarni & Barr, 2008), I argue that managers either focus their attention on the market environment or on the institutional environment. I also propose that such differences in scanning emphasis will affect whether dissimilar institutional logics such as patrimonial logic are framed by managers either as a threat or an opportunity, which in turn will affect their internationalization choices such as whether expand into developed countries, in which bureaucratic logic prevails, or into emerging countries, in which patrimonial logic prevails. Analysis of the panel data shows that managerial attention to the market environment is positively associated with firm expansion into developed countries, whereas managerial attention to the institutional environment is positively associated with firm expansion into emerging countries,. Thus, the essay contributes to the institutional explanations of internationalization strategy by demonstrating the cognitive underpinnings of internationalization strategy.

1.3.1 Methodology

This essay uses a panel of 152 U.S. manufacturing firms operating in global industries from 2003 to 2007 to test the arguments. The sample is limited to global industries only because firms within such industries pursue global strategies. The implication is that the market environment and the economic environment should be paramount for the decision makers of these firms, whereas institutional differences across countries should not draw considerable attention. If the results of this study support this argument for firms in global industries, however, then the findings can be easily generalized to firms in other industries, as managers in multi-domestic and transnational industries are under more pressures to adapt their strategies to local contexts, and hence are more likely to focus their attention on the institutional discrepancies between countries.

Following the extant sensemaking literature (Levy, 2005; Nadkarni et al., 2011), I use CEO's letters to shareholders published in the annual reports to elicit data for managerial sensemaking. I collect annual reports from *Mergent Web Reports*, as well as from firms' official websites. I was able to locate as much as 537 letters. Another 223 letters either could not be located or were not published. I obtain data regarding attention by using word counts from CEO's letters to shareholders published in annual reports. Word count has been typically employed in several studies to measure managerial sensemaking (Kaplan, 2008; Levy, 2005). Following Kaplan (2008), I develop a coding list mostly from the ground up. I select the phrases and words referring to different domains of the external environments after manually coding several letters from all the

industries represented in the sample. After the coding list was complete, I used *NVivo* to conduct automated coding on the whole sample.

Table 1.1: Dissertation overview

	Essay 1: *What's the logic behind political connectedness?*	**Essay 2:** *Making sense of political connectedness: Corruption or strategy?*	**Essay 3:** *Institutional logics, managerial sensemaking, and internationalization strategy*
Theoretical foundations	Institutional logics	Institutional logics, managerial sensemaking	Institutional logics, managerial sensemaking
Data	Perspective	Transcribed interview texts	Longitudinal database, CEO's letters to shareholders
Analytical techniques		Content analysis	Automated word count, negative binomial regression
Theoretical contributions	Provides a fresh perspective in studying political connectedness by explaining how different interplays among multiple logics differently shape firm-government interaction across countries.	Shows how different institutional logics differently shape managerial sensemaking and responses to political connectedness.	Demonstrates how managerial attention affects strategic responses to dissimilar institutional logics of firm-government interaction by shaping internationalization choices regarding whether to expand into developed countries or into emerging countries.

CHAPTER 2

WHAT IS THE LOGIC BEHIND POLITICAL CONNECTEDNESS?

> "Some call it **gratuities**. Some call them **questionable payments**. Some call it **extortion**. Some call it **grease**. Some call it **bribery**. I look at these payments as necessary to sell a product. **I never felt I was doing anything wrong.**" (New York Times, 2008)

Carl Kotchian, former chief operating officer (COO) and vice chairman of Lockheed reflected his bitterness in this way in a 1977 profile in the *New York Times*, at the Lockheed directors who ousted him from his positions in 1976 based on his $38 million of "questionable payments". He admitted paying millions of dollars over more than a decade to the Dutch, Japanese and West German politicians, to Italian officials and generals, and to other highly placed figures from Hong Kong to Saudi Arabia, in order to guarantee contracts for military aircrafts. This led to tremendous political upheaval in these countries in the 1970s: Japan's prime minister was jailed, the Italian President resigned, The Dutch Queen threatened to abdicate, etc.

Mr. Kotchian's confessions generated such a backlash in several countries because the payments he admitted making were considered as bribes, which are deemed unjustifiable on many grounds; e.g., from an economic perspective, they skew the allocation of resources and hence hinder economic development (Brouthers, Gao, & McNicol, 2008; Cuervo-Cazurra, 2006; Mauro, 1995; Schleifer & Vishny, 1993); from a

legal standpoint, they are illegal and hence undermine the rule of law (Bardhan, 1997; Cuervo-Cazurra, 2008; Kaufmann, 1997; Rose-Ackerman, 1999; Spencer & Gomez, 2011). However, Mr. Kotchian never admitted paying a bribe. Although he admitted paying government officials around the world to purchase his company's products, he maintained that those payments comprised a necessary part of an exchange between a corporation and a government. This raises questions such as "what constitutes a bribe?", and "how do we distinguish a bribe from a legitimate exchange between firm and the government?"

Research on corruption and political connectedness in international business is yet to address these questions (Svensson, 2005). In this regard, most studies have not sought to elaborate on the principle or set of principles that distinguish a legitimate exchange between a firm and a government from an illegitimate one (Harstad & Svensson, 2011). Instead, the boundary that separates between legitimate and illegitimate exchanges in researchers' countries – developed countries – has been taken for granted, and was imposed on countries – emerging countries – whose institutions are fundamentally dissimilar in kind (Jackson & Deeg, 2008; Tsui, 2007). In this regard, personalized exchanges between firms and governments that transcend beyond the legitimate practices of influence-buying such as lobbying and campaign contributions is labeled as corruption. As a result, most research have ended up applying rational-legal and economic standards to the issue (Bardhan, 1997), and have not accounted for; 1) the cognitive/symbolic elements by which people define a legitimate exchange, i.e. the elements by which people give meaning to a particular action or practice (Coleman, 1990); 2) the cross-country variations in these cognitive/symbolic elements, which may

shift the definitions of a legitimate exchange and make different types of action or practice “rational” or “normal” in different countries (Hall & Soskice, 2001; Witt & Redding, 2009). In this paper, I fill these voids by addressing two research questions:

> **Research question 1:** How is the boundary that separates legitimate and illegitimate exchanges between firms and governments in a society drawn?
>
> **Research question 2:** How does this boundary differ across countries?

I aim to answer to these questions by drawing on the institutional logics perspective (Friedland & Alford, 1991; Thornton, Ocasio, & Lounsbury, 2012). Institutional logics are defined as “overarching sets of principles that prescribe how to interpret organizational reality, what constitutes appropriate behavior, and how to succeed (Thornton, 2004: 70). Logics, in other words, provide guidelines on how to interpret and function in social situations (Greenwood et al., 2011: 318). The notion of institutional multiplicity or complexity in this perspective suggests that society is constituted through multiple institutional logics, each of whom governs an institutional order, such as the market, state, family, community, religion, etc. The logic of each institutional order differentially shapes the meanings that people give to the situations they face (Thornton et al., 2012). The logics of these institutional orders “are interdependent, and yet also contradictory” (Friedland & Alford, 1991: 250). In this regard, multiple institutional logics that are available to actors can interact and compete for influence in all societal domains (Nigam & Ocasio, 2010). As a result, the logic of one domain can be transposed to another domain and infuse the same practice with a

different meaning. Therefore, paying government officials to win government contracts may be considered as grease, or a breach of law, or kin loyalty, or a reciprocal obligation, depending on which logic is applied to make sense of the issue. Based on this, I argue that it is the outcome of the interplay among multiple institutional logics in a given context that determines how corporate actors draw the boundary separating legitimate and illegitimate exchanges between firms and governments.

As for the second research question, I argue that in many emerging countries, weak logics of the market and the state blend with the strong logics of the family and the community to generate patrimonial logic, which results in the prevalence of patronage ties between firms and governments. In developed countries, on the other hand, market logic and state logic dominate the institutional system, "insulating" the domain of firm-government relations against the logics of the family and the community. This results in bureaucratic logic, which leads to the prevalence of rule-based, impersonal exchanges between firms and governments.

2.1 Institutional logics

Institutional logics are defined as "overarching sets of principles that prescribe how to interpret organizational reality, what constitutes appropriate behavior, and how to succeed (Thornton, 2004: 70). Logics, in other words, shape individual and organizational behavior by providing guidelines on how to interpret and function in certain situations (Greenwood et al., 2011: 318). Although the institutional logics perspective (Friedland & Alford, 1991; Thornton et al., 2012) has long been used in management scholarship, its application in international business research has remained

limited. I employ institutional logics framework as the base theoretical foundation for this essay for three reasons.

First, the institutional logics perspective is based on the premise that institutions comprise both material and symbolic elements. Structures and practices materialize the ideas represented by symbols, while symbols give meaning to these structures and practices (Thornton & Ocasio, 1999; Zilber, 2008). This suggests that structures and common practices that constitute the business environment in emerging countries cannot be understood without their underlying meanings. For example, political connectedness may be corruption in developed countries, but it may be a non-market capability in emerging countries. In this regard, the institutional logics approach complements the social perspective in international business, which focuses solely on the observable material aspects of institutions and attaches a priori meanings to them.

Second, international business literature typically emphasizes either economic or social aspects of institutions. In this regard, the economic view focuses on the incentive structures determined by institutions, while the latter stresses the isomorphic pressures exerted by institutions, to explain responses to emerging country institutions. Yet, the institutional logics perspective suggests that actors can be motivated by both economic and social considerations (Friedland & Alford, 1991; Thornton et al., 2012). Organizations and individuals comply with logics to gain not only social endorsement but also economic benefits. Incorporation of logics does not make actors only legitimate, but also competitive (Thornton, 2002). This view thus has the potential to bridge the gap between the economic and social views in international business.

Finally, the institutional logics perspective suggests that organizational and individual sensemaking are nested within institutions that are simultaneously constraining and enabling (Thornton et al., 2012). Institutions *constrain* sensemaking in the sense that the interests, identities and assumptions of actors are embedded in prevailing institutional logics. In this respect, logics are rule-like, socially shared understandings that form the cognitive underpinnings of existing social structures and common practices. At the same time, institutional logics *enable* sensemaking in the sense that they provide actors with the opportunities to elaborate on and develop prevailing institutional logics. In this respect, institutional logics are toolkits that can be used by actors. This suggests that the way firms and decision makers respond to political connectedness can vary depending on the logic they use to make sense of it. For example, managers of a developed country firm can make sense of political connectedness as a non-market capability if they learn patrimonial logic and apply it to the firm-government context in emerging countries.

Institutional logics perspective is based on the notion of institutional complexity, i.e. institutions are composed of multiple and competing logics that simultaneously coexist, and that are interdependent on each other (Friedland & Alford, 1991; Kostova & Zaheer, 1999; Kostova, Roth, & Dacin, 2008; Kraatz & Block, 2008). Each institutional order represents a governance style that shape individual and organizational preferences and interests and the repertoire of behaviors by which interests and preferences are attained within the sphere of influence of that order (Frederick & Alford, 1991: 232). Table 2.1 represents how individuals and organizations, if influenced by any one institutional order, are likely to understand their sense of self and identity, i.e. who they

are, their logics of action, how they act, their vocabularies of motive, and what language is salient, etc.

The notion of institutional complexity explains heterogeneity in behavior and associated meanings not only across domains in a given society but also across societies. In this respect, we observe a variety of practices and meanings in a particular domain when different institutional orders come into play to different extents across countries. In other words, divergent practices are observed among countries because a variety of logics are applied, or transposed, to provide people with cognitive and behavioral guidelines. For example, bureaucratic nation-state, and consequently state logic, exists everywhere, but what it is and what it should do depend on its interactions with other institutional logics in a society. It can be argued that governments in developed countries are generally functional, i.e. they are to provide technical solutions to economic problems, such as supporting markets to sustain economic development. Governments in these countries are believed to play a crucial role in facilitating market exchange, as suggested by the World Bank governance indicators[1] (Kaufmann, Kraay, & Zoido-Lobaton, 1999), all of which concern state's capacity to support a modern market system. This notion of state is heavily influenced by market logic that is concerned with creating perfect, or self-regulated, markets, which is believed to result in utility maximization at the societal level and hence in increased social well-being. In emerging countries, on the other hand, state may have different functions. In Gulf countries, for example, paternalistic states led by sheikhs are responsible for looking after their subjects, who are supposed to show loyalty to their ruler in return. In this respect, a huge majority of citizens in these countries are employed by state organizations and state-owned enterprises. This indicates that the state

in such countries is theorized more as a family – or a tribe – comprised of network of individuals – i.e. family logic – or groups, than as a bureaucratic organization – i.e. state logic (Friedland & Alford, 1991). Under these circumstances, it is reasonable to expect the government in these countries to be governed more by family logic than state logic. This sort of interplay among logics should also influence the way firm-government relations occur, which will be discussed in the following section.

The concept of inter-institutional system was first introduced by Friedland and Alford (1991), whose purpose was to identify the central institutions of the contemporary Western societies. In this regard, they identified capitalist market, bureaucratic state, democracy, nuclear family, and Christianity as the pillars that shape preferences, interests, and behavior in those societies. This conceptualization was first modified by Thornton (2004), and subsequently by Thornton et al. (2012). The aim of these authors differed from that of Friedland and Alford (1991) in the sense that they sought to advance the theory of institutional logics by making it suitable for empirical inquiry through the development of a typology of ideal types (Thornton et al., 2012), rather than identifying the central institutional orders in a particular society or societies. To this end, Thornton et al. identified seven institutional orders: family, community, religion, state, market, profession, and corporation.

The strategies, values and economic systems associated with each order represent ideal types, i.e. they are unlikely to apply to any particular research context. However, the notion of institutional complexity suggests that behavior is determined not by the logic of one institutional order, but by how logics of different institutional orders come into play in a particular context. In this sense, all ideal types exist in every society to different

extents, and in different interactions with each other. Therefore, the way that logics of ideal types blend is what causes heterogeneity across time and space. Based on the extant literature, I identify four institutional orders, or ideal types, that shape behavior in the domain of firm-government interaction: market (Lui, 1985; Tanzi, 1998), state (Collins, 1980; Polanyi, 2001), family (Roth, 1968; Weber, 1968) and community (Budd, 2004; Fukuyama, 2011). I argue that the different blending of these four orders explain variations across countries in the way government-business relations take place.

2.1.1 Market logic

This logic is concerned with the activities human undertake in order to conduct exchange in the most efficient manner (Friedland & Alford, 1991). According to this, individuals' behavior is a consequence of independent, rational choices they make based on the objective assessments of their interests (Smith, 1776).

Market logic and firm-government interaction. Under market logic, self-regulated market is the perfect resource allocation mechanism through which both individual and social welfare can be achieved (Friedman 1962; Smith, 1776; Stigler, 1971). This regards the effect of any non-market element on exchange as an interference that disrupts the market and consequently hurts economic performance. As mentioned before, some economists who apply market logic to firm-government interaction attribute corruption to existence of the regulatory state (Stigler, 1971; Tanzi, 1988). The implication of this for firm-government interaction is that the degree of insertion of the regulatory state in the market leads to corruption (Bardhan, 1997).

However, many economists reject the notion of perfect markets. As Friedman (1962) states, markets work as long as transactions are voluntary and informed, but markets alone do not have any mechanisms to ensure this. Therefore, he argues that markets work only if states make and enforce the rules that enforce contracts, define property rights, and facilitate information sharing. North (1990) goes further and argues that market activities are shaped by not only formal, but also by informal rules. Many social science researchers similarly criticized market logic for focusing narrowly on the market and ignoring the other logics embedded in the broad institutional and social structures that shape market activities (DiMaggio & Powell, 1983; Friedland & Alford, 1991; Granovetter, 1985; North, 1990; Polanyi, 2001).

From an institutional logics approach, it can be argued that market logic alone cannot influence behavior. Though it may be the dominant logic in one context, other institutional orders may still have potential impact on judgment and behavior. Not every human activity can be converted into a commodity that has a monetary price and that can be exchanged in the market among rational utility maximizing individuals (Friedland & Alford, 1991). Other institutional orders generate symbolic utilities such as values. These are absolute utilities; not only they do not have explicit price, but they also cannot be traded off against each other. The implication is that, firms' strategic choices regarding how to deal with governments are not contingent on some objective assessments of utility, but are rather contingent on the whole inter-institutional system (Friedland & Alford, 1991). In other words, the rationality and legitimacy of an exchange between firms and governments is defined and shaped by the ongoing interaction among all institutional orders, not by the market forces alone.

2.1.2 State logic

This logic concerns the regulation and coordination of human activity through bureaucratic hierarchies, with the aim of increasing social well-being (Friedland & Alford, 1991; Weber, 1968). Bureaucratized state, the paramount actor in state logic, is based on specialized professional administrators and on a law made and applied by full-time professional jurists for a populace characterized by rights of citizenship (Weber, 1968; Collins, 1980).

The emergence of state logic dates back to the rise of the bureaucratic states in the late seventeenth- and eighteenth-century (Collins, 1980). Before that, legal systems were characterized by patrimonial or magical-religious procedures, by differential application to different social groups and by different localities, and by the practices of officials seeking private gain (: 930). The rise of bureaucratic state, however, led to the enforcement of written laws which ascribed culpability to the individual rather than groups (Friedland & Alford, 1991). In this sense, bureaucratic state constituted the individual as an abstract legal subject with rights –specified independently of social structure – before the law, responsible for his or her actions (: 239).

State logic and firm-government interaction. Through rationally calculable and universally applied system of law courts, state logic strictly separates between private and public spheres, in other words, between state and society, thereby inhibiting arbitrary political interference with markets (Collins, 1980; Friedland & Alford, 1991). In this regard, all exchanges between firms and governments are supposed to be strictly rule-based. Any personal discretion used by a government official represents a violation of the core principles of state logic, and hence under state logic, i.e. under the ideal type of state

institutional order, any personalized exchange between firms and governments are seen as illegitimate, and labeled as corruption.

A big problem emerges when state logic is transposed to understand firm-government interaction in emerging countries. Although we see some elements of state logic in these countries, it is not strong enough in the institutional system to impose a rational-legal order. The notion of bureaucratic states that attempt to convert diverse individual situations into the basis for routine official decisions (Friedland & Alford, 1991: 249), does not necessarily apply to the context of emerging countries. Consequently, we should see a shift in the boundary that defines legitimate exchanges between firms and governments where emerging countries are considered. This will be discussed in more detail in the subsequent sections of the paper.

2.1.3 Family logic

The logic of the family is the motivation of human activity through unconditional loyalty with the aim of increasing family reputation and honor **(**Friedland & Alford, 1991). In this regard, families attempt to convert all social relations into unconditional obligations oriented to meet collective needs. Patriarchalism, which Weber (1968) defines as the authority of a master over his household, epitomizes how this logic shapes governance. Patriarchal rulers need no bureaucratic machinery to enforce their policies. They rather depend on the willingness of their subjects to obey their “father”, who protects and provides for his “children”, and who elevates the status of the whole family in return.

Family logic and firm-government interaction. In developed countries, the unconditional loyalties which are the ideal of familial relations do not provide a legitimate model for economic behavior. In fact, the logic of the family is allowed to influence economic behavior only on the margins of Western societies, such as the Mafia, or small businesses that are rooted in immigrant communities (Fukuyama, 1996; Tan & Peng, 2002). Once such practices are spotted, they are regarded as deviant, traditionalistic, and even pathological (Friedland & Alford, 1991). In emerging countries, however, it is widely recognized that allegiance to kinship-based or clan-based loyalties often takes precedence over self-interest and formal rules (Bardhan, 1997, Budd, 2004; Fukuyama, 2011; Roth, 1968; Theobald, 1982; Uricoechea, 1980). Under such circumstances, it may be “rational” for people to continue to exchange with those who they are related with, to the exclusion of others, even though there are more profitable alternatives.

The situation described above is not limited to exchanges within the market, but also applies to exchanges between firms and governments. In the West, where legal standards – state logic – are applied to such exchanges, anonymous bureaucratic rules strictly regulate the relations between government and business. In developing countries, however, where legal standards are subdued by relational norms – or when state logic is subdued by family logic –, exchanges between business and government become personalized. Under these circumstances, use of public resources to cater to particularistic loyalties becomes quite common and routinely expected (Bardhan, 1997: 1330). For example, a common aphorism in some pre-1989 Soviet-dominated societies urged that “those who do not steal from the state steal from their families” (Misangyi et al., 2008:

753). This suggests that to the extent that exchanges between firms and governments are not subject to the formal rule of law, they are likely to be subject to the informal rules of relational obligations. It is this characteristic of developing countries that makes personalized, relationship-based exchanges between firms and governments “rational”, and “legitimate”.

2.1.4 Community logic

Contemporary communities approach (O'Mahony and Lakhani, 2011) defines community as “a group of people who coalesce around any number of identity sources”. This definition includes communities ranging from local communities, socio-political movements, religious groups, social classes, diaspora, etc. The logic of all these communities is based on the motivation of human activity through reciprocal obligations with the aim of increasing the status of the community (Thornton et al., 2012).

Community logic and firm-government interaction. Individual behavior in a community is aimed at serving collective interests by forming relational networks with other members (Thornton et al., 2012). Such relationships are not based on self-interest, but rather on trust and reciprocity among members. They are not governed by the formal rule of law, but rather by informal group norms and values. As a result, community logic shapes behavior quite differently from market logic and state logic. The implication for firm-government interaction is that if community logic prevails over state logic, then exchanges between firms and governments will be shaped by the informal norms that are embedded in the relational networks rather than by the formal rules. Thus, the influence of community logic in an institutional system is likely to lead to informal ties between

firms and governments. In short, the arguments made for the role of family logic in emerging countries can be made also for community logic. The difference between family logic and community logic is that the former concerns unconditional obligations based on kinship and clanship, whereas the latter is related to reciprocal obligations based on a shared identity (Bardhan, 1997; Fukuyama, 2011). In this regard, the influence of community logic in an institutional system is likely to lead to horizontal networks between firms and governments, or so-called cronyism, whereas that of family logic is likely result in vertical networks between firms and governments, or so-called patron-client relationships, or patronage ties.

2.1.5 Blending institutional logics

As explained before, the notion of institutional complexity in the institutional logics perspective suggests that multiple logics simultaneously exist and shape behavior (Thornton et al., 2012). In this sense, it is likely that firm-government interaction in a particular context is guided by multiple logics.

For example, the modern market system that exists in developed countries is governed by a blend of market and state logics. In this regard, market – as we know it – needs a strong bureaucratic state in order to function. As Friedman (1962) argues, free markets cannot exist without a state. State’s duties in this regard include maintaining law and order, defining property rights, adjudicating disputes about the interpretation of the rules, enforcing contracts, promoting competition, providing a monetary framework, etc (Cuervo-Cazurra & Dau, 2009; Kaufman, 1997; Khanna & Palepu, 2000; Kim, Kim, & Hoskisson, 2010; North, 1990; Peng, 2003). After all, it was the state logic that provided

the basis for a reliable system of banking, investment, property, and contracts, and set the stage for the industrial revolution in the first place (Collins, 1980). It was the strong bureaucratic states of the West that formed the institutional underpinnings of markets, and hence created Polanyi (2001) similarly argues that the modern market system – market logic – cannot be understood independent of the modern nation-state – state logic. In this regard, he gives a very detailed historical study of how markets, which did not exist prior to the Industrial Revolution, were created for the first time. In the 18th century British statesmen, who were informed by the theories of classical economists – i.e. market logic –, tried to create an economic system based on the notion of self-regulated markets. Though created and sustained by state logic, this system was thought to be independent of the state and society – in line with market logic. After market came to be successful with the Industrial Revolution in Britain, market logic spread throughout the world. In short, market – and its logic –, is not a natural phenomenon that has existed since the beginning of humanity, but rather a superimposition by the British State on its society in the 18th century (Collins, 1980; Polanyi, 2001). The implication is that market logic cannot take roots unless state logic is already developed. In this sense, a strong state logic may not necessarily lead to strong market logic, but is a prerequisite for it (Cuervo-Cazurra & Dau, 2009; Kaufman et al., 1999; Williamson, 2004).

Another example that shows how different logics interact with each other is the guanxi-based gift-economy, i.e. gifts in return for a favor. Despite seemingly being a simple market exchange, gift is more than a commodity in the practice of guanxi, because it is not independent of the social relationship in which it is exchanged (Yang, 1989). In this respect, Yang argues that the practice of *guanxi* is rooted in a culturally specific

relational conception of the person, where identities are constructed through the internalization of others' judgments. *Guanxi* thus depends upon creating identities, whatever the basis, between people such that norms of mutual obligation can be activated. Gift giving is an aggressive material and symbolical construction of commonality of insideness, from which obligation logically flows (Friedland & Alford, 1991: 258–259). Put in this way, guanxi-based gift giving reflects a community logic that aims to increase the community’s status by creating a common identity and reciprocal obligations between members. This is distinct from market logic that is based on impersonal, one-time exchanges. Yet, this is not to argue that guanxi-based gift-giving does not include any elements of market logic. It is not realistic to assume that parties of such an exchange are not driven by self-interest whatsoever. Yet, interests and how to maximize them are shaped by the interaction between market logic and community logic, rather than the former alone. In this sense, Chinese people are not necessarily repulsed by the notion of self-interest, but the blend of market logic and community logic provides them a different understanding of self-interest, as well as of how to achieve it.

2.2 Legitimacy of exchanges between firms and governments

2.2.1 Corruption

When used in the domain of firm-government interaction, the word corruption refers to an illegitimate exchange between a firm and the government. Thus, we need to look at how corruption is defined and studied if we want to understand how the boundary that separates between legitimate and illegitimate exchanges is drawn. In this regard,

research on corruption has been dominated by two perspectives. A careful reading of these perspectives reveals that they embody three logics. One perspective is solely concerned with the role of rational self-interest and efficiency pressures, and is thus dominated by market logic (Klitgaard, 1988; Leff, 1989; Lui, 1985; Tanzi, 1998). The other perspective deals with the regulation of corruption through both disciplinary market forces and law, and hence is more influenced by a blend of market and state logics (Bardhan, 1997; Cuervo-Cazurra, 2006; Kaufmann, 1997; La Porta et al., 1999; Mauro, 1995; Schleifer & Vishny, 1993).

The first perspective applies market logic to the issue of corruption. In other words, actors are considered to engage in corruption simply because they have incentives do so. One stream of research in this perspective even suggests that the presence of the state distorts supply and demand, while corruption is a mechanism that equalizes it (Leff, 1989; Lui, 1985). According to this, it is the state that creates the motivation for corruption by impeding free markets. This point is bluntly illustrated by Tanzi (1998): "If we abolish the state, we abolish corruption" (: 566). Overall, this perspective sees corruption either as a way to overcome excessive regulatory burdens that inhibit markets to operate, or as an incentive for the government officials to work harder. The former argument is usually applied to developing countries in which state intervention is an issue, whereas the latter applies to developed countries too (Mauro, 1995). Such arguments clearly epitomize market logic.

State logic constitutes the origin of a definition of corruption that is commonly used in research and practice: "Abuse of public power for private gain". This definition is widely adopted by the literature (Cuervo-Cazurra, 2006; Kaufmann, 1997; Schleifer &

Vishny, 1993; Rodriguez, Uhlenbruck, & Eden, 2005; Spencer & Gomez, 2011; Svensson, 2005; Treisman, 2000; Voyer & Beamish, 2004), and is also officially adopted by the World Bank, as well as Transparency International. The term "abuse of public power", of course, typically constitutes a breach of rule of law, and hence involves applying a rational-legal standard to the issue (Misangyi et al., 2008; Svensson, 2005). Thus, it can be argued that the lens through which we view, explain, and address corruption, is rooted in state logic. The approach of International Country Risk Guide (ICRG) to corruption epitomizes this. In this regard, the organization sees corruption as a serious threat to the government's ability to establish and maintain order, and hence a factor that dramatically increases country risk:

> "…insidious sorts of corruption are potentially of much greater risk to foreign business in that they can lead to popular discontent, unrealistic and inefficient controls on the state economy, and encourage the development of the black market.
>
> The greatest risk in such corruption is that at some time it will become so overweening, or some major scandal will be suddenly revealed, as to provoke a popular backlash, resulting in a fall or overthrow of the government, a major reorganizing or restructuring of the country's political institutions, or, at worst, a breakdown in law and order, rendering the country ungovernable." (ICRG, 2013)

Most studies on corruption, however, represent a blend of state logic and market logic, regarding corruption as a rational, self-interested behavior, conducted by persons who use their discretion to direct allocations to themselves or to other social actors who offer rewards in return for favorable discretionary treatment (Bardhan, 1997; Kaufmann, 1997; Rose-Ackerman, 2001; Schleifer & Vishny, 1993). Thus, the second perspective assumes that corruption is a rational utility maximizing response to situations that present opportunities for gain and the discretionary power to appropriate that gain (Misangyi et

al., 2008: 751). In this regard, corruption is thought to be best remedied both by curtailing discretionary power – e.g. strengthening rule of law, which is a manifestation of state logic – (Cuervo-Cazurra, 2006; La Porta et al., 1999; Mauro, 1995; Voyer & Beamish, 2004), and by incentives to avoid corrupt activities – e.g. increasing government officials' wages (Klitgaard, 1988), which is a manifestation of market logic. In addition to this, an influential stream of research within this perspective is based on the view that laws determine the level of corruption in a society indirectly by shaping incentive structures (Kaufmann, 1997; Schleifer & Vishny, 1993), e.g. strictly enforced laws increase the cost of corruption and hence deter people from engaging in it.

However, corruption is a complex phenomenon and understanding and changing a corrupt system requires a more holistic view. Institutional logics approach tells us that the institutional system is not confined to the logic of either the market or the state, but rather is composed of several orders. It may be true that it is predominantly market and state logics that influence actors' cognitive and behavioral repertoires in the West, but in other countries, different logics may be in play. As a result, practice that is perceived as a corrupt transaction in the West, may be interpreted as loyalty or as reciprocal obligation in other countries, which may increase the prevalence of that practice in those countries.

This holistic view of corruption is in line with the neo-institutional approach to corruption in international business, which takes into consideration the factors beyond the market and the state. In this regard, Spencer and Gomez (2011) demonstrate that when multinationals' managers perceive that a corrupt practice such as bribery has become institutionalized in a society, they are more likely to conform to those societal expectations to obtain legitimacy. Similarly, Collins and Uhlenbruck (2004) found

empirical evidence that managers in India who perceived corruption to reflect 'the way things are done' locally were more likely to engage in corrupt practices, even when they personally viewed them negatively. Uhlenbruck et al. (2006) show that multinationals' subsidiaries engage in corruption in highly corrupt countries in order to be congruent with local institutions. Despite extending the view on corruption by taking into consideration the domains other than the market and the state, this literature in international business has neglected to conceptualize corruption. Those scholars rather took the Western definition of corruption for granted, and applied it to emerging country contexts, assuming that multinationals either challenge or conform to the universally defined "corrupt" practices they face in emerging countries. As a result, the literature failed to address how multinationals and their decision makers draw the boundary that separates between legitimate and illegitimate exchanges.

As explained earlier, however, the definition of corruption is to a large extent shaped by state logic, which makes a clear distinction between legalized exchanges between firms and government such as campaign contributions and the illegal ones such as bribery. Since state logic is much weaker in emerging countries than in the West, the principles used to distinguish legitimate exchanges from illegitimate ones in those countries are likely to be different. Thus, we should expect to see different forms of exchanges between firms and governments than these two. In fact, many international business scholars argue that political connectedness, i.e. inter-personal ties between corporate and political actors, is the most common form of firm-government interaction in emerging countries (Peng & Heath, 1996; Shi, Markoczy, & Stan, 2014; Wan, 2005).

2.2.2 Political connectedness

International Country Risk Guide (2013) does not provide a definition of political connectedness but merely identifies it as a form of corruption: "Political connections represent a type of corruption, taking such forms as excessive patronage, nepotism, job reservations, 'favor-for-favors', or secret party funding". Yet, literature on political connectedness separates from the general corruption literature. This suggests that political connectedness is a distinct phenomenon from corruption.

Peng and Luo (2000) define political ties as individual connections with officers at various levels of government. Faccio (2006), in her pioneering empirical study on political connectedness around the world, defines a company as politically connected if "at least one of its large shareholders – anyone controlling at least 10 percent of voting shares – or one of its top officers – i.e. CEO, president, vice-president, chairman, or secretary – is a member of parliament, a minister, or is closely related to a top politician or party." (: 369). Similarly, Sun, Mellahi, and Wright (2012) define political connections as "boundary-spanning personal and institutional linkages between firms and the constituent parts of public authorities." (: 68). All these definitions suggest that political connectedness involves a long-term interpersonal relationship as opposed to a one-time exchange, which has been the main focus of the general corruption literature.

This aspect of political connectedness is also supported by the empirical work. Fisman (2001) demonstrates that politically well-connected firms in Indonesia lost more market value in reaction to the adverse rumors about the state of President Suharto's health than firms that are less connected. Similarly, Leuz and Oberholzer-Gee (2006) show that firms have difficulty re-establishing connections with a new government when

their patron falls from power, leading closely connected firms to underperform under the new regime. Siegel (2007) reports that Korean firms' network ties to the political regime increases their cross-border alliance activity, while their network ties to the enemies of the political regime decreases it. These empirical studies demonstrate that political connectedness concerns long-term and personal relationships embedded in the political system, and such relationships cannot be easily formed or abandoned, as opposed to impersonal exchanges, which are transient and business oriented in nature.

However, most studies do not elaborate on the nature of those relationships, despite some notable exceptions, such as Siegel (2007) and Sun et al. (2012). In this regard, the implicit assumption in most of the literature is that the parties build and maintain these relationships primarily because they benefit from them (Peng, 2003). This understanding embodies market logic that presumes rational behavior informed by the principles of utility maximization. Similarly, the literature influenced by state logic does not recognize relationships occurring outside the formal rules and roles. It does not distinguish corruption from political connectedness, and labels the exchanges that are facilitated by personal ties between firms and governments as corruption (Cuervo-Cazurra, 2006; Kaufmann, 1997; Rodriguez et al., 2005). Therefore, we need to look at other institutional logics such as family logic and community logic, in order to understand the boundaries that separate legitimate exchanges between firms and governments from the illegitimate ones in emerging countries. This paper is a step towards this direction.

2.3 The logic behind political connectedness

It is very well known that firms and governments are interconnected all over the world (Faccio, 2006). This includes the developed countries where state is largely withdrawn from the market, such as Canada, and the U.K. Business-government relations are believed to be very important for U.S. businesses too (Fisman et al., 2012). Otherwise there would not be 12,503 lobbyists in Washington D.C. (Reuters, 2009), the heart a political system that seemingly champions market logic at the expense of state logic around the world. In this sense, we can look at firm-government interaction as a universal phenomenon.

Yet, this is not to say that this interconnection is attained and utilized in the same manner globally. As explained before, most research on political connectedness has looked at informal ties in emerging countries. There is little evidence suggesting that business-government interaction in developed countries may also be facilitated by informal ties. In this regard, Fisman et al. (2012) examined U.S. firms' political ties to Vice President Dick Cheney. They estimated the value of these ties for firms precisely as zero, meaning that firms did not benefit from being connected to Dick Cheney. The conclusion drawn from this finding is that personal ties to politicians do not yield value to firms in the U.S. Fisman et al. attributed this to the existence of formal control mechanisms that regulate government-business relations in the U.S. In short, the study suggests that firms cannot leverage informal political ties in countries whose formal institutions are strong.

On the other hand, research on political connectedness in emerging countries indicates that both the prevalence and the utility of political connectedness are much

higher in these countries. Siegel (2007) shows that networks with the political regime increased the rate at which Korean companies formed cross-border strategic alliances. Claessens, Feijen, and Laeven (2008) find that Brazilian firms which provided contributions to elected federal deputies experienced higher stock returns than firms that did not. Peng and Luo (2000) document that managers' ties with politicians in China increase firm performance. Yiu and Lau (2008) report that network ties with the government in China increases the intensity of firms' engagement in corporate entrepreneurial activities, which in turn increases firms' relative performance. Yiu, Lau, and Bruton (2007) show that political network ties in China positively affect international venturing.

Overall, the literature regards political connectedness as a rational and interest-seeking response to the existing formal institutional arrangements in a country. Specifically, they see formal rules, i.e. laws and regulations enforced by the strong bureaucratic state, as necessary for the otherwise imperfect markets to perform (Khanna & Palepu, 1997; North, 1990; Peng, 2003; Wan, 2005). Absence, or weakness of a bureaucratic state, is thus seen as an institutional deficiency, or as it is widely known in the literature, institutional voids (Khanna and Palepu, 1997). Firms are believed to build political connections in order to fill, or substitute (Roth & Kostova, 2003) these voids. This view assumes that formal rules need to be set up and created by states so that markets can function properly and enhance economic performance. This understanding, similar to the dominant perspective in the corruption literature, reflects a combination of market logic and state logic.

Overall, most of the literature on political connectedness considers all sorts of informal exchanges between firms and governments as a consequence of institutional underdevelopment, and – either implicitly or explicitly – labels them all as inefficient forms of business-government interaction. Yet, political connectedness could just be one of many ways that enable strategic interaction between firms and governments. From an institutional logics perspective, different blends of logics across countries make different strategies of interacting with the government available to firms. Thus, the different forms of firm-government interaction we see between developed countries and emerging countries are primarily caused by different blending of institutional logics. In developed countries, market and state logics – i.e. impersonal logics – take precedence over family and community logics – i.e. relational logics –, which makes firm-government interaction subject to formal control mechanisms such as laws and regulations (North, 1990; Peng, 2003). As a result, exchanges between firms and governments in these countries tend to be impersonal and rule-based. In emerging countries, on the other hand, relational logics prevail over impersonal logics, which makes firm-government interaction subject to informal control mechanisms such as unconditional loyalties or reciprocal obligations. As a result, exchanges between firms and governments in these countries tend to be personalized and relationship-based.

Firms' rule-based, impersonal – formal – exchanges with governments are facilitated by political action committees, lobbying entities, as well as through inter-organizational ties with other government bodies, such as a joint venture with a state-owned enterprise (Sun, Mellahi, & Thun, 2010). On the other hand, personalized, relationship-based – informal – exchanges with governments are facilitated by variety of

political ties, such as those 1) between corporate executives and politicians or government officials, e.g. friendships and kinships; 2) between politicians and firms, e.g. politicians sitting on corporate boards; and 3) between corporate executives and political institutions, e.g. executives appointed as politicians (Faccio, 2006). Table 2.3 contrasts the two types of firm-government interaction.

2.4 Varieties of Firm Government Interactions

The domination of an institutional system by a combination of market logic and state logic is a mixture of the ideal economic systems of the two logics, i.e. market capitalism and welfare capitalism. The consequent economic system is one in which neither can market dominate for economic gain nor can state for social gain. This is in fact the case in all developed countries[2], in which the government provides with the legal and regulatory framework that regulates and coordinates market exchange with the aim of increasing social well-being, but also in which there is always some market exchange that exists beyond the state's reach. I call this blend of market and state logics *bureaucratic logic*.

Emerging countries, on the other hand, have other logics than those of the state and of the market that shape their economic systems. Weak state logic in these countries mean that rule of law is not strong. The implication is that although the states in these countries may attempt to regulate and coordinate economic activity, they are not subordinate to rational and legal standards when doing it. They also lack the capacity and legitimacy to exert control over economy. Furthermore, weak market logic means that exchanges are not always based on rational utility maximization. On the other hand,

strong family logic and community logic in these countries make unconditional loyalties and reciprocal obligations important factors that shape behavior. Drawing on the extant literature (Budd, 2004; Fukuyama, 2011; Roth, 1968; Theobald, 1982; Uricoechea, 1980), I call this blend of institutional logics – i.e. weak market and state logics, combined with strong family and community logics – *patrimonial logic*. In such a system, patronage ties between corporate actors and political actors constitute a common practice. Considering this, the existence of patrimonial logic as opposed to bureaucratic logic is probably the most important element that distinguishes emerging countries from developed countries.

The German sociologist Max Weber (1968) originally coined the term patrimonialism. According to him, patrimonialism meant that the governmental offices originate in the household administration of the patriarchal ruler. Patrimonialism, in this sense, is a result of the extension of patriarchal rule to the military, economic, and political functions of the state. In other words, patrimonialism occurs when the personage representing the ruling family is amalgamated with the state. This diffusion of patriarchal rule to bureaucracy corresponds to the blend between family logic and state logic in this paper. Scholars who built on Weber subsequently added community logic to this blend. For example, Fukuyama (2011) argues that patronage ties are based on the two principles of kin selection and reciprocal altruism. In this case, the former clearly corresponds to family logic, while the latter certainly amounts to community logic.

It is important to note that this paper diverges from the extant patrimonialism literature in its view of institutions. According to the latter, institutions differ across countries in degree, not in kind (Jackson & Deeg, 2008). Thus, the patrimonialism

literature sees patronage ties as a consequence of weak or absent impersonal institutions. In this regard, Weber identified patrimonialism as one of the three forms of traditional domination, the other two being charismatic leadership and feudalism. Although scholars like Fukuyama extended and contributed to Weber's original conceptualization of patrimonialism, the view of patronage ties as an inferior, archaic, exotic, and an ineffective form of governance has remained consistent in the literature. For example, Roth (1968) describes several features of patrimonialism including the survival of a traditional regime, "where the researcher, if he gains access at all, can almost perform the feat of travelling into the past" (p. 195-196). Uricoechea (1980), in his analysis of patrimonial foundations of the Brazilian Bureaucratic State, equates patrimonialism with the militarization of the Brazilian society and the consequent human rights abuses: "Monstrosity may be defined as a mode of being, the essential changes of which are contingent and accidental. If we accept this definition, we can readily apply it to patrimonial bureaucracy" (p. 43). Similar to this, Budd (2004) argues that patrimonialism hinders democracy and economic growth in emerging countries. Finally, Fukuyama (2011) sees patrimonialism as a source of political decay, and an impediment to state building.

As explained earlier, however, an important tenet of this paper is that institutions are not universal (Jackson & Deeg, 2008; Tsui, 2007; Whetten, 2009). Impersonal institutions, i.e. bureaucratic logic that shapes firm-government interaction in the West are not necessarily the norm. Neither is the patrimonial logic that shapes firm-government interaction in emerging countries should be seen as "voids", or "deviations" from the ideal-typical situation. Thus, the main argument of this paper is logic blending

gives rise not just to differences of degree, but the fundamental differences in kind (Jackson & Deeg, 2008). Overall, different forms of firm-government relations across countries are determined by different interplays among institutional logics that create a systemic logic that makes a certain form of firm-government interaction prevalent. In this sense, formal exchanges between firms and governments should be more common in countries where market logic and state logic are strong enough to confine family logic and community logic to their domains. On the other hand, informal exchanges between firms and governments should be more common in countries where logic of the family and community are strong enough to suppress the logics of the market and the state. Figure 2.2 shows countries according to the interplay among institutional logics.

2.5 Discussion

In developed countries, where bureaucratic logic dominates, the boundary that separates legitimate exchanges between firms and governments from the illegitimate ones is determined primarily determined by one principle: the exchange should be based on impersonal rules. Under bureaucratic logic, there is a strict separation between public and private, and hence government officials avoid personalized exchanges, as well as using their power for personal gain. Therefore, in developed countries, a legitimate firm-government interaction is mainly in the form of lobbying or campaign contributions. In emerging countries, however, where family and community logics dominate, exchanges between firms and governments are often personalized. Thus, it is legitimate for government officials in those countries to fulfill their familial or reciprocal obligations by using public power to favor relatives and "clients", as well as friends. In this sense, it is

normal and rational for exchanges between firms and governments to be facilitated by horizontal and vertical networks between corporate and political actors. This, however, is deemed as corruption in developed countries, as family and community logics are weak, while state logic is strong. This addresses the research questions of this paper by explaining 1) how the boundary between legitimate and illegitimate exchanges between firms and governments are drawn, and 2) how this boundary differs across countries.

There have been very few attempts to define what corruption and political connectedness are, and how they differ from each other. In this respect, one definition, "abuse of public power for personal gain", has been taken for granted, and deeply influenced the scholarly approach to the issue. This definition, however, embodies bureaucratic logic, which shapes the way firms and governments interact with each other in the West. In emerging countries, on the other hand, patrimonial logic provides different strategies of action, and hence leads to different forms of exchanges between firms and governments. In this regard, most studies on emerging countries have ended up imposing Western bureaucratic logic on non-Western phenomena (Tsui, 2007), and erroneously labeled all kinds of informal ties between firms and governments as corruption. Drawing from the institutional logics perspective, this study offers a fresh lens to study firm-government interaction in emerging country contexts, where, not only the logics of the market and the state, but also those of the family and the community together shape the boundary that separates legitimate and illegitimate exchanges between firms and governments.

This essay also contributes to the institutional logics literature by demonstrating that how dissimilar logics blend. In this regard, some of the extant literature has typically

focused on a single dominant logic that shapes the entire institutional system. For example, Lounsbury (2002) documented that during the 1980s, the regulatory logic that emphasized bank lending in the US financial sector yielded to a market logic, which gave rise to retail-oriented financial services competition. Similarly, Lounsbury (2007) demonstrated that the mutual fund industry in Boston is dominated by trustee logic, which represents a traditional, long-term oriented, and craft-based approach to money management. He found that the mutual fund industry in New York, on the other hand, is dominated by a performance logic, which represents a modern, short-term oriented, professional approach to money management. Although some other studies in the logics literature have acknowledged the co-existence of competing logics, these scholars have assumed that such different logics separately guide different actors. For example, Reay and Hinnings (2009) argued that physicians in the Canadian health care industry adhered to professional logic, whereas the government supported business logic. Marquis and Lounsbury (2007) argued that two logics in the US banking industry compete to dominate the organizational field: national logic manifested through national banks, and community logic reflected through community banks. Similarly, Greenwood et al. (2010) found that the downsizing decisions of large firms concentrated in regions whose governments champion regional distinctiveness are influenced by regional logic, whereas those of smaller firms are shaped by family logic. Luo (2007) identified two logics that determine training attitudes across countries: statism, which emphasizes state authority over civil society, and corporatism, which emphasizes a guild-based system with collective bargaining and apprenticeship over a market system with hire-and-fire practices. She found that countries with strong statist and corporate logics are more likely

to prefer continuous learning model of training. Although some exceptional studies have tried to explain how different how logics blend, such attempts have remained scarce. For example, Glynn & Lounsbury (2005) studied how the aesthetic logic that traditionally informs the practices of the symphony and the commercially oriented market logic blended with each other in the context of Atlanta Symphony Orchestra. This paper follows the footsteps of Glynn and Lounsbury by explaining logic blending in the international context of firm-government interaction.

2.5.1 Implications for International Business

The premise of the institutional logics perspective that institutions are simultaneously material and symbolic makes it distinct from neo-institutional frameworks used in international business (Busenitz, Gomez, & Spencer, 2000; Kostova & Roth, 2002). In this regard, institutional logics are more than regulative, normative, and cognitive structures that impose predictable patterns of behavior through legal and social sanctions, or cultural indoctrination. Logics shape behavior not due to the coercive, normative, and mimetic pressures they exert, but because logics define actors' interests and enable them to pursue their objectives in a certain way. In this sense, institutions are providers of resources and capabilities that allow its constituents to undertake some activities more successfully than others (Jackson & Deeg, 2008). The implication of this for firm-government interaction is that political connectedness occurs in emerging countries not because it is highly valued by people or imposed by law, but because it is a capability which firms employ when they interact with the government.

The notion of duality also distinguishes institutional logics approach from the new institutional economics in international business, which is based on the premise that

formal institutions determine firms' strategic choices by providing the incentive structures (Peng, 2003; Wan, 2005). According to the school of new institutional economics in international business, corruption and political ties occur in emerging countries considerably more than developed countries, because the benefits they provide exceed their costs in contexts where weaker formal institutions is associated with lower costs of engaging in such practices (Kim, Kim, & Hoskisson, 2010; Peng & Luo, 2000). From an institutional logics perspective, this explanation overlooks the role of informal norms and meanings associated with strategic action. This is not to say that institutional logics perspective does not recognize the importance of formal institutions in explaining behavior. In fact, it suggests that symbolic constructions do not make sense if the material world is not appropriately constructed. Transition economies epitomize such a situation. For example, the notion of an arm's length transaction does not hold in Eastern Europe, where formal institutions that enforce contracts remain weak (Buchan, 2009). However, institutional logics approach also suggests that deployment of material resources alone cannot organize people's lives if they do not find correspondence in society's shared beliefs and understandings. For example, exchanges in Japan are still facilitated by relational networks rather than contract laws, despite the strong rule of law in this country. This is because strong formal institutions associated with contract enforcement cannot make rule-based, impersonal contracting a common practice in Japan if Japanese people's propensity to trust others remains low (Yamagishi & Yamagishi, 1994). New institutional economics approach in international business, in this regard, mostly focuses on "the observable", and neglects "the unobservable", e.g. subtle meanings that underlie formal structures and common practices.

Institutional logics approach has also implications for the broader economic perspective in international business, which solely emphasizes the role of incentive structures as the primary cause of corruption and political connectedness. Regardless of the differences in the antecedents of the incentives – either formal institutions or pure market forces –, all economic perspectives converge on the assumption that actors engage in corruption and political connections mainly because they have interest in doing so. However, institutional logics approach suggests that there are no objective incentives that can be understood independently of actors' understandings. Institutional logics shape both the ends to which their behavior should be directed, and the means by which those ends are achieved (Friedland & Alford, 1991). In this sense, logics shape the rules by which utility is defined and pursued. As a result, incentives are not universal, but rather contingent on institutions.

2.6 Conclusion

This perspective paper addressed two research questions: 1) What draws the boundary that separates legitimate and illegitimate exchanges between firms and governments?, and 2) how does this boundary differ across countries? The essay drew on the institutional logics perspective to answer the questions. In this regard, I argued that people use logics to distinguish a legitimate form of firm-government interaction from an illegitimate one. Specifically, I proposed that informal, personal exchanges between firms and governments, i.e. political connectedness, is illegitimate under market logic and state logic, whereas it is legitimate under family and community logic. In order to answer the second research question, I explained the differences between developed countries and

emerging countries in the way that firms and governments interact with each other. In this respect, I argued that political connectedness in emerging countries arises from the interplay among four institutional orders: the market, the state, the family, and the community, which together generate a patrimonial logic. In developed countries, on the other hand, state logic and market logic come together to generate bureaucratic logic, which pervades the institutional systems of these countries, and insulates the logics of the family and the community from the domain of firm-government relations. This results in the prevalence of formal, impersonal exchanges between firms and governments in developed countries.

NOTES

[1] i.e. voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, control of corruption.

[2] In fact, no country's system in the world is either purely state or purely market driven.

Table 2.1: Institutional orders that shape firm-government interaction, adapted from Thornton, Ocasio, & Lounsbury (2012)

	Market	**State**	**Family**	**Community**
Basis of strategy	Self-interest	Social well-being	Family reputation & honor	Community status
Strategy	Commodification of human activity	Rationalization and regulation of human activity	Motivation of human activity for unconditional obligations	Motivation of human activity for reciprocal obligations
Control mechanisms	Rational, impersonal, universal	Formal, rational, impersonal, universal	Informal, non-rational, personal, particularistic	Informal, non-rational, personal, particularistic
Source of authority	Possession of ownership	Bureaucratic hierarchies	Patriarchal domination	Commitment to community values & ideology
Source of legitimacy	Economic performance, share price	Democratic participation	Unconditional loyalty	Unity of will, trust & reciprocity
Source of identity	Faceless	Citizenship in nation	Family membership	Community membership
Economic system	Market capitalism	Welfare capitalism	Family capitalism	Cooperative capitalism

Table 2.2: Institutional logics and corresponding remedies for corruption

	Market logic (Economic remedies)	**State logic (Legal remedies)**	**Blend of market logic and state logic**
Corresponding solutions to remedy corruption	-Mass privatization -Market liberalization -Trade liberalization -Macro-stabilization -Economic development -Competitive wages for government officials -Nothing (Corruption allows supply and demand to operate)	-Punitive laws -Strict regulations -Protection of property and contractual rights -Bureaucratic monitoring mechanisms	-Different combinations of economic and legal remedies

Table 2.3: Varieties of firm-government interactions, adapted from Faccio (2006) and Sun et al. (2010)

Formal exchanges	Informal exchanges
Political action committees	Personal ties between corporate executives and politicians or government officials (e.g. kinship, friendship)
Lobbying entities	Personal ties between politicians and firms (e.g. politicians sitting on corporate boards)
Inter-organizational ties between firms and political institutions (e.g. joint ventures between public firms and state owned enterprises)	Personal ties between corporate executives and political institutions (e.g. executives appointed as politicians)

Table 2.4: Blends of logics across countries

	Developed countries	Emerging countries
Market logic	Strong	Weak
State logic	Strong	Weak
Family logic	Weak	Strong
Community logic	Weak	Strong
	Bureaucratic logic	Patrimonial logic

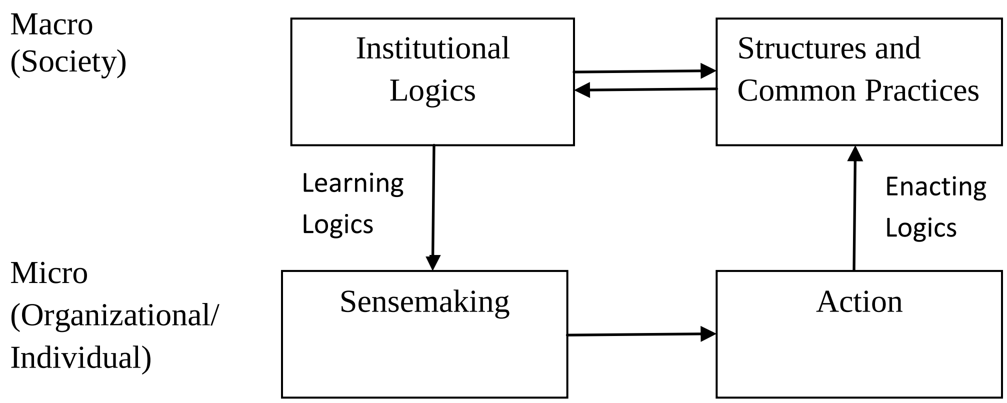

Figure 2.1: Cross-level model of institutional logics, adapted from Thornton et al. (2012)

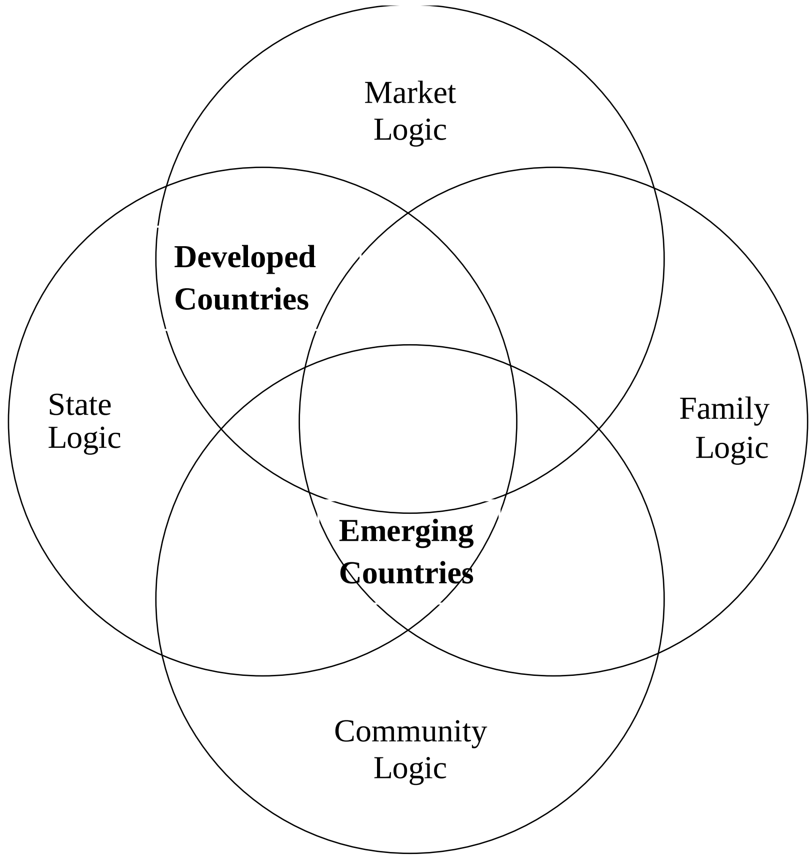

Figure 2.2: Interplay among institutional logics across countries

CHAPTER 3

MAKING SENSE OF POLITICAL CONNECTEDNESS: CORRUPTION OR STRATEGY?

3.1. Motivation

- JPMorgan Chase hired the son of a former Chinese banking regulator who is now the chairman of the China Everbright Group, a state-controlled financial conglomerate. After the chairman's son came on board, JPMorgan secured multiple coveted assignments from the Chinese conglomerate, including advising a subsidiary of the company on a stock offering.

- The Hong Kong office of JPMorgan hired the daughter of a Chinese railway official when The China Railway Group, a state-controlled construction company that builds railways for the Chinese government, was in the process of selecting JPMorgan to advise on its plans to become a public company. With JPMorgan's help, China Railway raised more than $5 billion when it went public in 2007. (New York Times, 2013)

Such hiring practices by JP Morgan in China epitomize the role of political connectedness in emerging countries. In this regard, the incentive for corporations to become politically connected has been recognized among scholars. The source of such value is not limited to preferential treatment by state-owned enterprises or the government, but also includes lighter taxation, relaxed regulatory oversight, or stiffer regulatory oversight of its rivals (Faccio, 2006). Given its importance, some international business scholars conceptualize political connectedness as a non-market capability that yields competitive advantage in emerging countries, where such practices are prevalent (Kim, Kim, & Hoskisson, 2010; Peng, 2003; Wan, 2005). These scholars view political

connectedness in emerging markets in economic and relational terms, and therefore frame them as an opportunity for firms.

Yet, forming direct or indirect ties to foreign government officials poses challenges to multinational enterprises from developed countries. Because such practices violate the legal and social norms in their home countries, developed country firms are likely to face legal and social sanctions if they engage in political connectedness abroad (Rodriguez et al., 2005; Spencer & Gomez, 2011). Thus, political connectedness may hurt a developed country firm's legitimacy not only in their home countries, but all around the world (Kostova & Zaheer, 1999). For instance, the Securities and Exchange Commission opened an anti-bribery into JP Morgan's hiring practices in China. Further, this investigation, along with the hiring practices themselves, is extensively reported by the global media, which negatively affects the JP Morgan's international reputation. In this respect, the international business literature on corruption conceptualizes political connectedness in social terms, and frames them as a threat to firms.

These two perspectives show that political connectedness creates a dilemma for multinationals. On one hand, political connectedness seems to be an important source of competitive advantage in many emerging countries. On the other hand, if uncovered, it may hurt a firm's legitimacy. In this sense, managers of multinationals need to take into account both strategic imperatives and legitimacy concerns when managing their firm's political ties. However, the academic literature has yet to combine these two perspectives in developing a holistic analysis of these issues. For instance, the corruption literature usually explores the case of a direct bribe between

economic and political actors (Bardhan, 1997; Kaufmann, 1997; La Porta et al., 1999; Schleifer & Vishny, 1993), without exploring the types of long-term inter-personal relationships such as those that JP Morgan sought to build in China.

This essay bridges this gap in the literature by looking at both economic and social aspects of political connectedness. Specifically, I look at the decision making processes by which local and expatriate managers in emerging countries come to define the boundaries between political connectedness and corruption. Thus, instead of trying to define an objective measure of when political connectedness turns into corruption, I aim to understand the way that decision makers themselves subjectively perceive, interpret, and respond to political connectedness in emerging countries:

> **Research Question 1:** How do expatriate managers in emerging countries make sense of political connectedness?
>
> **Research Question 2:** How does the way expatriate managers make sense of political connectedness affect firm strategy?

The conceptual framework that I develop to answer these questions, i.e. institutional sensemaking, explains the cognitive underpinnings of responses to political connectedness, thereby contributing to the institutional logics literature, which does not directly examine the cognitive mechanisms that link institutions with firm strategy. Moreover, the framework explains the institutional antecedents of sensemaking, thereby contributing to the managerial sensemaking literature, which does not take into account the impact of the wider social structures and beliefs on the cognitive processes occurring at the managerial-level.

This essay also has important practical implications because it will help managers be aware of distinction between their own preexisting knowledge systems, i.e. the

bureaucratic logic prevailing in their home countries, and the patrimonial logic prevailing in emerging countries. Consequently, managers can avoid biases both toward and against emerging countries, and better understand business phenomena in these countries. This will enable managers to develop appropriate strategic responses to the challenges they face in emerging countries, which will not only contribute to the economic performance of the multinationals they run, but also to that of the emerging countries in which they operate.

3.2 Literature Review

As explained earlier, there are two separate streams of research in international business related to political connectedness. On one hand, there is a literature that labels political connectedness as corruption or bribery (Cuervo-Cazurra, 2006; Meschi, 2009; Spencer & Gomez, 2011; Uhlenbruck et al., 2006). This research stream reflects a social perspective, and hence focuses on the legal and moral aspects of political connectedness. For example, Cuervo-Cazurra (2006) demonstrates that firms from countries with laws against bribery abroad are less likely to enter countries with high levels of corruption. Spencer & Gomez (2011) find that multinationals from countries with lower-levels of corruption engage in less bribery abroad. Uhlenbruck et al. (2006) show that multinationals are more likely to enter into joint ventures with local firms when they enter emerging markets with higher levels of corruption. Meschi (2009) documents that the more corrupt the host country is, the less likely multinationals are to terminate joint ventures with local firms. As these empirical findings show, this literature suggests that firms make sense of political connectedness as corruption and therefore try to avoid it.

On the other hand, there is a separate literature on political connectedness, which reflects an economic perspective. This literature thus focuses on the economic and relational aspects of political connectedness. Scholars in this literature use labels such as "political capital" (Yiu & Lau, 2008), "political embeddedness" (Sun et al., 2010), and "political networks" (Peng, 2003), to refer to the political connectedness phenomenon. Moreover, the empirical findings in this literature suggest that political connectedness is a source of competitive advantage in emerging markets. For example, Peng and Luo (2000) find political connectedness to be positively associated with firm performance in China, whereas Faccio (2006) shows that political connectedness increases firm value around the world. Similarly, Yiu & Lau (2008) demonstrate that political connectedness positively affects product and organizational innovation, as well as domestic and international venturing. Finally, Claessens et al. (2008) document that political connectedness increases stock returns in Brazil. Overall, this literature suggests that firms make sense of political connectedness as a source of competitive advantage, and therefore try to increase political connectedness.

As this review demonstrates, the international business literature concerning political connectedness portrays a black and white picture of political connectedness: Firms either make sense of political connectedness as corruption and avoid it, or make sense of political connectedness as strategy and they do it. In other words, the international business literature does not offer a complete picture of political connectedness, thereby failing to address the conflicting pressures that multinationals like JP Morgan face when they operate in countries such as China. This is because firm strategy, in the field of international business, has been generally explained based on

either techno-economic or institutional factors. In this regard, the techno-economic factors are emphasized by the economic perspective, which views firm strategy as a rational, interest-seeking response to incentives, whereas the institutional factors are stressed by the social perspective, which regards firm strategy as an irrational, endorsement-seeking response to legitimacy pressures. Despite the apparent contrasts between these two views, both presume that actors narrowly pursuit mechanical quests. Both consider firm strategy to be a function of exogenous, objective pressures, detached from firm's decision makers, who are actually the ones that formulate strategic responses (Dacin et al., 2002; George, Chattopadhyay, Sitkin, & Barden, 2006; Hambrick & Mason, 1984; Kennedy & Fiss, 2009; Nadkarni & Barr; 2008). According to those two views, firms are swept along by economic and institutional pressures, or in other words, run by them, not by people. Organizational decision makers, in this sense, are considered as nothing but faceless abstractions (Bettis & Prahalad, 1995). Thus, very little is known about how actors' sensemaking of the strategic issues affect their responses to them. In order to address these shortcomings in the international business literature, I draw on the managerial sensemaking literature (Daft & Weick, 1984; Kiesler & Sproull, 1982).

3.3 Theoretical Background

3.3.1 Managerial Sensemaking

The sensemaking literature suggests that organizational responses to environmental events are shaped by a sequential, tripartite cognitive process, consisting of *attention*, *interpretation*, and *action* (Daft & Weick, 1984; Kiesler & Sproull, 1982).

The first stage of the sensemaking process is attention, through which actors recognize and gather raw information about a new issue, or miss and ignore it altogether. Attention, in this sense, represents one's field of vision: information that falls outside this field goes unnoticed (Hambrick & Mason, 1984). Once an issue penetrates the filters (field of vision), however, the raw information is given meaning. This constitutes the interpretation stage, at which issues are framed or labeled. Then issues are categorized based on the labels attached to them (Dutton & Jackson, 1987). In this regard, two of the most salient labels or frames that are used for categorization are "threat" and "opportunity" (Dutton & Duncan, 1987; George et al., 2006; Thomas, Clark, & Gioia, 1993). Finally, action is the process in which those frames are acted upon and cause-effect relationships are put into practice (Daft & Weick, 1984). Decision makers who frame an issue differently generate a different set of action responses. For example, the sensemaking literature suggests that threat framing causes rigidity in decision making that restricts strategic repertoire, whereas opportunity framing promotes risk-taking that enhances it (George et al., 2006; Staw, Sandelands, & Dutton, 1981; Thomas et al., 1993).

Although the sensemaking literature has articulated the cognitive mechanisms that mediate responses to environmental issues and events (Daft & Weick, 1984; Hambrick & Mason, 1984; Nadkarni & Perez, 2007; Nadkarni et al., 2011), it has overlooked the impact of institutions on these cognitive mechanisms. In this sense, the sensemaking literature has typically adopted a decontextualized view of sensemaking, assuming that the tripartite cognitive process occurs independently of the environment (Barr, Stimpert, & Huff, 1992; Caproni et al., 1992; Chattopadhyay, Glick, & Huber, 2001; Daft,

Sormunen, & Parks, 1988; Garg, Walters, & Priem, 2003; Jackson & Dutton, 1988; Plambeck & Weber, 2009; Roth, 1995; Thomas et al., 1993) - although some exceptional studies have looked at the role of the industry or the cultural environment in shaping sensemaking (Barr & Glynn, 2004; Calori et al., 1994; Elenkov, 1997; May, Stewart, & Sweo, 2000; Nadkarni & Barr, 2008) -. As a result, the sensemaking literature has paid little attention to how organizational and managerial cognition is influenced by wider societal beliefs and structures (i.e. institutions at the macro level), and hence has overlooked the role of institutions as being the antecedent of individual and managerial cognition. In order to address this shortcoming of the managerial sensemaking literature, I draw on the institutional logics perspective (Thornton et al., 2012).

3.3.2 Institutional Sensemaking

Despite its contributions to our understanding of how institutions at the macro-level affect strategic action at the organizational and individual level, the institutional logics perspective has not elaborated on the cognitive mechanisms through which actors perceive, interpret, and act upon institutional prescriptions. Empirical studies drawing on the institutional logics perspective have only inferred such cognitive mechanisms, rather than directly examining them.

I address this void in the institutional logics literature by integrating the micro-level model of tripartite sensemaking with the cross-level model of institutional logics to develop a new conceptual framework, which I call institutional sensemaking. This framework explains 1) how institutional logics that firms and their decision makers learn and incorporate shape the way they make sense of the structures and common practices

that they face in emerging countries, and 2) how their sensemaking shapes their responses to those structures and common practices.

According to this framework, institutional logics enter the tripartite sensemaking process at the individual and organizational level as preexisting knowledge systems (Prahalad & Bettis, 1986), and affect all three stages. First, institutional logics shape attention (the type and amount of information actors gather about issues) by providing a set of implicit rules that regulate which issues, strategic contingencies, or problems become important. The meaning of an issue is not inherent in this raw information, however. Information is subsequently interpreted and infused with meanings (Dutton & Jackson, 1987). Therefore, it is neither the issue itself, nor the information gathered about the issue, but the interpreted information (the meanings attached to the issue), that shapes how the issues is acted upon. In this sense, Bettis and Prahalad (1995) distinguish raw information from appropriate actionable knowledge: A flood of information has no value if actors cannot appropriately interpret and act upon it. In this regard, logics provide frames such as threat and opportunity through which meaning is imposed on the information gathered about a strategic issue (Kennedy & Fiss, 2009). Third, logics affect action by providing range and type of behavior alternatives that can be conceived of, and that are considered appropriate (Thornton, 2004). When logics are socially shared and acted upon by the majority of society, the material aspects of institutions, i.e. structures and common practices come about. Institutional logics thus constitute the symbolic/cognitive foundation of the structures and common practices in a society.

3.4 Deconstructing the international business literature on political connectedness by using the institutional sensemaking framework

A careful reading of the international business literature related to political connectedness through the lens of institutional sensemaking reveals that the two separate research streams discussed earlier actually embody opposing logics. On one hand, the literature on corruption embodies bureaucratic logic. Under this logic, managerial attention will be directed to the legal and moral aspects of political connectedness. Therefore, managers will frame political connectedness as a threat, and hence will seek to avoid political connectedness. On the other hand, the literature on political connectedness embodies patrimonial logic. Under this logic, managerial attention will be directed to the economic and relational aspects of political connectedness. Therefore, managers will frame political connectedness as an opportunity, and hence will seek to increase political connectedness. In short, the deconstruction of these two literatures show how the two dissimilar logics differently shape the way managers make sense of and respond to political connectedness, as shown in Table 3.1. This theorization is also illustrated by the model of institutional sensemaking of political connectedness in Table 3.2 and Figure 3.3.

As the model of institutional sensemaking of political connectedness is based on the deconstruction the extant literature, however, it is limited by it. In other words, the model still portrays a black and white picture of political connectedness: managers make sense of political connectedness either as a threat and avoid it, or as an opportunity and do it. Such an either or neither nor sensemaking and response arising from two dissimilar logics fails to offer a complete explanation of political connectedness.

Sensemaking scholars, however, have highlighted the importance of cognitive complexity for addressing multiple conflicting pressures (Caproni et al., 1992; Calori et al., 1994; Nadkarni & Perez, 2007). Cognitive complexity is defined as the degree of differentiation and integration within a cognitive structure (Bartunek , Gordon, & Weathersby, 1983). In other words, it reflects the breadth and depth of the knowledge embedded in it (Calori et al., 1994). Differentiation represents the ability to perceive several dimensions in a stimulus array, whereas integration corresponds to the development of complex connections among the differentiated characteristics. In this regard, managers high in integration and low in differentiation are able to make use of the concepts in their cognitive structures simultaneously to make sense of a stimulus, however, they will find it hard to adopt multiple perspectives to that stimulus, as the number of concepts they can accommodate is limited. The implication is that managers high in integration but low in differentiation lack the variability and flexibility to learn dissimilar logics. On the other hand, managers high in differentiation and low in integration can hold several perspectives simultaneously, but fail to combine them to have a better understanding of the stimulus. Although such managers have the ability to adopt multiple perspectives, they lack the cognitive capabilities to link these perspectives with each other. The implication is that managers high in differentiation but low in integration lack the coherence to blend dissimilar logics.

The extant literature on cognitive complexity, however, shows that managers with cognitive complexity are high in both dimensions, possessing the cognitive capability to simultaneously hold and apply several competing and complementary interpretations of situations and events (Bartunek et al., 1983). Since these decision-makers can both

accommodate more concepts in their cognitive structures and link these concepts with each other, they can understand issues from multiple perspectives, and can simultaneously synthesize these perspectives to form a holistic view. The implication is that managers with cognitive complexity can learn dissimilar logics and blend these logics with each other.

In order to further our understanding of the interplay among institutional sensemaking, cognitive complexity, and political connectedness, a field research was conducted in China. The methodology used in this field research and the insights gained into the political connectedness phenomenon in China are explained below.

3.5 Methodology

3.5.1 Sample

As part of the field research, I interviewed fourteen expatriate managers in China. The interviews took place between August and October 2015. Of the fourteen expatriate managers, two were American, two were Canadian, two were Australian, one was British, one was German, one was Singaporean, and one was Japanese. Thus, all the expatriate managers were from countries where bureaucratic logic is prevalent (Fukuyama, 1995; Fukuyama, 2001; Fukuyama, 2011). Five expatriates were mid-level managers, whereas the rest of them either owned businesses in China or were the country managers of some American and Canadian multinationals. Three expatriate managers were based in Beijing, while all the others were based in Shanghai. The firms which expatriate managers worked for operated in a variety of industries, ranging from medical

device wholesale trade and consulting to logistics and commercial photography, thereby reducing the risk that my findings may be specific to certain industries or sectors.

I obtained access to the expatriate managers mostly by attending the American Chamber of Commerce events in Shanghai. Only the Australian and Singaporean participants, as well as one American participant, were accessed through existing personal connections. As is typical of this type of qualitative research, the resultant sample is neither totally random, nor is complete (McCracken, 1988; Witt & Redding, 2009).

3.5.2 Interviews

I obtained data from my sample of managers through in depth, semi-structured interviews, in which I used a scenario as a stimulus material to prompt participants to talk about such a sensitive topic as political connectedness. This is a common method used in ethnographic research (McCracken, 1988). Although the scenario was fictional, it was based on JP Morgan's hiring practices in China. The scenario is as follows:

> "Bob, the executive of the ABC company, hires a young college graduate named Xiaoqiang, who is qualified for the position. However, Bob chooses Xiaoqiang over more qualified candidates because Xiaoqiang's father is a senior government official. Some time after the hiring, Xiaoqiang's father takes charge of a government contract, in which the ABC company is one of the bidders. Xiaoqiang's father awards the contract to the ABC company, despite receiving more competitive bids from the ABC's rivals."

I gave this scenario to the participants and asked them to evaluate the practices described in it. This method allowed the participants to distance themselves from the characters and their behavior stated in the scenario. Thus, although the participants did

not have to share their personal experiences with me, they revealed their personal opinions about political connectedness when they evaluated the scenario.

3.5.3 Data

The interviews were all audio-recorded and transcribed. All the interviews were conducted in English and were transcribed by myself. It was these transcribed interview texts that comprised the data for eliciting managerial sensemaking.

In order to measure managerial sensemaking, I content analyzed the transcribed interview texts by using NVivo software. The content analysis involved coding the phrases and sentences that manifest attention focus and framing of political connectedness based on the model of institutional sensemaking of political connectedness. Thus, texts that manifest an attention focus on the legal and moral aspects of political connectedness were coded under a separate node from those that reflect an attention focus on the economic and relational aspects. Similarly, texts that manifest a threat framing of political connectedness were coded under a separate node from those that reflect an opportunity framing. Table 3.4 shows the sample sentences used for coding.

3.6 Content Analysis

Attention focus on legal and moral aspects of political connectedness were not coded independently, because the participants most of the time did not separate the two in the interviews. Legal remarks were usually followed by moral remarks, and vice versa. In this sense, legal and moral dimensions were intertwined: What is legally wrong was also

considered to be also morally wrong by the participants, which led to the negative framing of political connectedness. This in turn generated the intention to avoid political connectedness.

> "I am the legal rep of my company. If anything goes wrong in my company they can throw me in the jail or send me back to Canada. So if you are the legal rep, the legal rep is responsible for whatever the people do. The expat that was a legal rep for …, a big mining company, he is now in prison here. Two years ago he was convicted for paying bribes and he is Australian, but originally from China, Chinese-Australian, he is now prison. He was the legal rep. The more they prosecute I think it will help but it still goes on because everybody says I am not going to get caught." (Expatriate manager G)

As can be seen in this excerpt of the interview, the Canadian manager directs his attention to the legal dimension. He particularly emphasizes the role of punitive laws in anti-corruption efforts by showing some potential legal consequences for receiving bribes. At this point, he clearly labels political connectedness as bribery, and hence frames it in negative terms. This was a common pattern among the expatriate participants: Attention to the legal aspects leads the managers to label political connectedness as corruption, and to frame it as a threat. As a result, they intend to avoid political connectedness. Here is another example:

> "You cannot really promise something or offer something or receive anything that shows you get a financial benefit other than just the contract that you have. We cannot do anything like that. And if we were in a partnership with a firm here, and they did it, that is ground for breaking the contract. We cannot do that. We just cannot afford to do that. They are very strict here in China about corruption. They put people in jail here." (Expatriate manager F)

Attention to the moral dimension similarly leads the participants to refer to political connectedness as corruption or bribery and to frame it in negative terms. As

another Canadian manager based in Shanghai puts it, hiring employees based on their political connections is morally wrong and hence should be avoided:

> "This is unethical [hiring Xiaoqiang], especially for a multinational company. Because we should hire people not based on their relationships or family backgrounds, but we should hire people based on their competence, or on their knowledge of the product." (Expatriate manager H)

As can be seen, attention focus on the principle that people should be hired based on their qualifications leads to the perception that political connectedness is immoral. In fact, the same country manager equates hiring politically connected employees to giving bribes, which he says is very common in the healthcare industry, where his company operates. In this regard, he frames political connectedness as a threat not only to his company, but also to social welfare. This leads to the conclusion that political connectedness is something that should not only be avoided, but also be fought against:

> "…we should do the right thing in this country, and provide a very good service to the patient. Because if corruption happens, the patient will get a very expensive product, which is not worth it. Because some part of the price or profit will go to some people's pockets, which is not good. So if everything is clean, transparent, then the patient can enjoy the lowest price, and the doctor will also not have any trouble using your product. The companies will also be happy because they can provide the best service directly to the patient without having to pay money to doctors, which is illegal. So companies will also be happy. Everyone will be happy. The government will be happy, so why don't we do that? We should clean this market. We should do the right thing so that the patient can enjoy a very good product and they can have a better life in China." (Expatriate manager H)

Economic and relational aspects of political connectedness, similar to the legal and moral aspects, were often not seen as independent from each other by the participants. Participants suggested either that political connectedness brings benefits only when a personal relationship is involved, or that when there is a personal

relationship with a government official then there will be benefits. Because economic and relational aspects were intertwined, just like legal and moral aspects, they were not coded separately.

> "…you see very clearly that Chinese companies or multinationals that develop stronger kind of personal relationships with government officials are often going to win projects at a much higher rate than other companies. In my previous job, I would sometimes submit bids for various projects, and regardless of how qualified our bid was, we never won because we often did not have the right government connections." (Expatriate manager A)

This expatriate manager thus sees a positive association between networks with government officials and business outcomes. In this respect, she focuses his attention to the economic and relational aspects of political connectedness, which leads him to frame political connectedness as an opportunity. As a result, she suggests companies should hire people like Xiaoqiang if they want to operate in China. This is a clear manifestation of patrimonial logic. Overall, the content analysis of the interviews provides support for the model of institutional sensemaking of political connectedness.

3.7 Blending dissimilar logics of firm-government interaction

The field research suggests that patrimonial logic has a strong presence in China. Expatriate managers consistently said in the interviews that the practice of hiring politically connected people to win business is commonplace in China, and that most companies have well-connected employees.

As a result, most of the expatriate managers have come to think that political connectedness is essential in for companies to operate in China, and they do not consider it necessarily as corruption. In other words, most of the expatriate managers have learned

patrimonial logic: They have begun to focus their attention more on the economic and relational aspects of political connectedness, and hence to frame it as an opportunity. In this respect, an expatriate manager thought that it was normal for candidates' political connections to be considered as a factor in hiring decisions. He did not perceive it as corruption.

> "It is the same in everything. You want to go to see a concert and if you know someone you have got cheaper tickets, everything is like that in China. The government, every little thing. Just the way the country works. And it is the way the country has worked for a thousand years. And once you know, once you understand that, and you realize that nothing is black and white and anything is possible as long as you know the right people…" (Expatriate manager K)

Similarly, another expatriate manager acknowledges that connections in the Chinese government design institutes may play a role when he hires Chinese salespeople for his clients. In fact, he sometimes asks candidates about their political connections during job interviews:

> "…we have talked about relationships with [Chinese government design] institutes and things like that. Because you need to go in present your technology, they need to at least endorse it, like it, and say it is alright for Chinese companies to use us. In a case like that, that could factor to our decisions. All else being equal, somebody with a good network within the Chinese design institutes for a certain industry might have advantages over the other candidate that we were considering." (Expatriate manager E)

Thus, expatriates have learned patrimonial logic while in China and have come to see political connectedness as a necessary component of their operations in China rather than a corrupt practice. Yet, they have not totally adopted patrimonial logic either. They instead integrate the bureaucratic logic of their home country with the patrimonial logic of their host country to develop a hybrid logic. In other words, expatriates have come to find a middle ground. As an expatriate manager puts it:

> "Since we are in the middle, we try to find a balance between the two worlds, a balance point that works for both sides…As a company that represents American companies, and also as American we cannot give cash gifts but we can still show respect, we can still maybe entertain them a little bit taking them to dinner and give face, and try to appease them and befriend them in the Chinese way, without crossing the limits that are placed upon us because we are dealing with an American company and we are an American company, you understand? So we have to operate in kind of within two worlds. There is overlap, there are certain things you cannot do as an American company, there certain things they expect as a Chinese company, but we cannot always give it to them. But there are other things this is good in China and it is OK for us to do that as an American company so we are able to find that middle ground in a very Chinese way, give them respect and convince them that this is in their best interest, and give them face and whatever and get them to ally." (Expatriate manager E)

Thus, unlike the black and white picture portrayed by the literature, expatriate managers in China operate in a gray area. They avoid the black area, i.e. patrimonial logic, in which the practices are blatantly illegal and blatantly immoral in their home countries. In this sense, expatriate managers direct their attention to the legal and moral aspects of political connectedness. Yet, they are not committed to be in the white area either. This is because they at the same time want to be able to operate and perform well in their host country, which is not possible without political connectedness. In this sense, they also direct their attention to the economic and relational aspects of political connectedness. This leads them to frame political connectedness in both negative and positive terms. Thus, although they do not consider political connectedness necessarily as corruption, they think it can turn into corruption. In other words, they draw a boundary that separates between political connectedness and corruption, or between good political ties and bad political ties. In this regard, it is important to know how they draw this boundary, or the boundaries of the gray area shown in Figure 3.4.

The content analysis of interviews suggests that two factors affect how the expatriate managers distinguish political connectedness from corruption: 1) The intent to build and use political ties, and 2) The way these ties are utilized. As for the former, if the intent is to gain access, or to open doors, then political connectedness is not considered corruption. If the intent, however, is to gain an influence to get an unfair advantage, then political connectedness becomes illegal and immoral. As for the second factor, i.e. the way political ties are utilized, if exchange of favors between firms and governments occurs naturally, as part of a personal relationship, expatriate managers do not consider political connectedness as corruption. If the exchange of favors, however, occurs as part of a transactional relationship, then expatriate managers view political connectedness as both illegal and immoral:

> "As long as nothing was agreed to, either favors exchanged or promises of future contracts, then no, I would not see it as any problem if hiring him. In fact, I would see as part of his qualifications the fact that his dad IS a government official. Because he would say good things about our company at dinner, and that would be a good thing for us, and very influential. I would think it was **wrong** though if the dad asked us to hire his son and we agreed and we later came back to the dad, and were trying to a get a favor returned to us. That is very common practice in China called guanxi. And also I would think it was **wrong** if the dad hired us to work on a government project, and then his son got a commission or a kickback, or some kind of boost in salary because of that. That is also very common in China and that would be wrong. That would be **illegal** in the USA and **wrong** in the USA. If the son was not qualified for the job, and we hired him anyway, again I would think that is **wrong**. But again, that happens all the time in China." (Expatriate manager B)

Similar to this, the country manager of a Canadian multinational in Shanghai distinguishes using political connectedness to gain access from corruption or bribery. According to him, there is nothing wrong with the former:

> "It is normal to hire somebody who is very well-connected. But, why do you want those connections? You want those connections to help you do

> some business or to get some access, but you have to do that without giving bribes." (Expatriate manager G)

3.8 Conclusion

In this essay, I addressed two research questions: 1) How do expatriate managers in emerging countries make sense of political connectedness?, and 2) how does the way expatriate managers make sense of political connectedness affect firm strategy? To answer these questions, I combined the institutional logics and tripartite sensemaking frameworks, and developed the model of institutional sensemaking. This model explained how different logics differently shaped the way local and expatriate managers make sense of political connectedness in emerging countries. More specifically, I argued that bureaucratic logic directs managerial attention to legal and moral aspects of political connectedness. As a result, managers frame political connectedness as a threat, and seek to avoid political connectedness. On the other hand, patrimonial logic directs managerial attention to economic and relational aspects of political connectedness. As a result, managers frame political connectedness as an opportunity, and seek to increase political connectedness.

In order to apply and further the model of institutional sensemaking of political connectedness, I conducted field research in China and interviewed 14 expatriate managers. The insights gained from this field research provided support for the framework. The research also demonstrated that expatriate managers blend the bureaucratic logic of their home country with the patrimonial logic of their host country logic to make sense of political connectedness. Under this hybrid logic, expatriates make sense of political connectedness as a double edged sword: They focus their attention both

on legal/moral and economic/relational aspects of political connectedness, and they frame it as both opportunity and threat. As a result, they distinguish political connectedness from corruption: They separate legitimate political ties from illegitimate political ties, and while they try to increase the former, they seek to avoid the latter.

3.9 Discussion

This research provides unique insights into the political connectedness phenomenon in China. As opposed to the clear distinction made by the literature between the two dissimilar logics of firm-government interaction, the field research demonstrates that expatriates in China can learn patrimonial logic prevalent in their host country and blend it with the bureaucratic logic prevalent in their home country. The consequent hybrid logic directs their attention to both legal/moral and economic/relational aspects of political connectedness. This in turn leads to the framing of political connectedness simultaneously as a threat and an opportunity. As a result, expatriates in China can make more fine-grained distinctions between political connectedness and corruption, forging political ties that help them to operate more effectively in their host country without violating the legal and ethical norms in their home countries.

This study shows the importance of managerial sensemaking in studying multinationals responses to institutional complexity. Kostova and Zaheer (1999), in this regard, provided a model that explains how multinationals operating in complex environments respond to the conflicting institutional logics they face. Although Kostova and Zaheer primarily focused on the objective characteristics of the institutional environment and of the organization, this study documents that organizational responses

to institutional pressures depend on managers' subjective interpretations. Similarly, international business scholars have extensively studied whether multinationals from developed countries conform to or challenge the dissimilar logics they face in emerging countries (Bailey & Spicer, 2007; Hillman & Wan, 2005; Kostova & Roth, 2002; Peng, 2003; Spicer, McDermott, & Kogut, 2000). This study explains why there is diversity of organizational responses to the institutions in emerging countries, as well as why the issue at hand is more complicated than an either or, neither nor choice. By having a finer-grained understanding of the differences between dissimilar logics, organizations' decision makers can view strategic issues both as a threat and an opportunity, thereby managing to carve out a middle ground in the face of the conflicting pressures they encounter while they operate in emerging countries.

Sensemaking scholars are increasingly interested in the phenomenon of cognitive complexity (Calori et al., 1994; McNamara, Luce, & Tompson, 2002; Nadkarni & Perez, 2007; Nadkarni et al., 2011; Plambeck & Weber, 2010). This study shows that cognitive complexity explains the role of the cognitive competence of the managers in organizational coping with different institutional environments (Calori et al., 1994; Nadkarni & Perez, 2007; Nadkarni et al., 2011). In this regard, managers with cognitive complexity are not only able to learn and incorporate dissimilar logics, but they are also able to integrate these logics and blend them with each other. Studying the complexity of the cognitive structures of the managers can thus provide fresh insights into they make sense of and respond to political connectedness in emerging countries. In this regard, expatriate managers with more complex cognitive structures will probably be more likely to learn the patrimonial logic in their host country, and integrate it with the bureaucratic

logic they learned in their home country. Therefore, cognitive complexity will enable managers to have a better understanding of political connectedness, and will provide with them more strategic alternatives than an either or choice between avoiding and engaging in political connectedness. Future research should focus on the relationship between cognitive complexity/simplicity and responses to dissimilar logics in emerging countries.

3.9.1 Contributions to institutional research in international business

"*Ten years ago when GE senior managers discussed the global marketplace, they talked about the U.S., Europe, Japan, and the rest of the world…Now the 'rest of world' means the U.S., Europe, and Japan*". (Immelt, Govindarajan, & Trimbleet, 2009: 59)

This quote, which is taken from an article co-authored by Jeffrey R. Immelt, the chief executive officer (CEO) of General Electric, illustrates the general understanding emerging among both practitioners and scholars that the future of international business lies in emerging countries. In fact, double-digit economic growth is currently an emerging country phenomenon and in the past year, for the first time in history, foreign direct investment flows were greater to developing economies than developed economies. Emerging countries are estimated to contribute to the global economic growth more than developed countries (the former 57% as opposed to the latter 43%) during 2010-2020 (Accenture, 2012), while their multinationals have already begun to outgrow and outperform their developed country peers (Boston Consulting Group, 2011).

As emerging countries and their firms grow and become integrated to the rest of the world, however, their institutions remain fundamentally dissimilar to those of developed countries (Jackson & Deeg, 2008; Peng,Wang, & Jiang, 2008). This makes the

impact of emerging country institutions on international business outcomes conspicuous (Peng et al., 2008), and increases the need to understand the institutions in emerging countries. Consequently, emerging countries and their institutions now preoccupy both international business practitioners and scholars (Jackson & Deeg, 2008; Immelt et al., 2009; Kostova et al., 2008; Peng et al., 2009). In fact, the impact of institutions in emerging countries on business practices and strategy have been the main driving force behind the development of the field of international business in the last decade (Peng et al., 2008).

Despite the considerable advances to date, two factors have inhibited progress in our understanding of the relationship between emerging country institutions and international business outcomes. First, institutions have been generally treated as exogenous regulative, normative, and cultural constraints that determine the behavior of individuals and organizations. In this regard, studies on the interior cognitive that explain how actors make sense of and respond to the external constraints, have been rare. Consequently, international business scholars have not been able to address how multinationals' and their decision makers' evaluations of, and hence responses to, emerging country institutions vary. Second, instead of understanding the emerging country phenomena in its local form, scholars have superimposed their pre-existing theoretical tools (which were originally developed to explain the relationship between institutions and business outcomes in Western contexts) on emerging country contexts (Tsui, 2007; Whetten, 2009). In this sense, institutional differences across countries have been regarded as differences in degree, rather than differences in kind (Jackson & Deeg, 2008). As a result, Western market-oriented institutions are taken as the norm, and the

emerging country institutions that diverge from this ‘norm’ are implicitly or explicitly attached negative labels such as deviant, inferior, inefficient, etc. The outcome is that international business scholars have been preoccupied with objectively measuring the distance between two countries, as well as the impact of the costs associated with this distance on multinationals, which is known as liability of foreignness. As a result, the attempts in the field to formulate predictions with respect to how multinationals and their decision makers develop appropriate responses to emerging country institutions, and successfully navigate through these environments, have been rare.

This essay addresses these voids in the international business literature by providing a fresh perspective in studying such a prevalent emerging country phenomenon as political connectedness. Drawing from the institutional logics approach, my dissertation demonstrates that patrimonial logic and bureaucratic logic do not necessarily represent fundamentally dissimilar rules according to which the game is played, but they are rather guidelines that help actors to successfully play games that are fundamentally dissimilar. Therefore, the more firms’ decision makers understand the patrimonial logic prevailing in emerging countries - besides the bureaucratic logic prevailing in their home countries -, the better they get at playing the dissimilar game in emerging countries, and hence the less liability of foreignness they face.

Table 3.1: Two perspectives on political connectedness

	Political Connectedness as <u>Corruption</u>	**Political Connectedness as <u>Strategy</u>**
Definition	"Abuse of public power for private gain"	"Managers' personal ties with government officials" (Peng & Luo, 2000)
Goal	Social endorsement, legitimacy	Economic performance, competitive advantage
Labeling of political connectedness	Corruption Bribery	"Political networks" (Peng, 2003) "Political ties" (Li, Zhou, & Shao, 2009) "Political capital" (Yiu & Lau, 2008)
Framing of political connectedness	"Threat" to legitimacy	"Opportunity" to gain competitive advantage
General firm strategy	Compliance, isomorphism	Acquisition of non-market capabilities
Specific firm strategy	Avoid political connectedness	Increase political connectedness

Table 3.2: Institutional sensemaking of political connectedness

	Literature on Corruption	**Literature on Political Connectedness**
Logic	Bureaucratic logic	Patrimonial logic
Attention	Compliance Legal and moral aspects	Performance Economic and relational aspects
Interpretation	“Threat” to legitimacy	“Opportunity” to gain economic benefits
Strategy	Avoid political connectedness	Increase political connectedness

Table 3.3: Sample of expatriate managers by location, industry, and nationality

Identity	Location	Industry	Nationality
Expatriate manager A	Beijing	Business consulting	American
Expatriate manager B	Shanghai	Commercial photography	American
Expatriate manager C	Shanghai	Textile	American
Expatriate manager D	Shanghai	Automobile wholesale trade	American
Expatriate manager E	Shanghai	Business consulting	American
Expatriate manager F	Shanghai	Architectural consulting	American
Expatriate manager G	Shanghai	Business association	Canadian
Expatriate manager H	Shanghai	Medical equipment wholesale	Canadian
Expatriate manager I	Beijing	Investment consulting	Australian
Expatriate manager J	Beijing	Retail e-commerce	Australian
Expatriate manager K	Shanghai	Entertainment	British
Expatriate manager L	Shanghai	Logistics	German
Expatriate manager M	Shanghai	Translation services	Japanese
Expatriate manager N	Beijing	Legal consulting	Singaporean

Table 3.4: Sample sentences used for coding

Attention focus	Interpretation
Legal and moral aspects	**Threat framing**
"…the first thing it goes against most countries' Foreign Corrupt Practices Act, it goes against my country's, it goes against the US's. So we know that kind of behavior is unethical, and immoral." - Expatriate manager J	"…This [political connectedness] is just temporary. You see in China the government changes a lot. One day you are still the Mayor, but maybe the next day you get arrested, you never know." - Expatriate manager C
Economic and relational aspects	**Opportunity framing**
"…helping [government officials] means that you are more likely to get favors in return. Access to markets. They are [hiring people like Xiaoqiang] because of access to markets." - Expatriate manager I	"The more connections you have with the government, the better." - Expatriate manager M

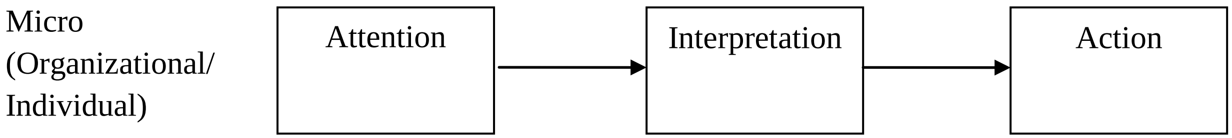

Figure 3.1: Micro-level model of sensemaking, adapted from Daft & Weick (1984)

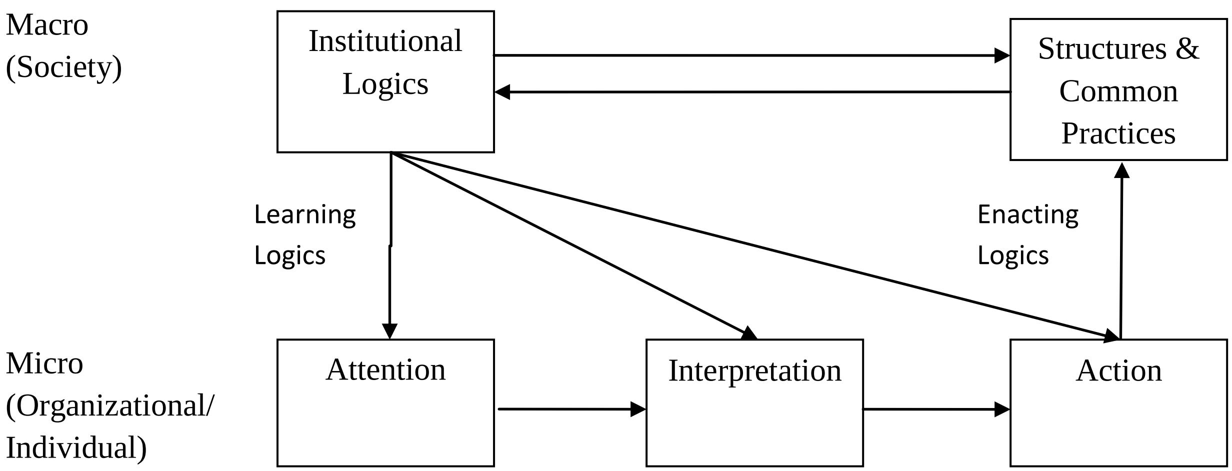

Figure 3.2: Cross-level model of institutional sensemaking

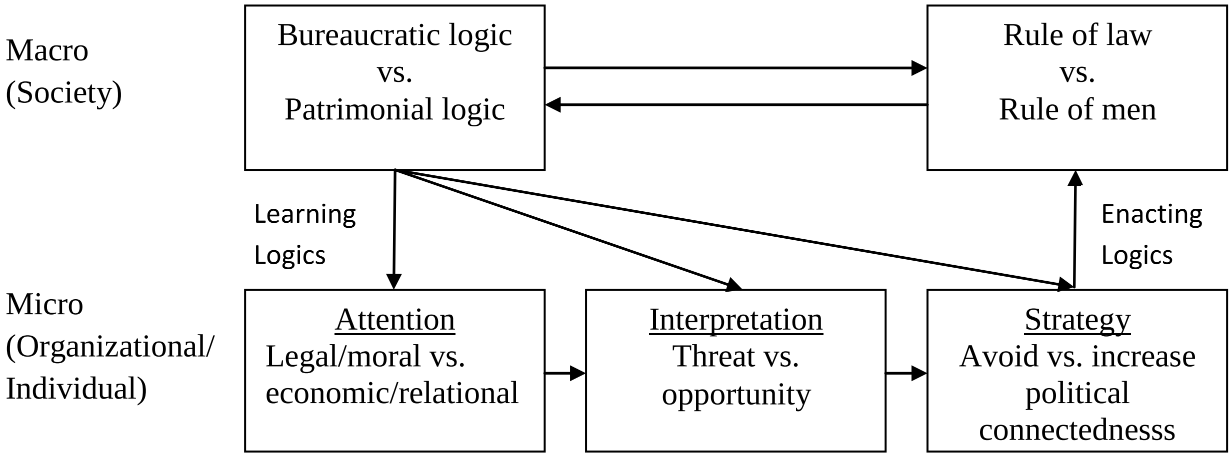

Figure 3.3: Model of institutional sensemaking of political connectedness

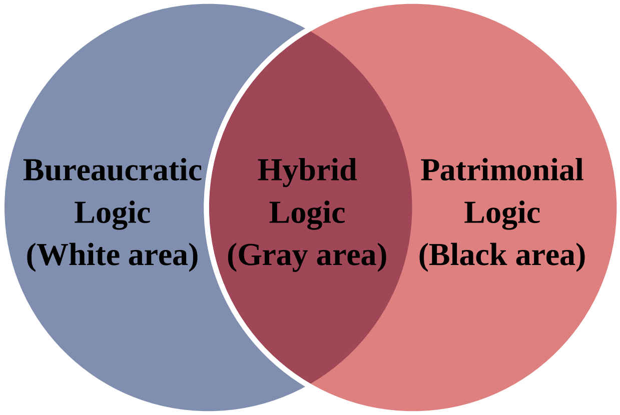

Figure 3.4: Blend of patrimonial logic and bureaucratic logic

CHAPTER 4

INSTITUTIONAL LOGICS, MANAGERIAL SENSEMAKING, AND INTERNATIONALIZATION STRATEGY: MANAGERIAL ATTENTION AS THE COGNITIVE UNDERPINNING OF FIRM'S STRATEGIC RESPONSES TO DISSIMILAR INSTITUTIONAL LOGICS OF FIRM-GOVERNMENT INTERACTION

When a firm is domestic, its operations are contained within a single home country, and therefore it is subject to relatively homogeneous pressures from the institutional environment (Nadkarni, Herrman, & Perez, 2011; Roth & Morrison, 1992). If the firm's operations transcend its home country, however, then it faces complex and diverse institutional pressures, unlike those found in the home country. Multinationals, in this sense, operate in an environment characterized by complexity, ambiguity, and equivocality (Kostova et al., 2008). Therefore, top management of multinationals has the critical task to provide meaningful interpretations for patterns of ambiguous information they receive (Thomas et al., 1993). Consequently, the imposition of meaning on complex and ambiguous strategic issues by managers, in other words, managerial sensemaking, have come to the forefront of internationalization strategy (Caproni, Lenway, & Murtha, 1992; George et al., 2006; Nadkarni & Perez, 2007).

The role of managerial sensemaking becomes particularly paramount where competition in emerging countries is considered (Dhanaraj & Khanna, 2011; George et al., 2006; Peng, 2003). These countries lack the bureaucratic logic that Western

businesses typically rely upon, such as the formal regulatory and legal frameworks that encourage predictable patterns of behavior (Tracey & Phillips, 2011). As a result, the "rules of the game" are not known, or constantly changing in these countries (Peng, Wang, & Jiang, 2008), which creates a great deal of uncertainty for the decision-makers of firms (Spicer et al., 2000). The absence or weakness of bureaucratic logic that makes and enforces the rules of market competition is known as institutional voids in the international business literature (Khanna & Palepu, 1997). It has been argued that the way managers make sense of these voids determines whether they recognize and try to work around them, or they overlook and seek to avoid them (Dhanaraj & Khanna, 2011; George et al., 2006).

In this regard, previous research on the relationship between institutional differences and internationalization strategy has demonstrated that when firms from developed countries in which bureaucratic logic is prevalent enter into emerging countries in which patrimonial logic is prevalent, they face an institutional environment that requires different strategies and capabilities to compete. This situation represents a hazard, and might lead these firms to avoid, or at least to reduce commitment in emerging countries (Henisz & Delios, 2001; Feinberg & Gupta, 2009; Phillips et al., 2009; Yiu & Makino, 2002; Xu & Shenkar, 2002). In this study, I extend this literature by drawing on the institutional research that emphasizes the socio-psychological foundations of institutional processes (George et al., 2006; Kennedy & Fiss, 2009). I argue that the strategic responses of developed country firms to institutional differences are not based on objective evaluations, but are rather based on how their decision-makers perceive, interpret, and act upon them (Dacin, Goodstein, & Scott, 2002). Specifically, I focus on

attention as the cognitive process through which managers of developed country firms make sense of dissimilar institutional logics. The literature shows that attention patterns of managers influence firm's strategic responses by shaping the way managers notice and make sense of their environment (Cho & Hambrick, 2006; Levy, 2005; Nadkarni & Perez, 2007). Drawing on this, I argue that multinationals are more likely to expand into 1) emerging countries when their top management pays more attention to the institutional environment; 2) developed countries when their top management pays more attention to the market environment. Those who direct their attention more towards the institutional environment will be are more likely to develop the strategies and capabilities required by patrimonial logic. In other words, these managers have better cognitive capabilities to comprehend the "rules of the game" (North, 1990: 3), and "sense and seize opportunities" (Teece, 2007: 1341) in emerging countries. Those whose attention is limited to the narrow market environment, however, are less likely to develop the strategies and capabilities required by patrimonial logic. When they face an institutional system in which patrimonial logic is prevalent, they are more likely to see threats, rather than an opportunities (Dhanaraj & Khanna, 2011), and hence are less likely to "play the game" in emerging countries.

This paper's approach to internationalization strategy has two theoretical implications. First, it contributes to the international management literature that focuses on the institutional similarities/differences between home and host countries as the main determinant of internationalization strategy (Berry, Guillen, & Zhou, 2010; Phillips et al., 2009; Xu & Shenkar, 2002). By examining the cognitive underpinning of internationalization strategy, I explain why firms, despite being embedded in the same

institutional environment and being subject to the same institutional pressures, take different strategic actions. I argue that internationalization is not just an automatic response to objectively measurable institutional differences, but is rather a consequence of how the decision makers of firms make sense of these institutional differences. Which issues managers give priority to, or focus their attention on, influences the way they interpret institutional differences, and this in turn influences the strategic actions they take. From this perspective, internationalization can be seen as much a question of strategic decision making as of institutional processes.

Second, this paper contributes to the institutional theory by highlighting the cognitive underpinnings of strategic responses to institutional logics. Despite being the socio-psychological foundation that institutions rest on (DiMaggio, 1997; Meyer & Rowan, 1977; Powell & Colyvas, 2008; Zucker, 1983), cognition has for the most part eluded institutional researchers (DiMaggio & Powell, 1991). The general tendency in institutional research has rather been to make self-serving attributions to cognition by looking merely at the organizational outcomes (Scott, 2008). This study, on the other hand, involves a direct examination of managerial cognition through the measurement of attention patterns, which can be seen as a step towards revealing the micro-foundations of institutions (DiMaggio & Powell, 1991).

4.1 Internationalization as a strategic response to dissimilar institutional logics

Research in international management has extensively studied the impact of institutional differences on country choice strategy. An important finding of this literature is that institutional differences between home and host countries make

internationalization less likely (Berry et al., 2010; Cuervo-Cazurra & Genc, 2008; Henisz & Delios, 2001). From an institutional theory perspective, this can be explained by the legitimacy issue. In this regard, institutional differences between two countries affect internationalization success by posing legitimacy challenges for the multinational (Hillman & Wan, 2005; Kostova & Zaheer, 1999; Lu & Xu, 2006). Especially a large institutional distance severely diminishes multinational's odds for growth and survival in the host country, and consequently deters it from investing in that country:

> "…Firms will refrain from investing in markets that are institutionally distant, because business activities in those markets require conformity to institutional rules and norms that conflict with those of the home country." (Xu & Shenkar, 2002: 614)

Where internationalization from developed countries into emerging countries is considered, as is the case in this study, the dissimilar patrimonial logic prevalent in emerging countries have the same effect as large institutional distance does (Phillips et al., 2009). In this sense, firms from developed countries intrinsically employ market strategies and market capabilities to compete in rule-based, stable environments supported by bureaucratic logic (Peng, 2003; Wan, 2005). Emerging countries, on the other hand, are characterized by uncertainty caused by weak bureaucratic logic (Spicer et al., 2000). This prevents developed country firms from pursuing market strategies and taking advantage of their market capabilities (Henisz, 2003). Patrimonial logic in these countries thus requires firms to employ strategies to manage the institutional environment rather than the market environment. However, many firms in developed countries are not equipped with the skills, knowledge, and mindsets required to pursuit these strategies (Dhanaraj & Khanna, 2011). The incapacity to address institutional differences thus poses significant challenges to developed country multinationals.

This argument has been supported by previous research, which demonstrates that developed country firms tend to respond to patrimonial logic by avoiding entry into emerging countries (Cuervo-Cazurra & Genc, 2008; Feinberg & Gupta, 2009; Henisz & Delios, 2001). These firms rather expand into other developed countries with similar institutional environments, which enable them to utilize their market capabilities. Despite providing useful insights into firm internationalization, this institutional account of internationalization fails to address the mechanisms through which institutional differences cause strategic responses. This is a "deficiency" in institutional theory that scholars still attempt to mitigate in current institutional work (Scott, 2008). As explained earlier, a direct examination of the cognitive processes that mediate between institutions and strategic responses is needed to address this gap, which is the primary objective of this study.

Furthermore, strategic response approach to internationalization has traditionally focused on organizations and has neglected managers' role in formulating organizations' strategic responses. This issue has recently started to receive attention from institutional scholars as current work in institutional theory is reconciling with the old institutionalist perspective (Selznick, 1957). As a result, managers come to be regarded as the actual bearers of the shared understandings within the organization (DiMaggio & Powell, 1991; Hirsch & Lounsbury, 1997). The implication is that how organizations "think" becomes a matter of how their key decision-makers "think" (Kennedy & Fiss, 2009), and this is what ultimately shapes organizational responses.

Moreover, firms that internationalize their operations typically operate under the jurisdiction of a diverse set of institutions, including dissimilar national environments that

are composed of multiple and -as in the case of emerging countries- emerging organizational fields. This environment poses a sharp contrast to the highly structured environment that is assumed by institutional theory (DiMaggio & Powell, 1983; Meyer & Rowan, 1977). The international environment thus provides firms and their decision-makers considerable latitude for the interpretation of institutional pressures, which results in heterogeneous strategic responses among firms.

4.2 Managerial Attention

At least since Simon's early work (1945), we have known that individuals focus their attention on selected aspects of a situation due to their cognitive limits. Selective attention thus leads to the exclusion of competing aspects, which might result in an alternative behavior. In this respect, "what decision-makers do depends on what issues and answers they focus their attention on." (Ocasio, 1997: 186). The implication of this for firms is that firm behavior may as well be a function of how managers distribute their attention across strategic issues surrounding the firm.

Attention, in this sense, is defined as the noticing, encoding, interpreting, and focusing of time and effort by organizational decision-makers (Ocasio, 1997: 189). This view of attention goes beyond simply paying attention to something (Levy, 2005). It is in fact a cognitive process with regard to managerial sensemaking. But how does attention affect strategic responses to institutional differences?

As explained earlier, managers direct their attention on a limited set of elements of their environment. In this respect, two environmental domains are identified in the extant literature (Bourgeois, 1980; Nadkarni & Barr, 2008; Roth & Morrison, 1992):

general environment and market environment. The former is bounded by country parameters (Roth & Morrison, 1992), and thus includes the institutional environment, e.g., social norms, widely-held beliefs and taken for granted assumptions in a country (Scott, 1995). Market environment, on the other hand, is the typical research context in strategic management. It resembles the notion of industry in the industrial organization paradigm as it is composed of customers, suppliers, competitors, technology, and as well as laws and regulations (Bourgeois, 1980). Managers can narrowly focus on sectors in the market environment or can scan broadly across different components of the general environment. I argue that these attention patterns affect how managers make sense of institutional voids, and thus influence the firm's strategic response to them.

4.3 Hypotheses

According to the view of attention that is adopted in this paper, attention provides a lens through which managers identify strategic issues and make strategic decisions (Nadkarni & Barr, 2008). In other words, attention is a sensemaking process through which managers construct a line of action for the firms they run. The implication is that unequal managerial attention across firms to different aspects of the environment should lead to different interpretations of environmental pressures, and naturally, to different strategic responses (Dutton & Duncan, 1987). This is the main idea of this paper.

This idea has been supported by the empirical results. Nadkarni and Barr (2008) find that attention to the market environment positively affects the speed of strategic responses to the events in the market environment, whereas it negatively affects the speed of the strategic responses to the events in the general environment. Levy (2005)

documents that firms are more likely to develop an expansive global strategic posture when their top management pays attention to the external environment and considers a diverse set of elements in this environment. Thomas *et al.* (1993) report that managers interpret strategic issues that they pay more attention to as positive and controllable, and such interpretations in turn enhance the potential for top managers' taking strategic change actions. On the other hand, they find less attention is associated with the interpretation of issues as negative and uncontrollable, which in turn makes strategic change actions less likely. Kaplan (2008) shows that CEO attention to a new technology is associated with subsequent increases in a firm’s investment in that technical domain. D’Avenni and McMillan (1995) find that managers of successful firms attend to critical success factors in firm’s external environment while those of failing firms deny focusing on these factors and instead direct their attention to firm’s internal environment. Cho and Hambrick (2006) document that a shift in managerial attention caused by deregulation leads to a change in firm strategy.

This literature, despite revealing the cognitive underpinnings of strategic responses, focuses to a large extent on the domestic and the market environment, and hence ignores strategic responses to the demands of the institutional environment. For a purely domestic firm operating in a developed country, a focus on the market environment may suffice to gain competitive advantage, as the prevalent bureaucratic logic maintains rule-based market competition. Where emerging countries are concerned, however, it is well established that the role of the institutional environment becomes conspicuous (Peng et al., 2008). Considering this, it can be argued that expansion into

emerging countries requires attention to different strategic issues than those required by domestic competition.

In this regard, I argue that expansion into emerging countries requires managers to shift their attention focus from the market environment to the institutional environment. Absence or weakness of bureaucratic logic means that markets to work the same way in these countries as they do in developed countries, which reduces the effectiveness of market strategies (Peng, 2003). An attention focus on the institutional environment, in this regard, will enable managers to recognize the institutional differences across countries, which will make them more likely to modify their market strategies accordingly. As a result, they will be more likely to address the challenges stemming from institutional differences and hence decide to internationalize.

In this sense, more attention to the institutional environment is associated with richer institutional knowledge, which allows managers to construct better interpretations of institutional differences and envision more alternative responses to them. On the other hand, more attention to the market environment, due to cognitive limits, will mean less attention to the institutional environment. This will translate into poor knowledge of patrimonial logic, which will hinder managers’ ability to develop non-market strategies required to respond to institutional differences. This will narrow down the opportunity set envisioned by managers, and hence will discourage them from expanding into emerging countries. Thus;

Hypothesis 1: Managerial attention to the institutional environment will be positively related to firm expansion into emerging countries.

Hypothesis 2: Managerial attention to the market environment will be negatively related to firm expansion into emerging countries.

On the other hand, I argue that entry into developed countries does not require different attention patterns than those of domestic competition. This is because a strong bureaucratic logic that underpins market competition is commonly shared by all developed countries. Although there may be differences in the "strength" of bureaucratic logic, "the rules of the game" do not really change when a develop country firm enters into another developed country. Strong bureaucratic logic, in this sense, provides a foundation on which a similar market competition, "the same game", takes place. For this reason, managers need to focus their attention on the market environment to understand the industry dynamics and the formal institutional environment, and develop market strategies to respond to this environment. On the other hand, managers do not need to pay attention to the institutional environment, as it does not significantly change across developed countries. In short, developed country firms do not need to gain knowledge of patrimonial logic when they expand into another developed country. Besides, more attention to the institutional environment will correspond to less mental resources and less effort spent on analyzing the market environment, which will hinder firm's ability to expand into developed countries. Thus;

Hypothesis 3: Managerial attention to the market environment will be positively related to firm expansion into developed countries.

Hypothesis 4: Managerial attention to the institutional environment will be negatively related to firm expansion into developed countries.

4.4 Methodology

4.4.1 Sample

The sample for this study was drawn from the COMPUSTAT database. Three criteria guided the sampling of US manufacturing firms. First, the sample was limited to global industries only. I drew on the extant literature to identify global industries (Nadkarni et al., 2011; Samiee & Roth, 1992; Zou & Cavusgil, 2002). Within such industries, industry structure transcends national boundaries, creating similar markets across countries. According to industrial organization paradigm, firms in these industries are under more competitive pressures and hence tend to pursue global strategies. This suggests that market environment should be paramount for managers of these firms if they are to internationalize, whereas institutional differences across countries should receive little or no attention as a firm is assumed to find itself in the same industry environment, regardless of the country it enters. However, I argue in this paper that industry environment is embedded in the institutional environment, and as the institutions of a potential host country differ from those of the home country, managers need to pay more attention to the institutional environment. Only then managers can make sense of the institutional differences and identify opportunities in an institutionally distant country. I contend it is this cognitive process that is the primary driver of internationalization choices. If the results of this study support this argument for firms in

global industries, then the findings can be easily generalized to firms in other industries, since managers in multi-domestic and transnational industries are under more pressures to adapt their strategies to local contexts and hence are more likely to focus their attention on the institutional differences between countries.

The second criterion that guided sample selection was firm size. I chose firms whose sales exceeded $100 million. This reduced the amounts of missing data as there is little publicly available data for smaller firms. Third, because young firms are in transition and their cognition is unstable, I focused on firms that were at least 10 years old (Barr, Stimpert, & Huff, 1992; Nadkarni & Perez, 2007). These criteria yielded 152 firms operating in 18 industries. Finally, I used data from 2004 to 2007 to measure the dependent variables, and one year lagged values for all independent and control variables, which aimed to address reverse causality issues.

4.4.2 Data sources for eliciting managerial cognition

Following the extant strategic cognition literature (Cho & Hambrick, 2006; Kaplan, 2008; Levy, 2005; Nadkarni & Barr, 2008), I used CEO's letters to shareholders published in the annual reports to measure their attention patterns. I collected annual reports from *Mergent Web Reports*, as well as from firms' official websites.

A major criticism of the use of letters to shareholders is that they may be used by managers as tools for impression management, and thus may not reflect their cognitions. Yet, the Global Reporting Initiative (GRI), now one of the leading organizations for corporate social responsibility (CSR) reporting, defines CEOs´ statements as one of the most important parts of the CSR reports (Castello & Lozano, 2011). As argued by the

GRI G3, the CEO/President's letter reports on the organization's strategy. Such letters state manager's priorities with regard to firm's internal and external environment, and how they affect firm strategy. In other words, these letters define the strategic lines of the firm and can in fact considered one of the most representative parts of the reports (Abrahamson & Amir, 1996).

There is also plenty of evidence in the business literature suggesting that letter to shareholders can be a reliable data source for the measurement of managerial cognition. For instance, Fiol (1995) compared public and private documents generated by executives in the forest products industry and found that non-evaluative cognitions—attribution of control—were significantly correlated across these two types of documents. D'Aveni & MacMillan (1990) similarly demonstrated that measures of top managers' cognitions drawn from the letters to shareholders were highly correlated with measures derived from other types of data. Even in the institutional literature (in which decoupling is a central concept), Greenwood and Suddaby (2006) found striking correspondence between public and private statements of the accounting firms they studied. In short, statements in letters to shareholders can safely be seen as an indirect indicator of the cognitive representations of managers from the sample firms.

4.4.3 Measuring Attention

I obtained data regarding managerial attention patterns by using word counts from letters to shareholders. Word count has been employed in several studies to measure managerial cognition (Cho & Hambrick 2006; D'Aveni & MacMillan 1990; Kaplan, 2008; Levy, 2005). A coding list was developed mostly from the ground up. I selected the

phrases and words referring to each element of the environment after manually coding several letters. I continued manual coding until I stopped coming across new phrases and words. After the coding list was complete, I used the "*Text Search*" option in *NVivo* to obtain the word counts for the whole sample. I used the proportion of the keywords in a letter to shareholder to measure how managerial attention is distributed across the firm's environment. Table 4.3 shows a sample of these keywords used for automated coding.

4.4.4 Independent variables

Attention to market environment and *attention to institutional environment.* I drew on the extant frameworks of the task environment (Bourgeois, 1980; Daft et al., 1988) to identify the concepts related to the market environment. I classified words and phrases related to competitors, suppliers, customers, and the regulatory environment under the market environment.

I used Scott's (1995) and North's (1991) framework of institutions to identify the words and phrases related to the institutional environment. I categorized words/phrases referring to social norms, ethics, corporate social responsibility, under the socio-cultural environment, whereas I classified the words/phrases regarding politics under the political environment.

In order to calculate the proportion of the key words, I used the coverage ratio provided by *NVivo*. This ratio gives the average of the percentage of characters coded —as text selections— and the percentage of the page area coded —as region selections—. Thus, this ratio provides a control for the length of the letter to shareholder.

4.4.5 Dependent variables

Internationalization. The number of subsidiaries has been widely used in the international business literature to measure the degree of internationalization (Dau, 2013; Lu & Beamish, 2004; Wan & Hoskisson, 2003). Thus, I capture expansion into emerging countries with the number of subsidiaries the firm has in emerging countries, and entry into developed countries with the number of subsidiaries the firm has in developed countries. In regards to categorization of countries, there is no established convention for the designation of "developed" and "developing" countries or areas in the United Nations system. IMF's classification of advanced economies does not seem to reflect the common practice, as its current grouping includes countries such as Czech Republic, Slovenia, and Slovakia, which have been treated as transition economies by scholars and practitioners alike. Therefore, I mainly use the conventional categorization of developed countries that consists of the U.S., Canada, Western European countries, Australia, New Zealand, and Japan (Makino, Lau, & Yeh, 2002). However, I slightly modify this by moving Israel, Hong Kong, Singapore, and South Korea to the developed country category, considering that they have been some of the highest income countries in the world during the past decade. Besides, I treat the Canadian subsidiaries of the sampled firms as domestic subsidiaries and thus do not include them in the measurement of the dependent variable.

4.4.6 Control variables

I controlled nine variables that are commonly known to affect internationalization: firm age, firm size, slack, R&D intensity, advertising intensity, export intensity, product diversification, firm international experience, and past

performance (Kirca et al., 2011; Lu & Beamish, 2004; Kim et al., 2010). Due to data availability issues regarding firm's international experience, I could not use the conventional measure of the number of years of international investment history (Henisz and Delios, 2001). Therefore, I created a categorical variables to measure firm's emerging country experience and firm's overall international experience: As of 2002, if a firm had had a subsidiary in a foreign country; 1) for 10 years or more, the variable was labeled as "vast international experience", and took the value of 2; 2) for less than 10 years, the variable was labeled as "limited international experience" and took the value of 1. If the firm did not have a subsidiary in a foreign country as of 2002, the variable was labeled as "no international experience" and took the value of 0. Similarly, if a firm had had a subsidiary in an emerging country as of 2002; 1) for 10 years or more, the variable was labeled as "vast emerging country experience", and took the value of 2; 2) for less than 10 years, the variable was labeled as "limited emerging country experience" and took the value of 1. If the firm did not have a subsidiary in a foreign country as of 2002, the variable was labeled as "no emerging country experience" and took the value of 0.

Since this study emphasizes the role of managers and their sensemaking in determining firm's internationalization strategy, I also controlled for the effect of the manager's background characteristics, such as prior experience in emerging countries and overall international experience. I defined international experience as the number of years spent on higher education and on work assignments abroad (Nadkarni & Perez, 2007). As for emerging country experience, I use a dummy variable that takes the value of 1 if the CEO worked or studied in at least one of the emerging countries. I used I measured firm size by the logarithm of the total employees. I used the ratio of liabilities to assets to

measure slack. For R&D intensity, I used R&D expenditures over sales. To measure advertising intensity, I used the ratio of advertising expenditures to sales. I capture export intensity with the ratio of exports to sales. As for product diversification, I used entropy measure, which is calculated as:

$$\text{Degree of product diversification} = \sum_i [P_i \times \ln(1/P_i)],$$

where P_i is the sales attributed to segment i and $\ln(1/P_i)$ is the weight given to each segment, or the natural logarithm of the inverse of its sales. Past performance was measured as the return on sales in the prior year. Finally, I controlled for the industry effects by using the two digit Standard Industry Classification Codes (SIC). In the sample, firms were distributed across seven industries, so I used six dummy variables. I derived all the firm-level data from the COMPUSTAT database, whereas I obtained the data regarding managerial background characteristics from *Dun and Bradstreet's Reference Book of Corporate Management*, as well as from biographies published in *Businessweek*.

4.5 Results

The means, standard deviations, and correlations are reported in Table 4.4. To check for a potential problem of multicollinearity, I used variance inflation factor analysis. The scores ranged from 1.13 to 4.03, which was well below 10, thus multicollinearity was not a problem in the regression analysis (Hair, Anderson, Tatham, & Black, 1998).

Table 4.5 contains the negative binomial regression results testing the hypotheses. Model 1 shows the effects of firm size, firm age, R&D intensity, advertising intensity,

slack, product diversification, export intensity, CEO international experience and past performance on firm expansion into developed countries, after controlling for the 7 dummy industry variables. R&D intensity and advertising intensity, the commonly used proxies for market capabilities that are accepted as the primary drivers of internationalization in the literature (Kirca et al., 2011), have significant and positive effects in this model.

In model 2, we see the effect of the same variables on firm expansion into emerging countries. The effects of R&D intensity and advertising intensity are again positive and significant, suggesting that market capabilities drive internationalization also into emerging countries.

Model 3 reports tests of Hypothesis 3 and 4. In this full model, attention to market environment is positively related to entry into developed countries ($p>0.05$), which supports Hypothesis 3. However, the effect of attention to institutional environment is not significant ($p<0.1$). As a result, hypothesis 4, which posited a negative relationship between managerial attention to the institutional environment and firm entry into developed countries, is not supported.

In model 4, attention to institutional environment is positively related to firm expansion into emerging countries ($p<0.05$), which provides support for hypothesis 1. The effect of attention to market environment is, however, not significant ($p<0.05$). As a result, hypothesis 2, which predicted a negative relationship between attention to market environment and entry into emerging countries, is not supported.

4.6. Discussion

At least since Oliver's (1991) seminal work, institutional scholars have known that organizations engage in active and interest-seeking behavior in response to institutional pressures. In other words, organizations can develop strategic responses to these pressures rather than passively yielding to institutional pressures in a uniform manner. This approach was a significant contribution to the earlier versions of institutional theory, because it explained the heterogeneity in organizational behavior despite the pressures for conformity and homogeneity. However, since this perspective treats the nature and the context of the institutional pressures as the main determinant of strategic responses, it does not address how organizations that are subject to identical pressures vary in their responses.

The objective of this study is to address this void in the literature by highlighting the role of individual sensemaking in determining organization's strategic responses to dissimilar institutional logics. By directly examining the cognitive processes through which managers make sense of their environment, I show that institutional differences between countries do not automatically lead to a choice between internationalization and no internationalization. The pressures stemming from institutional pressures are rather interpreted, given meaning, and responded to by the key decision makers of organizations (Dacin et al., 2002; George et al., 2006). In this regard, theory and findings of this study provide evidence supporting the theoretical arguments of the current work in institutional research, which views sensemaking at the individual level is a source of agency, as well as the main reason behind the heterogeneous strategic responses (George et al., 2006; Kennedy & Fiss, 2009; Lawrence & Suddaby, 2006; Powell & Colyvas, 2008).

Another contribution of this paper to institutional theory is its approach to uncertainty caused by weak bureaucratic logic. Since Meyer and Rowan (1977), institutional scholars have equated underdeveloped formal institutions with weaker pressures for conformity. Oliver (1991) similarly proposed that organizations will resist institutional pressures when the level of institutionalization is low. However, some recent institutional research has come to view the lack of institutionalization in emerging countries as an opportunity for more active institutional strategies, even for institutional entrepreneurship (Battilana, Leca, & Boxenbaum, 2009, Tracey & Phillips, 2011). In this respect, firm expansion from a developed country to an emerging country provides a different context to analyze organizations' strategic responses to dissimilar institutional logics. It shows that organizations can take advantage of the weak bureaucratic logic only if their decision-makers have the sensemaking capabilities to navigate through an institutional system dominated by patrimonial logic.

This work follows in the footsteps of George et al. (2006) and Kennedy and Fiss (2009), who drew on upper echelon theory and threat-rigidity hypothesis (Staw et al., 1981) to extend Oliver's (1991) model of strategic responses to institutional pressures. Integrating neo-institutional theory with cognitive science, this study provides a new conceptualization of the relationship between institutional distance and internationalization strategy. It offers a fresh perspective in studying internationalization by emphasizing the special role of managerial cognition in mitigating the difficulties arising from institutional differences.

4.7 Implications and further research

There is a general understanding among economists that internationalization (FDI) happens when firms (investors) feel secure, but we do not really know what makes them feel secure (Rodrik, 2006). This study can also be seen as an attempt to address this issue. In this regard, further research should study other cognitive processes than attention that shapes the way firms make sense of institutional differences, as well as how this sensemaking influences their subsequent action. Only then can we understand the real dynamics and processes of internationalization.

4.8 Conclusion

In this study, I drew on Xu and Shenkar (2002) and Phillips et al. (2009) to study internationalization as a strategic response to institutional differences between home and host countries. However, I integrated this line of work with the recent developments in institutional research that studies cognition as the micro-foundation of institutions (George et al., 2006; Kennedy & Fiss, 2009). By directly examining managerial sensemaking through attention focus, this study explains why there is a diversity of strategic responses among developed country firms to the patrimonial logic prevalent in emerging countries. The findings support the hypothesis that managerial attention to the market environment is positively related to firm expansion into developed countries, whereas, managerial attention to the institutional environment is positively related to firm expansion into emerging countries. I thus conclude that the variation in managerial attention focus on market and institutional environments is the cognitive underpinning of strategic responses to dissimilar institutional logics.

Table 4.1: Firm's external environment

Market Environment	**General Environment**
Competitors	Demographic Environment
Customers	Macro-Economic Environment
Suppliers	Socio-Cultural Environment
Legal/Regulative Environment	Political Environment

Institutional Environment

Table 4.2: Global industries in which sampled firms operate

SIC Code	Industry
2086	Bottled & canned drinks
2100	Soft drinks & carbonated water
2834	Pharmaceuticals
2844	Cosmetics
3533	Oil Field Machinery
3562	Ball and roller bearings
3570	Computers & office equipment
3571	Electronic computers
3577	Computer peripheral equipment
3651	Household audio and video equipment
3674	Semiconductors
3711	Automobiles
3714	Automotive parts
3721	Aircraft
3728	Aircraft parts
3844	X-Ray apparatus
3845	Electromedical apparatus
3861	Photographic equipment
3873	Watches and clocks

Table 4.3: Samples of keywords used for automated coding

Market Environment				Institutional Environment	
Competitors	**Customers**	**Suppliers**	**Legal/ Regulative**	**Socio-Cultural**	**Political**
Competitor	Customer	Supplier	Law	Ethics	Government
Acquisition	Market	Supply chain	Regulation	Corporate citizenship	State agencies
Barriers to entry	Consumer	Raw material	Legislation	Social responsibility	Policymakers

Table 4.4: Descriptive statistics and correlations

Variable	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12
1. Entry into developed countries	10.12	18.99												
2. Entry into emerging countries	4.53	10.89	0.92***											
3. Firm age	30.41	15.94	0.49***	0.47***										
4. Firm size	1.69	1.66	0.62***	0.56***	0.63***									
5. R&D intensity	0.11	0.15	–0.01	–0.02	–0.21***	–0.13**								
6. Advertising intensity	0.02	0.04	0.09*	0.13**	–0.04	–0.00	–0.06							
7. Slack	0.49	0.29	0.09*	0.09*	0.18***	0.33***	–0.07	0.38***						
8. Past performance	0.11	0.15	0.11**	0.11**	0.21***	0.18***	–0.35***	0.07	–0.22***					
9. Product diversification	0.33	0.45	0.28***	0.22***	0.32***	0.30**	–0.14**	–0.13**	0.05	0.04				
10. Export intensity	0.02	0.09	–0.04	–0.07	–0.08	–0.06	0.00	–0.04	–0.12**	0.11*	–0.03			
11. CEO international experience	1.98	5.29	0.16***	0.15***	0.06	0.13**	0.15***	0.01	0.03	0.08	–0.00	–0.07		
12. CEO attention to inst. environment	0.09	0.15	0.27***	0.26***	0.21***	0.34***	–0.05	0.02	0.17***	0.05	0.04	–0.01	0.02	
13. CEO attention to market environment	1.69	1.48	0.01	0.02	–0.07	–0.01	0.16***	–0.06	–0.04	–0.00	0.03	–0.01	0.00	–0.00

Summary statistics for the industry, CEO emerging country experience, and firm international experience variables are not included to save space.
N= 423. * $p < 0.05$; ** $p < 0.01$; *** $p < 0.001$.

Table 4.5: Results of analyses of managerial attention focus on internationalization choices

Independent Variables	**Model 1** *Entry into developed countries*	**Model 2** *Entry into emerging countries*	**Model 3** *Entry into developed countries*	**Model 4** *Entry into emerging countries*
Intercept	3.47***	4.49***	3.14***	4.29***
Firm age	1.85***	1.69***	1.87***	1.65***
Firm size	4.23***	5.14***	4.12***	5.15***
R&D intensity	1.43***	0.58*	1.27***	0.42
Advertising intensity	0.67***	0.79***	0.68***	0.77***
Slack	-0.39*	0.06	-0.39	0.67
Past performance	1.50***	0.28	1.44***	0.15
Export intensity	0.14	-0.01	0.09	-0.04
Product diversification	-0.24***	0.18***	-0.27***	0.17***
CEO international experience	1.23***	0.68***	1.23***	0.62***
CEO attention to market environment			0.76***	0.17
CEO attention to institutional environment			0.19	0.65*
N	425	423	425	423

*p < 0.05
**p < 0.01
***p < 0.001

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