

8-22-2014 12:00 AM

## Essays on the Relationship Between Host Market Corruption and Multinational Enterprise Strategy

Michael A. Sartor, *The University of Western Ontario*

Supervisor: Dr. Paul W. Beamish, *The University of Western Ontario*

A thesis submitted in partial fulfillment of the requirements for the Doctor of Philosophy degree in Business

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ESSAYS ON THE RELATIONSHIP BETWEEN HOST MARKET CORRUPTION  
AND MULTINATIONAL ENTERPRISE STRATEGY

(Thesis format: Integrated-Article)

by

Michael A. Sartor

Graduate Program in Business Administration

A thesis submitted in partial fulfillment  
of the requirements for the degree of  
Doctor of Philosophy

The School of Graduate and Postdoctoral Studies  
Western University  
London, Ontario, Canada

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## ABSTRACT

This dissertation is guided by three research questions. First, *how does host market corruption impact the equity-based market entry strategies implemented by multinational enterprises (MNEs) with respect to their foreign subsidiary investments?* Second, *does host market corruption increase the likelihood of market exit?* Third, *can MNEs implement strategies which reduce the likelihood of market exit under conditions of more pervasive host market corruption?*

In the first essay, I synthesize insights from institutional theory and integrative social contracts theory to disaggregate the concept of government corruption into two dimensions (*grand* and *petty*). My theory pertaining to informal institutional pluralism suggests that discrete institutions (such as government corruption) within a host market can be conceptualized as pluralistic phenomena constituted by distinct dimensions which exert a disparate impact on the foreign entry strategy of MNEs. The results support aspects of this theory.

In the second essay, I build on the concept of informal institutional pluralism, categorizing corruption into two dimensions (*public* and *private*) to study its impact on the structure of equity-based foreign subsidiary investments. My theory proposes that the primary mechanism that drives the distinct approaches to foreign entry is the firm's anticipated reliance on different sources of bargaining power to reduce information asymmetries that it expects to encounter in the host market.

In the third essay, I study the relationship between host market corruption pervasiveness, the subsidiary localization strategies implemented by MNEs and the likelihood of host market exit. In this context, the strategic insights proffered by resource dependence theory (RDT) and institutional theory (IT) are characterized by distinct spatial orientations. While RDT predicts that subsidiaries will implement *proximal* (or, host market-oriented) *localization strategies*, IT suggests that *distal* (or, home market-oriented) *localization strategies* are better-suited to reducing the likelihood of exit from increasingly corrupt host market environments. I find that a proximally-oriented *partnering strategy* heightens the likelihood of market exit under conditions of more pervasive host market *public corruption*, but not more pervasive *private corruption*.

Conversely, a distally-oriented *expatriate strategy* increases the likelihood of market exit under conditions of both more pervasive *public corruption* and *private corruption*.

Taken as a whole, this dissertation introduces new theory, constructs and insights into the relationship between host market corruption and the equity-based foreign entry strategies of MNEs.

Keywords: Corruption; Government Corruption; Grand Corruption; Petty Corruption; Public Corruption; Private Corruption; Foreign Direct Investment; Market Entry Strategy; Ownership Structure; Emerging Markets; Developed Markets; Institutional Pluralism; Informal Institutional Pluralism; Institutional Theory; Integrative Social Contracts Theory; Resource Dependence Theory; Bargaining Power Theory; Binary Logistic Regression; Multinomial Logistic Regression; Event History Analysis.

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## CHAPTER 1

### INTRODUCTION

In July 2000, the United Nations launched the Global Compact, an initiative designed to promote the adoption of socially responsible and sustainable business practices by corporations. The Compact's framework was originally constituted by nine principles that were organized under three broad categories - human rights, labor and the environment. However, in an effort to garner greater transparency in both the public and private sector, academics, non-governmental organizations and industry executives began to petition for the recognition of "the missing tenth principle", in reference to the institution of corruption (Waddock, 2004: 318). Their concerns were well-founded. Research by the World Bank estimated that global expenditures on bribery totaled approximately one trillion dollars per year, an amount equal to roughly three percent of global gross domestic product (Svensson, 2005). Consequently, by 2004, advocacy efforts culminated in the creation of the tenth canon of the Global Compact – *Businesses should work against corruption in all its forms, including extortion and bribery*.

Subsequent to the expansion of the Global Compact's purview, institutional scholars have directed their attention towards the development of theory that could be used to facilitate corruption-based inquiry (Lambsdorff, Taube, & Schramm, 2005). Moreover, international business strategy researchers have also emphasized the need to develop theory, frameworks, measures and methods within the domain of corruption-oriented international business scholarship (Rodriguez, Siegel, Hillman, & Eden, 2006). Notwithstanding the overlap between these research agendas, we continue to lack a comprehensive, theoretically-grounded and empirically-validated understanding of how host market corruption affects the subsidiary-level strategic behavior of multinational enterprises (MNEs) in foreign markets. I contend that two factors have precipitated this theoretical impasse. First, the literature pertaining to the relationship between MNE strategy and host market corruption has focused primarily on the interrelationship between global foreign direct investment flows and the degree of perceived corruption in host markets. Second, researchers that have focused on the impact of host market

corruption on subsidiary-level strategy have adopted an overly broad conceptualization of the corruption phenomenon.

The resultant theoretical deficiency has important practical consequences from the perspectives of both international strategy scholars and international business ethicists. Absent sufficiently precise theory, scholars are not able to formulate theoretically-grounded predictions with respect to the strategic behavior of MNEs under conditions of heightened host market corruption, nor are they able to recommend strategic configurations that will enhance the likelihood of achieving positive investment outcomes. Moreover, without a theoretically-based understanding of the interrelationship between host market corruption and subsidiary-level strategy in foreign markets, it becomes more difficult to prescribe how MNEs can effectively integrate the Global Compact's tenth principle into the business strategies, operations and structures of their foreign subsidiaries. Notably, in developing a framework designed to secure corporate commitment to the Global Compact's principles, the United Nations has suggested that the engagement of worldwide subsidiary operations is one of the most important avenues through which MNEs can scale-up corporate responsibility efforts (Kell, 2012).

As such, this dissertation is guided by three broad research questions. First, *how does host market corruption impact the equity-based market entry strategies implemented by MNEs with respect to their foreign subsidiary investments?* Second, *does host market corruption increase the likelihood of market exit?* Third, *can MNEs implement strategies which reduce the likelihood of market exit under conditions of more pervasive host market corruption?* As an international business scholar, my dissertation research is principally motivated by my commitment to bolstering MNEs' comprehension of the strategic impact of corruption in foreign markets. Nonetheless, my efforts to advance understanding with respect to the phenomenon of host market corruption do not preclude the possibility that normative insights might also emerge from this work. More specifically, it is anticipated that the theory and empirical findings associated with this dissertation will also be of interest to policy makers and business ethicists, particularly given that "understanding corruption...is vital to any effort to limit corruption" (Rodriguez et al., 2006: 739).

This chapter proceeds with a review of the extant literature pertaining to the relationship between MNE strategy and national corruption, before providing an overview of the manner in which corruption has been conceptualized by management scholars. It also briefly discusses the author's rationale for employing institutional theory as the core theoretical foundation that informs this dissertation research. This chapter concludes with an outline of each essay in order to provide an overview of the research that constitutes the dissertation.

### **The Strategic Responses of Multinational Enterprises to Corruption**

Historically, the corruption-oriented international business strategy research agenda has been primarily constituted by a rich body of macro-level studies that have focused on the role of host market corruption as a factor influencing the international flow of foreign direct investment (FDI). Two of the earliest studies yielded contradictory findings. While Mauro (1995) found that higher levels of corruption resulted in lower levels of FDI, Hines Jr. (1995) concluded that the level of corruption did not predict inward FDI, but he also found that FDI from the United States into more corrupt host countries decreased after the *Foreign Corrupt Practices Act* was enacted in 1977. More consistent with Mauro's (1995) work, subsequent studies have determined that MNEs invest less in countries that have higher levels of corruption (Smarzynska & Wei, 2000) and that an increase in the absolute difference in the level of corruption between an MNE's home and host markets negatively impacts upon the FDI decisions of MNEs (Habib & Zurawicki, 2002). Focusing more specifically on emerging markets, which Luo (2011) contends are more prone to corruption, Voyer and Beamish (2004) extended prior corruption-FDI studies when they found that heightened levels of corruption in emerging market countries predicted lower levels of FDI. While many of these prior studies measured the level of perceived host market corruption based upon the opinions of foreign executives situated in the host markets, subsequent research has found that the prevailing attitude towards corruption in the MNE's home market also impacts upon an MNE's FDI decisions. Cuervo-Cazurra (2006) found that MNEs that are headquartered in countries with higher levels of corruption tend to invest more in countries where corruption is more prevalent. He also concluded that MNEs headquartered in countries

that were signatories to the OECD convention that combats bribery in foreign markets were less likely to invest in markets characterized by greater corruption. Subsequent research has suggested that this is because laws against foreign bribery have made it more costly for MNEs to invest in countries characterized by higher levels of corruption (Cuervo-Cazurra, 2008).

While the insights garnered by studies pertaining to the relationship between the FDI decisions of MNEs and host market corruption have advanced comprehension of the phenomenon, more recently, international strategy scholars have begun to focus attention on the impact of host market corruption on subsidiary-level strategies. This smaller body of work serves as the starting point for this dissertation and it informs the associated theory-building efforts at the phenomenological level.

MNEs have been found to prefer joint equity investments in markets characterized by higher levels of corruption, unless the MNE is more technologically advanced, in which case the MNE will be less likely to engage in a joint venture (Smarzynska & Wei, 2000). In another study on the relationship between corruption and firm strategy that was based on a sample of emerging market-based subsidiary investments, Meschi (2009) found that government corruption is significantly related to the likelihood of foreign partners terminating an international joint venture (IJV). Further, Meschi determined that the country experience of foreign partners moderates the relationship between government corruption and changes in the equity stakes of foreign partners in emerging market-based IJVs.

Subsequent conceptual work by Rodriguez et al. (2005: 385) has characterized corruption in terms of its pervasiveness or, “the likelihood of encountering corruption in normal interactions with state officials.” In testing this theory, Uhlenbruck et al. (2006) found that as the pervasiveness of corruption increases, foreign investing firms are more likely to prefer nonequity modes of entry over equity modes (JV or WOS). This observation has been supported by Luo (2011) who found that an increase in the *pervasiveness* of host market corruption decreased the likelihood that MNEs would engage in subsidiary investments in emerging markets and increased the likelihood that they would adopt an export market orientation.

However, while an increase in the *pervasiveness* of host market corruption has been found to precipitate a preference among internationalizing MNEs for nonequity modes over equity modes of entry, the *pervasiveness* of host market corruption has not been found to be a significant predictor of the entry mode (JV versus WOS) employed by MNEs that engaged in equity-based foreign investments (Uhlenbruck et al., 2006). Given the ample evidence supporting the relationship between the *pervasiveness* of host market corruption and MNEs' preference for nonequity approaches to investing in foreign markets characterized by more *pervasive* corruption, it is surprising that the *pervasiveness* of host market corruption does not significantly predict the equity-based entry mode decisions of foreign-investing MNEs, particularly given the recent results of Spencer and Gomez (2011). They find that a positive relationship exists between the level of host country corruption and the pressure that foreign subsidiaries face to engage in host market bribery. Further, they observe that MNEs from less corrupt home countries report less pressure to engage in corrupt local practices when they do not partner with locals in foreign markets.

Rodriguez et al.'s (2005) conceptual work has provided a strong theoretical foundation for scholars to advance corruption-oriented international business strategy research. However, the qualified empirical support for its propositions suggests the need for further conceptual effort in order to refine the theory's precepts. Consistent with this position, Uhlenbruck et al. (2006: 411) have suggested that "...there may be underlying constructs behind pervasiveness that have conflicting effects on the firm's choice between joint venture and wholly-owned subsidiary. Further exploration of the institutional underpinnings of the pervasiveness of corruption is an important next step for corruption researchers."

In this dissertation, I contend that the traditionally-employed conceptualization of corruption is overly broad and, as a consequence, it has inhibited progress in advancing comprehension of the relationship between host market corruption and the subsidiary-level strategies of foreign-investing MNEs. In this regard, my work draws from Rodriguez et al. (2006: 739) who argue that the domain of corruption-based research would benefit from more attention being given to defining and conceptualizing the phenomenon.

## Defining and Conceptualizing Corruption

Settling upon a comprehensive definition of corruption has proven to be a challenging exercise for academics, policy-makers and business executives alike. While Argandoña (2003: 255) has acknowledged that corruption is “a varied and shifting phenomenon that is difficult to define in terms that are clear”, the chair of Transparency International’s Board of Directors recently lamented that “(The boundaries) of corruption are becoming harder to define, despite the best efforts of high profile international treaties and initiatives” (Labelle, 2010: 109). An extensive tradition of corruption research exists in the academic fields of law, political science and economics. While legal theorists have defined corruption as “the misuse of public office for private gain by an elected official” (Rose-Ackerman, 1996: 83), political scientists have framed corruption as “the exchange of money or favor for a benefit disbursed by a government official” (Oldenburg, 1987: 512). Similarly, economists have characterized corruption as “an arrangement contracted between a private individual and public official, (in which) the payment for, or the counterpart of the arrangement may be political patronage, tutelage or some other type of barter” (Macrae, 1982: 678).

These early efforts to conceptualize corruption have informed the more recent work of international business strategy scholars. As examples, in the leading conceptual and empirical work on the phenomenon, both Rodriguez et. al. (2005: 383) and Uhlenbruck et al. (2006: 402) define corruption as “the abuse of public power for private benefit.” In this dissertation, I contend that that there are two important limitations associated with this extant conceptualization of the phenomenon. First, the definition has encouraged scholars to focus only upon *public sector corruption* to the exclusion of *private sector corruption*. Second, it has prompted scholars to adopt an overly broad conceptualization of *public sector corruption*. As a consequence, the current conceptualization of host market corruption risks the possibility of muting the effects of the phenomenon upon the strategy of foreign-investing MNEs (Milliken, 1987).

This dissertation builds on Rodriguez et al.’s (2005: 385) extant conceptualization of host market corruption in terms of its *pervasiveness* or, “the likelihood of encountering corruption in normal interactions with state officials.” I propose that the concept of *pervasiveness* provides an appropriate foundation upon which to construct more robust

and theoretically-rich conceptualizations of the phenomenon. My work further dimensionalizes the phenomenon according to the host market sector within which it occurs (*public* versus *private*), and according to the origins of the norms that permit or prohibit the existence of corrupt transactions in the public sector of foreign markets (*grand* versus *petty*). In doing so, my theoretically-grounded efforts extend the scope of the *pervasiveness* construct, as well as establishing boundary conditions within and around the *government corruption pervasiveness* construct developed by Rodriguez et al. (2005). Ultimately, my efforts are consistent with the work of both Mezias and Mezias (2010: 284) which calls for “future research on the dimensionality and meaning of multiple measures of corruption”, and Uhlenbruck et al. (2006: 411) which proposes that “...there may be underlying constructs behind pervasiveness that have conflicting effects on the firm’s choice between joint venture and wholly-owned subsidiary.”

Notably, in addition to the theoretical relevance of the new dimensions that are proposed in this dissertation, a review of executive surveys pertaining to corruption and international legal compacts that have been designed to combat corruption, reveals that these dimensions are also relevant in practice. Accordingly, my dissertation employs these more nuanced conceptualizations of the phenomenon in order to investigate the impact of host market corruption upon several strategies, including *foreign entry strategy* (the choice between nonequity entry and equity entry), *equity entry strategy* (the choice between a joint venture and a wholly-owned subsidiary) and *partnering strategy* (the choice between a traditional joint venture and a crossnational joint venture), as well as exploring the longer-term implications of corruption upon the subsidiary’s continued existence.

## **Institutional Theory**

Despite the extensive tradition of management scholarship grounded upon institutional theory, the use of institutional theory in international business strategy research is more recent (Hoskisson, Eden, Lau, & Wright, 2000). Scott (2008) recently identified two important developments that have made institutional theory more pertinent to strategic management scholarship. First, Oliver’s (1991) efforts to incorporate the role of agency within institutional theory have challenged researchers to investigate the active



responses of firms and managers to the pressures precipitated by institutional environments. Second, the theory has evolved from one in which institutional phenomena were “restricted to realms lacking competitive processes” to one in which institutions are regarded as providing the boundaries for strategic action (2008: 437).

Institutional theory is employed as the base theoretical foundation in this dissertation for a combination of practical and philosophical reasons. First, the conceptual work upon which I build my theoretical contributions is broadly grounded in institutional theory (cf. Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003; Lambsdorff et al., 2005; Lambsdorff, 2007; Rodriguez et al., 2005; Uhlenbruck et al., 2006). Second, embedded in my research is a belief in the power of institutional theory to predict and provide explanations for the behavior of foreign-investing MNEs. This commitment traces its roots to my background as a lawyer and my ten years of executive-level experience in industry. My extensive involvement in both domestic and cross-border business activity has made me acutely aware of the routine impact of institutions upon strategic and operational decision-making.

Corruption is inherently difficult to study because “...the parties involved have every reason to keep the data hidden” (Klitgaard, 1991: 30). This challenge has grown even more imposing. In fact, Webster (2008: 807) notes that “Ten years ago, corruption was considered incidental to doing business internationally and, for better or worse, an inescapable reality. Today, corruption is considered to be...an enemy that must be defeated. Accordingly, the international community is focused, like never before, on efforts to reduce corruption.”

Notwithstanding the obstacles associated with pursuing scholarship pertaining to the phenomenon of corruption, institutional scholars have made considerable advances. Notably, both institutional economists and institutional sociologists have contributed to this research imperative. Accordingly, this dissertation leverages tenets from both of these theoretical perspectives, an approach advocated by Lambsdorf (2005: 1-3) who suggests that “the task is too complex to rely on a single theoretical tradition...only an interdisciplinary approach is likely to be successful...approaching corruption from an institutional economic perspective, as well as from a sociological one, can enrich our understanding.”

## Dissertation Overview

Building on Uhlenbruck et al.'s (2006: 411 ) proposition that “there may be underlying constructs behind pervasiveness”, this dissertation is organized as a collection of integrated essays. Figure 1 illustrates the structure of the dissertation, detailing the theoretical foundations underpinning each essay, along with the contributions that link the essays together. Essay 1 theoretically disaggregates *government (public) corruption* within host markets into *grand corruption* and *petty corruption*, in addition to building on early theory with respect to institutional pluralism to develop theory pertaining to the pluralistic nature of distinct informal institutions such as host market government corruption. Essay 2 builds on the theory elaborated in Essay 1 to develop a theoretically-grounded distinction between *public sector corruption* and *private sector corruption*, as well as drawing upon bargaining power theory to detail the theoretical mechanisms that link each type of host market corruption (*public* and *private*) to the foreign entry strategy of MNEs. Finally, Essay 3 investigates whether host market corruption increases the likelihood of market exit and whether MNEs can implement strategies which reduce the likelihood of market exit. Essay 3 theoretically categorizes the choice of strategies that MNEs implement as being either *proximal* (host market-oriented) or *distal* (home market-oriented).

## Essay 1

The first essay (Chapter 2) is entitled *Institutional pluralism: Host market government corruption and the equity-based foreign entry strategies of multinational enterprises*. It focuses specifically on two distinct manifestations of *government corruption* in the host market environment – *petty corruption* and *grand corruption*. This essay is motivated by both a theoretical question (*Can host market institutions, that have traditionally been regarded as discrete institutions, be conceptualized as pluralistic phenomena?*) and, an empirical question pertaining more specifically to the phenomenon of host market government corruption (*Do the different dimensions of government corruption (grand corruption versus petty corruption) each exert a distinct impact upon the equity-based foreign entry strategies of MNEs?*). While extant theory proposes that the pervasiveness of host market corruption will influence the equity

**FIGURE 1**  
Overview of the Dissertation

	Essay 1: <i>Institutional pluralism: Host market government corruption and the equity-based foreign entry strategies of multinational enterprises.</i>	Essay 2: <i>Public corruption, private corruption and the structure of equity-based foreign subsidiary investments in emerging markets.</i>	Essay 3: <i>Corruption pervasiveness, subsidiary localization strategy and host market exit.</i>
Primary theoretical foundation(s):	Institutional theory and integrative social contracts theory (I.S.C.T.)	Institutional theory and bargaining power theory	Institutional theory and resource dependence theory
Theoretical contributions:	<p><i>Informal institutional pluralism:</i> Conceptualizing host market informal institutions as pluralistic phenomena.</p> <p>Theoretically disaggregates <i>government corruption</i> into <i>grand corruption</i> (grounded on the I.C.S.T. concept of globally-oriented hyper norms) and, <i>petty corruption</i> (grounded on the I.S.C.T. concept of locally-oriented behavioral norms).</p>	Develops a theoretically-grounded distinction between <i>public sector corruption</i> and <i>private sector corruption</i> in host markets.	<p><i>Proximal and distal legitimization (localization) strategies:</i> Investigates the host market-oriented (<i>proximal</i>) or home market-oriented (<i>distal</i>) strategies employed by MNEs to facilitate efforts to localize and secure legitimacy in foreign markets, in order to ascertain the performance efficacy of these strategies.</p>
Conference presentations of earlier versions:	AIB 2013; SMS 2013 (Nominated <i>Best Conference Paper</i> , and <i>Best Paper for Practice Implications</i> ); AOM 2014.	AIB 2012.	AIB 2012; AOM 2014.
Doctoral consortium presentations:	AIB 2013 (Sheth Doctoral Dissertation Proposal Award winner); AOM 2013 (International Management division).		

ownership decisions of MNEs (Rodriguez et al., 2005), subsequent research has not found a statistically significant relationship that empirically validates these propositions (Uhlenbruck et al., 2006). These results are surprising, particularly given the substantial evidence that has been garnered which suggests that host market corruption influences both the global location of foreign direct investment (Cuervo-Cazurra, 2008) and an MNE's preference for non-equity involvement in markets characterized by heightened corruption (Luo, 2011; Uhlenbruck et al., 2006). In this Essay, I incorporate insights from integrative social contracts theory (Donaldson & Dunfee, 1994, 1999; Spicer, 2009) to argue that host market informal institutions, such as government corruption, should be conceptualized as pluralistic phenomena.

Building on conceptual work that draws a distinction between globally-oriented *hyper norms* (Donaldson & Dunfee, 1995) and locally-oriented *behavioral norms* (Spicer, 2009), I theoretically distinguish between *petty corruption* and *grand corruption* to develop hypotheses pertaining to the relationship between each dimension of corruption and the foreign entry decisions undertaken by MNEs. Trust and learning provide the bases for the central mechanisms upon which the hypotheses are developed in Essay 1. It contributes to the specification of theoretical boundary conditions within and around the *government corruption pervasiveness* construct developed by Rodriguez et al. (2005). It builds on recent international business-oriented business ethics research which has called for the active integration of the theoretical and conceptual traditions of international business strategy scholars and business ethicists, particularly when the research is grounded in the institutional theoretical tradition (Doh, Husted, Matten, & Santoro, 2010). Taken together, the empirical findings and the associated theory in Essay 1 facilitate the linkage between the concept of informal institutions and the notion of pluralism. In this regard, my work is consistent with prior conceptual work that has advocated efforts to pursue theoretical contributions that could emerge from the investigation of pluralistic phenomena, notwithstanding scholars' general preference for parsimony and generalizability in theory-construction (Glynn, Barr, & Dacin, 2000).

## Essay 2

The second essay (Chapter 3) is entitled *Public corruption, private corruption and the structure of equity-based foreign subsidiary investments in emerging markets*. It examines the relationship between the pervasiveness of host market corruption (Rodriguez et al., 2005) and the strategies that MNEs implement with respect to their foreign subsidiary investments. This Essay adopts the more comprehensive definition of corruption (*the abuse of authority for personal gain*) that has been proposed by Aguilera and Vadera (2008). In doing so, it extends the scope of corruption-based inquiry to include aspects of both public sector corruption and private sector corruption through the introduction of new constructs that categorize the phenomenon of host market corruption into two dimensions – *public corruption pervasiveness* and *private corruption pervasiveness*. This Essay seeks to answer the question, *How do public sector corruption and private sector corruption impact upon the foreign-entry strategies of multinational enterprises?*

## Essay 3

The third essay (Chapter 4) is entitled *Corruption pervasiveness, subsidiary localization strategy and host market exit*. It focuses on the MNE's pursuit of external legitimacy and the survival implications associated with various strategic initiatives that are implemented at the subsidiary level to secure legitimacy in increasingly corrupt host market environments. In this context, the strategic insights proffered by resource dependence theory (RDT) and institutional theory are characterized by distinct spatial orientations. RDT predicts that subsidiaries will implement *proximal* (host market-oriented) localization strategies in which local (host country) partners and employees are hypothesized to be best-suited to efforts to enhance the subsidiary's legitimacy and reduce its likelihood of exit from the host country market. Conversely, institutional theory suggests that *distal* (home market-oriented) localization strategies, in which subsidiaries prefer to engage home country partners and employees in the subsidiary investment, are better-suited to reducing the likelihood of subsidiary exit from increasingly corrupt host country market environments. A set of competing hypotheses based on RDT and institutional theory are developed in Essay 3 in order to examine the

relationship between host market corruption levels, MNE strategy and the likelihood of subsidiary exit. The results reveal the relative efficacy of home versus host market-based localization strategies that are designed to facilitate the survival of subsidiaries in increasingly corrupt foreign markets.

## Conclusion

Collectively, this dissertation research makes the following conceptual and empirical contributions:

1. Provides empirical and theoretical support for the foundational theory of host market corruption in international business strategy research (Rodriguez et al., 2005);
2. Extends the conceptualization of host market corruption in terms of its origins (*grand* versus *petty*) and in terms of its sector of origin (*public* versus *private*);
3. Advances theory with respect to the relationship between host market corruption and the subsidiary-level strategies of MNEs;
4. Contributes new tenets to institutional theory by introducing the concepts of *informal institutional pluralism* (conceptualizing informal institutions as pluralistic phenomena), *proximal* (host market-oriented) *localization* and *distal* (home market-oriented) *localization*;
5. Investigates whether MNEs can implement strategies which reduce the likelihood of market exit under conditions of more pervasive host market corruption.

## Dissertation-Related Presentations

Prior to the submission of this dissertation for final examination, the theory, constructs and empirical analyses presented within these three essays have evolved through extensive developmental feedback received from my doctoral supervisor, and through the presentation of the dissertation's constituent essays in multiple public forums. These presentation forums have included doctoral consortiums, academic conferences and invited scholarly presentations. Following my dissertation proposal's defense in April 2013, an overview of my dissertation proposal was presented in Istanbul, Turkey at the *Academy of International Business Annual Meeting* in July 2013 where it was recognized first among 41 other submitted dissertation proposals and awarded the *AIB-Sheth Doctoral Dissertation Proposal Award*. Additionally, my dissertation proposal was

also presented at the *Academy of Management Annual Meeting's* doctoral consortium (*International Management* division) in Orlando, U.S.A. during August 2013.

With respect to Essay 1 (Chapter 2 of this dissertation), earlier versions have been presented at the *Canadian Business Ethics Research Network's* (CBERN) Winter Ph.D. Meeting convened at York University in Toronto, Canada during March 2013; at the *Academy of International Business Annual Meeting* in a competitive session convened by the *Institutions, Governance and Corporate Social Responsibility* interest track in Istanbul, Turkey during July 2013; at the *Strategic Management Society Annual International Conference* in a paper session convened by the *Global Strategy* track in Atlanta, U.S.A. during October 2013; at the *Institutional Capacity and Corruption Symposium* co-convened by the Darla Moore School of Business and the School of Law at the University of South Carolina through the *Rule of Law Collaborative* during April 2014; and, the Essay has recently been accepted for presentation at the *Academy of Management Annual Meeting* in a paper session being convened by the *International Management* division in Philadelphia, U.S.A. during August 2014.

An earlier version of Essay 2 (Chapter 3 of this dissertation) was presented at the *Academy of International Business Annual Meeting* in a competitive session convened by the *Institutions, Governance and Corporate Social Responsibility* interest track in Nagoya, Japan during July 2011.

Finally, an earlier version of Essay 3 (Chapter 4 of this dissertation) has been presented at the *Academy of International Business Annual Meeting* in a competitive session convened by the *Institutions, Governance and Corporate Social Responsibility* interest track in Washington, D.C. during July 2012. More recently, the Essay has been accepted for presentation at the *Academy of Management Annual Meeting* in a paper session being convened by the *International Management* division in Philadelphia, U.S.A. during August 2014.

## **Grammatical Style and References**

While Chapters 1 and 5 of this dissertation have been written using first person singular pronouns ("I", "my"), Chapters 2, 3 and 4 have been written using first person plural pronouns ("we", "our"). This difference in grammatical style was implemented as

a matter of convenience for myself, as I anticipate that it is likely that I will pursue publication of these essays in peer-reviewed academic journals with one or more co-authors in the future. This difference in grammatical style should not be taken to imply anything other than this entire dissertation being my own work. I am the sole author of this thesis. Consistent with this, each of the presentations listed under the *Dissertation-Related Presentations* section of this chapter were presentations of single-authored manuscripts.

This dissertation has been prepared using the Integrated-Article format specified by the School of Graduate and Postdoctoral Studies (SGPS) at Western University, rather than using the Monograph format. In this regard, the Chapters are integrated through theory, empirics, concepts and materials that provide logical connections between the chapters. Consistent with SGPS' Thesis Regulation 8.3 which allows thesis chapters to include unpublished work, in Chapter 3, I have cited the research that I present in Chapter 2. Similarly, in Chapter 4, I have cited the research that I present in both Chapters 2 and 3.



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## CHAPTER 2

### **Institutional Pluralism: Host Market Government Corruption and the Equity-Based Foreign Entry Strategies of Multinational Enterprises**

*The question of how firms...manage when faced with public sector corruption continues to be among the most important and elusive research areas. (Rodriguez, Siegel, Hillman, & Eden, 2006: 736)*

## INTRODUCTION

The macroeconomic consequences of corruption are widely documented in the academic literature. Corruption has been found to adversely impact the flow of foreign direct investment (FDI) into global markets that are perceived to be more corrupt (Habib & Zurawicki, 2002). Further, while Mauro (1995) determined that corruption impaired national development and undermined economic growth, Gupta, Davoodi and Alonso-Terme (2002) concluded that it also distorts the distribution of national income and perpetuates poverty. Notwithstanding these advances regarding the detrimental effects of corruption at the national level, less is known about the relationship between corruption and multinational enterprise (MNE) strategy.

While extant theory has used the terms *government corruption* and *public sector corruption* interchangeably (Rodriguez, Uhlenbruck, & Eden, 2005; Uhlenbruck, Rodriguez, Doh, & Eden, 2006), in the interest of consistency, we adopt the term *government corruption* in our work. We investigate the impact of host market government corruption on the strategic foreign entry decisions of MNEs. Rodriguez et al. (2005) proposed that more pervasive government corruption in host markets will shape the equity-based ownership decisions of foreign-investing MNEs. However, efforts to empirically validate this proposition through the analysis of an MNE's foreign entry mode (joint venture (JV) versus wholly-owned subsidiary (WOS)) did not find a statistically significant relationship between the pervasiveness of host market corruption and an MNE's equity-based foreign entry strategy (Uhlenbruck et al., 2006). These results are surprising when juxtaposed against subsequent work which determined that host market corruption influences the investment behavior of MNEs (Cuervo-Cazurra,

2008b), and exacerbates the pressure on foreign subsidiaries to engage in host market bribery (Spencer & Gomez, 2011). In an effort to reconcile their non-significant empirical results with the foundational theory advanced by Rodriguez et al. (2005), Uhlenbruck et al. (2006: 411) conjectured that “...there may be underlying constructs behind pervasiveness that have conflicting effects on the firm’s choice between joint venture and wholly-owned subsidiary. Further exploration of the institutional underpinnings of the pervasiveness of corruption is an important next step for corruption researchers.” Building on this proposition, we develop more fine-grained theory to extend the conceptualization of *corruption pervasiveness* and employ it to test the aforementioned theory developed by Rodriguez et al. (2005) with respect to the relationship between host market government corruption and the equity-based entry strategies of foreign-investing MNEs.

Institutional theory holds that institutions include both the written rules and the norms of behavior that evolve in order to reduce uncertainty (North, 1990). While strong institutions attenuate uncertainty and facilitate efficient exchange, weak formal institutions in a host market precipitate the formation of institutional voids (North, 1990) which may be filled by informal institutions such as corruption (Puffer, McCarthy, & Boisot, 2010). In this respect, institutions can be a source of uncertainty and risk for internationalizing MNEs. Scholars have routinely formulated theory pertaining to MNE strategies under conditions of heightened institutional uncertainty by employing two constructs (North, 1990). *Formal institutions* are written rules, regulations and laws. *Informal institutions* are norms of behavior, values, practices, conventions and codes of conduct. Given the manifold regulatory regimes and systems of behavioral norms that MNEs encounter, international business strategy scholars frequently enlist the notion of institutional pluralism or, “the situation faced by an organization that operates within multiple institutional spheres” (Kraatz & Block, 2008: 243). However, this body of work has primarily concentrated on institutional pluralism across geographic space, highlighting the institutional diversity that exists between countries (Chan & Makino, 2007), between regions (Arregle, Miller, Hitt, & Beamish, 2013) or between the MNE and its global network of subsidiaries (Kostova & Roth, 2002). We extend this research tradition by focusing further on the concept of institutional pluralism, placing particular

emphasis upon the institutional diversity that exists within individual institutions that prevail in the host country market. A central premise of our work is that host market institutions that have been traditionally recognized as discrete institutions (such as “government corruption”) in the academic literature (Rodriguez et al., 2005) and the business press (The Economist, 2006, 2008), can be conceptualized as pluralistic institutional phenomena constituted by distinct dimensions which are disparate both in their origin and their impact on the foreign entry strategy of MNEs.

Our theory synthesizes insights from institutional theory and integrative social contracts theory, building on conceptual work by Doh, Husted, Matten and Santoro (2010). Institutional theory (IT) suggests that the uncertainty precipitated by informal institutions such as corruption in the host market environment will compel MNEs to implement strategic foreign entry decisions that are designed to attenuate the perceived level of uncertainty that the MNE encounters in the foreign market (Sartor & Beamish, 2014). Integrative social contracts theory (ISCT) proposes that a hierarchy of norms should be used by managers to guide their ethical decision-making. More specifically, ISCT has distinguished between globally-oriented *hyper norms* (Donaldson & Dunfee, 1994; Spicer, Dunfee, & Bailey, 2004) and locally-oriented *behavioral norms* (Spicer, 2009). We leverage this hierarchy of norms framework to inform our institutionally-oriented research. While scholars have traditionally conceptualized and operationalized government corruption as a broad, uniform construct (Uhlenbruck et al., 2006), we contend that this comprehensiveness might be masking more nuanced relationships between host market corruption and the equity-based entry strategies of MNEs. Consistent with this perspective, surveys of industry executives have revealed a more multifaceted conceptualization of the construct, drawing a distinction between *grand* and *petty* forms of corruption (Hardoon & Heinrich, 2011). We believe that this distinction is highly relevant to the work of scholars who are endeavoring to enhance our understanding of the relationship between corruption and firm strategy.

As such, our work is motivated by both: (1) a theoretical question: *Can discrete host market institutions be conceptualized as pluralistic phenomena?*; and, (2) an empirical question pertaining more specifically to the phenomenon of host market government corruption: *Do the different dimensions of government corruption (grand*

*corruption versus petty corruption*) each exert a distinct impact upon the equity-based foreign entry strategies of MNEs? Our work is developed in two stages. First, we theoretically distinguish between *grand corruption* and *petty corruption* in order to formulate hypotheses pertaining to the relationship between each dimension of government corruption and three strategic entry decisions that confront an MNE – namely, its *foreign entry strategy* (*nonequity-based entry* versus *equity-based entry*), its *equity entry strategy* (*JV* versus *WOS*) and its *partnering strategy* (*traditional JV* versus *crossnational JV*). Second, we test these hypotheses with a sample of 727 subsidiaries established in 32 host countries. We find that the results lend general support to our theory that host market institutions can be conceptualized as pluralistic phenomena characterized by distinct dimensions that exert differential impacts on various aspects of an MNE's foreign entry strategy.

Our research makes both theoretical and empirical contributions. Principal among these is our extension of the conceptual domain of institutional pluralism. More specifically, while prior work has focused on the strategic relevance of institutional pluralism precipitated by geographic space, we develop theory which proposes that discrete institutions within a host market can themselves be characterized as pluralistic institutional phenomena, constituted by distinct dimensions that each exert a unique impact upon the strategies of foreign-investing MNEs. Empirically, we independently replicate an important component of Uhlenbruck et al.'s (2006) findings, providing further support for the theory which proposed that MNEs would be more likely to favor nonequity-based entry over equity-based entry under conditions of more pervasive host market government corruption. However, we also present new theory that disaggregates the concept of *government corruption pervasiveness* into two distinct dimensions (*grand corruption pervasiveness* and *petty corruption pervasiveness*). Employing this refined conceptualization, we shed new light on the relationship between the equity-based foreign entry strategy of MNEs and the pervasiveness of government corruption, presenting three new insights. First, we find that more pervasive *grand corruption* increases the likelihood that foreign-investing MNEs will engage in JV investments with host country partners. Second, an increase in the pervasiveness of *petty corruption* was found to prompt the opposite outcome. Namely, under conditions of more pervasive *petty corruption*, firms

that chose to invest through a JV were found to be more likely to engage a partner from the foreign-investing MNE's home country. Third, an increase in the pervasiveness of *petty corruption* was found to attenuate the hypothesized increase in the likelihood that MNEs would invest in JVs with host country (local) partners under conditions of more pronounced *grand corruption pervasiveness*.

## LITERATURE REVIEW

### The Dimensions of Government Corruption

In order to advance understanding with respect to the relevance of host market corruption to the strategy of foreign-investing MNEs, scholars have routinely employed the theoretical paradigm which conceptualizes host market government corruption in terms of its *pervasiveness*, or *the likelihood of encountering corruption in normal interactions with state officials* (Rodriguez et al., 2005: 385). Leveraging this theory, firms have been found to pay larger bribes to government officials in host markets plagued by more pervasive corruption (Lee, Oh, & Eden, 2010). In turn, MNEs have learned to expect heightened costs in markets characterized by more pervasive corruption (Cuervo-Cazurra, 2008a) because corruption has become a regular part of business practices in those countries (Kwok & Tadesse, 2006). As previously indicated, efforts to empirically validate Rodriguez et al.'s (2005) theoretical framework found that an increase in the *pervasiveness* of host market corruption heightens the likelihood that foreign-entering MNEs will choose nonequity modes (arm's-length or contract-based modes of internationalization, such as management contracts and turnkey projects) over equity modes of entry (JV and WOS) (Uhlenbruck et al., 2006). However, the *pervasiveness* of host market corruption has not been found to be a significant predictor of the entry mode (JV versus WOS) executed by MNEs that engaged in equity-based foreign investments (Uhlenbruck et al., 2006). Motivated by their equivocal empirical results, we endeavor to build on Uhlenbruck et al.'s (2006: 411) concluding proposition that "...there may be underlying constructs behind pervasiveness that have conflicting effects on the firm's choice between joint venture and wholly-owned subsidiary."

Consistent with this perspective, Mezias and Mezias (2010: 284) have argued that acknowledging the dimensionality of corruption is required "to enhance understanding of

how firms adapt to global institutional realities.” We use the general definition of government corruption (*the abuse of public power or public office for private benefit*) that has emerged from research in the adjacent fields of economics, law and political science (Bardhan, 1997; Oldenburg, 1987; Treisman, 2000). Among the early studies that encouraged scholars to employ a multidimensional approach in efforts to build on this definition of government corruption, Husted (1999) suggested distinguishing between different instances of corruption based upon factors including, among others, the monetary amount involved in corrupt transactions, and the social or occupational status of the transactions’ recipients. This recommendation is consistent with the language employed by industry executives, non-governmental organizations, governments, parliamentarians and the media when describing government corruption. More specifically, in developing a dictionary of terms used by these diverse public and private sector stakeholders to describe “corruption”, among the principal criteria used by Transparency International to classify the multiple manifestations of government corruption have been “the amount of money lost and...where it occurs” (2009: 14). Accordingly, our work incorporates a consideration of the dimensionality of *corruption pervasiveness* that is based on the distinction between *grand corruption* and *petty corruption*. To do so, we employ Hardoon & Heinrich’s (2011: 18) definitions of *grand corruption* (*improper contributions made to political parties or to high-ranking officials and politicians to achieve influence*), and *petty corruption* (*improper payments to low-level officials to facilitate or speed up administrative processes*).

Economists, legal theorists and business ethicists have generally embraced this dichotomization of government corruption (*grand* versus *petty*) in their research. Aidt, Dutta and Sena (2008) have found that in countries characterized by stronger political institutions, *grand corruption* has a more pronounced negative impact on growth than in countries with weaker political institutions. Similarly, Rose-Ackerman (2002) observed that *grand corruption* produces serious distortions and undermines productive efficiencies such that the national competitiveness of more corrupt countries is reduced substantially. In the case of *petty corruption*, scholars have focused on the adverse corporate effects associated with allowing small disbursements to public officials. Facilitating payments create a culture of corruption in the firm, damage the company’s



reputation and foster the misperception among employees that sustainable competitive advantages can be secured through continued payments to low-level officials (Argandoña, 2005). Moreover, while a facilitation payment is typically small in quantum, in aggregate, *petty corruption* can be costly to firms (Jordan, 2010). In addition to the costs associated with navigating a complex international web of legislation and conventions, some of which prohibit facilitation payments (or, petty bribes) and some of which permit these disbursements, companies that pay petty bribes often become a target for industrious bribe-takers who escalate the frequency and amount of their demands for payment (Argandoña, 2005).

While extant literature supports our two-dimensional conceptual extension of the *corruption pervasiveness* construct, our expectation that each dimension will exert a disparate impact on the equity-based strategy of foreign-investing MNEs is based upon the belief that unique mechanisms underpin the relationship between each dimension of government corruption and MNE strategy. In turn, the uncommon nature of these mechanisms can be attributed to the distinct origins associated with each dimension of *corruption pervasiveness* (*grand* and *petty*). To explicate these distinct origins, we leverage theoretical insights from ISCT pertaining to the existence of a *hierarchy of norms* (Donaldson & Dunfee, 1994, 1999). In doing so, our efforts build upon conceptual work by Doh et al. (2010) who advocate constructive engagement between the international business and business ethics literatures, as well as the active integration of the disciplines' conceptual and theoretical traditions. Given the growing prominence of the institutional context in international business strategy scholarship, they propose that ISCT is particularly well-suited to enriching our understanding with respect to the strategic relevance of phenomena such as government corruption.

### **Integrative Social Contracts Theory: The Hierarchy of Norms**

Scholars maintain that ISCT can be theoretically distinguished from strategy-oriented research on the grounds that ISCT is a normative theory, rather than a predictive theory (Donaldson & Dunfee, 1995). Nonetheless, we believe that the tenets of ICST pertaining to the origins of norms (Donaldson & Dunfee, 2000) or, the *hierarchy of norms* (*hyper norms* and *behavioral norms*), can be leveraged to structure new theory that

facilitates the execution of more fine-grained analyses with respect to the relationship between the foreign-entry strategies of MNEs and host market corruption. Our epistemological perspective is consistent with recent conceptual work by Donaldson (2012) who proposed that predictive management theories can be developed by integrating principles derived from both positivist and normative traditions. In this regard, while ISCT may not be directly useful to our efforts to predict or explain strategic corporate behavior, the theory does offer the potential to enhance our understanding of the context within which host market corruption and MNE foreign entry strategies intersect.

ISCT is concerned with “economic ethics” or principles that delineate the boundaries governing proper behavior in the context of production and exchange (Donaldson & Dunfee, 1999). The theory endeavors to explain the origins of norms, values, behaviors and standards that prevail in communities (Nichols, 2009). According to the precepts of ISCT, host market countries can be assumed to enjoy *moral free space* or, the freedom to establish moral rules applicable to the constituents in the host market. Donaldson and Dunfee (1999: 38) contend that the moral rules adopted by a community “reflect the community’s particular goals, environments, resources, experiences and...specify boundaries for economic behavior, while reflecting the moral preferences of the members of the community.”

Norms that are generated within a host market’s *moral free space* are known as *authentic norms*. An *authentic norm* exists when a community garners a strong consensus with respect to the ethicality of a particular behavior, as well as a strong expectation that community members will act according to the specified behavior (Donaldson & Dunfee, 1999; Spicer, 2009). Locally-oriented *authentic norms* permit particular behaviors or standards to persist in the community. However, ISCT scholars have struggled to reconcile the notion that patently negative behaviors could be characterized as *authentic*, such as when certain acts of corruption become “normalized” in a community (Ashforth & Anand, 2003). Consequently, ISCT theorists have refined the conceptualization of *authentic norms* and introduced the concept of *behavioral norms*. Spicer (2009: 836) has suggested that *behavioral norms* exist when “community members have strong collective

expectations that a certain type of behavior is likely to be displayed, even if there is little consensus that such behavior is ethically desirable.”

It is important to note that the *moral free space* that communities enjoy is not unbounded. ISCT introduces an important qualification to the notion of *moral free space* and a community’s authority to generate *behavioral norms* that permit the persistence of particular moral standards or behaviors in the community (Donaldson & Dunfee, 1994). More specifically, globally-oriented *hyper norms* exist to establish boundaries that operate as ethical constraints around a community’s *moral free space* (Donaldson & Dunfee, 1999). *Hyper norms* are fundamental principles that constitute the standards by which *behavioral norms* are to be judged (Donaldson & Dunfee, 1999). In this regard, *hyper norms* represent a global convergence of beliefs and values (Dunfee & Donaldson, 2002). *Hyper norms* that prohibit specified behaviors effectively preclude the existence of any *behavioral norms* that are formulated in an effort to permit or legitimize behaviors that are prohibited by *hyper norms* (Donaldson & Dunfee, 1994, 1999).

### **Grand Corruption and Petty Corruption: Hyper Norms or Behavioral Norms?; Permissive or Prohibitive?**

In support of our theory-building efforts, we engage in a more rigorous analysis of our two-dimensional conceptualization of the government corruption pervasiveness phenomenon using the ISCT theoretical prism. To reiterate, the tenets of ISCT hold that both *hyper norms* and *behavioral norms* can operate to either prohibit or permit the legitimization of specified behaviors in a host market. However, the existence of a prohibitive *hyper norm* precludes the existence of a permissive *behavioral norm* that could conflict with the prohibitive *hyper norm* (Donaldson & Dunfee, 1994, 1999). Prior conceptual work by ISCT scholars who study corruption has concluded that a global *hyper norm* prohibiting *grand corruption* does exist (Dunfee & Donaldson, 2002; Fritzsche et al., 1995; Nichols, 1996). Conversely, no global *hyper norm* exists which proactively permits *grand corruption* in host countries (Donaldson & Dunfee, 1999), nor does a global *hyper norm* exist that permits *petty corruption* in host countries (Donaldson & Dunfee, 1999). Finally, an application of the core precepts of ISCT suggests that the existence of the aforementioned global *hyper norm* prohibiting *grand corruption*

precludes the existence of any local *behavioral norms* that can be relied upon to permit or to legitimize *grand corruption* in host country markets (Donaldson & Dunfee, 1994, 1999). Table 1 summarizes extant theory with respect to the existence or absence of global *hyper norms* or local *behavioral norms* that either prohibit or permit *grand corruption* and *petty corruption* in host markets.

Table 1 also illustrates that, notwithstanding the considerable theoretical insights proffered by this prior work, four key questions remain unresolved in the corruption-oriented ISCT literature to date (Dunfee & Donaldson, 2002). First, does a global *hyper norm* exist to prohibit *petty corruption*? Second, absent this, do local *behavioral norms* exist to prohibit *petty corruption* in host markets? Third, do local *behavioral norms* exist to permit *petty corruption* in host markets? Fourth, to what extent do local *behavioral norms* prohibiting *grand corruption* exist to reinforce the global *hyper norm* prohibiting *grand corruption*? These four unanswered questions are denoted in Table 1 as “unresolved.”

**TABLE 1**

**Summary of the Tenets of ISCT with Respect to the Existence or Absence of Global *Hyper Norms* or Local *Behavioral Norms* that Either Prohibit or Permit *Grand Corruption* and *Petty Corruption* in Host Markets**

		Grand corruption	Petty corruption
Global hyper norms	Prohibitive	Yes (Fritzsche et al., 1995; Nichols, 1996; Dunfee & Donaldson, 2002)	Unresolved
	Permissive	No (Donaldson & Dunfee, 1999)	No (Donaldson & Dunfee, 1999)
Local behavioral norms	Prohibitive	Unresolved	Unresolved
	Permissive	No (Donaldson & Dunfee, 1994; 1999)	Unresolved

To address these four questions, we are mindful that “the debate over what constitutes a hyper norm has impeded the application of ISCT in real-world empirical settings” (Doh et al., 2010: 488). Despite the inherent challenge that this poses to the work of ISCT theorists, Frederick’s (1991) study is methodologically instructive in

guiding researchers' efforts to determine whether other global *hyper norms* and local *behavioral norms* exist. To ascertain the existence of a global *hyper norm* pertaining to employee health and safety standards, Frederick (1991) scrutinized the written content of intergovernmental conventions and compacts. Notably, extant theory explicitly supports this practice of surveying the formal institutional environment (i.e., written rules, laws and regulations) to garner insights into the informal institutions (i.e., norms of behavior, values, practices) that prevail in a host market. More specifically, the core precepts of institutional theory hold that norms and values (or, informal institutions) are manifestations or elaborations of formal written laws and regulations (North, 1990: 40). Similarly, Ralston's (2008) crossvergence theory of values evolution in societies proposes that the formal legal system is one of the key drivers of the values and business ideologies that prevail in host markets. Accordingly, we expect that the content of existing national legislative provisions and international conventions will provide an indication of the norms that can be expected to prevail in host markets. As such, leveraging Frederick's (1991) methodology, we reviewed both national legislation and international conventions that establish formal rules and laws with respect to corrupt transactions in order to ascertain whether it is plausible to assume either the existence or absence of the global *hyper norms* and local *behavioral norms* that are unconfirmed in the four quadrants of Table 1 (namely, a global *hyper norm* prohibiting *petty corruption*, as well as local *behavioral norms* permitting *petty corruption*, prohibiting *petty corruption* and prohibiting *grand corruption*).

Appendix A lists the legislative standards that prevail in the 32 countries included in our study, as well as two intergovernmental conventions governing the execution of corrupt transactions. Consistent with the theory of Dunfee and Donaldson (2002), Fritzsche et al. (1995) and Nichols (1996), Appendix A provides general support for the prior recognition of a global *hyper norm* prohibiting *grand corruption*, as well as supporting Donaldson and Dunfee's (1994, 1999) theory that the existence of this global *hyper norm* precludes the existence of any local *behavioral norms* that permit or legitimize *grand corruption*. Nearly all of the host markets listed in Appendix A have enacted some form of local legislation that expressly prohibits all acts of *grand*

*corruption*. By deduction, the existence of these national standards also lends support to the widespread existence of local *behavioral norms* that prohibit *grand corruption*.

Conversely, the contents of Appendix A also suggest that there does not appear to be a global *hyper norm* prohibiting *petty corruption*. However, it could be argued that local *behavioral norms* that either prohibit or permit *petty corruption* do exist among the 32 countries that we study. While our legislative review determined that laws exist in 22% of these countries which could be expected to permit *petty corruption* in foreign markets, 16% of the 32 have not enacted any relevant legislation, while the balance have formally prohibited *petty corruption*. The intergovernmental conventions listed in Appendix A also offer modest support for the existence of local *behavioral norms* that permit *petty corruption*. Our conclusions are consistent with recent conceptual work by Spicer (2009) who has suggested that the anecdotal observation of wide-spread, low-level bribery in some host markets might reflect the existence of *behavioral norms* permitting these transactions. In our effort to propose answers to the four unresolved theoretical questions, we present Table 2 which extends the summary of extant theory that we presented in Table 1, by incorporating the findings that emerged from our legislative review for the 32 countries.

**TABLE 2**

**Proposed Extensions to the Tenets of ISCT with Respect to the Existence or Absence of Global *Hyper Norms* or Local *Behavioral Norms* that Either Prohibit or Permit *Grand Corruption* and *Petty Corruption* in Host Markets**

		<b>Grand corruption</b>	<b>Petty corruption</b>
<b>Global hyper norms</b>	<b>Prohibitive</b>	<b>Yes</b> (Fritzsche et al., 1995; Nichols, 1996; Dunfee & Donaldson, 2002)	<b>No</b>
	<b>Permissive</b>	<b>No</b> (Donaldson & Dunfee, 1999)	<b>No</b> (Donaldson & Dunfee, 1999)
<b>Local behavioral norms</b>	<b>Prohibitive</b>	<b>Yes</b>	<b>Yes</b>
	<b>Permissive</b>	<b>No</b> (Donaldson & Dunfee, 1994; 1999)	<b>Yes</b> (Spicer, 2009)

## THEORY AND HYPOTHESES DEVELOPMENT

While institutional theorists maintain that institutions are intended to bring order and efficiency to economic exchange (North, 2005), weak institutions heighten uncertainty for MNEs and increase the costs associated with transacting in foreign markets that lack a strong institutional foundation (Murrell, 2005). Consequently, MNEs will endeavor to execute strategies that are designed to attenuate this institutional uncertainty (Santangelo & Meyer, 2011). However, weak institutions do not exert a uniform impact upon the strategy of foreign-investing MNEs. In fact, the specific type of uncertainty garnered by informal institutions such as corruption is an important determinant of an MNE's strategic foreign entry decisions (Sartor & Beamish, 2014). North (1990: 43) has indicated that scholars should leverage the tenets of transaction cost theory (TCT) in order to more fully comprehend informal institutions because "informal institutions are not directly observable." TCT postulates the existence of two central types of uncertainty. While *behavioral uncertainty* is conceptualized as uncertainty related to the behavior of transaction partners (Griffith, Harmancioglu, & Droge, 2009), *environmental uncertainty* is the inability to predict the external environment within which the MNE and its subsidiaries are situated. One type of environmental uncertainty that is especially relevant to our research context, *response uncertainty*, is "the inability to predict the likely consequences of a response choice" and is expected to be particularly salient "when there is a perceived need to act because a pending event or change is perceived to pose a threat or to provide some unique opportunity to the organization" (Milliken, 1987: 137). While an increase in *behavioral uncertainty* has been found to prompt firms to prefer vertical integration, under conditions of heightened *environmental uncertainty*, firms will choose hybrids (Geyskens, Steenkamp, & Kumar, 2006).

Our literature review pertaining to the dimensionality of government corruption has suggested that *grand* and *petty corruption* can be distinguished qualitatively on the basis of the substantiveness of corrupt transaction payments and the social or occupational status of a transaction's recipient. The two dimensions can also be substantiated theoretically. Our ISCT-motivated legislative review suggests that the origin of the norms that either permit or prohibit *grand corruption* and *petty corruption* in host markets are distinct. In fact, Table 2 reveals that the origin of the overarching

attitude towards *grand corruption* is predominantly global in its orientation, while attitudes and values toward *petty corruption* vary more widely across countries. As such, two key assumptions emerge from Table 2. First, a global *hyper norm* prohibiting corruption does exist. Second, local *behavioral norms* exist which both permit and prohibit *petty corruption*, depending upon the country under consideration.

This theoretical distinction operates as the foundation for the mechanisms (Bromiley & Johnson, 2005; Davis & Marquis, 2005) through which we expect that the equity-based strategies of foreign-investing MNEs will differ under conditions of more pervasive *grand corruption* versus more pervasive *petty corruption*. Uncertainty in the context of corruption is a complex and multifaceted construct (Søreide, 2009). To briefly summarize our theory, we propose that the distinct origins of the norms pertaining to *grand corruption* and *petty corruption* effectively precipitate different types of uncertainty (*environmental* and *behavioral*) for foreign-investing MNEs which, in turn, motivate MNEs to vary their equity-based entry strategies. More precisely, under conditions of more pervasive *grand corruption*, we expect that the primary source of uncertainty will be *environmental (response) uncertainty*, while *behavioral uncertainty* will predominate under conditions of heightened *petty corruption pervasiveness*. As such, we theorize that the relationship between *petty corruption pervasiveness* and equity-based foreign entry strategy will be grounded in trust-based mechanisms due to the fact that *petty corruption* garners more pronounced *behavioral uncertainty* in the host market. Conversely, in the case of *grand corruption*, learning-based mechanisms will govern because *grand corruption* generates heightened *environmental (response) uncertainty*. Figure 3 provides an illustrative overview of our theory, which we present in comparison to our depiction of extant theory in Figure 2.



FIGURE 2

### Extant Conceptualization of Host Market Institutions (Using the Example of Government Corruption)

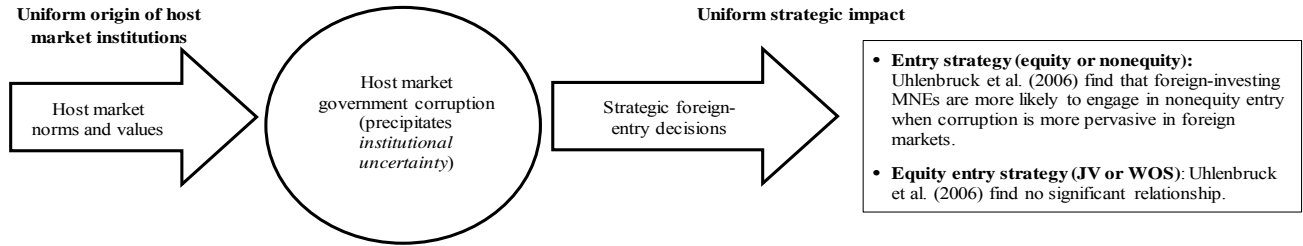
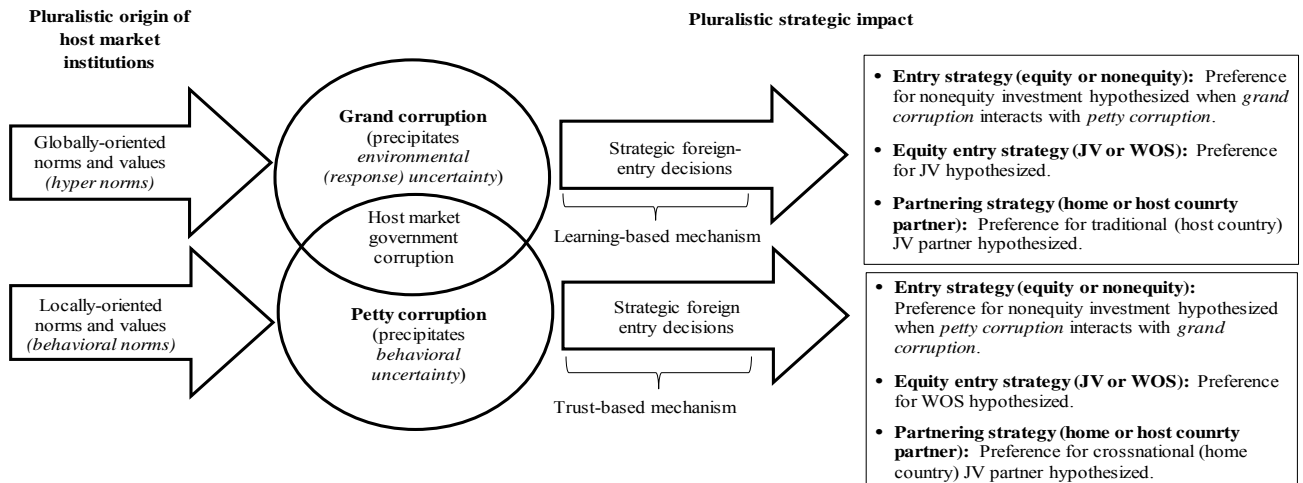


FIGURE 3

### Conceptualizing Host Market Institutions as Pluralistic Phenomena (Using the Example of Government Corruption)



### Grand Corruption, Petty Corruption and Foreign Entry Strategy (Equity Entry Versus Nonequity Entry)

Before we present our theory with respect to the impact of *grand corruption* and *petty corruption* upon the equity-based entry strategies of foreign-investing MNEs, we endeavor to ensure that our conceptual disaggregation of the *corruption pervasiveness* construct is theoretically congruent with prior research that motivates our work

(Rodriguez et al., 2005; Uhlenbruck et al., 2006). While we are not aware of any theoretical basis upon which it could be expected that either *grand corruption pervasiveness* or *petty corruption pervasiveness* would exert a distinct impact upon an MNE's choice between *nonequity*-based foreign market entry and *equity*-based foreign market entry, prior findings within this research domain implicitly suggest that the interaction between *grand corruption* and *petty corruption* should precipitate a preference for *nonequity-based* entry among internationalizing MNEs. Uhlenbruck et al. (2006) found that under conditions of more pervasive government corruption in foreign markets, MNEs were more likely to choose nonequity entry over equity entry. Notably, Uhlenbruck et al.'s (2006) measurement of government corruption was constituted by items which we would characterize as providing an indication of both *grand corruption* and *petty corruption*. They argue that whereas *equity*-based entry exposes the MNE to more frequent and longer-term interaction with potentially corrupt government officials and bureaucrats, *nonequity*-based entry provides the firm with three things - greater flexibility in more corrupt countries, the opportunity to minimize interaction with corrupt foreign governments and lower exit barriers from these markets when corruption levels are perceived to be too costly. Accordingly, we hypothesize that,

*Hypothesis 1: The interaction of grand corruption pervasiveness and petty corruption pervasiveness increases the likelihood that a foreign entrant will engage in nonequity entry.*

### **Grand Corruption and Equity Entry Strategy (JV Versus WOS)**

We have assumed that the worldwide moral, ethical and legal proscription against engaging in *grand corruption* is buttressed by the globally-oriented *hyper norm* that prohibits acts of *grand corruption*. When subsidiaries either receive or extend overtures to engage in *grand corruption* in foreign markets, the parent MNE can expect exposure to a number of positive and negative outcomes. In addition to the increased likelihood of access to potentially lucrative business opportunities and commercial benefits such as monopoly rights or exclusive supplier agreements (Søreide, 2009), another possible result is that a wide range of negative repercussions and sanctions, including adverse reputational effects (Metzger, Dalton, & Hill, 1993), civil penalties and criminal

liabilities may be levied against the firm and its executives (Koehler, 2012). In short, given that *grand corruption* is associated with a wide range of potentially positive and negative results, these transactions are characterized by substantial outcome uncertainty (Søreide, 2009). As such, we expect that foreign entrants into host markets characterized by more pervasive *grand corruption* will perceive more pronounced *environmental (response) uncertainty* which will complicate strategic decision-making and increase the costs of transacting in more corrupt host markets. While this uncertainty can make investing abroad difficult for MNEs, learning how to minimize the likelihood of exposure to the negative repercussions of *grand corruption* and learning how to handle *grand corruption* properly (Habib & Zurawicki, 2002) can contribute to attenuating this uncertainty. Foreign subsidiaries become compelled to learn in order to improve their performance (March, 1991) under conditions of more pronounced *grand corruption pervasiveness*. JV partners are an important source of learning and knowledge for MNEs that choose to enter foreign markets (Inkpen, 2000). Intermediaries such as equity partners who are experienced with *grand corruption* provide the MNE with valuable opportunities to learn how to execute these high risk transactions and to increase the probability of achieving positive outcomes. This learning improves the subsidiary's competence with respect to engaging in these acts of corruption (Ashforth & Anand, 2003; Rodriguez et al., 2005). Further, these intermediaries offer the added benefits of enhancing the enforceability and efficiency of these more costly corrupt transactions, as well as providing the MNE with a degree of exculpability (Lambsdorff, 2013). Accordingly, we hypothesize that,

*Hypothesis 2: A foreign-investing MNE is more likely to engage in joint ownership (JV) of a foreign subsidiary investment under conditions of more pervasive grand corruption.*

### **Grand Corruption and Partnering Strategy (Home Country Partner Versus Host Country Partner)**

Given the hypothesized willingness of MNEs to share ownership under conditions of more pervasive *grand corruption*, foreign MNEs have at least two options with respect to their choice of partner - a host country (local) partner or a home country partner

(Makino & Beamish, 1998). Based on our theory, we anticipate that MNEs will be more likely to select a local partner because a local partner is expected to offer the MNE a better opportunity to attenuate the risks associated with the heightened *environmental (response) uncertainty* precipitated by more pronounced *grand corruption pervasiveness*. Observing local partners engage in corruption contributes to vicarious learning within the foreign subsidiary (Mezias & Mezias, 2010). Local partners are deeply embedded in local social and business networks, in addition to being more intimately familiar with government officials (Meschi, 2009). Consequently, local partners are a particularly potent source of learning for the foreign subsidiary and they may be able to shield foreign subsidiaries from more arbitrary acts of *grand corruption* (Uhlenbruck et al., 2006). As such, we expect that foreign-investing MNEs will prefer to engage local partners in order to gain access to local resources that are needed to navigate the web of host market *grand corruption* more effectively and efficiently (Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003) and to overcome the liability of foreignness attendant with these transactions (Eden & Miller, 2004). The network ties or reputation of local equity partners can constitute intangible strategic assets for the subsidiary (Chen & Hennart, 2002). Foreign MNEs can employ these assets to comply with corrupt norms, while at the same time reducing the costs associated with the liability of foreignness which generally increases when government corruption is more pervasive (Doh et al., 2003; Meschi, 2009). Accordingly, we hypothesize that,

*Hypothesis 3: A foreign-investing MNE is more likely to engage a host country (local) partner, rather than a home country partner, in a foreign subsidiary investment under conditions of more pervasive grand corruption.*

### **Petty Corruption and Equity Entry Strategy (JV Versus WOS)**

We have assumed that, unlike the global *hyper norm* that prohibits *grand corruption* in host markets, local *behavioral norms* that either prohibit or permit *petty corruption* vary widely across countries. Local *behavioral norms* that contribute to the persistence of *petty corruption* in host markets permit these transactions to become institutionalized and a regular part of commercial activity (Anand, Ashforth, & Joshi, 2004). This precipitates substantial institutional uncertainty for foreign-investing MNEs.

Host markets characterized by more pervasive levels of *petty corruption* endure significantly lower levels of trust in government institutions (Doig & Theobald, 1999). In addition to exerting a corrosive impact on trust in administrative procedures (Argandoña, 2005), when *petty corruption* is a common practice in a host market, it causes transaction costs to increase in an unpredictable manner (Kaufman & Wei, 1999) and undermines the efficiency of the business environment. As an example of the cost and inefficiency bred by more pervasive *petty corruption* in foreign markets, British-based multinational alcohol conglomerate Diageo was recently reported as having one of its Guinness delivery trucks stopped at “roadblocks” 47 times during a 500 kilometer trip in the African country of Cameroon (The Economist, 2012).

*Behavioral uncertainty* prevails when lower levels of trust exist in host markets (Brouthers & Brouthers, 2003). Trust has been identified as an important consideration for firms when formulating their market-entry strategies (Beamish & Banks, 1987; Buckley & Casson, 1998). Among the many strategic decisions facing MNEs that establish subsidiaries in foreign markets, the choice of entry mode is contingent upon the level of trust, with an increase in trust precipitating an increase in the use of JVs (Erramilli, 1996). Trust fosters greater certainty with respect to a prospective partner’s anticipated behavior (Madhok, 1995). The existence of trust can attenuate the need for formal controls as a means to enhancing confidence in a partner’s behavior (Das & Teng, 1998). However, behaviorally-based control mechanisms such as trust take time to develop and the effectiveness of these informal control mechanisms may be reduced when cultural differences are more pronounced (Woodcock, Beamish, & Makino, 1994). Similarly, the costs associated with formally monitoring and enforcing property rights in the context of shared governance are significant, particularly when institutions such as those prohibiting *petty corruption* are routinely violated (Reuer & Tong, 2005). Consequently, absent the ability to trust local partners, MNEs will prefer to retain full ownership (Dikova & van Witteloostuijn, 2007). Accordingly, we hypothesize that,

*Hypothesis 4: A foreign-investing MNE is more likely to engage in a wholly-owned foreign subsidiary (WOS) investment under conditions of more pervasive petty corruption.*

### **Petty Corruption and Partnering Strategy (Home Country Partner Versus Host Country Partner)**

Notwithstanding an MNE's hypothesized preference for retaining full ownership under conditions of more pervasive *petty corruption*, some MNEs might still choose to engage a partner in the foreign subsidiary investment. As such, the MNE must select an acceptable partner. We have theorized that trust-based mechanisms undergird the relationship between the pervasiveness of *petty corruption* in the host market and the equity-based entry strategies of foreign-investing MNEs. Consistent with political scientists' conceptualization of trust as being "ultimately dependent on certain characteristics of the (individual or group being) trusted" (Nannestad, 2008: 415), theorists have distinguished between *generalized trust* and *particularized trust*. While *particularized trust* or, in-group trust, is "trust only in people like yourself" (Uslaner, 2005: 77), *generalized trust* or, "trust in people one does not know" (Nannestad, 2008: 418) refers to a broader social trust that includes out-group members.

Trustworthiness has been found to decline when partners hail from different nationalities or races (Glaeser, Laibson, Scheinkman, & Soutter, 2000). Moreover, Li and Wu (2010) have concluded that as the level of corruption in a country increases, *generalized trust* declines and *particularized trust* becomes paramount. Taken together, we would expect that when MNEs invest through JVs in foreign markets under conditions of more pervasive *petty corruption*, a home country partner will be preferred over a host country (local) partner. This strategy seems well advised. JV partners have been found to be more opportunistic when host market institutions are weaker (Luo, 2007). Further, heightened levels of corruption in host markets have been found to amplify the pressure that foreign subsidiaries face to engage in host market bribery, particularly when the parent MNE invests with a local partner (Spencer & Gomez, 2011). As such, we hypothesize that,

*Hypothesis 5: A foreign-investing MNE is more likely to engage a home country partner, rather than a host country (local) partner, in a foreign subsidiary investment under conditions of more pervasive petty corruption.*

## **The Interaction Between Grand Corruption Pervasiveness and Petty Corruption Pervasiveness**

The allocation of organizational attention between competing institutions has become a fertile area of debate for management scholars who research the plurality of institutions (Dunn & Jones, 2010; Molina, 2012). While this discourse has sometimes revolved around an assessment of the relative primacy of competing institutional logics, our theory pertaining to institutional pluralism in the context of increasingly corrupt host foreign market environments is couched in the tradition of transaction cost (TC) scholarship. While TC theory has traditionally been more concerned with the organizational structure that results from the interaction between asset specificity and uncertainty (Williamson, 1985), more recently, scholars have advocated the need to develop theory and investigate the interaction effects that result from different types of uncertainty (Cuypers & Martin, 2009; Miller, 1993). In examining the equity-based entry strategies (or, organizational control decisions) of MNEs that engaged in innovation offshoring, Sartor & Beamish (2014) found that weak informal institutions which precipitate *behavioral uncertainty* effectively moderate the impact of weak informal institutions that induce *environmental (demand) uncertainty* on the foreign entry strategies of MNEs. We have proposed that while an increase in the pervasiveness of *grand corruption* in the host market precipitates more pronounced *environmental (response) uncertainty* for foreign-investing firms, an increase in *petty corruption pervasiveness* heightens *behavioral uncertainty*. As such, applying the theory of Sartor & Beamish (2014), we would expect that the effects of *petty corruption* would predominate over those of *grand corruption* when the two dimensions of corruption interact. Accordingly, we hypothesize that,

*Hypothesis 6: The positive relationship between grand corruption pervasiveness and the likelihood that a foreign-investing MNE will engage in joint ownership (JV) of a foreign subsidiary investment is weakened as petty corruption pervasiveness increases.*

*Hypothesis 7: The positive relationship between grand corruption pervasiveness and the likelihood that foreign-investing MNEs will invest through a JV with a host country (local) partner is weakened as petty corruption pervasiveness increases.*

## METHODS

### Data Sources and Key Variables

We tested our hypotheses using a sample of 727 subsidiaries established in 32 countries<sup>1</sup> between 2004 and 2007. Our study period was determined by the availability of country data pertaining to the pervasiveness of *petty corruption* and *grand corruption* in the host foreign markets. Information pertaining to the foreign subsidiary investments was gathered from the 2004-2007 editions of the *Kaigai Shinshutsu Kigyō Souran*, a compendium of Japanese global FDI that has been shown to be close to the population of foreign affiliates of public and private Japanese companies (Hennart, 1991; Yamawaki, 1991). Observations pertaining to the dependent variables in our study were lagged by one year relative to the observations pertaining to the measures of *petty corruption* and *grand corruption*.

Building on Rodriguez et al.'s (2005: 385) extant conceptualization of host market corruption in terms of its *pervasiveness* or, “the likelihood of encountering corruption in normal interactions with state officials”, we have proposed that the concept of *government corruption* should be disaggregated according to the extensiveness of the payment and the status of the recipient. In order to develop measures for both *grand corruption* (*improper contributions made to political parties or to high-ranking officials and politicians to achieve influence*), and *petty corruption* (*improper payments to low-level officials to facilitate or speed up administrative processes*) (Hardoon & Heinrich, 2011: 18), we selected items from the *Global Competitiveness Reports* (GCR). The GCR collects executive opinion survey data to gauge the perceptions of international business executives with respect to the prevailing economic and business environment in host markets around the world. Based on our theory, data pertaining to five different indicators of the pervasiveness of host market government corruption were taken from the GCR surveys and subjected to factor analysis. We executed a principal components analysis with an orthogonal (varimax) rotation which suggested a two factor solution

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<sup>1</sup> The number of subsidiary investments in each country is in brackets: Argentina (2), Australia (4), Austria (1), Belgium (9), Brazil (5), Canada (2), China (348), Czech Republic (7), France (8), Germany (12), Hong Kong (22), Hungary (2), India (20), Indonesia (13), Italy (2), Korea (38), Luxembourg (1), Malaysia (6), Mexico (8), Netherlands (13), New Zealand (2), Philippines (9), Poland (7), Russia (8), Singapore (18), South Africa (2), Spain (3), Switzerland (1), Taiwan (21), Thailand (58), United Kingdom (11), United States (64).



(using an eigenvalue cutoff of 1), the results of which are presented in Table 3. Consistent with our theory, three items (*irregular payments in public utilities*; *irregular payments in loan applications*; and, *irregular payments in tax collection*) were found to load in a manner that reflected our adopted definition of *petty corruption* (*improper payments to low-level officials to facilitate or speed up administrative processes*). Only one item (*the prevalence of illegal political donations*) was found to be related to the definition of *grand corruption* (*improper contributions made to political parties or to high-ranking officials and politicians to achieve influence*). The fifth and final item in our factor analysis (*irregular payments in government policymaking*) exhibited a high cross-loading on both the factor indicating *petty corruption* (0.75) and on the *grand corruption* factor (0.62). Given the high cross-loading, we dropped the item from the composition of the *petty corruption* latent construct. However, given the definition of *grand corruption* that we adopted (*improper contributions made to political parties or to high-ranking officials and politicians to achieve influence*), we reasoned that the item which demonstrated a high cross-loading (*irregular payments in government policymaking*) exhibited a degree of face validity which made it plausible that the item could be an indicator of *grand corruption*. As such, we developed two measures to operationalize *grand corruption* in our regression models. First, *grand corruption* was constituted as a dual-item latent construct (incorporating both *the prevalence of illegal political donations*, and *irregular payments in government policymaking*). Second, we also operationalized *grand corruption* as a single-item construct (using *the prevalence of illegal political donations* indicator alone). Although both the single-item construct and the dual-item construct were developed to operationalize *grand corruption* in our regression models, to avoid any confusion, we refer to the dual-item construct as *grand corruption*, while the single-item construct is referred to as *illegal political donations*. One benefit associated with constituting the *grand corruption* variable both as a single-item latent construct, and also as dual-item construct, is that it provides a built-in robustness check of our regression estimations with respect to *grand corruption*. The Cronbach's alpha for *petty corruption* (0.97) and the dual-item measure of *grand corruption* (0.75) both exceeded the 0.70 cutoff specified by Nunnally & Bernstein (1994).

**TABLE 3**  
**Factor Analysis Results**

<b>Construct and associated items</b>		<b>Factor loading</b>
<b>Petty corruption pervasiveness:</b>		Cronbach's alpha: <b>0.97</b>
Irregular payments in public utilities	In your industry, how commonly would you estimate that firms make undocumented extra payments or bribes when getting connected to public utilities (eg, telephone or electricity)? (1 = common, 7 = never occurs).	0.97
Irregular payments in loan applications	In your industry, how commonly would you estimate that firms make undocumented extra payments or bribes connected with loan applications? (1 = common, 7 = never occurs).	0.97
Irregular payments in tax collection	In your industry, how commonly would you estimate that firms make undocumented extra payments or bribes connected with annual tax payments? (1 = common, 7 = never occurs).	0.94
<b>Grand corruption pervasiveness:</b>		Cronbach's alpha: <b>0.75</b>
Prevalence of illegal political donations	How common are illegal donations to political parties in your country? (1 = common, 7 = never occurs).	0.99
Irregular payments in government policymaking	In your industry, how commonly would you estimate that firms make undocumented extra payments or bribes connected with influencing laws and policies, regulations, or decrees to favor selected business interests? (1 = common, 7 = never occurs).	0.62

Given that the *petty corruption* and *grand corruption* constructs were based upon raw data in which higher scores indicate lower levels of corruption, to enhance the ease of interpreting our results, we reverse-coded the raw data so that more pervasive *petty corruption* and *grand corruption* would be indicated by higher scores. Furthermore, our measures of *petty corruption* and *grand corruption* provide an indication of the absolute level of each type of corruption in the host market, consistent with leading conceptual and empirical strategy work pertaining to corruption (Rodriguez et al., 2005; Uhlenbruck et al., 2006).

### **Dependent Variables**

We tested the impact of more pervasive host market *petty corruption* and *grand corruption* upon three strategic decisions executed by MNEs with respect to their subsidiary investments – *foreign entry strategy*, *equity entry strategy* and *partnering strategy*.

***Foreign Entry Strategy.*** *Foreign entry strategy* captures the MNE's choice between *nonequity*-based foreign market entry and *equity*-based foreign market entry (JV or, WOS). While *nonequity* foreign market entry has been recognized in the literature as including transactions such as exporting, licensing and franchising, the measurement of *nonequity entry* is made more difficult by the shortage of statistical data pertaining to *nonequity transactions* (UNCTAD, 2011). In addition to the lack of data, the measurement of *nonequity* entry is also complicated by the fact that "...the web of directly-owned, partially-owned, contract-based and arm's-length forms of international operation...is tangled and some of the distinctions between the different modes are blurred" (UNCTAD, 2011: 130). In the absence of the relevant statistics needed to measure *nonequity* entry, UNCTAD (2011) has advocated the use of estimates pertaining to the scale and scope of *nonequity* transactions. Pan & Tse (2000: 539) have noted that *equity* entry can be distinguished from *nonequity* entry on the basis of "resource commitment, risk, return, (and) control." Similarly, Uhlenbruck et al. (2006: 404) suggest that *equity* entry, unlike *nonequity* entry, can be evidenced by a degree of "ownership and control involving a long-term commitment to the country."

In order to gauge the degree of ownership and control that an MNE exercises with respect to a foreign subsidiary investment, extant research has employed measures pertaining to the MNE's commitment of equity capital (Malhotra & Gaur, 2014) and human capital to the investment (Caligiuri & Stroh, 1995; Shay & Baack, 2004). When a MNE retains less than 5% of the equity in a foreign corporate entity, researchers have routinely regarded this more nominal commitment of equity capital as a portfolio investment by the MNE, rather than as an equity-based foreign subsidiary investment (Brouthers, 2002; Dhanaraj & Beamish, 2004). Similarly, subsidiaries which employ fewer than twenty individuals are more likely to be sales offices or sales agencies designed to facilitate export sales, and are less likely to be equity-based foreign subsidiary investments (Beamish & Inkpen, 1998). Building on Uhlenbruck et al.'s (2006) conceptualization of *equity entry* as including foreign investments characterized by a degree of ownership and control that indicates a long-term commitment to the host country, in addition to the body of work that has specified threshold levels of equity capital and human capital that are pertinent to the distinction between *equity entry* and *nonequity entry*, we operationalized *nonequity entry* as those foreign entries in which the focal MNE owned less than 5% of the equity and fewer than twenty employees were enlisted to staff the overseas office associated with the investment. Based on this operationalization, 74 (10.2%) of the 727 entry events in our sample were categorized as *nonequity entries*, while 653 (89.8%) were *equity entries*.

***Equity Entry Strategy.*** *Equity entry strategy* captures the MNE's choice between a JV and a WOS when making an *equity*-based foreign investment. This distinction was defined according to two conventions employed in the literature. We estimated models using both an 80 percent equity ownership cutoff and a 95 percent equity ownership cutoff to distinguish JVs from WOSs (Yiu & Makino, 2002). Employing both definitions in our estimations provided us with an opportunity to test the robustness of our results. While the regression models that we report in the regression tables employ the dependent variable that is based on the 80 percent equity ownership cutoff, we also report the results using the 95 percent cutoff in the footnotes at the end of the *Results* section. Utilizing the 80 percent equity ownership cutoff to distinguish between JVs and WOSs, 432 (66.2%) of the 653 *equity entries* were categorized as WOSs and 221 (33.8%) were JVs

(compared to 397 (60.8%) and 256 (39.2%) respectively using the 95 percent cutoff). We integrated the measurement of both of the aforementioned strategic decisions (*foreign entry strategy* and *equity entry strategy*) by employing a trichotomous dependent variable which included *nonequity*, *joint venture* and *wholly-owned subsidiary* as the three possible outcomes.

**Partnering Strategy.** The taxonomy of JV partnerships developed by Makino and Beamish (1998) was utilized to measure the *partnering strategy* employed by firms that organized their foreign entry through a JV ownership structure. As such, each JV in our sample was categorized as either a *cross-national JV* (a JV in which the MNE engages a home country equity partner) or a *traditional JV* (in which the MNE engages a host country equity partner). Makino and Beamish's (1998) taxonomy includes a third category of JV - *trinalational JV* (a JV in which the MNE engages a partner from a foreign country other than the MNE's home country). Consistent with their observation that the *trinalational JV* occurs less frequently (constituting only 2.4% of the JVs in their study), only 4.5% of the JVs in our sample were *trinalational JVs* (10 investments). As such, our models with respect to the *partnering strategy* dependent variable focused on the distinction between *traditional JVs* and *cross-national JVs*. Employing the 80 percent cutoff, 171 (81.1%) of the remaining 211 JVs were categorized as *traditional JVs* and 40 (18.9%) were categorized as *crossnational JVs*, while 193 (78.5%) and 53 (21.5%) were categorized as *traditional JVs* and *crossnational JVs* respectively using the 95 percent cutoff.

### Control Variables

We included variables in our study to control for country, regional, temporal, industry, parent MNE and subsidiary-level effects. We controlled for *subsidiary size* and *subsidiary capitalization* using data pertaining to, respectively, the total number of employees in the subsidiary and the subsidiary's total capitalization. Several parent MNE-level variables, including firm size (Boyacigiller, 1990; Stopford & Wells, 1972), leverage (Reuer & Ragozzino, 2006), profitability and international experience (Johanson & Vahlne, 1977; Makino & Delios, 1996), have also been found to influence the decisions of MNEs with respect to elements of firm strategy such as entry strategy and

partner choice. *Size* was measured using the parent's total sales while *leverage* was measured using the difference between total assets and total debt as a percentage of total assets to control for slack financial resources (Reuer & Ragozzino, 2006). We controlled for *profitability* using the parent's return on assets. We measured *experience* in terms of the number of subsidiary years of prior experience in the same host market. Given that a firm's status as a service industry constituent has been found to predict its foreign entry strategies (Brouthers & Brouthers, 2003; Erramilli & Rao, 1993), we employed a dummy variable to control for industry effects by categorizing firms as either service or non-service entities. Annual exchange rates for Japanese currency (JPY/USD) were used to control for temporal effects (Klein & Rosengren, 1994). We controlled for regional effects (Rugman & Verbeke, 2004) using a dummy variable which we used to distinguish subsidiaries hosted in Asian countries from subsidiaries established in other regions. Prior studies have also revealed that the economic, institutional and cultural environment impacts MNEs' strategic entry decisions. *Host market size* was measured using a host country's total gross domestic product (Uhlenbruck et al., 2006). *FDI restrictions* in the host market (Gomes-Casseres, 1990) were measured using data from the Heritage Foundation's *Investment Freedom Index* where a higher score indicates a less restrictive investment regime. The degree of *infrastructure development* (Uhlenbruck et al., 2006), in the host country was based on data from IMD's *World Competitiveness Yearbooks*. The dependent variable was lagged by one year relative to the annual observations with respect to these covariates. *Cultural distance* was calculated between Japan and the host countries using Hofstede's scores (2001) and Kogut & Singh's (1988) cultural distance measure. Skewed control variables (*subsidiary size*, *subsidiary capitalization*, *parent size* and *host market size*) were log transformed before we tested our hypotheses (Tabachnick & Fidell, 2007).

### **Estimation Methods**

To investigate the effects of *grand corruption pervasiveness* and *petty corruption pervasiveness* on a MNE's *foreign entry strategy* (nonequity entry versus equity entry), we executed multinomial logistic regression models in which nonequity entry was designated as the reference group that was compared to two other possible outcomes in

the dependent variable (JV or, WOS). The hypotheses pertaining to an MNE's *equity entry strategy* (JV versus WOS) and *partnering strategy* (traditional JV partnership versus crossnational JV partnership) were tested using binary logistic regression. While the regression models in Table 5 test Hypothesis 1 which predicts that MNEs will be more likely to engage in nonequity entry under the combined effect of more pervasive *grand corruption* and *petty corruption*, the models in Table 6 test Hypotheses 2, 4 and 6 pertaining to both the main effects and interaction effect of *grand* and *petty corruption* on a firm's *equity entry strategy* (JV or, WOS). Finally, Table 7 presents the results of the regression models that were executed to test Hypotheses 3, 5 and 7 with respect to the main and interaction effects associated with the two dimensions of host market corruption on an MNE's *partnering strategy*. Before investigating the effects of any of the interaction terms in our models, the focal independent variables (*petty corruption* and *grand corruption*) were centered about the mean (Aiken & West, 1991).

## RESULTS

Descriptive statistics for our sample are presented in Table 4. Tables 5, 6 and 7 present the results of the regression estimations conducted in order to test our hypotheses. Our conclusion that multicollinearity was not a concern in our models is supported by the fact that all of the variance inflation factor (VIF) scores reported for our models in Tables 5-7 are less than the maximum VIF (10) that is prescribed in global strategy research for regression analyses (Reuer & Leiblein, 2000). Further, none of the correlations for variables in the same models exceed the recommended cutoff of 0.70 (Tabachnick & Fidell, 2007).

In each of Tables 5-7, we first present a base model which excludes the effects of the focal corruption variables, along with models that introduce the effects associated with *grand* and *petty corruption*.<sup>2</sup> Table 5 illustrates the results of the multinomial logistic regression models that were executed to test Hypothesis 1 pertaining to *foreign*

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<sup>2</sup> The regression results reported in Tables 5-7 employ the 80 percent cutoff convention used to distinguish between JVs and WOSs. The results using the 95 percent cutoff (Yiu & Makino, 2002) were largely similar, with the primary exceptions being that the interaction effect in Model 1F, the main effect of *grand corruption* in Model 3 and the main effect of *petty corruption* in Model 3C and 3E became non-significant. In all cases, the focal independent variables became only marginally non-significant. Further, the signs of each of these coefficients continued to be consistent with our theory.

**TABLE 4**  
**Descriptive Statistics and Correlations**

Variable	Mean	S.D.	1	2	3	4	5	6	7	8	9
1 Foreign entry strategy <sup>a</sup>	-	-									
2 Partnering strategy <sup>b</sup>	-	-	0.91								
3 Subsidiary size (log)	1.13	0.70	0.32	0.31							
4 Subsidiary capitalization (log)	2.29	1.00	0.12	0.11	0.14						
5 Parent size (log)	5.23	0.91	0.16	0.11	0.27	0.12					
6 Parent profitability (ROA)	0.06	0.08	0.02	0.02	-0.05	-0.05	0.02				
7 Parent leverage	0.83	0.12	-0.09	-0.08	-0.11	-0.06	-0.45	0.26			
8 Parent experience	173.94	499.02	0.15	0.12	0.12	0.03	0.58	-0.05	-0.46		
9 Industry dummy	-	-	-0.05	-0.07	-0.11	0.00	0.05	-0.03	-0.25	0.12	
10 Exchange rate	0.01	0.00	-0.01	-0.02	0.01	0.00	0.01	0.02	0.00	-0.03	-0.01
11 Region dummy	-	-	0.19	0.17	0.20	0.17	-0.05	-0.02	0.03	-0.10	0.03
12 Host market size (log)	3.05	0.55	-0.06	0.01	0.02	-0.07	-0.06	-0.06	-0.06	0.07	0.04
13 Infrastructure development	5.42	1.43	-0.14	-0.10	-0.18	-0.15	-0.13	-0.02	0.07	-0.01	-0.06
14 FDI restrictions	5.19	2.57	-0.11	-0.13	-0.20	-0.16	0.00	-0.02	0.02	0.02	-0.09
15 Cultural distance	2.69	0.61	0.01	0.03	-0.01	0.03	0.06	-0.04	-0.04	0.04	0.10
16 Petty corruption	1.92	0.76	0.17	0.17	0.25	0.17	0.09	0.00	-0.06	-0.02	0.08
17 Grand corruption	2.33	0.77	0.09	0.05	0.09	0.07	0.16	0.02	-0.03	0.03	0.02
18 Illegal political donations	2.36	1.01	0.05	-0.01	0.02	0.02	0.14	0.02	-0.01	0.02	-0.01
19 Petty corruption x grand corruption	0.30	0.81	-0.13	-0.09	-0.13	-0.04	0.06	0.00	-0.04	0.06	0.04
20 Petty corruption x illegal political donations	0.18	0.91	-0.10	-0.07	-0.10	0.00	0.08	0.00	-0.06	0.06	0.06

Variable	10	11	12	13	14	15	16	17	18	19
11 Region dummy	0.04									
12 Host market size (log)	0.03	-0.25								
13 Infrastructure development	0.15	-0.11	-0.02							
14 FDI restrictions	-0.02	-0.43	-0.29	0.40						
15 Cultural distance	0.04	0.00	-0.08	0.19	-0.20					
16 Petty corruption	-0.05	0.55	0.09	-0.69	-0.59	-0.10				
17 Grand corruption	-0.08	0.08	-0.24	-0.61	0.16	-0.35	0.53			
18 Illegal political donations	-0.05	-0.07	-0.32	-0.45	0.36	-0.38	0.24	0.94		
19 Petty corruption x grand corruption	-0.04	-0.25	-0.34	0.28	0.14	0.50	-0.40	-0.29	-0.19	
20 Petty corruption x illegal political donations	-0.07	-0.17	-0.34	0.17	0.09	0.54	-0.25	-0.21	-0.18	0.96

<sup>a</sup> Trichotomous dependent variable: *Non-equity entry*, *joint venture* or *wholly-owned subsidiary*.

<sup>b</sup> Dichotomous dependent variable: *Traditional joint venture* or *crossnational joint venture*.

Correlations with an absolute value greater than 0.08 are statistically significant at the  $p < 0.05$  level. All are two-tailed tests.



TABLE 5

**Results of Regression Analyses of Grand Corruption Pervasiveness and Petty Corruption Pervasiveness on *Foreign Entry Strategy***

Variables	Foreign Entry Strategy <sup>a</sup>					
	Base Model		Interaction Effect		Interaction Effect	
	Model 1A Wholly-owned	Model 1B Joint venture	Model 1C Wholly-owned	Model 1D Joint venture	Model 1E Wholly-owned	Model 1F Joint venture
Intercept	2.77 (4.69)	0.83 (5.15)	2.22 (4.75)	1.61 (5.22)	2.25 (4.74)	1.46 (5.22)
<i>Subsidiary effects</i>						
Subsidiary size (log)	1.03 (0.28) ***	1.69 (0.29) ***	1.03 (0.28) ***	1.68 (0.29) ***	1.04 (0.28) ***	1.68 (0.29) ***
Subsidiary capitalization (log)	-0.07 (0.16)	0.13 (0.17)	-0.07 (0.16)	0.12 (0.17)	-0.07 (0.16)	0.13 (0.17)
<i>Parent effects</i>						
Parent size (log)	-0.65 (0.21) **	-0.41 (0.23) <sup>t</sup>	-0.64 (0.21) **	-0.38 (0.23) <sup>t</sup>	-0.65 (0.21) **	-0.38 (0.23) <sup>t</sup>
Parent profitability (ROA)	2.48 (1.54)	2.41 (1.98)	2.45 (1.54)	2.41 (2.01)	2.47 (1.54)	2.42 (2.01)
Parent leverage	0.67 (1.32)	-0.38 (1.46)	0.77 (1.34)	-0.50 (1.48)	0.76 (1.33)	-0.49 (1.47)
Parent experience	0.00 (0.01) <sup>t</sup>	0.00 (0.01) **	0.00 (0.01)	0.00 (0.01) **	0.00 (0.01)	0.00 (0.01) **
<i>Industry effects</i>						
Industry dummy	0.99 (0.31) **	0.76 (0.34) *	0.99 (0.31) **	0.73 (0.35) *	0.99 (0.31) **	0.74 (0.35) *
<i>Temporal effects</i>						
Exchange rate <sup>b</sup>	0.59 (4.87)	1.03 (5.31)	1.10 (4.91)	0.59 (5.38)	113.37 (493.34)	54.69 (539.7)
<i>Region effects</i>						
Region dummy	-0.69 (0.36) <sup>t</sup>	-1.37 (0.42) ***	-0.77 (0.47) <sup>t</sup>	-1.04 (0.52) *	-0.82 (0.46) <sup>t</sup>	-1.09 (0.52) *
<i>Country effects</i>						
Host market size (log)	-0.23 (0.27)	-0.14 (0.31)	-0.15 (0.31)	-0.42 (0.36)	-0.10 (0.31)	-0.37 (0.36)
Infrastructure development	0.01 (0.12)	-0.23 (0.13) <sup>t</sup>	-0.03 (0.17)	-0.22 (0.19)	-0.01 (0.17)	-0.24 (0.19)
FDI restrictions	-0.09 (0.08)	0.02 (0.09)	-0.06 (0.09)	-0.02 (0.11)	-0.08 (0.09)	0.00 (0.1)
Cultural distance	0.39 (0.25)	0.34 (0.28)	0.31 (0.28)	0.59 (0.32) <sup>t</sup>	0.26 (0.29)	0.56 (0.33) <sup>t</sup>
<i>Main effects</i>						
Petty corruption			0.06 (0.42)	-0.10 (0.46)	-0.04 (0.35)	0.01 (0.39)
Grand corruption			-0.12 (0.35)	0.00 (0.39)		
Illegal political donations					-0.01 (0.22)	-0.01 (0.25)
<i>Interaction effects</i>						
Petty corruption x grand corruption			0.12 (0.25)	-0.52 (0.28) <sup>t</sup>		
Petty corruption x illegal political donations					0.17 (0.21)	-0.39 (0.24) <sup>t</sup>
Variance inflation factor range	1.04 - 2.28		1.05 - 5.94		1.05 - 4.31	
$\chi^2$	175.05 ***		190.20 ***		190.46 ***	
R <sup>2</sup> (ΔR <sup>2</sup> )	0.26		0.28 (0.02)		0.28 (0.02)	

<sup>a</sup> The reference group in the multinomial logistic regression models is *non-equity entry* which is compared to two other possible outcomes in the *foreign entry strategy* dependent variable: *wholly-owned subsidiary* and *joint venture*.

<sup>b</sup> Rescaled by a factor of 10<sup>-2</sup>.

*n* = 727.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Standard errors are in parentheses.

TABLE 6

**Results of Regression Analyses of Grand Corruption Pervasiveness and Petty Corruption Pervasiveness on *Equity Entry Strategy***

Variables	Equity Entry Strategy <sup>a</sup>									
	Base Model		Main Effects				Interaction Effects			
	Model 2A		Model 2B		Model 2C		Model 2D		Model 2E	
Intercept	-3.15	(3.24)	-3.27	(3.29)	-3.25	(3.29)	-1.20	(3.32)	-1.40	(3.32)
<i>Subsidiary effects</i>										
Subsidiary size (log)	0.63	(0.14) ***	0.63	(0.14) ***	0.63	(0.14) ***	0.62	(0.14) ***	0.61	(0.14) ***
Subsidiary capitalization (log)	0.21	(0.09) *	0.21	(0.09) *	0.21	(0.09) *	0.20	(0.09) *	0.21	(0.09) *
<i>Parent effects</i>										
Parent size (log)	0.23	(0.14) <sup>t</sup>	0.23	(0.14) <sup>t</sup>	0.23	(0.14) <sup>t</sup>	0.24	(0.14) <sup>t</sup>	0.25	(0.14) <sup>t</sup>
Parent profitability (ROA)	-0.06	(1.68)	-0.05	(1.68)	-0.05	(1.68)	0.02	(1.69)	0.01	(1.69)
Parent leverage	-1.03	(0.96)	-1.07	(0.97)	-1.06	(0.97)	-1.27	(0.98)	-1.22	(0.97)
Parent experience	0.00	(0.01) <sup>t</sup>	0.00	(0.01) <sup>t</sup>	0.00	(0.01) <sup>t</sup>	0.00	(0.01) <sup>t</sup>	0.00	(0.01) <sup>t</sup>
<i>Industry effects</i>										
Industry dummy	0.25	(0.23)	0.25	(0.23)	0.25	(0.23)	0.28	(0.24)	0.29	(0.24)
<i>Temporal effects</i>										
Exchange rate <sup>b</sup>	0.46	(3.22)	0.35	(3.23)	0.35	(3.24)	-0.75	(3.3)	-0.86	(3.31)
<i>Region effects</i>										
Region dummy	0.72	(0.31) *	0.74	(0.36) *	0.73	(0.36) *	0.30	(0.38)	0.31	(0.37)
<i>Country effects</i>										
Host market size (log)	0.15	(0.23)	0.18	(0.25)	0.18	(0.25)	-0.18	(0.27)	-0.18	(0.27)
Infrastructure development	-0.24	(0.09) **	-0.22	(0.12) <sup>t</sup>	-0.23	(0.12) <sup>t</sup>	-0.20	(0.13)	-0.23	(0.13) <sup>t</sup>
FDI restrictions	0.12	(0.06) *	0.10	(0.08)	0.10	(0.07)	0.05	(0.08)	0.10	(0.07)
Cultural distance	-0.02	(0.18)	0.00	(0.19)	0.00	(0.19)	0.30	(0.21)	0.32	(0.21)
<i>Main effects</i>										
Petty corruption			-0.08	(0.29)	-0.04	(0.25)	-0.15	(0.29)	0.05	(0.26)
Grand corruption			0.11	(0.25)			0.11	(0.26)		
Illegal political donations					0.06	(0.16)			-0.01	(0.16)
<i>Interaction effects</i>										
Petty corruption x grand corruption							-0.64	(0.18) ***		
Petty corruption x illegal political donations									-0.55	(0.16) ***
Variance inflation factor range	1.04 - 2.41		1.04 - 5.88		1.05 - 4.24		1.05 - 5.92		1.06 - 4.24	
$\chi^2$	96.97 ***		97.16***		97.12***		111.83 ***		111.94 ***	
R <sup>2</sup> ( $\Delta R^2$ )	0.19		0.19 (0.00)		0.19 (0.00)		0.22 (0.03)		0.22 (0.03)	

<sup>a</sup> The dependent variable *equity entry strategy* is coded as follows: 0: *wholly-owned subsidiary*; 1: *joint venture*.

<sup>b</sup> Rescaled by a factor of 10<sup>-2</sup>.

*n* = 653.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Standard errors are in parentheses.

TABLE 7

**Results of Regression Analyses of Grand Corruption Pervasiveness and Petty Corruption Pervasiveness on *Partnering Strategy***

Variables	Partnering Strategy <sup>a</sup>									
	Base Model		Main Effects				Interaction Effects			
	Model 3A		Model 3B		Model 3C		Model 3D		Model 3E	
Intercept	-3.68	(7.02)	-4.21	(7.53)	-4.79	(7.48)	-3.66	(7.49)	-3.35	(7.45)
<i>Subsidiary effects</i>										
Subsidiary size (log)	-0.09	(0.29)	-0.20	(0.29)	-0.20	(0.29)	-0.21	(0.29)	-0.21	(0.3)
Subsidiary capitalization (log)	-0.17	(0.19)	-0.20	(0.19)	-0.20	(0.19)	-0.20	(0.19)	-0.20	(0.2)
<i>Parent effects</i>										
Parent size (log)	-0.34	(0.28)	-0.36	(0.31)	-0.37	(0.29)	-0.36	(0.29)	-0.37	(0.3)
Parent profitability (ROA)	1.31	(4.14)	2.27	(4.41)	2.24	(4.39)	2.27	(4.39)	2.26	(4.39)
Parent leverage	1.71	(2.18)	1.80	(2.22)	1.72	(2.21)	1.81	(2.22)	1.83	(2.23)
Parent experience	0.00	(0.01)	0.00	(0.01)	0.00	(0.01)	0.00	(0.01)	0.00	(0.01)
<i>Industry effect</i>										
Industry dummy	-0.40	(0.53)	-0.49	(0.56)	-0.51	(0.55)	-0.49	(0.56)	-0.50	(0.55)
<i>Temporal effects</i>										
Exchange rate <sup>b</sup>	0.15	(0.69)	0.21	(0.71)	0.26	(0.71)	0.20	(0.72)	0.21	(0.72)
<i>Region effects</i>										
Region dummy	-0.81	(0.68)	-1.71	(0.89) <sup>t</sup>	-1.74	(0.89) <sup>*</sup>	-1.73	(0.94) <sup>t</sup>	-1.92	(0.93) <sup>*</sup>
<i>Country effects</i>										
Host market size (log)	1.03	(0.55) <sup>t</sup>	0.77	(0.59)	0.75	(0.59)	0.76	(0.61)	0.69	(0.6)
Infrastructure development	0.01	(0.22)	-0.04	(0.28)	0.00	(0.28)	-0.05	(0.29)	-0.06	(0.3)
FDI restrictions	-0.05	(0.13)	0.24	(0.19)	0.18	(0.18)	0.24	(0.19)	0.19	(0.18)
Cultural distance	-0.14	(0.48)	-0.20	(0.52)	-0.22	(0.52)	-0.18	(0.56)	-0.08	(0.58)
<i>Main effects</i>										
Petty corruption			1.83	(0.73) <sup>*</sup>	1.36	(0.64) <sup>*</sup>	1.82	(0.73) <sup>*</sup>	1.39	(0.65) <sup>*</sup>
Grand corruption			-1.31	(0.66) <sup>*</sup>			-1.32	(0.67) <sup>*</sup>		
Illegal political donations					-0.72	(0.39) <sup>t</sup>			-0.79	(0.42) <sup>t</sup>
<i>Interaction effects</i>										
Petty corruption x grand corruption							-0.05	(0.59)		
Petty corruption x illegal political donations									-0.32	(0.56)
Variance inflation factor range	1.06 - 2.85		1.07 - 4.42		1.07 - 3.86		1.07 - 4.47		1.08 - 3.87	
$\chi^2$	19.60		27.43 <sup>*</sup>		26.64 <sup>**</sup>		27.43 <sup>*</sup>		27.01 <sup>*</sup>	
R <sup>2</sup> ( $\Delta R^2$ )	0.14		0.20 (0.06)		0.19 (0.05)		0.20 (0.06)		0.19 (0.05)	

<sup>a</sup> The dependent variable *partnering strategy* is coded as follows: 0: *traditional joint venture* (with a host country / local partner); 1: *crossnational joint venture* (with a home country partner).

<sup>b</sup> Rescaled by a factor of 10<sup>-3</sup>.

*n* = 211.

<sup>t</sup> *p* < 0.10; <sup>\*</sup> *p* < 0.05; <sup>\*\*</sup> *p* < 0.01; <sup>\*\*\*</sup> *p* < 0.001

All are two-tailed tests. Standard errors are in parentheses.

*entry strategy*. The results of Models 1D and 1F are both consistent with and lend further support to the theory and empirical findings of Uhlenbruck et al. (2006) who found that MNEs were more likely to engage in nonequity-based foreign entry rather than equity-based foreign entry under conditions of more pervasive host market *government corruption*. To reiterate, we believe that their broad measure of *government corruption* effectively incorporated indicators pertaining to both *petty corruption* and *grand corruption*. As such, we replicated Uhlenbruck et al.'s (2006) results by investigating the how the interaction between *grand corruption* and *petty corruption* impacted upon an MNE's choice between nonequity-based and equity-based entry. Model 1D ( $\chi^2 = 190.20$ ,  $p < 0.001$ ,  $R^2 = 0.28$ ) suggests that MNEs are more likely to engage in nonequity entry than equity entry via a JV investment when *petty corruption* interacts with our two-indicator measure of *grand corruption* ( $\beta = -0.52$ ,  $p < 0.10$ ). Further, Model 1F ( $\chi^2 = 190.46$ ,  $p < 0.001$ ,  $R^2 = 0.28$ ) also suggests that interaction effect between *grand* and *petty corruption* will precipitate an increased likelihood that MNEs will choose nonequity- over equity-based entry when *grand corruption* is measured using only the pervasiveness of *illegal political donations* in the host market ( $\beta = -0.39$ ,  $p < 0.10$ ). Notably, the results of Model 1C ( $\beta = 0.12$ ,  $p > 0.05$ ) and Model 1E ( $\beta = 0.17$ ,  $p > 0.05$ ) indicate that the interaction between *grand* and *petty corruption* does not exert a significant effect upon an MNE's choice between nonequity-based foreign entry and equity entry via a WOS. As such, we find partial support for Hypothesis 1.

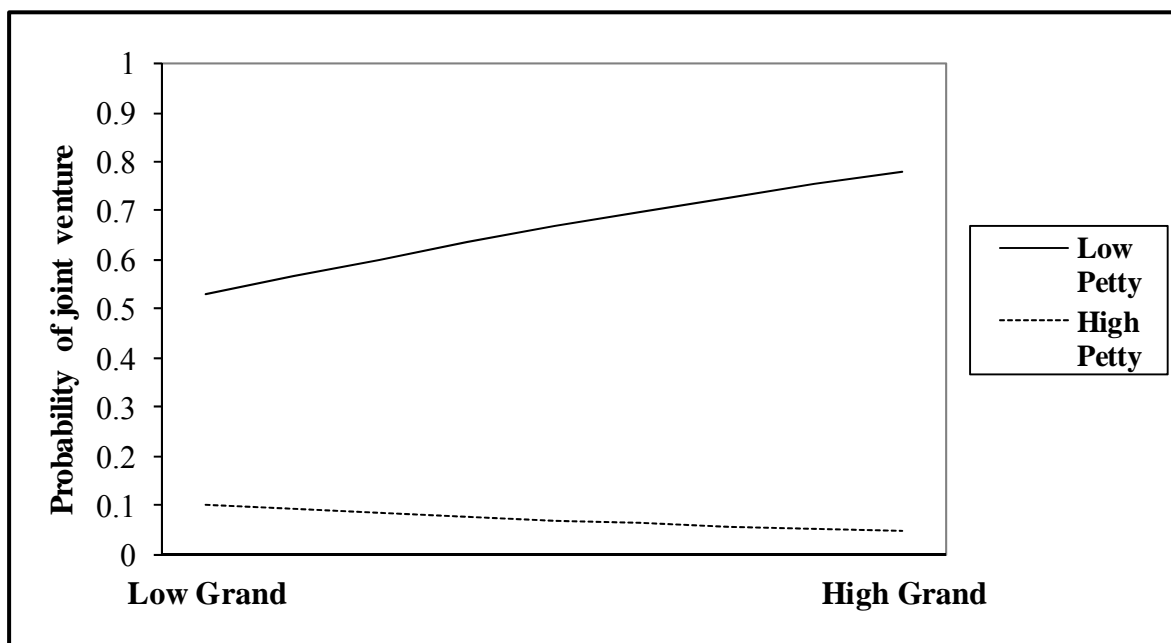
Table 6 presents the results of the regression models that were executed to test the hypotheses pertaining to an MNE's *equity entry strategy* (JV or, WOS). While the signs of the coefficients for the main effects of *grand* and *petty corruption* in Models 2B and 2C are consistent with our theory, the results indicate that these main effects do not exert a statistically significant impact upon the choice of equity-based foreign entry mode. However, the results reported in Model 2D ( $\chi^2 = 111.83$ ,  $p < 0.001$ ,  $R^2 = 0.22$ ) and Model 2E ( $\chi^2 = 111.94$ ,  $p < 0.001$ ,  $R^2 = 0.22$ ), which introduce the interaction effects, indicate that the combined effect of the two dimensions of government corruption in the host market is significant. More precisely, the interaction effect in Model 2D ( $\beta = -0.64$ ,  $p < 0.001$ ), in which *grand corruption* is operationalized as a two-indicator measure, reveals that the increased likelihood of an MNE engaging in a JV under conditions of more

pervasive *grand corruption* is weakened by an increase in the pervasiveness of *petty corruption* in the host market environment. Similar results were observed for Model 2E ( $\beta = -0.55$ ,  $p < 0.001$ ), in which *grand corruption* is measured using only the pervasiveness of *illegal political donations* in the host market. Figure 4 illustrates the interaction effect between *grand* and *petty corruption pervasiveness* on an MNE's *equity entry strategy* (Aiken & West, 1991; Dawson, 2014). The Figure suggests that at lower levels of *petty corruption*, MNEs are increasingly likely to engage in a JV in host markets under conditions of more pervasive *grand corruption*. However, this likelihood is diminished as *petty corruption* becomes more pervasive.

Finally, Table 7 reports the results of our regression analyses with respect to the main and interaction effects associated with *grand* and *petty corruption* upon an MNE's *partnering strategy*. While the interaction effects in Model 3D and Model 3E were not significant, the results reported for the main effects of *grand* and *petty corruption pervasiveness* in Model 3B (Grand:  $\beta = -1.31$ ,  $p < 0.05$ ; Petty:  $\beta = 1.83$ ,  $p < 0.05$ ;  $R^2 = 0.20$ ), Model 3C (Grand:  $\beta = -0.72$ ,  $p < 0.10$ ; Petty:  $\beta = 1.36$ ,  $p < 0.05$ ;  $R^2 = 0.19$ ), Model 3D (Grand:  $\beta = -1.32$ ,  $p < 0.05$ ; Petty:  $\beta = 1.82$ ,  $p < 0.05$ ;  $R^2 = 0.20$ ) and Model 3E (Grand:  $\beta = -0.79$ ,  $p < 0.10$ ; Petty:  $\beta = 1.39$ ,  $p < 0.05$ ;  $R^2 = 0.19$ ) were all highly consistent with our theory. These results support our contention that an increase in the pervasiveness of *grand corruption* bolsters the likelihood that an MNE will engage a host country (local) partner in a *traditional JV* investment, while an increase in *petty corruption pervasiveness* heightens the likelihood that an MNE will engage a home country partner through a *crossnational JV* arrangement (if the MNE chooses to invest through a JV).

FIGURE 4

**Interaction Effect of Grand Corruption Pervasiveness and Petty Corruption Pervasiveness on *Equity Entry Strategy* <sup>a</sup>**



<sup>a</sup> High Petty and Low Petty refer to petty corruption pervasiveness one standard deviation above and below the mean for petty corruption pervasiveness. Likewise, High Grand and Low Grand refer to grand corruption pervasiveness one standard deviation above and below the mean for grand corruption pervasiveness.

## DISCUSSION AND CONCLUSIONS

Government corruption is a prominent example of an informal institution operating within a host market's borders (Calhoun, 2002; Eden & Miller, 2004). Our work has been motivated by both a theoretical question (*Can discrete host market institutions be conceptualized as pluralistic phenomena?*), and an empirical question pertaining more specifically to the phenomenon of host market government corruption (*Do the different dimensions of government corruption (grand corruption versus petty corruption) each exert a distinct impact upon the equity-based foreign entry strategies of MNEs?*). In developing this research, we have responded to the enduring challenge posed by Glynn, Barr and Dacin (2000: 726) whose work reminds scholars of the need to consciously balance the competing demands of parsimony and accuracy in theory-building efforts when they observe that “the focus in much...theorizing is to homogenize what is essentially a pluralistic world...the result has been to overlook the variety embedded in plurality...To capture a more accurate and nuanced view of the world...scholars need to incorporate more explicitly diversity...” Consistent with this perspective, researchers in the neighboring academic disciplines of economics and law have cautioned against the development of theory which suggests that firms respond uniformly to all dimensions of corruption and instead, they contend that different types of government corruption might have different implications for firm strategy (Søreide, 2009). To this end, institutional theorists have suggested that whereas some “researchers consider corruption to be just another application of preexisting theories without sufficiently considering their adequacy...we may fail to understand corruption without considering its intrinsic dynamics and logic. Applying old theories then falls short of an adequate understanding of the phenomenon” (Lambsdorff, 2007: 1).

Our work makes a number of conceptual contributions, both through the introduction of new theory and through the validation of prior theory. First, we have theorized that discrete informal institutions (such as government corruption) can be conceptualized as pluralistic phenomena characterized by distinct dimensions that exert differential impacts on various aspects of an MNE's equity-based foreign entry strategy. We have facilitated this extension to IT by synthesizing insights from ISCT which advocates the recognition of a hierarchy of norms. Leveraging this theory, we concluded

that the origin of the overarching prohibition against *grand corruption* is predominantly global in its orientation, while attitudes and values toward *petty corruption* vary more widely across countries. Given this, we proposed that the distinct origins of the norms pertaining to *grand corruption* and *petty corruption* effectively precipitate different types of uncertainty (*environmental* and *behavioral*) for foreign-investing MNEs which, in turn, motivate MNEs to vary their equity-based entry strategies. More precisely, under conditions of more pervasive *grand corruption*, we theorized that the primary source of uncertainty will be *environmental (response) uncertainty*, while *behavioral uncertainty* will predominate under conditions of heightened *petty corruption pervasiveness*. As such, we proposed that the relationship between *petty corruption pervasiveness* and equity-based foreign entry strategy would be grounded in trust-based mechanisms due to the fact that *petty corruption* induces more pronounced *behavioral uncertainty* in the host market. Conversely, in the case of *grand corruption*, learning-based mechanisms should predominate because *grand corruption* generates heightened *environmental (response) uncertainty*.

Our results reveal that government corruption is, in fact, more nuanced than has been previously recognized in the literature. We found that an increase in the pervasiveness of *grand corruption* and *petty corruption* precipitated distinctly different strategic responses from foreign-investing MNEs. More specifically, while the heightened pervasiveness of *grand corruption* increased the likelihood that foreign-investing MNEs would engage in JV investments with host country partners, an increase in the pervasiveness of *petty corruption* was found to precipitate the opposite outcome. Namely, under conditions of more pervasive *petty corruption*, firms that chose to invest through a JV were found to be more likely to engage a partner from the foreign-investing MNE's home country. Further, an increase in the pervasiveness of *petty corruption* was found to reduce the hypothesized increased likelihood that MNEs would invest in JVs under conditions of more pronounced *grand corruption pervasiveness*. Our conceptual disaggregation of the government corruption pervasiveness construct has yielded empirical results that are theoretically relevant and cast new light on the relationship between the pervasiveness of corruption in the host market and the equity-based entry strategies of MNEs. Upon finding that the pervasiveness of government corruption was



not a statistically significant predictor of an MNE's equity-based foreign investment strategy, Uhlenbruck et al. (2006) speculated that the government corruption construct may be multidimensional. Our work effectively presents evidence in support of their proposition's validity.

Second, our finding that the interaction between more pervasive levels of *grand corruption* and *petty corruption* would increase the likelihood that MNEs would choose nonequity entry over equity-based (joint venture) entry independently replicates the results proffered by Uhlenbruck et al. (2006). They found that MNEs were more likely to invest through nonequity modes when government corruption was more pervasive in the host market. As such, our work provides further empirical support for the theory of Rodriguez et al. (2005) which first introduced the *corruption pervasiveness* construct.

Third, while scholars have frequently enlisted the broad notion of institutional pluralism, their work has primarily focused upon institutional pluralism across geographic space, highlighting the institutional diversity that exists between countries, between regions or between the MNE and its expansive subsidiary network. We have extended this research tradition by examining the concept of institutional pluralism more narrowly, focusing specifically on the institutional diversity that exists within a discrete institution that prevails in the host country market. In doing so, we provide the impetus for further inquiry into the strategic relevance of pluralistic host market institutions, both formal and informal. Our theory suggests that similarly nuanced strategic responses might be expected when MNEs encounter equally complex, potentially-pluralistic host market institutions such as political power which emanates from the local, provincial and national domains of the host market, as one example (Kozhikode & Li, 2012).

Fourth, by integrating conceptual insights from IT and ISCT to inform our theory-building efforts, we have not only advanced the corruption-oriented international business strategy research agenda, we have also contributed to the business ethics research domain. More specifically, in Table 1, we identified four questions that had yet to be resolved with respect to the existence or absence of *hyper norms* and *behavioral norms* pertaining to corruption. Our review of the prevailing legislative standards pertaining to acts of corruption in the countries that we studied presented evidence that supports the recognition of the existence of local *behavioral norms* that prohibit *grand*

*corruption*, as well as local *behavioral norms* that either permit or prohibit *petty corruption*, depending upon the country under consideration. Further, our legislative review also suggested that a global *hypernorm* prohibiting *petty corruption* does not exist. These findings should be of interest to scholars whose business ethics research assumes a global focus, particularly given that approximately 80% of worldwide FDI flows during our period of study terminated in either Japan or one of the 32 host countries included in our study (UNCTAD, 2004-2007). In this regard, our research supports Doh et al.'s (2010: 483) contention that "IB (international business) and its disciplinary antecedents may usefully inform BE (business ethics) research."

Finally, our work also extends recent theory developed by Sartor and Beamish (2014) with respect to informal institutions. In their effort to develop a theoretical framework that could be used to enhance scholars' comprehension of informal institutions, they argue that the type of uncertainty precipitated by informal institutions is central to understanding the impact of these institutions on the organizational control decisions of foreign-investing MNEs. Motivated by their concern that informal institutions are frequently aggregated and characterized as being conceptually synonymous with culture, they disaggregated the *informal institutions* construct and proposed that informal institutions should be categorized based on the uncertainty that they generate – behavioral or environmental (technological or demand). We extend the scope of their theory by employing it to disaggregate and identify distinct dimensions (*grand corruption* and *petty corruption*) within an informal institution that has traditionally been recognized as a discrete informal institution ("government corruption"). More specifically, in explicating the mechanisms behind the relationships that we hypothesized, we proposed that *grand corruption* and *petty corruption* would generate more pronounced *environmental (response) uncertainty* and *behavioral uncertainty* respectively. Our empirical findings were broadly supportive of this theory.

### **Limitations and Future Directions**

Notwithstanding the contributions that emanate from our work, we acknowledge several limitations. First, our empirics are based on a sample of firms that originate from a single home country. Future work should seek to confirm our findings with a sample

constituted by MNEs that are headquartered in one or more countries other than Japan. Second, while Rodriguez et al.'s (2005) foundational theory with respect to the relationship between host market government corruption and the foreign entry strategies of MNEs introduced theory pertaining to both the *pervasiveness* and the *arbitrariness* of host market corruption, we lacked sufficient data to develop and test theory pertaining to the *arbitrariness* of each dimension of corruption that we studied. However, future research should seek to build and test theory with respect to *grand corruption arbitrariness* and *petty corruption arbitrariness*, focusing particularly on the interaction between the two constructs, as well as between the *pervasiveness* and *arbitrariness* of both *grand* and *petty corruption*.

Our work also poses implications for future research that should be considered within the domain of corruption-oriented international business scholarship. Following the stock market collapses in 2000 and 2008, parliamentarians, non-governmental organizations and business ethicists (Aguilera & Vadera, 2008; Aldrichi, 2009; Andriyanto, 2011; Argandoña, 2003; Gopinath, 2008) have all become increasingly concerned with another type of corruption that exists without the involvement of bureaucrats or government officials – private sector corruption. Notwithstanding the need to better understand this phenomenon, the work of international business strategy scholars has continued to focus on public sector corruption (or, government corruption) to the exclusion of private sector corruption. Our theory pertaining to the pluralistic nature of discrete host market informal institutions such as corruption provides the theoretical foundation upon which an even more robust conceptualization of “host market corruption”, construed more broadly to include private sector corruption, could be cultivated. Developing theory pertaining to the impact of host market *private corruption* on the strategic behavior of foreign-investing MNEs would provide an opportunity to unpack the *corruption pervasiveness* concept further. Finally, building on our work pertaining to a host market's informal institutions, researchers should also investigate the prevalence of institutional plurality within the domain of a host market's formal institutions. Each of these research endeavors could contribute to ameliorating scholars' concerns that “pluralism, if undefined and unquestioned, will continue to compromise the accuracy of organizational theories” (Glynn et al., 2000: 732).

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## APPENDIX A

### Summary of National Legislative Provisions and Intergovernmental Conventions Used to Evaluate the Existence or Absence of Laws Either Prohibiting or Permitting Grand Corruption or Petty Corruption Towards Public Sector Officials

Country	Grand Corruption		Relevant Legislation	Petty Corruption	
	Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?		Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?
International	No	No	OECD Convention <sup>a</sup>	No	Yes (but policy change pending) (Jordan, 2010).
International	No	No	United Nations Convention Against Corruption <sup>b</sup>	No	Defers to national laws.
Argentina	No	No	National Penal Code	No	No
Australia	No	No	Criminal Code Act	No	Yes
Austria	No	No	Criminal Code	No	No
Belgium	No	No	Criminal Code	No	No
Brazil	No	No	Criminal Code	No	No
Canada	No	No	Corruption of Foreign Public Officials Act; Criminal Code	No	Yes
China	No	No	Criminal Law; Foreign Bribery Article	No	No
Czech Republic	No	No	Criminal Code; Commercial Code; Accounting Act; Conflict of Interests Act; Capital Markets Act	No	No
France	No	No	Criminal Act; French Penal Code; French Code of Criminal Procedure	No	No

<sup>a</sup> OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

<sup>b</sup> United Nations Convention Against Corruption.

## APPENDIX A (continued)

Country	Grand Corruption		Relevant Legislation	Petty Corruption	
	Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?		Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?
Germany	No	No	Criminal Code; EU Corruption Act; International Corruption Act	No	No
Hong Kong	No	No	Prevention of Bribery Ordinance; Local bribery laws.	No	No
Hungary	No	No	Criminal Code	No	No
India	No	No	Prevention of Corruption Act; Foreign Contribution Regulation Act; Central Vigilance Commission Act	No	Not explicitly prohibited by law.
Indonesia	No	No	Criminal Code; Eradication of the Criminal Act of Corruption; Anti-Corruption Law (forthcoming)	No	Not explicitly prohibited by law.
Italy	No	No	Criminal Code	No	No
Japan	No	No	Penal Code; Unfair Competition Prevention Act	No	Only if the payment results in illicit gains to the official.

### APPENDIX A (continued)

Country	Grand Corruption		Relevant Legislation	Petty Corruption	
	Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?		Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?
Korea	No	No	Criminal Code; Specific Economic Crimes Act; Anti-Corruption Act;	No	Yes
Luxembourg	No	No	Penal Code	No	No
Malaysia	No	No	Malaysian Anti-Corruption Commission Act; Customs Act; Anti-Money Laundering and Anti-Terrorism Financing Act	No	No
Mexico	No	No	Federal Criminal Code; Federal Law on Administrative Accountability of Public Officials	No	No
Netherlands	No	No	Criminal Code	No	Yes
New Zealand	No	No	Crimes Act; Bribery of Foreign Public Officials Act	No	Yes
Philippines	No	Not explicitly prohibited by law.	Revised Penal Code; Anti-Graft and Corrupt Practices Act	No	Not explicitly prohibited by law.
Poland	No	No	Criminal Code	No	No
Russia	No	No	Criminal Code; Federal Law on Counteraction Against Corruption	No	No
Singapore	No	Not explicitly prohibited by law.	Penal Code; Prevention of Corruption Act	No	No

## APPENDIX A (continued)

Country	Grand Corruption		Relevant Legislation	Petty Corruption	
	Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?		Permissible Towards Domestic Public Officials?	Permissible Towards Foreign Public Officials?
South Africa	No	No	Prevention and Combating of Corruption Act	No	No
Spain	No	No	Criminal Code	No	No
Switzerland	No	No	Penal Code; Unfair Competition Act	No	Yes
Taiwan	No	No	Criminal Code; Corruption Punishment Statute; Money Laundering Control Act; Political Donations Act; Lobbying Act	No	No
Thailand	No	Not explicitly prohibited by law.	Criminal Code	No	Not explicitly prohibited by law.
United Kingdom	No	No	Bribery Act; Anti-Terrorism, Crime and Security Act	No	Law is uncertain.
United States	No	No	United States Code (Title 18 - Federal Crimes); Foreign Corrupt Practices Act	No	Yes (facilitation payments)

## CHAPTER 3

### **Public Corruption, Private Corruption and the Structure of Equity-Based Foreign Subsidiary Investments in Emerging Markets**

#### INTRODUCTION

While corruption has received considerable attention as an imposing force that influences the level and global directionality of foreign investment (Cuervo-Cazurra, 2008a; Habib & Zurawicki, 2002), less attention has been given to the impact of corruption on multinational enterprise (MNE) strategy (Mezias & Mezias, 2010). We investigate the foreign entry strategies of MNEs under conditions of more pervasive host market corruption, focusing specifically on the experience of developed market MNEs that invest in emerging markets. In 2012, foreign direct investment (FDI) flows into developing economies exceeded the inflows to developed economies for the first time ever (UNCTAD, 2013). Given the growing prominence of emerging markets as a global destination for FDI from developed markets (UNCTAD, 2012), and in light of the endemic nature of corruption in these host markets presumed by both academics (Khanna & Palepu, 2010; Sharma, 2010) and the business media (Barchfield, 2014), a strong imperative exists to enhance our comprehension of the impact of corruption upon the strategic decisions of MNEs that enter into emerging markets (Rodriguez, Siegel, Hillman, & Eden, 2006).

To date, our understanding of the relationship between corruption and firm strategy has been characterized as embryonic (Rodriguez et al., 2006) for two principal reasons. First, although theoretically-motivated studies of corruption have primarily employed two perspectives - institutional theory (IT) and transaction cost economics (TCE), more often, corruption-based studies have used an empirically-driven, atheoretical lens (Judge, McNatt, & Xu, 2010). Second, while scholarly efforts to advance the conceptualization of corruption have prompted international strategy researchers to focus on manifestations of *public sector corruption* (Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003; Uhlenbruck, Rodriguez, Doh, & Eden, 2006), international business ethics scholars have increasingly advocated the need to incorporate considerations of *private sector corruption* (Aguilera & Vadera, 2008; Argandoña, 2003; Gopinath, 2008).

Coincident with this divergence in the stream of corruption research, Rodriguez et al. (2006: 739) have suggested that “scholarship on corruption would benefit from more attention to definitions. Corruption is still most commonly defined to preclude private corruption.”

As such, we build on extant MNE theory that conceptualizes host market corruption and its impact on MNE strategy in terms of the *pervasiveness* of corruption (Rodriguez, Uhlenbruck, & Eden, 2005) and we introduce two more explicit latent constructs – *public corruption pervasiveness* and *private corruption pervasiveness*. Our conceptual work is grounded in recent research within the domain of corruption-oriented international business scholarship (Sartor, 2014) which has built on the notion of institutional pluralism or, “the situation faced by an organization that operates within multiple institutional spheres” (Kraatz & Block, 2008: 243) While international business research has traditionally focused on the strategic relevance of institutional pluralism precipitated by the geographic space that exists between countries (Chan & Makino, 2007), between regions (Arregle, Miller, Hitt, & Beamish, 2013) and even between the MNE and its global network of subsidiaries (Kostova & Roth, 2002), more recently, researchers have proposed that discrete institutions within a host market can themselves be characterized as pluralistic institutional phenomena “constituted by distinct dimensions....which are disparate both in their origin and their impact on the foreign entry strategy of MNEs” (Sartor, 2014). In finding that an increase in the pervasiveness of *grand corruption* and *petty corruption* precipitated distinctly different strategic responses from foreign-investing MNEs, Sartor (2014) determined that government corruption is more nuanced than has been previously recognized in the international business strategy literature. His results and the associated theory lend support to the proposition advanced by Uhlenbruck et al. (2006: 411) who suggested that their own non-significant findings with respect to the relationship between government corruption and MNE strategy might be attributable to “underlying constructs behind (government corruption) pervasiveness that have conflicting effects on the firm’s choice between joint venture and wholly-owned subsidiary.”

Building on this theoretical foundation, and motivated by Uhlenbruck et al.’s (2006: 411) suggestion that “further exploration of the institutional underpinnings of the



pervasiveness of corruption is an important...step for corruption researchers”, we develop more fine-grained theory to further extend the conceptualization of *corruption pervasiveness*. Moreover, we employ our theory to introduce new insights into the relationship between host market corruption (which we conceptualize as including both *public sector corruption* and *private sector corruption*) and the equity-based entry strategies of foreign-investing MNEs. To do so, we focus on explicating the theoretical mechanism that substantiates our expectation that each dimension of corruption (*public* and *private*) will exert a disparate impact on the strategies of foreign-investing MNEs. More specifically, we draw upon the research tradition in which a MNE’s foreign market entry and ongoing operations have been conceptualized in terms of its bargaining power in the host country (Fagre & Wells Jr, 1982; Kobrin, 1987). Subsequent conceptual advances in bargaining power theory by joint venture and alliance scholars have extended this theory to elaborate two primary types of bargaining power (Ren, Gray, & Kim, 2009; Yan & Gray, 2001). While *context-based bargaining power* focuses on the power that an MNE derives from possessing outside alternatives during a negotiation, *resource-based bargaining power* focuses on the power that an MNE obtains from both its financial and noncapital resources. When MNEs enter into foreign markets, they routinely engage in both public sector transactions (or, transactions with the government) and private sector transactions (transactions with private entities, companies and individuals) (Teegen, Doh, & Vachani, 2004). We propose that the primary type of bargaining power upon which an MNE relies may differ for its public sector transactions and its private sector transactions. More precisely, we theorize that an MNE’s reliance on different sources of bargaining power functions as the mechanism through which *public corruption* and *private corruption* impact upon the foreign entry strategy of the MNE. Consequently, despite the fact that we anticipate that the two types of corruption will be highly correlated, we expect that MNEs will employ different entry strategies under conditions of more pronounced *public* versus *private corruption pervasiveness* in foreign host markets.

Employing these two new corruption constructs, we explore the impact of heightened host market corruption upon three foreign market entry decisions considered by an MNE – its *foreign entry strategy*, *equity entry strategy* and *partnering strategy*. Our theory predicts that when *public corruption* in the host market is more pervasive, MNEs

will be more likely to enter through a joint venture (JV) with a host country partner, rather than a home country partner. Conversely, heightened *private corruption pervasiveness* will precipitate entry via a wholly-owned subsidiary (WOS). Further, given that public and private corruption are widely regarded as existing simultaneously in host markets (Rodriguez et al., 2006), we theorize that the interaction effect between both types of corruption should result in an MNE's preference for shared ownership with host country partners under conditions of heightened *public corruption pervasiveness* being moderated by an increase in the pervasiveness of *private corruption*.

In addition to refining the conception of corruption to incorporate both its public and private sector dimensions, our empirical analysis provides support for and extends extant theory pertaining to the relationship between host market corruption and firm strategy (Rodriguez et al., 2005). Further, by focusing on the role of a firm's bargaining power in shaping its strategic foreign entry decisions under conditions of more pervasive host market corruption, our work contributes to efforts to more closely integrate market and nonmarket strategy research. More specifically, we draw attention to an important theoretical mechanism that could also be used to bridge the institutionally-oriented and resource-oriented perspectives that have been advocated by strategy theorists as a means to enhance our understanding of the strategic relevance of contemporary nonmarket phenomena such as corruption (Doh, Lawton, & Rajwani, 2012).

## LITERATURE REVIEW

### **Conceptualizing Corruption: Public and Private Corruption Pervasiveness**

Extant research in economics, law and political science (Bardhan, 1997; Oldenburg, 1987; Treisman, 2000) has defined corruption as the abuse of public power or public office for private benefit. While the received definition of corruption is parsimonious, it has limited the scope of strategy-based inquiry to purely public realms (Argandoña, 2003; Gopinath, 2008; Husted, 1994). The failure to incorporate considerations of *private sector corruption* into strategy scholarship risks muting the more fine-grained insights that can be garnered by corruption-oriented research (Milliken, 1987). In this regard, our efforts to theoretically and empirically extend the construct to include *private sector corruption* are motivated, in part, by Kurer (2005) who

has lamented the lack of theoretical progress in defining and measuring corruption during the past 40 years.

Given that “corruption involves expropriating what rightfully belongs to others” (Uslaner, 2005: 77), we conceptualize corruption as an informal institutional constraint that undermines property rights (Eden & Miller, 2004; North, 1990) and heightens the degree of uncertainty encountered by internationalizing MNEs (Miller, 1992). *Informal institutional pluralism* is a concept that has been developed to describe the properties of informal institutions that have been traditionally recognized as discrete institutions within a host market (such as “corruption”). More specifically, *pluralistic informal institutions* are informal institutions in host markets that are constituted by distinct dimensions which are disparate both in their origin and their impact on the foreign entry strategy of MNEs (Sartor, 2014). Our research focuses on two distinct dimensions of corruption that emanate from two disparate sectors in the host market institutional environment – the public sector and the private sector.

We build on Aguilera and Vadera’s (2008) broader conceptualization of corruption (*the abuse of authority for personal gain*) to define *public corruption* as *the abuse of public authority or trust for personal gain*, and *private corruption* as *the abuse of private authority or trust for personal gain*. Using these definitions, we extend prior theory that conceptualizes host market corruption in terms of its *pervasiveness* to introduce two new latent constructs – *public corruption pervasiveness* which we define as *the average firm’s likelihood of encountering corruption in its normal interactions with public officials* (Rodriguez et al., 2005: 385), and *private corruption pervasiveness* (*the average firm’s likelihood of encountering corruption in its normal interactions with private entities, companies and individuals*).

In support of our theory’s face validity and to ensure that our theorizing is relevant to practice, we align our decomposition of the corruption construct with the policy orientation of international legislative initiatives (Argandoña, 2003). The *United Nations Convention Against Corruption* (UNCAC) (2004) has encouraged its member states to enact national criminal legislation designed to prohibit the most rampant forms of both “private sector corruption” and “public sector corruption.” As one example of the commitment to the UNCAC’s recognition of the importance of private sector corruption,

the United Kingdom's recently enacted *Bribery Act* (2010) implicitly prohibits payments that induce improper performance by individuals employed in the private sector, in addition to prescribing penalties for acts of public sector corruption, including bribing either domestic or foreign public officials and government employees. At the same time, Transparency International (2009a) has also begun to decompose corruption on a sectorial basis. In defining "corruption", it has recently suggested that corruption should be classified on the basis of the sector (public or private) within which it occurs.

Notably, when compared to the task of defining corruption, measuring the institution has proven to be more difficult (Cuervo-Cazurra, 2008b) due to the need to rely on perceptual measures. While data with respect to the perceived level of public sector corruption in host markets is widely available (Svensson, 2005), private sector corruption continues to be under-researched by management scholars, primarily due to a dearth of information and aggregate data with respect its constituent elements (Argandoña, 2003; Faria, Morales, Pineda, & Montesinos, 2012). Despite these challenges, in order to study *private sector corruption*, our research conceptualizes the phenomenon in terms of the prevalence of insider trading, tax evasion and organized crime or racketeering in host markets. Economists, finance scholars and legal theorists have explicitly recognized insider trading (Argandoña, 2003; Mills & Weisberg, 2007), tax evasion (Christensen, 2011) and racketeering or organized crime (Rose-Ackerman, 1999) as manifestations of private sector corruption. Racketeering is a legal term encompassing a range of corrupt activities found to occur in the private sector, including the payment of bribes to the employees of potential customers to secure contracts ("kickbacks"), extortion and the embezzlement of property in the private sector (Beare, 2007), activities that have been highlighted as some of the most prevalent forms of private sector corruption by the UNCAC (2004). Historically, countries have enacted anti-racketeering laws to combat the existence of organized crime. However, beginning in the 1980s (Bratton & Levitin, 2012), the purview of anti-racketeering laws has been extended to encompass a wider range of corrupt activities occurring in the private sector (Cove, 1983). As recent examples, racketeering laws have been employed to prosecute several publicly-traded MNEs, including a pharmaceutical company for fraudulent marketing and an oil and gas corporation for misleading its investors (Coppola &

DeMarco, 2012), as well as a global investment bank for manipulating interest rates (Scheiner & Broda, 2012). Therefore, despite the data-driven challenges to date associated with operationalizing the private sector corruption construct (Argandoña, 2003; Faria et al., 2012), we contend that the prevalence of racketeering-associated activities such as kickbacks and embezzlement, as well as insider trading and tax evasion in host markets provide an appropriate indication of the pervasiveness of *private corruption pervasiveness* within a country.

## THEORY AND HYPOTHESES DEVELOPMENT

### Entering Foreign Markets: Institutions and Bargaining Power

Strong institutions and legal rules are designed to reduce uncertainty and facilitate efficient exchange (North, 1990). Emerging markets have been characterized as having relatively weaker institutional environments (Wright, Filatotchev, Hoskisson, & Peng, 2005). When a host market's formal institutions are weak, institutional voids form (North, 1990) which may be filled by informal institutions such as corruption (Puffer, McCarthy, & Boisot, 2010). In fact, corruption is more rampant in emerging markets primarily due to ineffective institutional systems (Doh et al., 2003). Our theory is impartial with respect to whether MNEs will prefer to partake in, or avoid, acts of public corruption and private corruption in host foreign markets. Prior research has advanced arguments that favor both perspectives on the propensity and willingness of MNEs to initiate or participate in foreign market corruption. While engaging in corruption may be strategically advantageous to some MNEs (Boddewyn, 1988; Boddewyn & Brewer, 1994), potential legal ramifications (Cuervo-Cazurra, 2008b), moral apprehension (Robertson & Watson, 2004) and adverse financial effects (Wei, 2000) operate as potent disincentives to corrupt behavior.

Either way, heightened levels of corruption operate as an informal institutional constraint that exacerbates information asymmetries (Argandoña, 2005; Calhoun, 2002), reduces trust (Uslaner, 2008) and undermines legal contract enforcement (Lambsdorff, 2002b), all of which increase the risks and costs associated with entering into and operating within more corrupt host market environments (Hoskisson, Eden, Lau, & Wright, 2000; Williamson, 1985). Despite these heightened risks and costs, MNEs are

not always willing or able to defer investment in these countries (Bray, 2005; Doh et al., 2003). Our theory proposes to explain *how the structure of equity-based foreign subsidiary investments is impacted by the pervasiveness of public corruption and private corruption in host markets*. When an MNE enters into a market characterized by higher levels of corruption, it can be expected to structure its investment in a manner that is designed to attenuate information asymmetries in order to reduce the uncertainty and costs associated with its ongoing operations in that country (Brouthers, 2002; Rodriguez et al., 2005). An MNE's ongoing operations in a host country will be constituted by both its public sector transactions (or, transactions with the government) and its private sector transactions (transactions with private entities, companies and individuals) (Teegen et al., 2004). The tradition of conceptualizing an MNE's foreign entry and ongoing operations as a negotiation or bargain between the MNE and the host country (Fagre & Wells Jr, 1982; Kobrin, 1987) has persisted in contemporary international business strategy research pertaining to host market corruption. Business ethicists and corruption scholars who work at the intersection of IT and TCE in order to advance the anti-corruption research agenda have studied the relationship between firms and governments by drawing upon elements of bargaining power theory. An MNE's bargaining power has been found to dictate its ability to successfully manage the risks and costs associated with operating in increasingly corrupt host markets (Lee, Oh, & Eden, 2010).

Bargaining power has been defined as the ability of one party to influence a negotiation in its own favor (Argyres & Liebskind, 1999). Alliance scholars studying the relationship between bargaining power and the distribution of management control in JVs have proposed that an MNE's bargaining power derives from two different sources. *Context-based bargaining power* is a function of the *stakes* (or, the bargainer's dependence on the outcome of a negotiation), as well as the availability of *alternatives* (or, "other parties with whom to negotiate or, other channels through which to accomplish the same mission that is to be achieved") (Yan & Gray, 1994: 1492). An MNE that is less dependent upon the outcome of a bargain and that has more alternatives available to it enjoys greater *context-based bargaining power*, while an MNE that is more dependent upon the outcome of a particular negotiation by virtue of a lack of alternatives wields less *context-based bargaining power* (Inkpen & Beamish, 1997). *Resource-based*

*bargaining power* is a function of both a negotiator's *capital-based bargaining power* (power attributable to a bargainer's financial or physical assets) and its *noncapital-based bargaining power* (power attributable to a bargainer's tacit resources such as local knowledge and expertise, political clout or relational networks) (Yan & Gray, 2001). Notably, if an MNE experiences a deficiency in its *context-based bargaining power*, it will be more difficult for the firm to achieve its goals and, consequently, the firm will be more likely to engage in strategic decisions that are designed to increase its *resource-based bargaining power* (Ren et al., 2009). Consistent with this perspective, in order to attenuate the costs of opportunism associated with transacting with government officials in more corrupt countries, firms have been found to engage in strategies designed to enhance the firm's power (Lambsdorff, 2002a).

#### **Public Corruption Pervasiveness: Equity Entry Strategy (JV or WOS) and Partnering Strategy (Home or Host)**

MNEs with operations in emerging markets routinely report pressure from government officials to engage in corrupt transactions (Spencer & Gomez, 2011). As such, when an MNE enters into increasingly corrupt host markets, it will endeavor to structure its subsidiary investments in a manner that attenuates the information asymmetries that it expects to encounter in its ongoing public sector transactions (Brouthers, 2002; Rodriguez et al., 2005). We theorize that under conditions of more pervasive *public corruption*, the firm's *resources* are likely to be a more prominent source of bargaining power in its public sector transactions, when compared to the bargaining power that the firm derives from its *context* (or, other alternatives). Prior research has found that when a host government is involved in a negotiation, an MNE's alternatives can become significantly restricted (Yan & Gray, 1994). Indeed, the tradition of conceptualizing an MNE's foreign entry and ongoing operations as a negotiation or bargain between the MNE and the host country's government has resulted in extensive scholarly attention being given to framing an MNE's resources and capabilities as its primary source of bargaining power when negotiating with the government (Moon & Lado, 2000). This is because when an MNE enters into a foreign market, it often possesses a constrained range of alternatives with respect to the issues that it needs to

resolve or the resources that it needs to secure through transactions and negotiations with the government (i.e., procurement contracts, licenses, utilities, customs clearances, tax abatements and favorable regulatory rulings or judicial decisions) (Boddewyn, 1988; Rose-Ackerman, 1997). In these situations, we would expect that an MNE which is motivated to commence operations in the host market will expect to be relatively dependent upon the outcome of these ongoing transactions and negotiations. Taken together, this suggests that in the case of public sector transactions, an MNE is less likely to possess the degree of context-based bargaining power that it needs to reduce more pronounced information asymmetries in increasingly corrupt host markets. Consequently, the MNE can be expected to engage in efforts to increase its resource-based bargaining power (Ren et al., 2009). More precisely, we believe that efforts to augment an MNE's noncapital-based bargaining power through the addition of resources such as local knowledge and relational networks represents an important opportunity to reduce the heightened information asymmetries that it may encounter during the course of its public sector transactions in increasingly corrupt host markets.

Public corruption can be highly unpredictable, given that government officials possess the power to change policies and procedures at any time (Lambsdorff, 2002b). As such, an equity partner can enhance the resource-based bargaining power of the MNE and assist efforts to lessen the information asymmetries that the MNE encounters in its public sector transactions in at least three important ways. First, a partner can reduce or even eliminate the need for the MNE to interact with the government directly (Doh et al., 2003). Second, the MNE can access the partner's knowledge of the local environment (Tsang, 2002). More specifically, an equity partner can teach the MNE how to bargain with government agents more effectively (Rodriguez et al., 2005). Finally, a partner can provide an MNE with access to local networks (Meyer, Wright, & Pruthi, 2009). Inclusion in these networks enhances the bargaining power of the MNE because the repeated transactions and reputation that characterize these networks are resources that can be leveraged to contain the costs associated with bargaining with government officials in more corrupt host markets (Lambsdorff, 2002a).

In addition to determining whether to structure these subsidiary investments as JVs or WOSs, foreign MNEs must also determine whether to invest with host country (local)



partners, home country partners or third country partners (Makino & Beamish, 1998). A major risk associated with local partners in more corrupt host markets is that they may cheat, expose the foreign firm to blackmail or, cause the foreign firm to overpay in corrupt transactions (Bray, 2005). However, local partners can also enhance the resource-based bargaining power of MNEs in ways that foreign partners cannot. Relying on a local partner's knowledge of corrupt institutions prevailing in the host country can position a foreign-investing firm to reduce its transaction costs (Meschi, 2009). Local partners can help with local knowledge and local access once the MNE enters into the host country, both of which are critical factors that contribute to the improved performance of a JV (Makino & Beamish, 1998). This is because local partners enjoy a more precise knowledge of and intimate familiarity with the host market's bureaucratic stakeholders and business networks (Meschi, 2009). A local partner is more socially embedded in the host market's business culture and, as such, these trusted social relationships can be employed to attenuate information asymmetries (Lambsdorff, 2002b). Given that the host government and local firms are more culturally similar relative to the degree of cultural similarity between the government and foreign firms, host firms enjoy an advantage over these foreign firms because they have a better understanding of the nature and culture of *public corruption* in the host market (Calhoun, 2002). As such, given the lower level of context-based bargaining power that the MNE is likely to exercise under conditions of more pervasive *public corruption* in the host market, the benefits associated with enhancing the firm's resource-based bargaining power through efforts to engage a local JV partner are expected to outweigh the risks of partnering. Accordingly, we hypothesize that,

*Hypothesis 1: A foreign-investing MNE is more likely to invest through a JV with a host country (local) partner under conditions of heightened public corruption pervasiveness.*

### **Private Corruption Pervasiveness: Equity Entry Strategy (JV or WOS) and Partnering Strategy (Home or Host)**

We theorize that in the case of its private sector transactions within a host country, the firm's *context* or, the availability of alternatives within the host country, is likely to be a more prominent source of bargaining power than it is in the case of its public sector transactions. While it is possible that an MNE might encounter private sector monopolies when executing some of its private sector transactions, a host market's private sector tends to offer a broad range of counterparties with whom a firm may transact, including suppliers, customers, employees and other private sector stakeholders (Calhoun, 2002). Expanded bargaining alternatives provide the MNE with an important source of context-based bargaining power in host markets characterized by more pervasive *private corruption*. While we have proposed that partnering can enhance the MNE's efforts to reduce information asymmetries under conditions of more pervasive *public corruption*, we theorize that the MNE will not be compelled to engage a partner when *private corruption* is more pervasive. This is because the MNE's ability to negotiate with multiple private sector counterparts in the host market will provide the MNE with an opportunity to reduce information asymmetries on its own, without having to share ownership or profits. Seeking information and generating alternatives can improve a party's bargaining position and the outcome of its transactions by reducing information asymmetries (Kim, Pinkley, & Fragale, 2005). When information asymmetries are lower, the MNE's transactions will be more open and competitive such that special safeguards, including partnering, are less useful or necessary (Husted, 1994).

Furthermore, since corruption fosters information asymmetries, it also positions local partners to take advantage of foreign partners (Doh et al., 2003). In fact, weak legal institutions in emerging markets have been found to stimulate partner opportunism (Luo, 2007). Partners that are more embedded in local networks tend to be approached more frequently by corrupt agents and are more inclined to comply with their demands (Meschi, 2009) which would effectively undermine an MNE's context-based bargaining power in its private sector transactions. As such, the MNE would have less control over corrupt negotiations and thus, the MNE may continue to be exposed to the risks and costs of information asymmetries as it is pressured by local partners to comply outright with

corrupt overtures in the private sector (Bray, 2005). As such, given that the MNE can expect that its context-based bargaining power in the private sector will provide it with an opportunity to attenuate more pronounced information asymmetries that exist under conditions of more pervasive *private corruption*, there may be fewer benefits for the MNE to gain in exposing itself to the potential risks and costs that may result from partnering. As such, we hypothesize that,

*Hypothesis 2: A foreign-investing MNE is more likely to invest through a WOS under conditions of heightened private corruption pervasiveness.*

### **The Interaction Between Public Corruption Pervasiveness and Private Corruption Pervasiveness**

Public and private corruption are not mutually exclusive in host country environments (Husted, 1994). In fact, Rodriguez et al. (2006: 739) maintain that “it is clear that government corruption and private corruption often go hand in hand.” Our conceptual disaggregation of the host market corruption construct into its public and private components, in addition to our theory regarding the distinct impact of each upon MNE entry strategy, implicitly suggests the possibility that an interaction effect between the two types of corruption may influence the entry decisions of MNEs that invest in more corrupt host emerging markets.

Doh et al. (2003) has argued that heightened government corruption in emerging markets should motivate an MNE to engage a local JV partner rather than investing through a WOS because local partners can help MNEs to learn how to mitigate the risks of host market corruption. Subsequent conceptual work has proposed the opposite outcome, namely, that more pronounced government corruption would increase the likelihood that an MNE would enter into an emerging market via a WOS rather than with a local JV partner (Rodriguez et al., 2005; Uhlenbruck et al., 2006). The authors suggested that, not only do partners not reduce the costs of confronting corruption but, local partners might take advantage of foreign firms by exploiting the local firm’s more extensive experience with weak institutions. Collectively, this research highlights a tension in the literature with respect to perceptions regarding the utility versus the

riskiness of local partners in emerging markets under conditions of heightened *public sector corruption*.

We suggest that host market corruption is more nuanced than previously recognized. We have hypothesized that more pervasive *public corruption* in the host market will increase the likelihood that MNEs will invest via JVs with local partners, while more pervasive *private corruption* will prompt MNEs to invest through WOSs. Paradox theorists have noted that when a firm engages in decisions with respect to how to structure its operations, contradictory pressures on the firm become increasingly salient (Smith & Lewis, 2011). The conflicting demands of *public corruption* and *private corruption* in the host market complicate an MNE's efforts to devise its foreign entry strategy and illuminate competing concerns with respect to the utility and the riskiness of local partners in more corrupt host markets.

Ultimately, we believe that an MNE will resolve these opposing pressures associated with its foreign entry strategy by considering the implications for its bargaining power in the host market and its ability to reduce information asymmetries. While transaction cost theorists have traditionally assumed that firms are risk neutral (Williamson, 1985), scholars have subsequently proposed that a firm's decisions with respect to its governance are based upon variable risk preferences and the firm's perceptions pertaining to the trustworthiness of a prospective partner (Chiles & McMackin, 1996). While we have theorized that a local JV partner may improve the MNE's noncapital resource-based bargaining power under conditions of heightened *public corruption*, we have not theorized that the decision to retain full ownership (WOS) under heightened *public corruption* would further undermine the MNE's resource-based bargaining power in its public sector transactions. Conversely, under conditions of heightened *private corruption*, we have explicitly theorized that the decision to take on a local partner does risk undermining the MNE's context-based bargaining power and, as such, the MNE will be more likely to retain full ownership (WOS) upon entering into the host emerging market. Our theory is consistent with both Rodriguez et al.'s (2005) and Uhlenbruck et al.'s (2006) base contention that local partners threaten to exploit the MNE's foreignness in more corrupt host market environments. These concerns are well-founded in light of recent findings that JV partners in emerging markets are more

opportunistic when legal institutions are weaker (Luo, 2007). As such, an increase in the pervasiveness of *private corruption* is expected to negatively moderate the likelihood that an MNE will engage in a JV with a local partner under conditions of more pervasive *public corruption*. Accordingly, we hypothesize that,

*Hypothesis 3: The positive relationship between public corruption pervasiveness and the likelihood that a foreign-investing MNE will invest through a JV with a host country (local) partner is weakened as private corruption pervasiveness increases.*

### **Public Corruption, Private Corruption and Foreign Market Entry Strategy (Nonequity or Equity Entry)**

While firms may consider deferring entry into foreign markets characterized by more pervasive corruption, an MNE is not always willing or able to defer investment in these countries, particularly when its competitors are not deferring entry (Bray, 2005; Doh et al., 2003). The unprecedented growth in the prominence of emerging markets as a global destination for FDI provides anecdotal evidence in support of this position (UNCTAD, 2013). Consequently, firms may choose to implement alternative measures to manage the risks and costs associated with investments in more corrupt foreign markets. Among the most prominent alternative measures, firms have been found to adjust their entry mode, implement anti-corruption corporate codes of conduct, provide anti-corruption training to both expatriate employees and local market employees, as well as engaging in social contributions or public donations in the host country that are designed to forestall corrupt overtures from public officials (Doh et al., 2003).

Although our research focuses on the equity-based entry strategies of foreign-investing MNEs, we recognize that some MNEs may choose to engage in nonequity modes of entry into more corrupt emerging market countries. Indeed, extant theory has proposed that under conditions of more pervasive host market corruption, foreign-investing MNEs from a home country with anti-corruption laws will be more likely to engage in nonequity modes of entry which involve a local agent producing or distributing the MNE's good or services in the host country (Rodriguez et al., 2005). Subsequent efforts to empirically validate this proposition found that an increase in the pervasiveness of government corruption in host emerging markets heightens the likelihood that MNEs

will choose nonequity modes (arm's-length or contract-based modes of internationalization such as management contracts and turnkey projects) over equity modes of entry (JV and WOS) (Uhlenbruck et al., 2006). Further, when government corruption was disaggregated into *grand corruption* and *petty corruption*, although the main effects associated with each type of corruption did not exert a statistically significant impact on the choice between *nonequity*- and *equity*-based entry, the interaction between more pervasive *grand* and *petty corruption* did precipitate an increased likelihood that MNEs would choose *nonequity*- over *equity*-based (JV) entry (Sartor, 2014). By extension, although *public* and *private corruption* are distinct dimensions constituting the host market corruption phenomenon, the interaction between both types of corruption could also be expected to prompt MNEs to prefer nonequity entry over equity entry. Accordingly, we hypothesize that,

*Hypothesis 4: The interaction of public corruption pervasiveness and private corruption pervasiveness increases the likelihood that a foreign entrant will engage in nonequity entry.*

## METHODS

### Data Sources and Key Variables

Our work endeavors to explain how the structure of equity-based foreign subsidiary investments is impacted by the pervasiveness of *public corruption* and *private corruption* in host emerging markets. As such, our hypotheses were tested with a sample of 665 subsidiaries established in 16 emerging market countries.<sup>1</sup> This sample of market entries was taken from the 1998-2005 editions of the *Kaigai Shinshutsu Kigyō Souran* which reports on the worldwide investment activity of Japanese MNEs. To ensure that our observations with respect to the dependent variable were lagged by one year relative to the observations with respect to our measures of *public* and *private corruption* in the host markets, the starting date for our study period was 1998 because 1997 was the first

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<sup>1</sup> The number of subsidiary investments in each host country is indicated in brackets: Argentina (2), Brazil (11), China (424), Czech Republic (12), Hungary (6), India (17), Indonesia (19), Korea (53), Malaysia (15), Mexico (8), Philippines (15), Poland (7), Russia (4), South Africa (5), Thailand (65), Turkey (2). Host countries were identified as “emerging markets” based upon the definition utilized by Michigan State University’s Center for International Business Education and Research (CIBER) which has published an annual *Market Potential Index for Emerging Markets* covering the period 1996-2013.

year for which some of the indicators were available to measure the *private corruption* construct using the data sources that we describe below. The end date for our study period (2005) was determined by similar limitations on the availability of data.

Motivated by Rodriguez et al.'s (2005) conceptualization of corruption in terms of its pervasiveness, our measures for the focal independent variables in our study (*public corruption* and *private corruption pervasiveness*) were derived from data which provide an indication of the degree to which public and private sector corruption are a "regular and meaningful part of commercial activity in a given country" (Rodriguez et al., 2005: 385). Researchers have acknowledged that levels of corruption vary significantly among emerging market countries (Gray & Kaufmann, 1998; Uhlenbruck et al., 2006). The development of our independent variables is informed, in part, by extant studies that have been conducted to test the foundational conceptual framework within the realm of corruption-oriented international business research (Rodriguez et al., 2005), notwithstanding the fact that these prior studies have yielded mixed results. More specifically, Uhlenbruck et al. (2006) did not find a statistically significant relationship between host market corruption and the equity-based entry strategies (JV versus WOS) of developed market MNEs that entered into emerging markets. However, disaggregating "government corruption" into *grand corruption* and *petty corruption*, Sartor (2014) hypothesized that MNEs would be more likely to engage in JVs under conditions of more pervasive *grand corruption*, and WOSs when *petty corruption* was more pervasive in both developed and emerging host markets. Subjecting these hypotheses to empirical scrutiny, they found that an increase in the pervasiveness of *petty corruption* attenuated the hypothesized increased likelihood that MNEs would invest in JVs under conditions of more pronounced *grand corruption pervasiveness*. The mixed results generated by these two studies are surprising in light of Spencer and Gomez's (2011) recent emerging market-based findings which revealed the existence of a positive relationship between the level of host country corruption and the pressure that foreign subsidiaries face to engage in corruption in emerging markets.

We speculate that there may be at least two possible reasons why Sartor (2014) finds that government corruption (or, the interaction between *grand* and *petty corruption*) exerts a statistically significant impact on an MNE's choice between JV and WOS, while

Uhlenbruck et al.'s (2006) finds a non-significant relationship. First, consistent with the recommendation of Uhlenbruck et al. (2006: 411), Sartor (2014) theoretically decomposes *government corruption* (which has traditionally been conceptualized as a discrete institution) into two distinct dimensions (*grand* and *petty corruption*). Second, each study employs a different data source to measure government corruption. While Uhlenbruck et al. (2006) operationalize government corruption pervasiveness using data from the World Business Environment Survey (WBES), Sartor's (2014) dual measures of pervasiveness employ data from the World Economic Forum's *Global Competitiveness Reports* (GCR).

Accordingly, consistent with the work of Spencer and Gomez (2011), we employ a broader-based measure of host market *public corruption* which is based upon multiple data sources (including the GCR) and has been found to be very highly correlated with the WBES (Uhlenbruck et al., 2006). More precisely, we measured *public corruption pervasiveness* using Transparency International's *Corruption Perceptions Index* (CPI). The CPI provides a comprehensive measure of the perceived level of public corruption in countries around the world. Collected since the mid-1990's, the Index is arguably the most widely used indicator of host market public sector corruption by industry executives and government officials (Svensson, 2005), as well as by academics who have regularly employed the CPI to measure public corruption in international business and strategic management research (see, as examples, Brouthers, Gao, & McNicol, 2008; Chen, Ding, & Kim, 2010; Steensma, Tihanyi, Lyles, & Dhanaraj, 2005).

Although aggregate data with respect to the perceived level of *private corruption* in host countries does not currently exist in the form of a comprehensive index similar to the CPI (Faria et al., 2012), Transparency International (2009b) has recommended that the measurement of *private corruption* should incorporate a consideration of activities such as insider trading, tax evasion, corporate embezzlement and commercial bribery ('kickbacks'). Insider trading has been explicitly recognized as an act of private corruption in which corporate insiders with preferential access to corporate information through their position of authority act on this information to the detriment of other stakeholders (Aldrichi, 2009; Argandoña, 2003; Mills & Weisberg, 2007). Tax evasion generally involves the under-reporting of income, or the over-reporting of expenses, and



has been affiliated with other instances of *private sector corruption* such as corporate fraud and embezzlement (Argandona, 1999). This is because tax offences are “intrinsically linked with other (private sector) financial crimes...such as...investment fraud, extortion...(and) embezzlement” (OECD, 2013: 7). In fact, high levels of tax evasion have been associated with more pronounced levels of corruption (Uslaner, 2007). Racketeering is a legal term that subsumes a wide range of corrupt activities found to occur in the private sector, including the payment of bribes to the employees of potential customers to secure contracts (‘kickbacks’), extortion and the embezzlement of property in the private sector (Beare, 2007). These activities have been highlighted as some of the most prevalent forms of *private sector corruption* by the United Nations Convention Against Corruption (2004). Historically, countries have enacted anti-racketeering laws to combat the existence of organized crime. However, beginning in the 1980s (Bratton & Levitin, 2012), the purview of anti-racketeering laws has been extended to encompass a wider range of corrupt activities occurring in the private sector, including the manipulation of interest rates (Scheiner & Broda, 2012) and misleading investors (Coppola & DeMarco, 2012), to name a few.

Accordingly, in order to develop a measure of private sector corruption, our research leverages perceptual data pertaining to the prevalence of insider trading, racketeering and tax evasion in host markets. We operationalized *private corruption* utilizing data from IMD’s *World Competitiveness Yearbooks* (WCY) pertaining to insider trading and tax evasion, in addition to using data from the World Economic Forum’s *Global Competitiveness Reports* pertaining to racketeering / organized crime. A principal components analysis was conducted with an orthogonal (varimax) rotation and an eigenvalue cutoff equal to 1, using a holdout sample of subsidiaries that were established in the same emerging market countries during the period 1998-2005. This analysis suggested a one factor solution which was theoretically expected. Table 8 presents the factor loadings for each indicator on the *private corruption pervasiveness* construct. We also conducted a reliability analysis and concluded that the Cronbach’s alpha for these three indicators (0.71) was sufficient to establish internal consistency (Nunnally & Bernstein, 1994).

Given that both our *public* and *private corruption* constructs were based upon raw data in which high scores indicate lower levels of corruption, for ease of interpretation with respect to our results, we reverse-coded the raw data so that more pervasive *public corruption* and *private corruption* for the host emerging market countries in our study would be indicated by higher scores. Consistent with leading conceptual and empirical strategy research pertaining to corruption (Rodriguez et al., 2005; Uhlenbruck et al., 2006), our measures of *public corruption pervasiveness* and *private corruption pervasiveness* provide an indication of the absolute level of each type of corruption in the host market.

**TABLE 8**  
**Factor Analysis Results**

Latent construct and associated items		Factor loading
<b>Private corruption pervasiveness <sup>a</sup>:</b>		
Tax evasion	Tax evasion is (1 = a common practice, 10 = not a common practice) in your country.	0.81
Insider trading	Insider trading is (1 = common in the stock market, 10 = not common in the stock market).	0.77
Prevalence of racketeering & extortion	(Racketeering & extortion) in your country (1 = imposes significant costs on business, 7 = does not impose significant costs on business).	0.81

<sup>a</sup> Cronbach's alpha = 0.71

### Dependent Variables, Control Variables and Estimation Methods

We investigate the impact of heightened host market corruption upon three strategic foreign entry decisions that MNEs consider – *foreign entry strategy* (nonequity entry versus equity entry), *equity entry strategy* (JV versus WOS) and *partnering strategy* (host country partner versus home country partner). *Foreign entry strategy* captures the

MNE's choice between *nonequity*-based foreign market entry and *equity*-based foreign market entry (JV or WOS). Notably, the measurement of *nonequity* entry has traditionally been complicated by the fact that "...the web of directly-owned, partially-owned, contract-based and arm's-length forms of international operation...is tangled and some of the distinctions between the different modes are blurred" (UNCTAD, 2011: 130). Therefore, consistent with both Uhlenbruck et al.'s (2006) and Pan and Tse's (2000) conceptualization of *equity entry* as including foreign investments characterized by a degree of ownership, control and resource deployment that indicates a long-term commitment to the host country, we utilize the measure of *nonequity* entry employed by Sartor (2014) who operationalized *nonequity* entry as including those foreign entries in which the focal MNE owned less than 5% of the equity and fewer than twenty employees were enlisted to staff the office associated with the investment. Based on this operationalization, 65 (10%) of the 665 entry events in our sample were categorized as *nonequity* entries, while 600 (90%) were *equity* entries.

*Equity entry strategy* captures the MNE's choice between JV and WOS modes of entry. Models were estimated using both the 80 percent equity ownership cutoff convention and the 95 percent cutoff to distinguish between JVs and WOSs (Yiu & Makino, 2002). While 373 (62%) of the 600 subsidiary investments were categorized as WOSs and 227 (38%) as JVs using the 80 percent cutoff, pursuant to the 95 percent cutoff, 335 (56%) and 265 (44%) were categorized as WOSs and JVs respectively. *Partnering strategy* is based on the taxonomy of JV partnerships developed by Makino and Beamish (1998). Each JV arrangement was categorized as either a *traditional JV* (a JV in which the MNE engages a host country (local) equity partner in the subsidiary investment) or a *cross-national JV* (in which the MNE engages a home country partner). While Makino and Beamish's taxonomy also includes *tri-national JVs* (in which the MNE engages a third country partner), these JVs constituted only 2% (14 investments) of the subsidiaries in our study and were not included in our empirical analyses. Accordingly, using the 80 percent cutoff, 187 (88%) of the remaining 213 JVs were categorized as *traditional JVs* and 26 (12%) were categorized as *cross-national JVs*. Using the 95 percent cutoff, 206 (82%) and 45 (18%) were categorized as *traditional JVs* and *cross-national JVs* respectively.

To investigate the effects of *public corruption pervasiveness* and *private corruption pervasiveness* on the three strategic foreign entry decisions in our study, two estimation techniques were utilized. Hypotheses 1, 2 and 3 pertaining to an MNE's *equity entry strategy* and *partnering strategy* were tested in Models 1A-1F. We integrated the measurement of both the *equity entry* and *partnering* strategic decisions by employing a trichotomous dependent variable that included *WOS*, *traditional JV* and *cross-national JV* as the possible outcomes. As such, these models were estimated using multinomial logistic regression in which *WOS* was designated as the comparison group. Hypothesis 4 pertaining to an MNE's *foreign entry strategy* (nonequity entry versus equity entry) was tested in Models 2A-2C using binary logistic regression.

Variables were included to control for country, regional, temporal, industry, parent MNE and subsidiary effects, all which have been found to influence a firm's decisions with respect to its foreign market entry strategies. These control variables are summarized in Appendix B.

## RESULTS

Table 9 provides descriptive statistics for the sample. Table 10 presents the results of the multinomial logistic regression estimations conducted in order to test Hypotheses 1, 2 and 3, while Table 11 presents the results of our test of Hypothesis 4. We concluded that multicollinearity was not a concern in our models for two reasons. First, the highest variance inflation factor (VIF) score reported for our models (3.27) in Tables 10 and 11 is substantially less than the maximum VIF (10) that is routinely prescribed for multivariate regression analyses in strategy research (Reuer & Leiblein, 2000). Second, none of the correlations presented in Table 9 between variables that are included in the same regression models exceed the recommended 0.70 cutoff (Tabachnick & Fidell, 2007).

**TABLE 9**  
**Descriptive Statistics and Correlations**

Variable	Mean	S.D.	1	2	3	4	5	6	7	8
1 Foreign entry strategy <sup>a</sup>	-	-								
2 Equity entry strategy <sup>b</sup>	-	-	0.55							
3 Subsidiary size (log)	1.30	0.68	0.25	0.34						
4 Subsidiary capitalization (log)	2.17	1.06	0.03	0.08	0.04					
5 Parent size (log)	5.40	0.83	-0.02	0.12	0.20	0.10				
6 Parent profitability (ROA)	0.04	0.06	-0.08	-0.05	-0.01	-0.02	-0.04			
7 Parent leverage	0.80	0.12	-0.01	-0.10	-0.06	-0.11	-0.46	0.32		
8 Parent experience	11.18	23.70	-0.04	0.03	0.04	0.05	0.55	-0.13	-0.37	
9 Industry dummy	-	-	-0.06	-0.01	-0.17	-0.02	0.09	-0.05	-0.21	0.09
10 Exchange rate	0.01	0.00	0.03	-0.01	-0.02	0.06	0.08	0.04	0.02	0.01
11 Region dummy	-	-	0.10	0.09	0.09	-0.07	-0.14	-0.04	0.04	-0.17
12 Host market size (log)	2.85	0.46	0.04	-0.01	0.00	0.08	-0.10	0.02	-0.01	-0.10
13 Infrastructure development	4.70	0.86	0.04	0.00	-0.07	-0.10	-0.10	-0.06	0.07	-0.09
14 FDI restrictions	4.95	1.25	-0.03	0.00	-0.05	-0.09	0.14	0.00	-0.03	0.11
15 Cultural distance	2.63	0.55	0.09	0.11	0.06	0.09	-0.07	-0.03	0.01	-0.12
16 Public corruption	6.53	0.54	0.02	0.11	0.14	0.08	0.00	0.05	0.00	-0.06
17 Private corruption	5.03	0.50	-0.05	-0.03	0.03	0.08	-0.01	0.09	-0.04	0.03
18 Public corruption x private corruption	0.13	0.38	0.03	0.01	-0.09	-0.06	0.01	0.02	0.04	-0.03

Variable	9	10	11	12	13	14	15	16	17
10 Exchange rate	0.05								
11 Region dummy	0.04	0.01							
12 Host market size (log)	0.03	0.08	0.38						
13 Infrastructure development	-0.05	0.04	0.35	0.00					
14 FDI restrictions	-0.06	-0.15	-0.59	-0.67	-0.09				
15 Cultural distance	0.04	0.03	0.43	-0.01	0.18	-0.34			
16 Public corruption	0.05	0.03	0.25	0.14	-0.48	-0.29	0.28		
17 Private corruption	0.01	-0.11	-0.12	0.29	-0.62	-0.19	-0.04	0.48	
18 Public corruption x private corruption	0.02	0.09	0.04	-0.32	0.22	0.15	0.34	-0.43	-0.39

<sup>a</sup> Dichotomous dependent variable: *Nonequity entry* or *equity entry*.

<sup>b</sup> Trichotomous dependent variable: *Wholly-owned subsidiary*, *traditional JV* or *cross-national JV*.

N = 665.

Correlations with an absolute value equal to or greater than 0.08 are statistically significant at the  $p < 0.05$  level. All are two-tailed tests.

**TABLE 10**

**Results of Multinomial Logistic Regression Analyses of  
Public Corruption and Private Corruption on Equity Entry Strategy <sup>a</sup>**

Variables	Equity Entry Strategy and Partnering Strategy <sup>a</sup>					
	Base Model		Main Effects		Interaction Effect	
	Model 1A Traditional JV	Model 1B Crossnational JV	Model 1C Traditional JV	Model 1D Crossnational JV	Model 1E Traditional JV	Model 1F Crossnational JV
Intercept	-2.83 (2.84)	-8.85 (5.67)	-2.91 (4.04)	-11.98 (7.91)	-1.37 (2.99)	-9.05 (6.03)
<i>Subsidiary effects</i>						
Subsidiary size (log)	1.03 (0.17) ***	0.45 (0.33)	1.01 (0.17) ***	0.44 (0.33)	1.06 (0.17) ***	0.42 (0.33)
Subsidiary capitalization (log)	0.27 (0.09) **	0.20 (0.21)	0.27 (0.09) **	0.21 (0.21)	0.28 (0.09) **	0.19 (0.21)
<i>Parent effects</i>						
Parent size (log)	0.30 (0.16) <sup>t</sup>	0.27 (0.35)	0.27 (0.16) <sup>t</sup>	0.24 (0.35)	0.25 (0.17)	0.26 (0.36)
Parent profitability (ROA)	-1.79 (1.74)	2.67 (4.75)	-1.44 (1.77)	2.57 (4.72)	-1.71 (1.77)	2.66 (4.78)
Parent leverage	-1.50 (1.07)	-0.18 (2.45)	-1.61 (1.08)	-0.25 (2.45)	-1.74 (1.09)	-0.09 (2.47)
Parent experience	0.00 (0.01)	-0.02 (0.03)	0.00 (0.01)	-0.02 (0.03)	0.00 (0.01)	-0.02 (0.03)
<i>Industry effects</i>						
Industry dummy	-0.61 (0.26) *	1.44 (1.05)	-0.57 (0.27) *	1.47 (1.05)	-0.56 (0.27) *	1.47 (1.05)
<i>Temporal effects</i>						
Exchange rate	-366.99 (197.82) <sup>t</sup>	366.14 (417.96)	-474.41 (203.53) *	320.86 (424.82)	-589.75 (210.42) **	353.48 (429.85)
<i>Region effects</i>						
Region dummy	-1.87 (0.64) **	0.91 (0.88)	-1.27 (0.68) <sup>t</sup>	1.20 (0.94)	-0.96 (0.68)	1.04 (0.99)
<i>Country effects</i>						
Host market size (log)	0.14 (0.34)	-0.24 (0.61)	0.33 (0.35)	-0.20 (0.62)	0.55 (0.36)	-0.35 (0.64)
Infrastructure development	0.14 (0.13)	-0.03 (0.27)	0.17 (0.19)	0.15 (0.39)	0.37 (0.21) <sup>t</sup>	0.04 (0.42)
FDI restrictions	0.31 (0.15) *	-0.14 (0.26)	0.29 (0.15) *	-0.11 (0.27)	0.26 (0.15) <sup>t</sup>	-0.14 (0.27)
Cultural distance	0.31 (0.23)	0.32 (0.39)	0.24 (0.23)	0.23 (0.44)	-0.22 (0.31)	0.46 (0.52)
<i>Main effects</i>						
Public corruption			0.57 (0.27) *	0.49 (0.56)	1.20 (0.39) **	0.28 (0.59)
Private corruption			-0.58 (0.31) <sup>t</sup>	-0.09 (0.59)	-0.53 (0.31) <sup>t</sup>	-0.14 (0.63)
<i>Interaction effect</i>						
Public corruption x private corruption					1.06 (0.46) *	-0.78 (0.83)
Variance inflation factor range	1.07 - 2.79		1.08 - 2.85		1.08 - 3.27	
$\chi^2$	120.07 ***		127.42 ***		134.68 ***	
R <sup>2</sup> ( $\Delta R^2$ )	0.23		0.25 (0.02)		0.26 (0.03)	

<sup>a</sup> The reference group in the multinomial logistic regression models is *wholly-owned subsidiary (WOS)* which is compared to two other possible outcomes in the *equity entry strategy* dependent variable: *traditional joint venture* (with a host country / local partner) and *crossnational joint venture* (with a home country partner).  
n = 586.

<sup>t</sup> p < 0.10; \* p < 0.05; \*\* p < 0.01; \*\*\* p < 0.001

All are two-tailed tests. Standard errors are in parentheses.

**TABLE 11**  
**Results of Binary Logistic Regression Analyses of**  
**Public Corruption and Private Corruption on Foreign Entry Strategy <sup>a</sup>**

Variables	Foreign Entry Strategy <sup>a</sup>					
	Base Model		Main Effects		Interaction Effect	
	Model 2A		Model 2B		Model 2C	
Intercept	-6.59	(3.92) <sup>t</sup>	-1.25	(5.41)	-5.38	(4.02)
<i>Subsidiary effects</i>						
Subsidiary size (log)	1.82	(0.29) ***	1.85	(0.29) ***	1.85	(0.29) ***
Subsidiary capitalization (log)	0.11	(0.14)	0.11	(0.14)	0.12	(0.14)
<i>Parent effects</i>						
Parent size (log)	-0.41	(0.25) <sup>t</sup>	-0.43	(0.25) <sup>t</sup>	-0.44	(0.25) <sup>t</sup>
Parent profitability (ROA)	-8.82	(3.28) **	-8.55	(3.27) **	-8.72	(3.29) **
Parent leverage	0.77	(1.44)	0.75	(1.44)	0.75	(1.44)
Parent experience	0.00	(0.01)	0.00	(0.01)	0.00	(0.01)
<i>Industry effects</i>						
Industry dummy	-0.17	(0.35)	-0.18	(0.35)	-0.19	(0.35)
<i>Temporal effects</i>						
Exchange rate	328.28	(268.78)	275.34	(272.61)	254.46	(276.58)
<i>Region effects</i>						
Region dummy	0.59	(0.64)	0.59	(0.68)	0.50	(0.69)
<i>Country effects</i>						
Host market size (log)	0.72	(0.41) <sup>t</sup>	0.84	(0.43) *	0.88	(0.44) *
Infrastructure development	0.05	(0.19)	-0.20	(0.26)	-0.15	(0.28)
FDI restrictions	0.39	(0.19) *	0.36	(0.19) <sup>t</sup>	0.34	(0.19) <sup>t</sup>
Cultural distance	0.45	(0.32)	0.66	(0.39) <sup>t</sup>	0.57	(0.44)
<i>Main effects</i>						
Public corruption			-0.29	(0.45)	-0.16	(0.52)
Private corruption			-0.48	(0.41)	-0.45	(0.42)
<i>Interaction effect</i>						
Public corruption x private corruption					0.29	(0.64)
Variance inflation factor range	1.06 - 2.76		1.07 - 2.81		1.08 - 3.18	
$\chi^2$	72.19 ***		74.62 ***		74.84 ***	
R <sup>2</sup> ( $\Delta R^2$ )	0.22		0.23 (0.01)		0.23 (0.01)	

<sup>a</sup> The dependent variable *foreign entry strategy* is coded as follows: 0: *nonequity-based entry*, 1: *equity-based entry*. *n* = 665.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Standard errors are in parentheses.

In both Tables 10 and 11, we present a base model which excludes the effects of the two focal corruption variables, along with models that include the main effects and interaction effect associated with the two dimensions of corruption that we studied. The estimates reported in Table 10 are based upon the 80 percent equity ownership convention used to distinguish between a JV and a WOS.<sup>2</sup> Consistent with our theory, the results with respect to Models 1C and 1D (which tests Hypothesis 1) reveal that the *public corruption pervasiveness* construct was a significant predictor of an MNE's equity-based entry strategy and partner choice ( $\chi^2 = 127.42$ ,  $p < 0.001$ ,  $R^2 = 0.25$ ). The results suggest that firms are more likely to invest in a JV with a local partner than they are to invest through a WOS (Model 1C:  $\beta = 0.57$ ,  $p < 0.05$ ) when entering into host emerging markets under conditions of heightened *public corruption pervasiveness*. The results for Hypothesis 2, which was also tested in Models 1C and 1D, were also consistent with our theory. More specifically, heightened *private corruption pervasiveness* was found to predict an increased likelihood that an MNE would invest through a WOS (Model 1C:  $\beta = -0.58$ ,  $p < 0.10$ ) rather than through a traditional JV partnership. Notably, the analyses presented in Model 1D which tested the likelihood of an MNE choosing to invest through a crossnational JV rather than a WOS under conditions of more pervasive *public corruption* and more pervasive *private corruption* did not yield statistically significant results. This result is consistent with Roy & Oliver (2009) who found that host country corruption does not influence partnering.

Before investigating the effect of the interaction term, the focal independent variables (*public corruption pervasiveness* and *private corruption pervasiveness*) were centered about the mean (Aiken & West, 1991). The results associated with Models 1E and 1F ( $\chi^2 = 134.68$ ,  $p < 0.001$ ,  $R^2 = 0.26$ ) which tests Hypothesis 3 reveal that the interaction effect between *public corruption pervasiveness* and *private corruption pervasiveness* does have a significant impact upon the equity-based foreign strategies of MNEs (Model 1E:  $\beta = 1.06$ ,  $p < 0.05$ ). The coefficients reported for the main effects in Model 1E continue to indicate that more pervasive *public corruption* (Model 1E:  $\beta = 1.20$ ,  $p < 0.01$ ) and *private corruption* (Model 1E:  $\beta = -0.53$ ,  $p < 0.10$ ) will increase the

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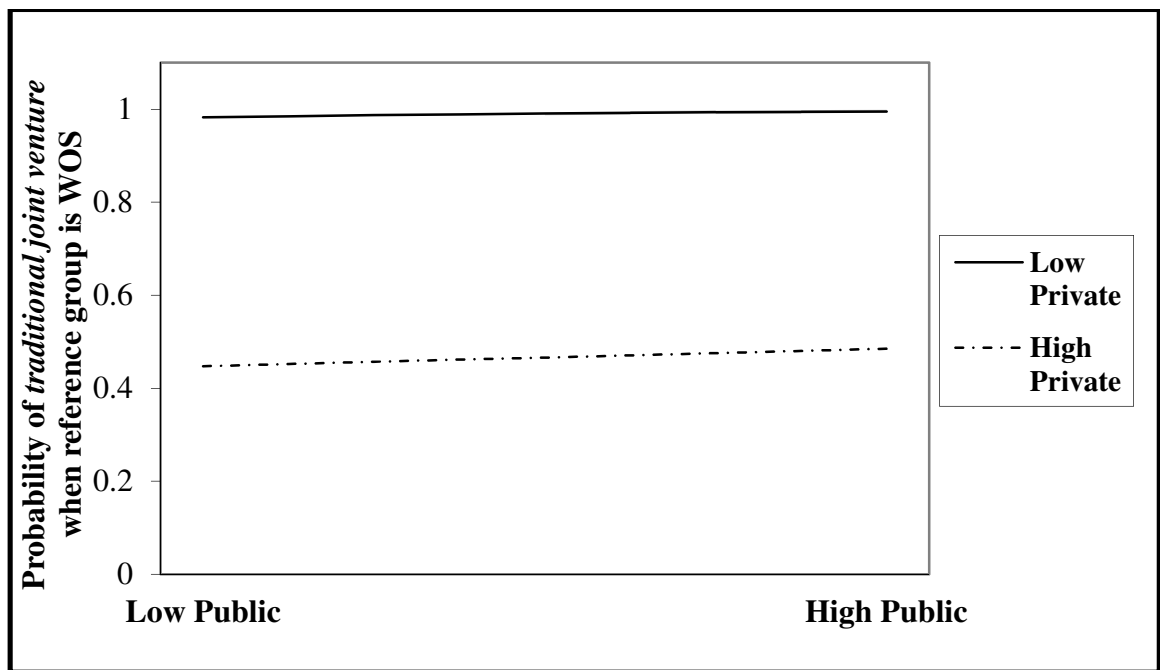
<sup>2</sup> The results using the 95 percent equity ownership cutoff (Yiu & Makino, 2002) were substantially similar.



likelihood that an MNE will invest through a JV with local partners and through a WOS, respectively. In order to explore the nature of the moderation effect more fully, Figure 5 plots the interaction estimated in Model 1E. The Figure indicates that although MNEs are more likely to invest via a JV with a local partner under conditions of more pronounced *public corruption pervasiveness* in the host market, an increase in the pervasiveness of *private corruption* negatively moderates this relationship. Therefore, Hypothesis 3 is supported. As such, for any given level of *public corruption pervasiveness*, an increase in the pervasiveness of *private corruption* reduces the likelihood that the MNE will enter via a JV with a local partner.

**FIGURE 5**

**Interaction Effect of Public Corruption Pervasiveness and Private Corruption Pervasiveness on Equity Entry Strategy (the Choice Between Wholly-Owned Subsidiary and Traditional Joint Venture) <sup>a b</sup>**



<sup>a</sup> High Private and Low Private refer to private corruption pervasiveness one standard deviation above and below the mean for private corruption pervasiveness. Likewise, High Public and Low Public refer to public corruption pervasiveness one standard deviation above and below the mean for public corruption pervasiveness.

<sup>b</sup> The dependent variable is the probability of a *traditional joint venture* (with a host country / local partner) when the reference group is WOS.

Finally, the results associated with Model 2C in Table 11 reveal that Hypothesis 4 was not supported. The interaction between more pervasive *public corruption* and *private corruption* did not exert a statistically significant impact upon an MNE's choice between *nonequity*-based entry and *equity*-based entry. While the interaction coefficient was not statistically significant, the results are insightful nonetheless because they introduce an important boundary condition with respect to the relationship between the pervasiveness of corruption in the host market and the *foreign entry strategy* (*nonequity* versus *equity* entry) of MNEs. Extant research has found that "government corruption" increases the likelihood that an MNE will engaged in *nonequity* entry (Uhlenbruck et al., 2006). Further, the interaction between *grand* and *petty corruption* has been found to have the same effect (Sartor, 2014). However, the results presented in Table 11 suggest that the main effects of more pervasive *public corruption* and *private corruption*, as well as the interaction effect between the two dimensions of corruption, do not impact upon a MNE's *foreign entry strategy* when entering into emerging markets.

## DISCUSSION AND CONCLUSIONS

While emerging markets have grown dramatically in prominence as a global destination for FDI (UNCTAD, 2013), our limited understanding of the strategic impact of corruption in these host markets has precipitated the need for more extensive academic scrutiny (Rodriguez et al., 2006). When an MNE enters into a foreign market, it can be expected to structure its investment in a manner that is designed to minimize the costs of its ongoing operations (Brouthers, 2002) which will be constituted by a combination of public sector transactions and private sector transactions (Teegen et al., 2004). Our research has been designed to investigate how the structure of equity-based foreign subsidiary investments is impacted by the pervasiveness of *public corruption* and *private corruption* in host emerging markets. In doing so, our work makes several contributions. First, our theory and findings broaden the corruption-oriented international business strategy literature by bridging the work of strategy scholars and business ethicists whose work has increasingly emphasized two distinct corruption domains – public sector corruption and private sector corruption (Argandoña, 2003; Montiel, Husted, & Christmann, 2012; Uhlenbruck et al., 2006). A number of studies support our contention

that expanding the scope of corruption-based strategy research to incorporate private sector corruption bears merit. Private corruption has been argued to engender a wide range of organizational consequences including, among others, inefficient resource allocation (Gopinath, 2008) and the deterrence of capability-building (Luo, 2005). In addition to amplifying the negative social, political and distributional effects of public corruption (Gopinath, 2008), private corruption has also been implicated for undermining shareholder value both indirectly, as a consequence of fines and penalties (Bishara & Schipani, 2009) and, directly through a depreciation in the market capitalization of firms (Narayanan, Schipani, & Seyhun, 2007).

Second, this study both supports and extends Rodriguez et al.'s (2005) foundational theory on the relationship between corruption and firm strategy. With respect to the issue of entry mode strategy, they proposed that an increase in the pervasiveness of *government corruption* would motivate MNEs to choose WOS over JV entry. Subsequent efforts to test this theory did not find a significant relationship between the pervasiveness of host market corruption and an MNE's choice between JV and WOS entry (Uhlenbruck et al., 2006). However, motivated by the notion of institutional pluralism, Sartor (2014), determined that each of the distinct dimensions (*grand corruption* and *petty corruption*) constituting the *government corruption* construct exerted a differential impact on an MNE's market entry strategy. We apply Sartor's (2014) theory to support not only our conceptual disaggregation of the host market corruption phenomenon (*public* versus *private*), but also our propositions with respect to the distinct mechanisms that undergird the relationship between each dimension of corruption and the equity-based entry strategies of foreign-investing MNEs. Our efforts to parse the corruption construct into its public and private components have generated more nuanced and unequivocal results pertaining to *equity entry strategy*, while also extending insights into the realm of partner choice when MNEs enter into more corrupt host market environments. An increase in *public corruption pervasiveness* was found to increase the likelihood that MNEs will invest through JV ownership with a host country (local) partner, while an increase in *private corruption pervasiveness* was found to increase the likelihood that MNEs will invest via WOS ownership when entering foreign emerging markets. Further, an increase in the pervasiveness of *private corruption* was

found to negatively moderate the likelihood that MNEs would invest in a JV with a local partner under conditions of more pervasive *public corruption*.

Third, we leveraged theoretical insights from the JV and alliance literature pertaining to the multifaceted nature of an MNE's bargaining power (Ren et al., 2009; Yan & Gray, 2001). Juxtaposing this theoretical lens against Rodriguez et al.'s (2005) general proposition that a relationship exists between the pervasiveness of host market corruption and an MNE's equity-based entry strategy, we have introduced a finer-grained perspective which contends that an MNE's reliance on different sources of bargaining power (*context-based* versus *resource-based*) in its public and private transactions functions as the mechanism through which *public corruption* and *private corruption* impact upon the foreign entry strategy of the MNE. In doing so, we have built on the work of strategy scholars who have advocated the integration of institutionally-oriented and resource-oriented perspectives in order to advance both the nonmarket strategy research agenda, and our understanding of contemporary nonmarket phenomena such as corruption (Doh et al., 2012). Our work contributes to these objectives by elaborating how bargaining power could be employed as a theoretical mechanism to link the institutional and resource perspectives. As we hypothesized, the two dimensions of the informal institution that we studied exerted a disparate impact upon the resource-oriented foreign market entry strategy of the firms in our study.

Fourth, our research also offers important insights for policy makers. Two key assumptions have traditionally underpinned the policy recommendations of anti-corruption scholars. First, corruption is primarily conceptualized as occurring within firm-government transactions. Second, engaging a partner is assumed to be a key strategy employed by firms to manage the increased uncertainty, information asymmetries and transaction costs precipitated by heightened government corruption. Building on these assumptions, scholars have formulated policy recommendations that are designed to reduce the efficacy of the transaction cost-reducing strategies employed by firms to facilitate corrupt transactions (Lambsdorff, 2002b; Svensson, 2003). However, our research suggests that policy prescriptions designed to curb MNE engagement in foreign market corruption must consider the multidimensional nature of the construct in order to ensure that policy efforts are not misguided. Our findings that *public corruption* and

*private corruption* each exert a distinct impact upon the foreign-investment decisions of MNEs, coupled with our findings pertaining to the interaction effect between both types of corruption upon these foreign entry strategies, suggests the need for more nuanced anti-corruption initiatives.

Despite the increasing recognition that public sector and private sector manifestations of corruption are distinct (Transparency International, 2011), an important limitation in our study has been the absence of a comprehensive index to operationalize the *private corruption pervasiveness* construct, akin to the *Corruption Perceptions Index* that is available to measure *public corruption*. We hope that our work will stimulate efforts to collect the data needed to develop and maintain such an index in the longer run. A second limitation in our study is the use of a sample of firms from a single home country. While scholars have argued that this approach can be beneficial because it minimizes the impact of differences between multiple home countries upon the dependent variables (Coeurderoy & Murray, 2008), future research should consider opportunities to verify our results with a sample of non-Japanese MNEs. Notwithstanding these limitations, the patterns that emerge from our work provide additional opportunities for future research. Corruption clearly exerts a nuanced impact on the structure and strategic entry decisions of foreign-investing MNEs. Researchers should explore the subsidiary survival implications associated with adopting different strategic configurations in more corrupt host market environments, with particular attention being given to the multiple dimensions of corruption which have been explicated to date (public, private, grand and petty). In addition to *equity entry strategy* and *partnering strategy*, future work should also consider the implications associated with expatriate deployment strategies that are formulated to facilitate entry into and ongoing operations within more corrupt host market environments. Finally, our theory-building efforts have focused upon prior scholarship related to the *pervasiveness* of host market corruption (Rodriguez et al., 2005). While a consideration of the *arbitrariness* of corruption (Rodriguez et al., 2005) was beyond the limits of available data and the theoretical scope of our work, future research should examine the arbitrariness of both *public sector* and *private sector corruption*, particularly in relation to the three elements of foreign market entry strategy that we have studied.

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## APPENDIX B

### Description of Measures for Control Variables

Variable	Description of measure	Rationale for inclusion	Data source
Subsidiary size	Total subsidiary employees (log)	Parent and subsidiary characteristics that have been found to predict foreign entry strategies (Delios & Beamish, 1999)	Company data
Subsidiary capital	Subsidiary capitalization (log)		Company data
Parent size	Total sales (log)		Company data
Parent profitability	Return on assets		Company data
Parent experience	Prior number of entries by parent MNE into host market		
Parent leverage	(Total assets-total debt) / total assets	Parent's slack financial resources (Reuer & Ragozzino, 2006)	Company data
Service industry	Dummy variable (1: service industry constituent; 0: not)	Industry effects (Brouthers & Brouthers, 2003)	Company data
Exchange rate	Annual exchange rates for Japanese currency (JPY/USD)	Temporal effects (Klein & Rosengren, 1994)	Bank of Japan
Region	Dummy variable (1: subsidiary established in Asia; 0: not)	Regional effects (Arregle et al., 2013)	United Nations Statistics Division
Host market size	Total gross domestic product (log)	Country effects: Host market's economic, institutional and cultural environment (Henisz & Delios, 2001; Kogut & Singh, 1988; Uhlenbruck et al., 2006)	World Competitiveness Yearbooks and Hofstede, 2001 data
FDI restrictions	Managerial perceptions with respect to restrictiveness of foreign ownership laws		
Infrastructure development	Managerial perceptions with respect to the degree of infrastructure development		
Cultural distance	Cultural distance values between the home and host markets		

## **CHAPTER 4**

### **Corruption Pervasiveness, Subsidiary Localization Strategy and Host Market Exit**

#### **INTRODUCTION**

A foreign subsidiary's ability to secure legitimacy in host markets that are characterized by more pronounced levels of corruption is assumed to be vital to the subsidiary's continued existence in these environments (Rodriguez, Uhlenbruck, & Eden, 2005). A growing body of theoretical and empirical work has examined the relationship between host market corruption and multinational enterprise (MNE) strategy (Cuervo-Cazurra, 2008a; Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003; Sartor, 2014a, 2014b; Uhlenbruck, Rodriguez, Doh, & Eden, 2006). However, this research has provided MNEs with limited insights into the relative efficacy of various strategies (Mezias & Mezias, 2010) that have been implemented to bolster the continued existence of subsidiary investments in foreign markets plagued by heightened corruption.

Institutional theorists maintain that weak formal institutions in the form of written rules, laws and regulations in a host market (North, 1990) precipitate institutional voids which may be filled by informal institutions (or, norms of behavior, values, practices and standards of conduct) such as corruption (Puffer, McCarthy, & Boisot, 2010). Goodrick and Salancik (1996: 4) suggest that informal institutions generate uncertainty when these norms of behavior or standards of practice are "ambiguous, unknown or inconsistent." Given that corrupt transactions are most frequently "sealed in secrecy" and unenforceable in courts of law (Lambsdorff, 2005: 142), the norms and standards of conduct surrounding these extralegal transactions in foreign markets can be highly indeterminate and opaque from the foreign-investing MNE's perspective. Consistent with this, Fisman and Gatti (2006: 137) found "that there is substantial variation across countries in the extent to which firms know the amount of illicit payments necessary to do business." In part, this uncertainty can be traced to the wide-ranging variability in attitudes and values towards corruption both within countries and between countries (Bailey & Spicer, 2007; Sartor, 2014a; Spicer, 2009). Since organizations may seek legitimacy by conforming to institutional norms in foreign markets (Eden & Miller, 2004; Kostova & Zaheer, 1999),

any uncertainty surrounding informal institutions such as corruption threatens to undermine the firm's ability to navigate the standards of practice or conduct that are required to secure legitimacy in the host market. Consequently, a central premise of our work is that regardless of the MNE's willingness or reluctance to engage in corrupt transactions in the host market, and regardless of whether corrupt transactions are sanctioned or prohibited in the MNE's home market, corruption encountered in foreign markets functions as a source of considerable uncertainty for internationalizing MNEs, particularly in markets characterized by more pervasive corruption. In turn, this poses a threat to the firm's legitimacy in these host markets and heightens the likelihood of market exit.

We investigate the relationship between host market corruption pervasiveness, MNE strategy and host market exit. Given that foreign expansion offers the MNE a wide range of benefits including, among others, experience, risk reduction through geographic diversification, foreign knowledge acquisition, augmented market power and international scale (Contractor, 2007), our theory conceptualizes market exit as a negative outcome. This assumption is thematically-consistent with the large body of literature that has explored the adverse effects of host market corruption on foreign direct investment flows (Brouthers, Gao, & McNicol, 2008; Cuervo-Cazurra, 2008b; Habib & Zurawicki, 2002).

As such, our research is motivated by two closely-related research questions. First, *does the pervasiveness of host market corruption impact the likelihood of market exit?* Second, *do strategies implemented by the MNE moderate the impact of host market corruption on the likelihood of market exit?* We anticipate that the answers to these questions will be made more complex by recent research that suggests that host market corruption is not a one-dimensional phenomenon. Instead, informal institutions that have been traditionally recognized as discrete institutions within a host market (such as "corruption") have been found to be constituted by distinct dimensions (Sartor, 2014a). We leverage Sartor's (2014a) notion of *informal institutional pluralism* and adopt the conceptualization of host market corruption which distinguishes between *public corruption pervasiveness* and *private corruption pervasiveness*. In doing so, our work

endeavors to facilitate a more nuanced understanding of the role of MNE strategy in moderating the impact of host market corruption pervasiveness on host market exit.

Just as the focal phenomenon in our study has been characterized as pluralistic, the theoretical foundation that informs our conceptual work can also be regarded as pluralistic. More specifically, as Hillman, Shropshire and Cannella (2007: 943) have noted, “resource dependence theory mirrors institutional theory in that legitimacy and conformity to societal expectations are considered key components to organizational survival in both theories.” However, the core precepts of resource dependence theory (RDT) and institutional theory (IT) cast divergent predictions with respect to the strategic responses that can be expected from an MNE that is endeavoring to secure legitimacy in more corrupt host markets. While RDT would suggest that an MNE will pursue legitimacy by undertaking strategic actions to control the subsidiary’s dependence upon other firms for legitimacy (Casciaro & Piskorski, 2005; Pfeffer & Salancik, 2003), IT proposes that an MNE can secure legitimacy through strategic efforts to conform to the institutional environment (Kostova & Zaheer, 1999). Juxtaposing these two theoretical prisms against one another to study the relationship between corruption pervasiveness, MNE strategy and host market exit reveals that the two perspectives are characterized by distinct spatial orientations. More specifically, RDT suggests that subsidiaries will implement *proximal localization strategies* (or, host market-oriented localization strategies) in which host country employees and equity partners (Belderbos & Heijltjes, 2005; Hannon, Huang, & Jaw, 1995; Shan, 1991) are regarded as best-suited to efforts to enhance the subsidiary’s legitimacy, thereby reducing the likelihood of exit from the host country market. Conversely, IT predicts that *distal localization strategies* (or, home market-oriented localization strategies) in which the MNE engages home country employees and equity partners (Doh et al., 2003; Mezas & Mezas, 2010) in the subsidiary investment are better-suited to reducing the likelihood of market exit from increasingly corrupt host countries. Leveraging this theoretical tension, we develop a set of competing hypotheses in order to investigate the comparative impact upon market exit that results from the implementation of *proximal* versus *distal* localization strategies in increasingly corrupt host market environments. Our efforts are consistent with the work of Van de Ven & Johnson (2006: 816) who remind scholars that “important knowledge

advances to theory and practice” are more likely to occur “if the study is designed so that it juxtaposes and compares competing plausible explanations of the phenomenon being investigated.”

While the MNE’s pursuit of legitimacy in the host market underpins the mechanisms that we describe, our empirical work does not focus on measuring legitimacy, nor does it focus on ascertaining whether or not the MNEs in our study actually secure legitimacy. Instead, we assume that the pervasiveness of corruption in the host market threatens to undermine the legitimacy of foreign-investing firms in the host market environment. Consequently, we investigate the efficacy of strategies implemented by the MNE to attenuate this assumed legitimacy deficiency by investigating how MNE strategies moderate the relationship between corruption pervasiveness in the host market and the MNE’s likelihood of host market exit.

We test our hypotheses using a sample of subsidiary investments in 31 countries during the period between 1998 and 2005 using event history analysis. More specifically, we test the moderating effect of an MNE’s *partnering strategy* and *expatriate staffing strategy* upon the relationship between host market corruption and host market exit. Our results reveal an interesting dichotomy. Whereas a proximally-oriented *partnering strategy* (i.e., engaging a host country partner rather than a home country partner in the subsidiary investment) was found to heighten the likelihood of market exit under conditions of more pervasive host market *public corruption*, the opposite outcome was observed in the case of *expatriate strategy*. More specifically, a distally-oriented *expatriate strategy* (i.e., employing a greater proportion of home country nationals in the subsidiary investment) was found to increase the likelihood of market exit under conditions of more pervasive *public corruption* and *private corruption*. Our research advances theory by making two principal contributions. First, we explicate two distinct approaches towards facilitating a subsidiary’s localization into the host country market (*proximal* versus *distal*). Second, we enhance understanding of the veiled relationship between corruption pervasiveness, MNE strategy and host market exit. In doing so, our work provides theoretically-grounded and empirically-supported guidance to MNEs that seek insights with respect to the relative efficacy of various localization strategies that can be implemented in host markets characterized by heightened corruption.



## LITERATURE REVIEW

### **Subsidiary Localization Strategies: Proximal Versus Distal Orientation**

The concept of localization has been researched extensively in the human resource management realm of the international business strategy field in an effort to describe the extent to which expatriate managers are replaced by competent host country employees (Law, Song, Wong, & Chen, 2009). Prior work in this area has focused on the identification of conditions under which localization efforts can be predicted to succeed (Fryxell, Butler, & Choi, 2004). More recently, scholars have endeavored to link successful localization initiatives to enhanced financial performance. In addition to proposing that localization facilitates reductions in operating costs, it also augments the transfer of expertise between expatriates and local employees. Moreover, scholars have maintained that the social ties and networks of local managers foster better communication with employees, customers and government officials, all of which contribute to improved financial performance (Law et al., 2009).

We build on this work and extend the notion of *localization* to conceptualize *subsidiary localization strategies* as *the portfolio of strategic decisions implemented by an MNE in order to facilitate its efforts to integrate a subsidiary within the host country market environment*. Our theory with respect to subsidiary localization builds upon extant scholarship pertaining to an MNE's embeddedness (Andersson, Forsgren, & Holm, 2002) which has been identified as an important antecedent of firm survival (Uzzi, 1996). However, whereas human resource scholars have assumed that successful localization is contingent upon sourcing human capital from within the host country market, we contend that a MNE's portfolio of localization strategies should be evaluated from a broader spatial orientation. Foreign-investing MNEs make innumerable decisions with respect to the geographic origin of the equity capital and human capital that they need to establish and sustain foreign subsidiary operations. As such, scholars have advocated giving more attention to the spatial orientation of a subsidiary's strategies (Dunning, 2009; McCann & Mudambi, 2005) because "aspects of the strategy of MNEs can...be enhanced by a deeper understanding of spatial issues" (Buckley & Ghauri, 2004: 91). Accordingly, we define *proximal localization strategies* as *strategies which employ host market equity capital and human capital to facilitate a subsidiary's integration within the host country*

*market. Conversely, distal localization strategies include strategies which facilitate integration within the host country market by employing equity capital and human capital sourced outside of the host country market.*

## **THEORY AND HYPOTHESES**

### **Host Market Corruption Pervasiveness and Host Market Exit**

Extant theory has conceptualized host market corruption in terms of its *pervasiveness* (Cuervo-Cazurra, 2008a; Rodriguez et al., 2005; Uhlenbruck et al., 2006). The concept of *informal institutional pluralism* suggests that discrete informal institutions such as “corruption” can be conceptualized as being constituted by distinct dimensions. Leveraging this theory, scholars have disaggregated the concept of host market corruption into *public corruption pervasiveness* or, “the average firm’s likelihood of encountering corruption in its normal interactions with public officials” (Rodriguez et al., 2005: 385), and *private corruption pervasiveness* (“the average firm’s likelihood of encountering corruption in its normal interactions with private entities, companies and individuals”) (Sartor, 2014b).

Corruption scholars have defined legitimacy as the “perception...that an organization’s actions are appropriate within a socially constructed system of norms and values” (Pfarrer, Decelles, Smith, & Taylor, 2008: 731). Notwithstanding RDT and IT’s shared conceptualization of “legitimacy” (Hillman et al., 2007), we propose that a distinct spatial orientation characterizes each theory’s predictions with respect to MNE strategies that may be implemented in order to secure legitimacy in more corrupt host market environments. Nevertheless, we do not believe that there is any basis upon which to propose that either theoretical lens would predict different outcomes with respect to the direct relationship between corruption pervasiveness and the likelihood of host market exit. Instead, we expect that as the pervasiveness of both *public corruption* and *private corruption* in the host market increases, the uncertainty that MNEs experience with respect to the prevailing norms and standards of conduct in the host market will become more pronounced. In turn, this poses a more pronounced threat to their legitimacy in the host market and increases the likelihood of market exit. Further, consistent with Husted’s (1994) observations that host market *public corruption* and *private corruption* are not

mutually exclusive, Rodriguez et al. (2006: 739) concluded that “it is clear that government corruption and private corruption often go hand in hand.” Accordingly, we also expect that the interaction between both dimensions of host market corruption will also increase the likelihood of market exit. As such, we hypothesize that

*Hypothesis 1: An MNE is more likely to exit a host market when public corruption is more pervasive in the market.*

*Hypothesis 2: An MNE is more likely to exit a host market when private corruption is more pervasive in the market.*

*Hypothesis 3: The positive relationship between the pervasiveness of public corruption in a host market and an MNE’s likelihood of market exit becomes stronger as the pervasiveness of private corruption increases.*

Beyond these general relationships between these two distinct dimensions of corruption and the likelihood of market exit, we are most interested in exploring the impact of MNE strategies which might moderate the link between corruption pervasiveness (both *public* and *private*) and market exit. More specifically, we propose that, under conditions of more pervasive corruption in the host country market, the spatial orientation of a subsidiary’s strategic decisions will exert a distinct impact upon the likelihood of market exit. In this regard, we compare the relative efficacy of the *proximal localization strategies* that are advocated by RDT with the *distal localization strategies* suggested by IT, giving particular attention to an MNE’s *expatriate strategy* (Hypotheses 4 and 6) and *partnering strategy* (Hypotheses 5 and 7). In doing so, we propose that the *proximal* orientation of an MNE’s *localization strategies* will be manifest in the firm’s preference for joint venture (JV) partnership arrangements that engage a host country equity partner, as well as its preference for a smaller proportion of expatriate employees in the subsidiary investment. Conversely, the *distal* orientation of an MNE’s *localization strategies* will be evidenced by a preference for JV partnerships that engage a home country equity partner and a greater proportion of expatriate employees.

### **Corruption Pervasiveness, Proximal Localization Strategies and Market Exit**

Resource dependence theorists contend that organizations require resources from their environment (Pfeffer & Salancik, 2003) when they are unable to generate these resources internally (Pfeffer, 1982). Consequently, organizations experience resource deficiencies and become interdependent with organizations or entities that control or influence the supply of the required resource (Pfeffer, 1982). Interdependent organizations attempt to manage their resource dependencies by engaging in inter-organizational efforts to reduce these dependencies (Pfeffer & Salancik, 2003). More recently, RDT scholars have extended Pfeffer & Salancik's (2003) conceptualization of the interdependency dynamic to suggest that, more precisely, a power imbalance characterizes the relationship between the resource dependent organization and the entity controlling the required resources (Casciaro & Piskorski, 2005). In this regard, the resource deficiency operates as a constraint on the organization. As such, when a firm encounters a resource deficiency, it will engage in actions that are intended to absorb this constraint (Casciaro & Piskorski, 2005).

Legitimacy has been characterized by RDT theorists as a resource that is critical to firm survival (Zimmerman & Zeitz, 2002). RDT specifies a number of options that are available to a firm in its effort to absorb its external constraints (Scott & Davis, 2007), including among others, the maintenance of alternative suppliers of the resource, engaging in alliances, JVs or other associations to secure access to the resource or, managing the dependence through a merger or acquisition of the organization controlling the resource (Scott & Davis, 2007). Each of these strategies provides the firm with an opportunity "to have its operations redefined as legitimate by associating...with other generally accepted legitimate...institutions or individuals" (Pfeffer & Salancik, 1978: 196). We focus on the role of partnering and staffing strategies in an MNE's efforts to secure legitimacy in increasingly corrupt host country markets.

RDT suggests that JV partnering arrangements can have the effect of reducing environmental uncertainty (Pfeffer & Salancik, 2003). Similarly, international business scholars maintain that the opportunity to secure legitimacy under conditions of heightened environmental uncertainty is one motivation for an MNE's decision to engage in an international JV (IJV) (Schuler, 2001) with a foreign partner (i.e., a non-home

country partner). In IJV partnering arrangements, foreign-investing MNEs have been found to trade ownership for the opportunity to reduce their resource dependence on the broader population of firms in the host market (Shan, 1991). Each parent's share of control over the IJV is dependent, in part, upon their ability to supply resources that the IJV requires to survive and thrive in the local environment (Child & Yan, 1999). In an examination of the resource antecedents of parent control in IJVs, Chen, Park and Newburry (2009) determined that the contribution of tacit resources predicts each parent's degree of control over the IJV.

RDT also suggests that an organization's human resource practices can bolster the organization's ability to manage its dependencies (Pfeffer & Salancik, 2003). In the context of foreign subsidiary investments, heightened local resource dependence has been found to predict an increased use of host market employees by foreign-investing MNEs (Hannon et al., 1995). Consequently, expatriate deployment to the subsidiary investment is less likely (Belderbos & Heijltjes, 2005). Similarly, while Boyacigiller (1990) found that heightened dependence between a subsidiary and its headquarters predicted increased utilization of expatriates in the foreign subsidiary, she speculated that if the main sources of dependence were situated within the host country market, then it could be expected that fewer expatriates would be utilized because host market employees would be better suited to managing the uncertainty associated with dependencies that arise in the host country.

We have proposed that both *public corruption* and *private corruption* exacerbate uncertainty with respect to norms and standards of conduct in more corrupt host market environments, which threatens to undermine the legitimacy of foreign-investing MNEs and heightens the likelihood of market exit. Under conditions of more pronounced host market corruption, RDT theorists have suggested that foreign firms suffer from a legitimacy deficiency (Su, Mitchell, & Sirgy, 2007). Notwithstanding the existence of this deficiency, firms are able to access resources, including legitimacy, "through illegal, unethical and / or unconventional actions" (Zimmerman & Zeitz, 2002: 417). In fact, previous research has revealed that engaging in corruption may help firms to overcome uncertainties associated with the political, legal and financial systems in corrupt host market environments (Zhou & Peng, 2012). Consequently, the foreign firm can be

expected to engage in coordinated behaviors (Pfeffer & Salancik, 2003) designed to access and secure legitimacy from presumably more powerful firms (prospective host market equity partners) and individuals (prospective host country employees) that already possess the legitimacy resource (Steidlmeier, 1999). This is because when a venture becomes networked with established organizations and host country employees, the venture becomes identified with these partners and employees in a manner that confers legitimacy on the new venture (Zimmerman & Zeitz, 2002).

As such, the strategic prescriptions advanced by the RDT perspective are characterized by a spatial orientation that envisions the integration of host country (local) partners and employees into the subsidiary investment in order to bolster the MNE's efforts to secure legitimacy and reduce the likelihood of market exit. Accordingly, we hypothesize that

*Hypothesis 4: The positive relationship between the pervasiveness of host market corruption (public or private) and an MNE's likelihood of market exit is weakened by a decrease in subsidiary expatriate intensity.*

*Hypothesis 5: The positive relationship between the pervasiveness of host market corruption (public or private) and an MNE's likelihood of market exit is weakened when a host country (local) partner is engaged in the JV subsidiary investment.*

### **Corruption Pervasiveness, Distal Localization Strategies and Market Exit**

IT suggests that the strategic actions of firms can be interpreted as being structured by the institutional environment within which the firm is situated. In this context, institutions impose restrictions on activity, as well as providing guidelines for taking action (Scott, 2001). IT suggests that environments characterized by institutional uncertainty create risk for firms. According to this perspective, the survival of the firm is contingent upon its ability to respond to the demands and expectations emanating from the institutional environment (Meyer & Rowan, 1977) and, the ability of the firm to secure external legitimacy from the environment's constituents (DiMaggio & Powell, 1983). IT focuses on the efforts of firms to respond to institutional pressures by acquiescing to local values and norms (DiMaggio & Powell, 1983). Legitimacy has been

characterized by IT theorists as the degree of cultural support for an organization (DiMaggio & Powell, 1983). Meyer & Rowan (1977) maintain that legitimacy is intertwined with access to resources, stability and enhanced prospects for firm survival. In this regard, foreign-investing MNEs are able to secure legitimacy through efforts to conform to the demands of the institutional environment in the host country market (Kostova & Zaheer, 1999).

Corruption can become so intrinsically embedded in a host market that it becomes a fundamental component of a country's institutional environment (Spencer & Gomez, 2011). When firms face uncertainty that is attributable to the institutionalization of corruption, they tend to conform to the pressures emanating from the institutional environment (Uhlenbruck et al., 2006). Spencer & Gomez (2011) found that more pronounced host market corruption will heighten a subsidiary's need to engage in bribery. Prior conceptual work has proposed that an MNE is more likely to enter foreign markets via a wholly owned subsidiary when host market corruption is more pervasive (Rodriguez et al., 2005). Under these circumstances, it has been suggested that MNEs can secure legitimacy by directly complying with corrupt agents, thereby reducing the need to integrate into local networks (Rodriguez et al., 2005).

Despite the fact that MNEs might prefer to enter into increasingly corrupt host market environments via a wholly-owned subsidiary, firms have empirically demonstrated a preference for partnering when host market corruption is highly arbitrary (Uhlenbruck et al., 2006). Further, when cultural distance between the home and host country market is greater, JVs between home country partners have been found to enjoy heightened survivability when compared to JVs constituted by both home and host country partners (Makino & Beamish, 1998). Given that local partners are more embedded in local networks, they tend to be approached more frequently than foreign partners by corrupt agents (Meschi, 2009). Under these circumstances, foreign partners are exposed to heightened costs because the foreign partners rarely have input into the corrupt negotiations and the local partners are more inclined to comply with the demands of the corrupt agent in a less restricted manner (Rodriguez et al., 2005). A firm lacking social legitimacy in a host country market will likely select a partner that has proven its ability to conform to the expectations of institutional constituents with respect to

appropriate business behavior (Dacin, Oliver, & Roy, 2007). We contend that under conditions of heightened host market corruption, the MNE is more likely to choose a partner from the MNE's home country. A partner from the MNE's home country is equally capable of sharing risk and oversight with the foreign-investing MNE (Roy, 2012), as well as providing the MNE with local knowledge and learning (Parkhe, 1993) with respect to how the MNE can interface most efficiently with corrupt agents.

Given the hypothesized preference for either wholly-owned governance or home market-oriented JV partnerships in foreign markets under conditions of heightened corruption pervasiveness, a foreign-investing MNE will require resources from its headquarters in order to support the subsidiary's efforts to directly conform to the institutional environment. Resource support from parent MNEs is often contingent upon the subsidiary's efforts to conform to norms dictated by the headquarters (Hillman & Wan, 2005; Kostova, 1999). Accordingly, we expect that the tension between local adaptation and global standardization in the subsidiary's management practices (Björkman, 2006) will be resolved in favor of global standardization. An increase in the number of expatriates in a subsidiary has been found to predict heightened standardization (Rosenzweig & Nohria, 1994). In fact, the presence of expatriates activates the diffusion of an MNE's standardized practices within a foreign subsidiary (Lu & Bjorkman, 1997).

Taken together, the strategic prescriptions advanced by the IT perspective are characterized by a spatial orientation that envisions the integration of home country employees and partners into the subsidiary investment in order to bolster the MNE's efforts to secure legitimacy and reduce the likelihood of market exit under conditions of more pervasive host market corruption. Accordingly, we hypothesize that

*Hypothesis 6: The positive relationship between the pervasiveness of host market corruption (public or private) and an MNE's likelihood of market exit is weakened by an increase in subsidiary expatriate intensity.*

*Hypothesis 7: The positive relationship between the pervasiveness of host market corruption (public or private) and an MNE's likelihood of market exit is weakened when a home country partner is engaged in the JV subsidiary investment.*



## METHODS

### Data Sources and Key Variables

We tested our hypotheses using a sample of subsidiary investments established in 31 countries<sup>1</sup> during the period 1998 through 2005. The sample was taken from annual editions of the *Kaigai Shinshutsu Kigyō Souran* covering this time period (Toyo Keizai). This data source reports on the worldwide foreign direct investment (FDI) activity of Japanese multinational enterprises (MNEs). To avoid left truncation problems, any subsidiaries for which a founding date was not reported were precluded from the sample. Japanese MNE parents established 4,399 subsidiaries in these 31 foreign markets between 1998 and 2005. The number of subsidiaries included in each of the regression models reported in Tables 14-16 was reduced due to missing values (unreported data), primarily with respect to parent and subsidiary covariates employed in our study. After removing subsidiaries that lacked sufficient data to conduct our regression analyses, our study's sample was constituted by 5,099 observations for 1,239 subsidiary investments situated in the 31 countries during the study period. We lagged our observations of the dependent variable by one year relative to the observations with respect to the measures of *public corruption* and *private corruption* in the host markets. Given that 1997 was the first year for which some of the indicators were available to measure *private corruption* and 2004 was the last year for which data pertaining to one of these indicators was available, our study period was determined by the availability of country-level data.

### Dependent Variable

The dependent variable in our study was a binary measure in which subsidiaries still in existence at the end of the study period were coded with the value of 0, while subsidiaries that exited the market before the end of the study period were coded with the value of 1. Market exit was defined as the disappearance of a subsidiary listed in a previous edition of the *Kaigai Shinshutsu Kigyō Souran* from the subsequent edition of

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<sup>1</sup> The number of subsidiary investments in each country is in brackets: Argentina (2), Australia (17), Austria (1), Belgium (18), Brazil (9), Canada (8), China (371), Czech Republic (8), France (31), Germany (39), Hong Kong (63), Hungary (5), India (15), Indonesia (18), Korea (47), Malaysia (11), Mexico (6), Netherlands (22), New Zealand (6), Philippines (14), Poland (7), Russia (4), Singapore (67), South Africa (4), Spain (9), Switzerland (6), Taiwan (80), Thailand (56), Turkey (2), United Kingdom (52), United States (241).

the data source (Chung & Beamish, 2005). In this regard, subsidiaries that were delisted from the sample were treated as exits because our data source (*Kaigai Shinshutsu Kigyō Souran*) has previously been recognized as closely approximating the population of Japanese FDI (Delios & Makino, 2003; Dhanaraj & Beamish, 2004). Further, prior research has also confirmed that the instances of exit reported in our data source were authentic instances of exit by comparing exits reported in the data source with externally reported accounts of exit (Delios & Beamish, 2004). Further, following prior research, we also treated all instances in which full Japanese ownership of the subsidiary investment was sold off as an instance of market exit by the parent firm (Dai, Eden, & Beamish, 2013). Subsidiaries that continued in existence at the end of the study period were treated as right-censored (Cleves, Gould, Gutierrez, & Marchenko, 2008). As such, our data set provided empirical data indicating the status of each subsidiary at the end of the observation period (2005), as well as the longevity of those subsidiaries that exited prior to the end of the observation period, both of which are required to model the likelihood of market exit (Cleves et al., 2008). In total, we observed 180 exits associated with the subsidiary investments in our sample during the study period.

### **Focal Independent Variables**

*Proximal and distal localization strategies.* We elaborated our theory pertaining to *proximal localization strategies* and *distal localization strategies* by focusing on two different strategies – expatriate strategy and partnering strategy. An MNE's expatriate strategy captures the degree to which the MNE deploys expatriate employees to the subsidiary investment and has routinely been measured in terms of the subsidiary's *expatriate intensity* (or, the ratio of expatriate employees working in the subsidiary to total employees in the subsidiary). Prior research has found that Japanese MNEs have demonstrated a tendency to either not use third country employees in subsidiary investments (Gong, 2003; Tung, 1982) or, to use them very sparingly (Peterson, Napier, & Shul-Shim, 2000). As such, an increase or decrease in Japanese subsidiary *expatriate intensity* implicitly conveys an indication of the MNE's choice between a greater proportion of either home country employees (expatriates) or host country employees.

Partnering strategy focuses on the MNE's choice of partner. Makino and Beamish (1998) developed a taxonomy of JV partnership arrangements which distinguishes between three different JV configurations - *traditional JV* (a JV in which the MNE engages a host country (local) equity partner in the subsidiary investment), *crossnational JV* (in which the MNE engages a home country partner) and *trinational JV* (in which the MNE engages an equity partner from a third country other than the home or host countries). We estimated models using two different cutoff conventions that have been used in the literature to distinguish JV investments from wholly-owned subsidiaries (Yiu & Makino, 2002). Using the 80 percent cutoff, 316 of the subsidiaries in our sample were JV investments, of which 252 (79.7%) were *traditional JVs*, 46 (14.6%) were *crossnational JVs* and 18 (5.6%) were *trinational JVs*. The 95 percent cutoff convention resulted in 367 of the subsidiaries being categorized as JV investments, 280 (76.2%) of which were *traditional JVs*, 69 (18.8%) were *crossnational JVs* and 18 (4.9%) were *trinational JVs*. Consistent with Makino and Beamish's (1998) finding that *trinational JVs* constituted close to 3% of the JV investments in their sample, we also found that *trinational JVs* constituted a relatively nominal proportion of our sample of JVs. As such, given the small proportion of *trinational JVs* in our sample and given that the decision to choose a third country partner does not constitute one of the strategies contemplated by our theory, these JVs were not included in our empirical analyses pertaining to an MNE's partnering strategy.

To summarize, based on our dichotomized conceptualization of a subsidiary's localization strategies as being either *proximal* or *distal*, a subsidiary executing *proximal localization strategies* could be expected to prefer a traditional JV ownership structure (with a home country (local) partner) and to employ a smaller proportion of expatriates in the foreign subsidiary. Conversely, a subsidiary that chooses to implement *distal localization strategies* would be expected to invest through a crossnational ownership structure (with a home country partner), as well as an increased preference for expatriate employees.

***Public corruption pervasiveness and private corruption pervasiveness.*** Prior work that has conceptualized host market corruption in terms of two distinct dimensions (*public* versus *private*) has operationalized *public corruption pervasiveness* using

Transparency International's *Corruption Perception Index* (CPI) scores (Sartor, 2014b). Similarly, we employed the measure of *private corruption pervasiveness* developed by Sartor (2014b), utilizing data from IMD's *World Competitiveness Yearbooks* (WCY) pertaining to insider trading and tax evasion, as well as indicators from the World Economic Forum's *Global Competitiveness Reports* (GCR) with respect to racketeering / organized crime. We conducted a principal components analysis with an orthogonal (varimax) rotation and an eigenvalue cutoff equal to 1 using a holdout sample of subsidiaries that were established in the same host markets during the period 1998-2005. The results supported the theoretically-expected one factor solution. Table 12 presents the factor loadings for each indicator on the *private corruption pervasiveness* construct. A reliability analysis was also conducted and we concluded that the Cronbach's alpha for these three indicators (0.88) was sufficient to establish internal consistency (Nunnally & Bernstein, 1994). Given that the CPI, WCY and GCR data are reported such that low scores indicate high corruption and high scores indicate low corruption, in order to enhance the ease of interpretation of our regression estimations, we reverse-coded all three data sources so that higher scores were indicative of more pronounced corruption pervasiveness in our regression models.

### **Control Variables**

Our study incorporated subsidiary, parent, industry, regional and country-level control variables that have been found to be significant predictors of the likelihood of an MNE exiting a host market. *Subsidiary size* was measured as the log of the subsidiary's capitalization (Chung & Beamish, 2010) and included as a covariate because a positive relationship has been shown to exist between subsidiary size and subsidiary survival (Li, 1995). The focal MNE's proportionate share of equity in the subsidiary investment (*parent ownership level*) has also been found to exert a positive impact on the likelihood of the subsidiary continuing to operate in the host market (Dai et al., 2013). We controlled for *parent size* using the log of the parent MNE's total worldwide sales because larger size provides inertia against instability (Delacroix, 1993). Further,

**TABLE 12**  
**Factor Analysis Results**

Latent construct and associated items		Factor loading
<b>Private corruption pervasiveness <sup>a</sup>:</b>		
Tax evasion	Tax evasion is (1 = a common practice, 10 = not a common practice) in your country.	0.85
Insider trading	Insider trading is (1 = common in the stock market, 10 = not common in the stock market).	0.91
Prevalence of racketeering & extortion	(Racketeering & extortion) in your country (1 = imposes significant costs on business, 7 = does not impose significant costs on business).	0.83

<sup>a</sup> Cronbach's alpha = 0.88

corruption has been found to impair the growth of small firms but not larger firms (Zhou & Peng, 2012). We also controlled for *parent profitability* using the parent MNE's return on assets (the log ratio of income to total assets), as well as *parent leverage* (the difference between total assets and total debt as a percentage of total assets), reasoning that stronger profitability and a greater availability of slack financial resources (Reuer & Ragozzino, 2006) would provide greater stability for the parents' subsidiaries. We controlled for *parent experience* using the ratio of an MNE's foreign sales (exports) to total sales (Chang & Rosenzweig, 2001) because experience has been found to exert a negative impact on subsidiary survival (Gaur & Lu, 2007). Industry effects were controlled for using a dummy variable that categorized firms as either manufacturing or non-manufacturing entities. Given that more than 55% of the subsidiary investments in our study were situated in Asia, we employed a dummy variable (*region*) to distinguish between subsidiaries hosted in Asian countries and subsidiaries established in other regions. *Host market size* has also been found to exert a negative impact on the likelihood

of market exit (Dai et al., 2013). We operationalized *host market size* using the log of each host country's total gross domestic product (Uhlenbruck et al., 2006). Further, our research focuses on the impact of host market corruption pervasiveness (an informal institution) on the likelihood of market exit. Accordingly, we also controlled for the effects of formal institutions on the persistence of these subsidiary investments by operationalizing formal institutions in terms of *FDI restrictions* which we measured using the Heritage Foundation's score for each country pertaining to the restrictiveness of the foreign investment regime in the host market. In doing so, we reasoned that more restrictive formal institutions would provide an indication of the challenges to subsidiary survival posed by the formal institutional environment. Finally, we controlled for *cultural distance*. Among other uses (Robertson & Watson, 2004), the cultural distance construct has been employed in research to explain differences in firm success (Shenkar, 2001). *Cultural distance* was computed as the difference between Japan and the host countries using Hofstede's scores (2001) and Kogut and Singh's (1988) measure of cultural distance.

### **Estimation Method**

Event history analysis or, survival analysis, involves substituting the assumption of normally distributed residuals that characterizes OLS regression (Cleves et al., 2008). Even though linear regression is robust to non-normality, it is not robust to the non-symmetrical distributional features that characterize the survival variable in most data sets employed in event history analysis (Cleves et al., 2008). While the Cox proportional hazards model provides a convenient alternative to linear regression in the context of event history analysis, the technique assumes that at any point in time, the ratio of the hazards for any two subsidiaries will be constant (Allison, 1984). However, if this assumption regarding the proportionality of hazards is wrong, misleading coefficients will be generated (Cleves et al., 2008). As such, analysis based on the Cox proportional hazards model should be accompanied by a test of the proportional hazards assumption to confirm the veracity of the assumption (Allison, 1984). Unfortunately, scholars routinely neglect to test the proportional hazards assumption in studies that use the Cox proportional hazards model (Baba & Goko, 2009). Following the proportional hazards

assumption tests specified in Cleves et al. (2008), we determined that the assumption of proportional hazards could not be verified for our sample. As such, we needed to ascertain a more appropriate distributional assumption with respect to the residuals. Fortunately, parametric event history analysis contemplates the substitution of a more appropriate distributional assumption with respect to the residuals (Cleves et al., 2008). Parametric models offer the advantage of more precise estimates of the coefficients for the variables that predict survival. When the shape of the hazard function is unknown, the Akaike information criterion (AIC) provides a statistically-based approach to determine the most appropriate parametric model (Cleves et al., 2008). The results of our AIC analysis suggested that the lognormal and loglogistic models were the most appropriate parametric models for our sample.

While Model 1 (which is presented in Table 14) was employed to test Hypotheses 1, 2 and 3, Model 2 (presented in Table 15) reports the results associated with our tests of Hypotheses 4 and 6 with respect to *expatriate strategy*. Finally, Table 16 presents Model 3 which tests Hypotheses 5 and 7 pertaining to *partnering strategy*. Robust standard errors were estimated to account for heteroskedasticity (Chung & Beamish, 2010; Dai et al., 2013). Before investigating the effects of any of the interaction terms in our models, the continuous focal independent variables (*public corruption*, *private corruption* and *expatriate intensity*) were centered about their means (Aiken & West, 1991)

## RESULTS

Table 13 presents descriptive statistics and a correlation matrix for our sample. The results of our estimations are presented in Tables 14, 15 and 16. Our regression tables present a base model which excludes the focal corruption variables and the MNE strategy variables (*expatriate strategy* and *partnering strategy*), along with models that introduce the interaction effects predicted in our hypotheses and the associated main effects.

Notably, the correlation between *public corruption pervasiveness* and *private corruption pervasiveness* was found to be 0.95 for our sample. Prior research that focused

**TABLE 13**  
**Descriptive Statistics and Correlations**

Variable	Mean	S.D.	1	2	3	4	5	6	7	8	9
1 Exit	-	-									
2 Expatriate strategy (log)	-0.75	0.58	-0.03								
3 Partnering strategy <sup>a</sup>	-	-	-0.05	-0.23							
4 Subsidiary size (log)	2.17	1.01	-0.02	-0.07	0.08						
5 Parent ownership level	75.82	35.14	-0.05	0.17	0.06	-0.02					
6 Parent size (log)	5.22	0.79	0.10	-0.18	-0.01	0.04	-0.15				
7 Parent profitability	0.01	0.06	-0.03	0.00	-0.01	-0.03	0.01	-0.06			
8 Parent experience	0.16	0.19	-0.02	-0.14	0.00	0.02	0.03	0.13	-0.03		
9 Parent leverage	0.99	0.03	0.01	-0.08	0.01	0.01	-0.07	0.20	0.26	0.08	
10 Industry dummy	-	-	0.09	0.09	-0.07	0.00	0.03	0.09	0.02	-0.12	-0.01
11 Region dummy	-	-	-0.12	-0.21	0.12	0.03	-0.04	-0.03	-0.04	0.01	0.08
12 Host market size (log)	3.01	0.66	0.00	0.10	-0.08	0.03	-0.02	-0.09	-0.02	-0.07	-0.09
13 FDI restrictions	5.96	2.07	0.06	0.16	-0.04	-0.08	0.07	-0.01	0.06	0.00	-0.06
14 Cultural distance	2.88	0.87	-0.02	0.01	0.00	-0.07	0.04	-0.04	0.02	-0.02	0.03
15 Public corruption pervasiveness	4.28	2.29	-0.13	-0.28	0.10	0.08	-0.13	0.08	-0.05	0.05	0.06
16 Private corruption pervasiveness	4.94	1.20	-0.13	-0.24	0.09	0.09	-0.10	0.07	-0.05	0.04	0.06
17 Public corruption x expatriate strategy (log)	-	-	-0.04	0.38	-0.06	0.09	0.07	-0.01	-0.01	-0.03	0.03
18 Private corruption x expatriate strategy (log)	-	-	-0.04	0.35	-0.05	0.09	0.05	0.00	0.00	-0.03	0.02
19 Public corruption x partnering strategy	-	-	0.09	0.14	0.30	-0.04	0.07	-0.06	0.03	-0.01	-0.04
20 Private corruption x partnering strategy	-	-	0.10	0.12	0.25	-0.05	0.05	-0.07	0.04	-0.01	-0.04

Variable	10	11	12	13	14	15	16	17	18	19
11 Region dummy	-0.14									
12 Host market size (log)	0.16	-0.50								
13 FDI restrictions	0.01	-0.37	-0.15							
14 Cultural distance	0.10	0.32	-0.23	-0.11						
15 Public corruption pervasiveness	-0.15	0.61	-0.10	-0.58	-0.21					
16 Private corruption pervasiveness	-0.14	0.51	-0.03	-0.59	-0.32	0.95				
17 Public corruption x expatriate strategy (log)	0.03	0.05	0.04	-0.10	-0.10	0.13	0.15			
18 Private corruption x expatriate strategy (log)	0.02	0.02	0.07	-0.08	-0.16	0.15	0.18	0.95		
19 Public corruption x partnering strategy	0.08	-0.40	0.08	0.39	0.18	-0.68	-0.66	-0.24	-0.25	
20 Private corruption x partnering strategy	0.08	-0.34	0.04	0.41	0.26	-0.66	-0.71	-0.24	-0.27	0.96

<sup>a</sup> Dichotomous dependent variable: *Traditional joint venture* (with a host country (local) partner) or *crossnational joint venture* (with a home country partner).

Correlations with an absolute value greater than 0.08 are statistically significant at the  $p < 0.05$  level. All are two-tailed tests.



TABLE 14

**Results of Event History Analyses of Public Corruption Pervasiveness and  
Private Corruption Pervasiveness on the Likelihood of Market Exit**

Variables	Public and Private Corruption Pervasiveness <sup>a</sup>				
	Base Model	Main Effects			Interaction Effect
	Model 1A	Model 1B	Model 1C	Model 1D	Model 1E
Intercept	1.96 (1.13) <sup>t</sup>	1.59 (1.14)	0.69 (1.17)	1.58 (1.07)	1.65 (1.08)
<i>Subsidiary effects</i>					
Subsidiary size (log)	-0.06 (0.04)	-0.06 (0.04)	-0.06 (0.04)	-0.05 (0.04)	-0.05 (0.04)
<i>Parent effects</i>					
Parent ownership level <sup>b</sup>	0.04 (0.01) **	0.04 (0.01) **	0.04 (0.01) **	0.04 (0.01) **	0.04 (0.01) **
Parent size (log)	-0.16 (0.07) *	-0.16 (0.07) *	-0.17 (0.07) *	-0.16 (0.07) *	-0.16 (0.07) *
Parent profitability	2.49 (0.79) **	2.46 (0.79) **	2.42 (0.79) **	2.42 (0.78) **	2.44 (0.78) **
Parent experience	-0.16 (0.25)	-0.18 (0.25)	-0.19 (0.25)	-0.18 (0.24)	-0.18 (0.24)
Parent leverage	2.06 (0.94) *	2.09 (0.94) *	2.10 (0.92) *	2.07 (0.89) *	2.06 (0.89) *
<i>Industry effect</i>					
Industry dummy	-0.54 (0.11) ***	-0.54 (0.11) ***	-0.53 (0.10) ***	-0.52 (0.10) ***	-0.53 (0.10) ***
<i>Region effects</i>					
Region dummy	0.54 (0.12) ***	0.38 (0.16) *	0.30 (0.16) <sup>t</sup>	0.43 (0.17) *	0.43 (0.17) *
<i>Country effects</i>					
Host market size (log)	0.22 (0.08) **	0.20 (0.08) *	0.16 (0.09) <sup>t</sup>	0.15 (0.09) <sup>t</sup>	0.13 (0.09)
FDI restrictions	-0.05 (0.02) <sup>t</sup>	-0.03 (0.02)	0.00 (0.03)	0.00 (0.03)	0.00 (0.03)
Cultural distance	-0.10 (0.05) <sup>t</sup>	-0.03 (0.06)	0.03 (0.06)	0.03 (0.06)	0.04 (0.07)
<i>Main effects</i>					
Public corruption pervasiveness		0.06 (0.03) <sup>t</sup>		-0.17 (0.09) *	-0.17 (0.09) <sup>t</sup>
Private corruption pervasiveness			0.20 (0.08) **	0.50 (0.18) **	0.49 (0.18) **
<i>Interaction effect</i>					
Public corruption x private corruption					-0.02 (0.03)
Variance inflation factor range	1.02 - 2.00	1.02 - 3.42	1.02 - 3.13	1.02 - 13.78	1.02 - 13.89
Number of observations	5,099	5,099	5,099	5,099	5,099
Number of exits	180	180	180	180	180
$\chi^2$	108.60 ***	108.15 ***	108.52 ***	110.98 ***	114.05 ***
AIC	1497.61	1496.93	1490.95	1488.08	1489.81
Log likelihood	-735.81	-734.46	-731.47	-729.04	-728.90
$\Delta$ log likelihood <sup>c</sup>		1.35	4.34	6.77	6.91

<sup>a</sup> The dependent variable is coded as follows: 0: *survived*; 1: *exited*.

<sup>b</sup> Rescaled by a factor of 10<sup>-1</sup>.

<sup>c</sup> When compared to the base model.

*n* = 1,239 subsidiary investments.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Robust standard errors are in parentheses.

TABLE 15

**Results of Event History Analyses of Public Corruption Pervasiveness,  
Private Corruption Pervasiveness and Expatriate Strategy  
on the Likelihood of Market Exit**

Variables	Expatriate Strategy <sup>a</sup>				
	Interaction Effect: Public Corruption x Expatriate Strategy		Interaction Effect: Private Corruption x Expatriate Strategy		
	Base Model Model 2A	Model 2B	Model 2C	Model 2D	Model 2E
Intercept	1.92 (0.99) <sup>t</sup>	2.68 (1.81)	2.60 (1.83)	2.64 (1.84)	2.63 (1.84)
<i>Subsidiary effects</i>					
Subsidiary size (log)	-0.05 (0.04)	-0.08 (0.07)	-0.08 (0.07)	-0.08 (0.07)	-0.08 (0.07)
<i>Parent effects</i>					
Parent ownership level <sup>b</sup>	0.04 (0.01) **	0.10 (0.02) **	0.10 (0.02) **	0.10 (0.02) **	0.10 (0.02) **
Parent size (log)	-0.14 (0.07) *	-0.23 (0.11) *	-0.23 (0.11) *	-0.23 (0.11) *	-0.23 (0.11) *
Parent profitability	2.24 (0.73) **	2.33 (0.90) **	2.32 (0.90) *	2.33 (0.89) **	2.35 (0.89) **
Parent experience	-0.21 (0.25)	0.04 (0.44)	0.03 (0.45)	0.06 (0.44)	0.05 (0.45)
Parent leverage	1.78 (0.80) *	1.64 (1.64)	1.64 (1.66)	1.67 (1.67)	1.65 (1.67)
<i>Industry effect</i>					
Industry dummy	-0.52 (0.10) ***	-0.47 (0.16) **	-0.46 (0.16) **	-0.47 (0.16) **	-0.46 (0.16) **
<i>Region effects</i>					
Region dummy	0.44 (0.12) ***	0.32 (0.26)	0.34 (0.26)	0.32 (0.24)	0.37 (0.26)
<i>Country effects</i>					
Host market size (log)	0.17 (0.08) *	0.18 (0.12)	0.16 (0.14)	0.16 (0.13)	0.15 (0.13)
FDI restrictions	-0.04 (0.02) <sup>t</sup>	-0.06 (0.03) <sup>t</sup>	-0.05 (0.04)	-0.06 (0.04)	-0.05 (0.04)
Cultural distance	-0.09 (0.05) <sup>t</sup>	-0.08 (0.09)	-0.06 (0.10)	-0.05 (0.10)	-0.05 (0.10)
<i>Subsidiary localization strategy</i>					
Expatriate strategy (log)		-0.27 (0.16) <sup>t</sup>	-0.26 (0.16) <sup>t</sup>	-0.26 (0.16)	-0.26 (0.16)
<i>Main effects</i>					
Public corruption pervasiveness		0.01 (0.05)	-0.05 (0.14)		-0.06 (0.14)
Private corruption pervasiveness			0.15 (0.33)	0.05 (0.13)	0.16 (0.31)
<i>Interaction effects</i>					
Public corruption x expatriate strategy (log)		0.11 (0.07) <sup>t</sup>	0.11 (0.07) <sup>t</sup>		
Private corruption x expatriate strategy (log)				0.33 (0.15) *	0.32 (0.15) *
Variance inflation factor range	1.02 - 2.00	1.04 - 3.35	1.04 - 13.89	1.04 - 3.43	1.04 - 13.86
Number of observations	5,099	3,176	3,176	3,176	3,176
Number of exits	180	77	77	77	77
$\chi^2$	89.97 ***	52.00 ***	52.18 ***	53.36 ***	53.98 ***
AIC	1508.99	706.09	707.66	706.09	707.66
Log likelihood	-741.49	-337.04	-336.83	-335.15	-335.01
$\Delta$ log likelihood <sup>c</sup>		404.45	404.66	406.34	406.48

<sup>a</sup> The dependent variable is coded as follows: 0: *survived*; 1: *exited*.

<sup>b</sup> Rescaled by a factor of 10<sup>-1</sup>.

<sup>c</sup> When compared to the base model.

*n* = 665 subsidiary investments.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Robust standard errors are in parentheses.

TABLE 16

**Results of Event History Analyses of Public Corruption Pervasiveness,  
Private Corruption Pervasiveness and Partnering Strategy on the Likelihood of Market Exit**

Variables	Partnering Strategy <sup>a b</sup>				
	Base Model		Interaction Effect: Public Corruption x Partnering Strategy		Interaction Effect: Private Corruption x Partnering Strategy
	Model 3A	Model 3B	Model 3C	Model 3D	Model 3E
Intercept	-0.96 (6.53)	-1.34 (6.51)	-1.35 (6.54)	-1.35 (6.52)	-1.37 (6.55)
<i>Subsidiary effects</i>					
Subsidiary size (log)	-0.01 (0.06)	-0.01 (0.07)	-0.02 (0.07)	-0.01 (0.07)	-0.01 (0.07)
<i>Parent effects</i>					
Parent ownership level	0.01 (0.00) *	0.01 (0.00) *	0.01 (0.00) *	0.01 (0.00) *	0.01 (0.00) *
Parent size (log)	-0.21 (0.11) <sup>t</sup>	-0.22 (0.11) *	-0.22 (0.11) *	-0.22 (0.11) *	-0.22 (0.11) *
Parent profitability	2.37 (1.83)	2.31 (1.85)	2.31 (1.86)	2.35 (1.84)	2.36 (1.85)
Parent experience	-0.55 (0.42)	-0.45 (0.40)	-0.45 (0.40)	-0.44 (0.41)	-0.45 (0.40)
Parent leverage	5.93 (6.56)	6.47 (6.56)	6.57 (6.59)	6.47 (6.57)	6.56 (6.59)
<i>Industry effect</i>					
Industry dummy	-0.70 (0.15) ***	-0.71 (0.16) ***	-0.73 (0.16) ***	-0.72 (0.16) ***	-0.72 (0.16) ***
<i>Region effects</i>					
Region dummy	0.05 (0.21)	-0.03 (0.26)	-0.02 (0.25)	0.02 (0.25)	-0.01 (0.26)
<i>Country effects</i>					
Host market size (log)	-0.02 (0.16)	-0.04 (0.15)	-0.03 (0.16)	-0.04 (0.15)	-0.02 (0.16)
FDI restrictions	-0.09 (0.03) **	-0.09 (0.03) **	-0.10 (0.03) **	-0.10 (0.03) **	-0.10 (0.03) **
Cultural distance	-0.13 (0.08)	-0.12 (0.09)	-0.15 (0.09)	-0.14 (0.09)	-0.16 (0.08) <sup>t</sup>
<i>Subsidiary localization strategy</i>					
Partnering strategy		-0.26 (0.23)	-0.26 (0.23)	-0.27 (0.23)	-0.26 (0.23)
<i>Main effects</i>					
Public corruption pervasiveness		0.03 (0.05)	0.10 (0.11)		0.08 (0.11)
Private corruption pervasiveness			-0.16 (0.22)	0.02 (0.10)	-0.13 (0.22)
<i>Interaction effects</i>					
Public corruption x partnering strategy		-0.19 (0.11) <sup>t</sup>	-0.19 (0.11) <sup>t</sup>		
Private corruption x partnering strategy				-0.33 (0.22)	-0.34 (0.21)
Variance inflation factor range	1.04 - 1.81	1.05 - 2.76	1.06 - 10.36	1.05 - 2.88	1.05 - 10.54
Number of observations	1,302	1,302	1,302	1,302	1,302
Number of exits	52	52	52	52	52
$\chi^2$	46.53 ***	51.82 ***	53.60 ***	50.73 ***	53.23 ***
AIC	384.01	385.90	387.40	387.39	387.39
Log likelihood	-179.01	-176.95	-176.70	-177.38	-177.10
$\Delta$ log likelihood <sup>c</sup>		2.06	2.31	1.63	1.91

<sup>a</sup> The dependent variable is coded as follows: 0: *survived*; 1: *exited*.

<sup>b</sup> The *partnering strategy* independent variable is coded as follows: 0: *traditional JV* (with a host country (local) partner; 1: *crossnational JV* (with a home country partner).

<sup>c</sup> When compared to the base model.

*n* = 298 subsidiary investments.

<sup>t</sup> *p* < 0.10; \* *p* < 0.05; \*\* *p* < 0.01; \*\*\* *p* < 0.001

All are two-tailed tests. Robust standard errors are in parentheses.

on emerging markets as a research context used the same indicators of *public corruption* and *private corruption* that we employed in this study and found a 0.48 correlation between the two constructs (Sartor, 2014b). When we isolated the emerging market-based subsidiaries in our sample, we found a correlation of 0.53 between the two constructs, whereas the correlation was 0.90 for developed market-based subsidiaries. Given Rodriguez et al.'s (2006: 739) proposition that "it is clear that government corruption and private corruption often go hand in hand", we believe that there are both theoretical and practical reasons for which it can be expected that *public corruption* and *private corruption* exist simultaneously in host markets. Consequently, it seems theoretically imperative that both variables should be included in the same regression estimations. However, in light of the high correlation between the *public corruption* and *private corruption* variables in our study, we recognize that this would pose an increased risk of multicollinearity in our regression estimates. An increase in collinearity is important for at least two reasons. First, the regression equation's standard errors can become inflated and, second, its estimated parameters can become increasingly uncertain or unreliable (Tabachnick & Fidell, 2007). This is manifest in an increased variance inflation factor score (VIF) for the regression model. The normally recommended maximum VIF score in international business strategy research is 10 (Stephan & Uhlaner, 2010). Beyond the high correlation between the *public corruption* and *private corruption* variables, none of the correlations for variables included in the same models in our study exceed the recommended cutoff of 0.70 (Tabachnick & Fidell, 2007). Given this, we implemented two strategies to ensure that the results that we present in Tables 15-16 are robust and unencumbered by concerns regarding multicollinearity.

First, in Tables 15 and 16, we present a model which includes both the interaction effect and one of the corruption main effects, along with a corresponding model which includes the interaction effect and both of the corruption main effects. For example, in Table 15, Model 2B presents a regression estimation which includes the interaction effect between *public corruption* and *expatriate intensity*, along with the main effect of *public corruption* and the main effect of *expatriate intensity*. Our expectation that multicollinearity would not be a concern in this model was supported by the Model's

relatively low maximum VIF score (3.35). Model 2C includes these same three effects and adds the *private corruption* main effect to the model as a covariate. We were not surprised to find that the addition of this highly correlated main effect as a covariate would result in a high maximum VIF score (13.89) for the model. However, our approach allows for a comparison of the focal coefficient (the interaction effect) under conditions of both low multicollinearity and high multicollinearity. We reasoned that if the focal interaction coefficient was relatively similar under both conditions, then this would support our position that multicollinearity was not driving our results.

Second, we re-executed Models 1-3 as two additional sets of estimations by segregating our study's full sample (1,239 subsidiaries) into two sub-samples. One sub-sample was constituted by subsidiaries hosted in developed markets (660 subsidiaries) and the other by subsidiaries hosted in emerging markets (579 subsidiaries). The results associated with these sub-sample robustness checks are presented in Appendix C.

***Public corruption, private corruption and market exit.*** Table 14 presents the results pertaining to the hypotheses that were developed to test the direct relationship between host market corruption and the likelihood of market exit. Both Hypothesis 1 (*public corruption*) and Hypothesis 2 (*private corruption*) predicted that an MNE is more likely to exit a market when corruption is more pervasive in the host market. The significant main effect for *public corruption* ( $\beta = 0.06$ ,  $p < 0.10$ ) in Model 1B ( $\chi^2 = 108.15$ ,  $p < 0.001$ ) provided support for Hypothesis 1. Similarly, the significant main effect for *private corruption* ( $\beta = 0.20$ ,  $p < 0.01$ ) in Model 1C ( $\chi^2 = 108.52$ ,  $p < 0.001$ ) provided support for Hypothesis 2. The maximum VIF was 3.42.

Consistent with Husted's (1994) observations that host market *public corruption* and *private corruption* are not mutually exclusive, Model 1D ( $\chi^2 = 110.98$ ,  $p < 0.001$ ) tests the main effects associated with both dimensions of host market corruption simultaneously. The results reveal that both *public corruption* ( $\beta = -0.17$ ,  $p < 0.05$ ) and *private corruption* ( $\beta = 0.50$ ,  $p < 0.01$ ) significantly predict the likelihood of market exit. However, the results suggest that whereas an increase in the pervasiveness of *private corruption* increases the likelihood of market exit, an increase in *public corruption* reduces the likelihood of exit. As such, while the results support Hypothesis 2, the sign of

the coefficient for *public corruption* is in the opposite direction of the sign predicted by Hypothesis 1. In order to test the interaction effect in Hypothesis 3, Model 1E ( $\chi^2 = 114.05$ ,  $p < 0.001$ ) was estimated to include the main effects for each dimension of corruption, along with the interaction effect between *public* and *private corruption*. The main effects of *public corruption* ( $\beta = -0.17$ ,  $p < 0.10$ ) and *private corruption* ( $\beta = 0.49$ ,  $p < 0.01$ ) both continued to be significant and the signs of the coefficients were unchanged. However, the interaction effect between the two dimensions of corruption was not significant. As such, Hypothesis 3 was not supported. While Models 1D and 1E exhibited high maximum VIF scores (13.78 and 13.89, respectively), when we re-executed these models using the two sub-samples (developed market-based subsidiaries and emerging market-based subsidiaries), the maximum VIF score dropped below the recommended upper limit of 10 (Stephan & Uhlaner, 2010). Further, the interaction effect became significant when we used the emerging market-based sample of subsidiaries. We discuss these results in more detail in the Appendix.

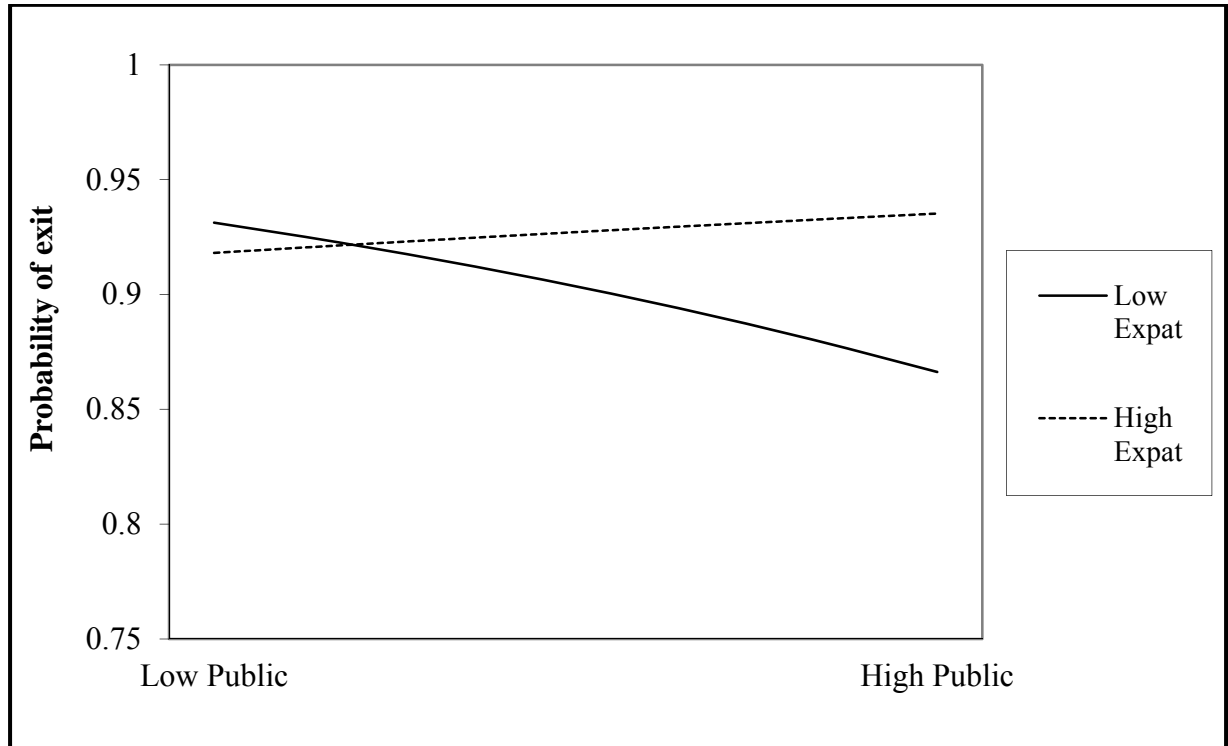
***Expatriate strategy and public corruption.*** Table 15 presents the results with respect to Hypotheses 4 and 6 pertaining to the moderating effect of *expatriate strategy* on the relationship between host market corruption and market exit. Given that some of the MNEs in our full sample did not report the number of expatriates employed in the subsidiary investment, it was not possible to calculate some subsidiaries' *expatriate intensity* for our analyses pertaining to an MNE's *expatriate strategy*. As such, our sample of 1,239 subsidiaries was reduced due to this missing data and our estimations in Table 15 were based on 3,176 observations pertaining to 665 subsidiaries. A total of 77 exits occurred within this sample during the study period. Model 2B ( $\chi^2 = 52.00$ ,  $p < 0.001$ ) was used to test the competition between Hypothesis 4 (which predicted that a decrease in *expatriate intensity* would reduce the likelihood of market exit under conditions of heightened *public corruption*), and Hypothesis 6 which predicted the opposite outcome (an increase in *expatriate intensity* would reduce the likelihood of market exit under conditions of heightened *public corruption*). As discussed above, Model 2B (maximum VIF is 3.35) tests this interaction effect between *public corruption* and *expatriate intensity* without controlling for the main effect of *private corruption*, in

order to allay concerns regarding multicollinearity. Model 2C ( $\chi^2 = 52.18$ ,  $p < 0.001$ ) tests the same interaction effect while also controlling for *private corruption*. Testing this interaction between *public corruption* and *expatriate intensity* revealed a significant effect ( $\beta = 0.11$ ,  $p < 0.10$ ) in both Models 2B and 2C. Figure 6 plots the interaction (Dawson, 2014). The Figure reveals an interesting dichotomy. When the pervasiveness of *public corruption* is low, a decrease in *expatriate intensity* appears to increase the likelihood of market exit. However, as *public corruption* becomes more pervasive in the host market, a decrease in the subsidiary's *expatriate intensity* decreases the likelihood of market exit. As such, we concluded that while the results of Model 2B and 2C are generally supportive of Hypothesis 4 at higher levels of *public corruption*, Hypothesis 6 is supported only at low levels of *public corruption*.

***Expatriate strategy and private corruption.*** Models 2D ( $\chi^2 = 53.36$ ,  $p < 0.001$ ) and 2E ( $\chi^2 = 53.98$ ,  $p < 0.001$ ) in Table 15 were also used to test the comparison between Hypothesis 4 (a decrease in *expatriate intensity* will reduce the likelihood of market exit under conditions of heightened *private corruption*) and Hypothesis 6 which predicted the opposite result (an increase in *expatriate intensity* would reduce the likelihood of market exit under conditions of heightened *private corruption*). These estimations revealed a significant interaction effect (Model 2D:  $\beta = 0.33$ ,  $p < 0.05$ ; Model 2E:  $\beta = 0.32$ ,  $p < 0.05$ ). Notably, the results for the interaction effect coefficient in the model that controlled for *public corruption* (Model 2E) were very similar to the results in the model that did not control for *public corruption* (Model 2D: maximum VIF = 3.43), which supports our position that multicollinearity was not responsible for the focal results. We plotted this interaction in Figure 7 and found that as *private corruption* becomes more pervasive in the host market, a decrease in *expatriate intensity* reduces the likelihood of market exit. As such, we concluded that Hypothesis 4 was supported in the case of *private corruption*, but Hypothesis 6 was not supported.

**FIGURE 6**

**Interaction Effect of Public Corruption Pervasiveness and  
Expatriate Strategy on the Likelihood of Market Exit<sup>a b c</sup>**



<sup>a</sup> High Public and Low Public refer to public corruption pervasiveness one standard deviation above and below the mean for public corruption pervasiveness.

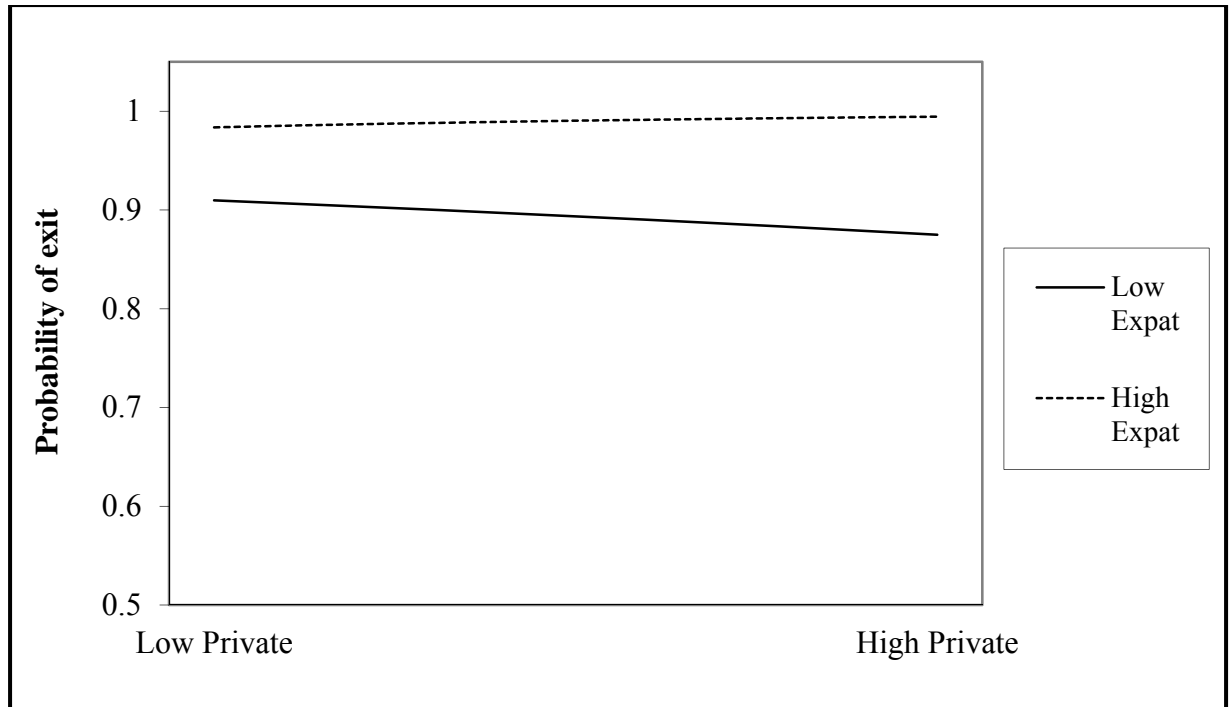
<sup>b</sup> High Expat and Low Expat refer to expatriate intensity one standard deviation above and below the mean for expatriate intensity.

<sup>c</sup> The dependent variable is the probability of subsidiary exit from the host country (the variable is coded as follows: 0: *survived*; 1: *exited*).



**FIGURE 7**

**Interaction Effect of Private Corruption Pervasiveness and  
Expatriate Strategy on the Likelihood of Market Exit<sup>a b c</sup>**



<sup>a</sup> High Private and Low Private refer to private corruption pervasiveness one standard deviation above and below the mean for private corruption pervasiveness.

<sup>b</sup> High Expat and Low Expat refer to expatriate intensity one standard deviation above and below the mean for expatriate intensity.

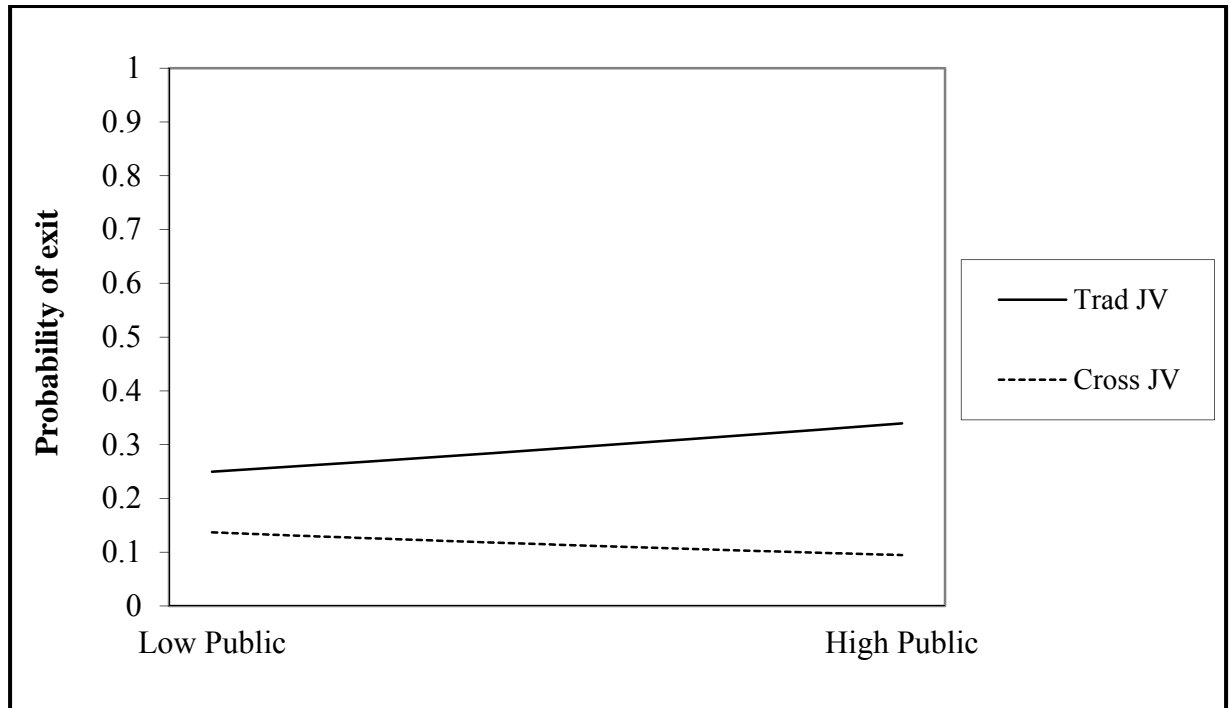
<sup>c</sup> The dependent variable is the probability of subsidiary exit from the host country (the variable is coded as follows: 0: *survived*; 1: *exited*).

***Partnering strategy and public corruption.*** Table 16 presents the results with respect to Hypotheses 5 and 7 pertaining to the moderating effect of *partnering strategy* on the relationship between host market corruption and market exit. This Table is based upon the 80 percent cutoff convention used to distinguish between JVs and wholly-owned subsidiaries (Makino & Beamish, 1998). The results associated with using the 95 percent convention were substantially similar. Model 3B ( $\chi^2 = 51.82$ ,  $p < 0.001$ ) and Model 3C ( $\chi^2 = 53.60$ ,  $p < 0.001$ ) were used to test the competition between Hypothesis 5 (which predicted that engaging a host country partner in the subsidiary investment would reduce the likelihood of market exit under conditions of heightened *public corruption*), and Hypothesis 7 which predicted the opposite outcome (engaging a home country partner in the subsidiary investment would reduce the likelihood of market exit under conditions of heightened *public corruption*). While Model 3C controls for *private corruption*, Model 3B (maximum VIF = 2.76) does not include this main effect. Testing the interaction between *public corruption* and *partnering strategy* produced a significant effect ( $\beta = -0.19$ ,  $p < 0.10$ ) in both Models 3B and 3C. We plotted the interaction in Figure 8 and found that as *public corruption* increases, the decision to engage a home country partner rather than a host country partner in the JV investment reduces the likelihood of market exit. As such, in the case of more pervasive *public corruption* we concluded that Hypothesis 7 was supported, but Hypothesis 5 was not supported.

***Partnering strategy and private corruption.*** Models 3D ( $\chi^2 = 50.73$ ,  $p < 0.001$ ) and 3E ( $\chi^2 = 53.23$ ,  $p < 0.001$ ) both produced a non-significant interaction effect between *private corruption pervasiveness* and *partnering strategy*. As such, we concluded that neither Hypothesis 5, nor Hypothesis 7 was supported in the case of *private corruption*. However, we note that the signs of the focal coefficients in these two models were consistent with the predictions developed in Hypothesis 7. Further, the coefficients for the interaction effects were only marginally non-significant in both Model 3D ( $p = 0.12$ ) and Model 3E ( $p = 0.10$ ).

**FIGURE 8**

**Interaction Effect of Public Corruption Pervasiveness and Partnering Strategy on the Likelihood of Market Exit<sup>a b c</sup>**



<sup>a</sup> High Public and Low Public refer to public corruption pervasiveness one standard deviation above and below the mean for public corruption pervasiveness.

<sup>b</sup> Trad JV (*traditional JV*) refers to a JV with a host country (local) partner. Cross JV (*crossnational JV*) refers to a JV with a home country partner.

<sup>c</sup> The dependent variable is the probability of subsidiary exit from the host country (the variable is coded as follows: 0: *survived*; 1: *exited*).

## DISCUSSION AND CONCLUSIONS

While corruption has become an increasingly important challenge facing MNEs, the phenomenon has been under-researched to date (Rodriguez et al., 2006) and scholars have provided little guidance to MNEs with respect to the relative efficacy of various strategies (Mezias & Mezias, 2010) that could reduce the likelihood of market exit. Our study has investigated the relationship between host market corruption pervasiveness, the subsidiary localization strategies implemented by MNEs and the likelihood of host market exit. We have conceptualized host market corruption as an informal institution that precipitates uncertainty for foreign-investing MNEs because the norms or standards of practice pertaining to these extralegal transactions are frequently ambiguous and indeterminate (Fisman & Gatti, 2006; Lambsdorff, 2005) from the perspective of the foreign-investing MNE. Given that organizations may seek legitimacy in foreign markets by attempting to conform to the prevailing institutional norms in these markets, the uncertainty surrounding informal institutions such as corruption can pose a threat to the firm's ability to navigate the standards of practice or conduct that are required to secure legitimacy. As such, regardless of the MNE's willingness or reluctance to engage in corrupt transactions in the host market, host market corruption functions as a source of uncertainty for foreign-investing MNEs, particularly in markets characterized by more pervasive corruption. In turn, this poses a threat to the firm's legitimacy in the host market and heightens the likelihood of market exit. Given the range of benefits associated with internationalization (Contractor, 2007), our theory has been based on the assumption that market exit is a negative outcome.

In light of the foregoing, our research questions were developed to advance two broad propositions. First, more pervasive host market corruption can be expected to increase the likelihood that MNEs will choose to exit the market. Second, MNEs can implement strategies that reduce the increased likelihood of market exit in countries characterized by more pervasive corruption. To elaborate our theory, we expanded the conceptualization of localization strategies and specified two broad categories of strategies that we believe are pertinent to an MNE's efforts to localize its subsidiary operations and secure legitimacy within a host market environment. While *proximal localization strategies* were defined to include *strategies which employ host market*

*equity capital and human capital to facilitate a subsidiary's integration within the host country market, distal localization strategies include those which facilitate integration within the host country market by employing equity capital and human capital sourced outside of the host country market.* To test our hypotheses pertaining to the efficacy of *proximal* (host market-oriented) *localization strategies*, we investigated the effects of an MNE's increased reliance on host country employees and equity partners to enhance the subsidiary's legitimacy and reduce the likelihood of host market exit. Conversely, the efficacy of *distal* (home market-oriented) *localization strategies* was assessed in terms of an MNE's preference for home country employees and equity partners.

The nuanced results that emerged from our empirical analyses were highly consistent with recent theory pertaining to informal institutional pluralism (Sartor, 2014a). More specifically, the results reveal that the answers to our research questions pertaining to the direct effects of corruption on market exit, as well as the moderating impact of an MNE's subsidiary localization strategies, are dependent upon both the dimension of corruption being considered (*public* or *private*) and the host market context (developed market or, emerging market). Although our theory was not developed to elaborate the market context distinction, our results suggested its inclusion through our robustness analyses. Our findings reveal that while the interaction effect between *public corruption* and *private corruption* significantly increases the likelihood of market exit from emerging markets (as reported in Appendix C), this effect was not significant when we conducted the same estimations using our full sample of subsidiaries (both developed market-based and emerging market-based) or, when we tested the developed market sample alone. Taken together, these results could be interpreted as suggesting that the adverse effects of corruption are more pertinent to an MNE's decisions regarding market exit when the subsidiary investment is situated in an emerging market, rather than in a developed market.

Table 17 summarizes our findings from Tables 15-16 and broadly suggests that with respect to a foreign-investing MNE's *expatriate strategy*, an increasingly *proximal* (host market-oriented) approach can be expected to reduce the likelihood of market exit under conditions of more pervasive *private corruption* and *public corruption* (except at very low levels of *public corruption*). However, in considering its *partnering strategy*, a

more *distal* (home market-oriented) approach can enhance an MNE's efforts to reduce the likelihood of market exit under conditions of more pervasive *public corruption*, but not *private corruption*. Furthermore, while we did not find that *expatriate strategy* exerted a statistically significant moderating effect in the sub-sample estimations

**TABLE 17**  
**Summary of Findings Pertaining to Moderating Effects**

Strategy	Localization Strategy	Corruption Dimension	Market Context (Location of Subsidiaries) <sup>a</sup>	Likelihood of Host Market Exit
Expatriate	Proximal (lower expatriate intensity)	Public	Both DM & EM	<b>Mixed results</b> <sup>b</sup>
			DM	N/S <sup>c</sup>
			EM	N/S
		Private	Both DM & EM	<b>Decreased</b>
			DM	N/S
			EM	N/S
	Distal (higher expatriate intensity)	Public	Both DM & EM	<b>Mixed results</b> <sup>d</sup>
			DM	N/S
			EM	N/S
		Private	Both DM & EM	<b>Increased</b>
			DM	N/S
			EM	N/S
Partnering	Proximal (host country (local) JV partner)	Public	Both DM & EM	<b>Increased</b>
			DM	N/S
			EM	<b>Increased</b>
		Private	Both DM & EM	N/S
			DM	N/S
			EM	N/S
	Distal (home country JV partner)	Public	Both DM & EM	<b>Decreased</b>
			DM	N/S
			EM	<b>Decreased</b>
		Private	Both DM & EM	N/S
			DM	N/S
			EM	N/S

<sup>a</sup> DM = developed markets; EM = emerging markets.

<sup>b</sup> Increased likelihood of market exit at low levels of public corruption and decreased likelihood of market exit as public corruption increases (see Figure 1).

<sup>c</sup> N/S = no significant moderating effect found.

<sup>d</sup> Decreased likelihood of market exit at low levels of public corruption and increased likelihood of market exit as public corruption increases (see Figure 1).

pertaining to the developed market- and emerging market-based subsidiaries, our re-estimations with respect to the emerging market sample did reveal that a more *distal* (home market-oriented) *partnering strategy* continued to weaken the positive relationship between *public corruption pervasiveness* and host market exit.

We acknowledge that our interpretation of the empirical results is contingent upon an assumption that underpins our theory, namely, that market exit is a negative outcome. For example, in finding that an increase in expatriate intensity increases the likelihood of market exit under conditions of more pervasive host market corruption, our theory would attribute this relationship to the inability of expatriate employees to facilitate the MNE's efforts to secure legitimacy in increasingly corrupt host markets. Based on this assumption, market exit is conceptualized as a reactive decision. Reversing our assumption regarding market exit reveals an alternative interpretation with respect to our results. Market exit can also be assumed to be a positive outcome because it facilitates an MNE's efforts to minimize the sunk costs associated with languishing foreign investments (Hill, Hwang, & Kim, 1990). From this perspective, the fact that an increase in expatriate intensity increases the likelihood of market exit under conditions of more pervasive host market corruption could be interpreted as evidencing an MNE's heightened visibility into the current state of its subsidiary operations. An MNE's more nuanced comprehension of the challenges (i.e., corruption) encountered by the subsidiary in the host market environment may result from deploying a greater proportion of expatriates to the foreign investment (Boyacigiller, 1990) and lead to a proactive decision to exit the market.

### **Limitations and Future Directions**

Either way, the results of our empirical analyses provide general support for our theory pertaining to the spatial orientation (Buckley & Ghauri, 2004; Dunning, 2009) of an MNE's localization strategies (*distal* versus *proximal*). Nevertheless, we also acknowledge several limitations in our work. First, our study was conducted using a sample of firms from a single home country (Japan). Future work should seek to confirm our findings and test our theory using a sample of subsidiary investments that originate in a home market other than Japan or, from multiple home markets. Second, while our study

endeavored to investigate the relationship between corruption, MNE strategy and market exit, we are not yet able to explain how these firm strategies interact in practice with the phenomenon of corruption to either heighten or diminish the likelihood of market exit. This dilemma is not surprising given the elusive nature of the norms surrounding informal institutions such as corruption (Lambsdorff, 2005). We believe that intensive, case study-driven qualitative research might be the most productive approach towards fostering a richer comprehension of these mechanisms. Nevertheless, we are cognizant that corruption is inherently difficult to study because "...the parties involved have every reason to keep the data hidden" (Klitgaard, 1991: 30). Third, while the MNE's quest for external legitimacy (within the host country market) in more corrupt host countries underpins the mechanisms in our theory, a consideration of the relevance of internal legitimacy (within the MNE network) (Lu & Xu, 2006) was beyond the scope of our work. However, we contend that, using appropriate data, future research with respect to efforts to secure internal legitimacy could be conducted in an effort to advance our spatially-oriented theory pertaining to subsidiary localization strategies. In this regard, our theory is useful to institutional theorists because the tension that emerges from a subsidiary's efforts to secure both external legitimacy and internal legitimacy frequently manifests itself in a decision between proximally- and distally-oriented localization strategies. Consequently, our dichotomization of *subsidiary localization strategies* could be employed by IT scholars to study the strategic localization efforts of foreign subsidiaries confronted by a diverse array of institutional stimuli in the host country market. Finally, our research also reveals that in addition to studying the phenomenon of corruption broadly across the MNE's global network of subsidiary investments, corruption-oriented research should also consider partitioning the MNE's investments into developed market-based and emerging market-based investments in order to secure a more nuanced understanding of the relationships being investigated.



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## APPENDIX C

### Results of the Robustness Checks Using Two Separate Sub-Samples (Developed Market-Based Subsidiaries and Emerging Market-Based Subsidiaries)

In order to ensure that the results presented in Tables 14-16 are robust and unencumbered by concerns regarding multicollinearity, we re-executed Models 1-3 as two additional sets of estimations by segregating our study's full sample of 1,239 subsidiaries into two sub-samples. While one sample was constituted by subsidiaries hosted in developed markets (660 subsidiaries), the other included only subsidiaries hosted in emerging markets (579 subsidiaries). Although these robustness analyses are not presented in tables, the results can be made available upon request.

#### Model 1 (Table 14): Corruption and Market Exit

**Developed market-based subsidiaries.** Re-executing Model 1 using the sample of developed market-based subsidiaries, Model 1D ( $\chi^2 = 102.87$ ,  $p < 0.001$ ) revealed that the signs of the coefficients remained unchanged and the level of significance improved (Public corruption:  $\beta = -0.89$ ,  $p < 0.001$ ; Private corruption:  $\beta = 1.06$ ,  $p < 0.001$ ). While these results continued to support Hypothesis 2, they did not support Hypothesis 1. Model 1E ( $\chi^2 = 104.14$ ,  $p < 0.001$ ) yielded results which were also consistent with the results for the full sample that are presented in Table 14. More specifically, both the main effects of *public corruption* ( $\beta = -0.86$ ,  $p < 0.001$ ) and *private corruption* ( $\beta = 1.10$ ,  $p < 0.001$ ) continued to be significant, the signs of the coefficients were unchanged from those presented in Table 14, and the interaction effect between the two dimensions of corruption continued to be not significant. As such, Hypothesis 3 was not supported. Notably, the maximum VIF (8.71) in these re-executed models dropped below the commonly accepted upper limit of 10 (Stephan & Uhlaner, 2010)

**Emerging market-based subsidiaries.** Re-executing Model 1D ( $\chi^2 = 58.76$ ,  $p < 0.001$ ) yielded results which supported neither Hypotheses 1 nor 2. However, Model 1E ( $\chi^2 = 69.36$ ,  $p < 0.001$ ) did produce results which supported Hypothesis 1 with respect to the main effect of *public corruption* ( $\beta = 0.25$ ,  $p < 0.10$ ). While *private corruption* ( $\beta = -0.47$ ,  $p < 0.05$ ) was found to be significant, the sign of the coefficient was opposite of the predicted sign and, as such, Hypothesis 2 was not supported. However, most interesting

was our finding that the interaction effect ( $\beta = 0.75$ ,  $p < 0.01$ ) in Model 1E was significant, suggesting that the combined effect of an increase in the pervasiveness of *public corruption* and *private corruption* in a host emerging market heightens the likelihood that an MNE will exit the market. As such, Hypothesis 3 was supported when Model 1E was re-executed using the sample of emerging market-based subsidiaries. Given the considerably lower correlation between *public corruption* and *private corruption* for the sample of emerging market-based subsidiaries (0.53), when compared to the same correlation for the developed market-based subsidiaries (0.90), we were not surprised to find that using the sample of emerging market-based firms to re-estimate Models 1D and 1E resulted in a maximum VIF score (3.89) which was substantially lower than the maximum VIF (13.89) presented in Table 14.

#### **Model 2 (Table 15): Corruption, Expatriate Strategy and Market Exit**

Using the sample of developed market-based subsidiaries and the emerging market-based subsidiaries, we re-executed the Model 2 estimations in Table 15 that were developed to test Hypotheses 4 and 6 pertaining to *expatriate strategy*. In each of these re-executed models, the interaction effect was rendered not significant. However, when re-executing the models in Table 15 using the sample of developed market-based subsidiaries, the signs of the interaction effect coefficients in each of these models were entirely consistent with the results presented in Table 15 using the full sample which supported Hypothesis 4.

#### **Model 3 (Table 16): Corruption, Partnering Strategy and Market Exit**

Using the sample of developed market-based subsidiaries and the emerging market-based subsidiaries, we re-executed the Model 3 estimations in Table 16 that were developed to test Hypotheses 5 and 7 pertaining to *partnering strategy*. Interestingly, we found much more nuanced results than we did in re-executing the *expatriate strategy* models.

*Developed market-based subsidiaries.* Re-executing Models 3B and 3C rendered the interaction effect between *public corruption* and *partnering strategy* non-significant for the developed market-based subsidiaries. Consistent with our findings for the full

sample in Models 3D and 3E of Table 16, the interaction between *private corruption* and *partnering strategy* continued to be not significant.

***Emerging market-based subsidiaries.*** Re-executing Models 3B ( $\chi^2 = 46.54$ ,  $p < 0.001$ ) and 3C ( $\chi^2 = 61.44$ ,  $p < 0.001$ ) using the sample of emerging market-based subsidiaries yielded results in which the focal coefficients for both the main and interaction effects were highly consistent with the results using the full sample. Both models produced a significant interaction effect (Model 3B:  $\beta = -0.63$ ,  $p < 0.05$ ; Model 3C:  $\beta = -0.64$ ,  $p < 0.01$ ) which revealed that, under conditions of more pronounced *public corruption*, engaging a home country partner in the JV reduced the likelihood of market exit. As such, these models were supportive of Hypothesis 7. The maximum VIF in these models was 3.50.

The interaction effect between *private corruption* and *partnering strategy* was not significant when Models 3D and 3E were re-executed using the sample of emerging market-based subsidiaries. However, just as the coefficients were consistent with Hypothesis 7 and only marginally non-significant when Models 3D and 3E were executed using the full sample, the same was also true for the coefficients in these re-executed Models 3D ( $p = 0.11$ ) and 3E ( $p = 0.10$ ). The maximum VIF in these models was 3.52.



## CHAPTER 5

### GENERAL CONCLUSIONS

Institutional scholars and international business strategy researchers have recognized the need to develop theory, frameworks and constructs to facilitate corruption-based inquiry (Lambsdorff, Taube, & Schramm, 2005; Rodriguez, Uhlenbruck, & Eden, 2005). Nevertheless, we have continued to lack a comprehensive, theoretically-based and empirically-validated understanding of how host market corruption affects the subsidiary-level strategic behavior of multinational enterprises (MNEs) in foreign markets. This is problematic because it undermines scholar's ability to formulate theoretically-grounded predictions with respect to the strategic behavior of MNEs under conditions of heightened host market corruption, as well as their ability to recommend strategies that will enhance the likelihood of achieving positive investment outcomes. As such, this dissertation has been developed to address two broad research questions. First, *how does host market corruption impact the equity-based market entry strategies implemented by MNEs with respect to their foreign subsidiary investments?* Second, *how do subsidiary-level strategies moderate the influence of host market corruption upon the continued existence of these subsidiary investments?*

*Essay 1* (Chapter 2) synthesized insights from institutional theory and integrative social contracts theory to disaggregate the concept of "government corruption" (Rodriguez et al., 2005) into two dimensions – *grand corruption* and *petty corruption*. While extant theory has used the terms *government corruption* and *public sector corruption* interchangeably (Rodriguez et al., 2005; Uhlenbruck, Rodriguez, Doh, & Eden, 2006), in the interest of consistency, I adopted the term *government corruption* in *Essay 1*. Although prior research found that more pervasive host market government corruption precipitates an MNE's preference for nonequity-based entry over equity-based entry into foreign markets (Uhlenbruck et al., 2006), less was known about MNEs that choose equity-based strategies. Rodriguez et al. (2005) suggested that the pervasiveness of host market corruption would influence the equity ownership decisions of these MNEs. However, subsequent research never found a statistically significant relationship that empirically validated this proposition. *Essay 1* built upon Uhlenbruck et al.'s (2006)

observation that the phenomenon of corruption might be more nuanced than had been previously expected. As such, the theory developed in *Essay 1* extended the concept of institutional pluralism (Kraatz & Block, 2008) and introduced the notion of *informal institution pluralism*. In doing so, it proposed that discrete informal institutions (such as government corruption) within a host market could be conceptualized as pluralistic phenomena constituted by distinct dimensions which are disparate both in their origin and their impact on the foreign entry strategy of MNEs. Leveraging integrative social contract theory's *hierarchy of norms* concept, I suggested that the distinct origins of the norms pertaining to *grand corruption* and *petty corruption* effectively precipitate different types of uncertainty (*environmental* and *behavioral*) for foreign-investing MNEs which, in turn, motivate MNEs to vary their equity-based entry strategies. More precisely, under conditions of more pervasive *grand corruption*, I theorized that the primary source of uncertainty will be *environmental (response) uncertainty*, while *behavioral uncertainty* will predominate under conditions of heightened *petty corruption pervasiveness*. My empirical analyses revealed that more pervasive *grand corruption* increases the likelihood that foreign-investing MNEs engage in joint venture (JV) investments with host country partners. Second, an increase in the pervasiveness of *petty corruption* was found to precipitate the opposite outcome. Namely, under conditions of more pervasive *petty corruption*, firms that chose to invest through a JV are more likely to engage a partner from the foreign-investing MNE's home country. Finally, an increase in the pervasiveness of *petty corruption* was found to weaken the hypothesized positive relationship between *grand corruption pervasiveness* and the likelihood that MNEs would invest in JVs.

*Essay 2* (Chapter 3) employed the theory pertaining to *informal institutional pluralism* to investigate the structure of equity-based foreign subsidiary investments in emerging markets, focusing specifically upon the *public* and *private* dimensions of corruption pervasiveness in foreign host markets. I theorized that an MNE's choice of structure and entry strategy is contingent upon the pervasiveness of each dimension of corruption in the host market. Further, I proposed that the primary mechanism driving the distinct approaches to foreign entry was the firm's anticipated reliance on different sources of bargaining power to reduce information asymmetries that it expects to

encounter in its public sector transactions and private sector transactions in the host market. More specifically, I hypothesized that under conditions of more pervasive *public corruption*, the firm's *resources* are likely to be a more prominent source of bargaining power in its public sector transactions, when compared to the bargaining power that the firm derives from its *context* (or, its other alternatives). Conversely, under conditions of more pervasive *private corruption*, I expected that the firm's *context* or, the availability of alternatives within the host country, is likely to be a more prominent source of bargaining power than it is in the case of its public sector transactions. In this study, an increase in *public corruption pervasiveness* was found to increase the likelihood that MNEs will invest via JV ownership with a host country (local) partner, while an increase in *private corruption pervasiveness* was found to increase the likelihood that MNEs will invest through a wholly-owned structure when entering foreign emerging markets. Further, an increase in the pervasiveness of *private corruption* was found to negatively moderate the likelihood that MNEs would invest in a JV with a local partner under conditions of more pervasive *public corruption*.

*Essay 3* (Chapter 4) focused on the relationship between host market corruption pervasiveness, the subsidiary localization strategies implemented by MNEs and the likelihood of host market exit. I assumed that the pervasiveness of corruption in the host market threatens to undermine the legitimacy of foreign-investing firms in the host market environment. Despite the fact that the tenets of resource dependence theory and institutional theory converge on the conceptualization of "legitimacy", the theories are also characterized by a degree of divergence, particularly when the theories are employed to study the phenomenon of corruption. Leveraging this theoretical tension, I extended the prior literature on localization to introduce the concept of *subsidiary localization strategies* which I disaggregated into *proximal localization strategies* (*strategies which employ host market equity capital and human capital to facilitate a subsidiary's integration within the host country market*) and *distal localization strategies* (*those strategies which facilitate integration within the host country market by employing equity capital and human capital sourced outside of the host country market*). I investigated the relative efficacy of these strategies by developing hypotheses that posed divergent predictions with respect to the moderating impact of *proximal* and *distal* localization

strategies upon the likelihood of market exit in increasingly corrupt host market environments. First, I hypothesized that *proximal* (or, host market-oriented) *localization strategies*, in which subsidiaries prefer to engage host country partners and employees in the subsidiary investment, would be better-suited to reducing the likelihood of exit from increasingly corrupt host market environments. Next, I predicted that *distal* (or, home market-oriented) *localization strategies*, in which home country partners and employees are engaged in the subsidiary investment, would be best-suited to efforts to enhance the subsidiary's legitimacy and reduce the likelihood of host market exit. My empirical analyses revealed that a proximally-oriented *partnering strategy* heightened the likelihood of market exit under conditions of more pervasive host market *public corruption*, but not more pervasive *private corruption*. Conversely, a distally-oriented *expatriate strategy* increased the likelihood of market exit under conditions of both more pervasive *public corruption* and *private corruption*.

### **Contributions**

This dissertation makes a number of conceptual and empirical contributions. To broadly summarize, I have presented empirical and theoretical support for the foundational theory of host market corruption in international business strategy research (Rodriguez et al., 2005). Moreover, I have extended the conceptualization of host market corruption in terms of its ethical origins (*grand* versus *petty*), in terms of its sectoral origin (*public* versus *private*), and in terms of its impact upon the strategy and structure of MNEs' foreign subsidiary investments. I have also contributed new tenets to institutional theory by introducing the concepts of *informal institutional pluralism* (conceptualizing informal institutions as pluralistic phenomena), *proximal* (host market-oriented) *localization* and *distal* (home market-oriented) *localization strategies*.

More precisely, in *Essay I*, I extended the conceptual domain of institutional pluralism (Kraatz & Block, 2008). While prior work has focused on the strategic relevance of institutional pluralism created by geographic space, my theory suggests that discrete institutions within a host market can themselves be characterized as pluralistic institutional phenomena, constituted by distinct dimensions that exert different impacts upon the strategies of foreign-investing MNEs. Empirically, I independently replicated an

important component of Uhlenbruck et al.'s (2006) findings, providing further support for the theory which proposed that MNEs would be more likely to favor nonequity-based entry over equity-based entry under conditions of more pervasive host market government corruption. However, I also presented new theory that disaggregates the concept of *government corruption pervasiveness* into two distinct dimensions (*grand corruption pervasiveness* and *petty corruption pervasiveness*). Employing this refined conceptualization, I shed new light on the relationship between the *equity*-based foreign entry strategy of MNEs and the pervasiveness of government corruption.

In *Essay 2*, I synthesized the research of international business strategy scholars and business ethicists by refining the conceptualization of “host market corruption” to incorporate a consideration of both its public and private sector dimensions. By focusing on the role of a firm’s bargaining power in shaping its strategic foreign entry decisions under conditions of more pervasive host market corruption, my work contributes to efforts to more closely integrate market and nonmarket strategy research. More specifically, I have drawn attention to an important theoretical mechanism that could be used to bridge the institutionally-oriented and resource-oriented perspectives that have been advocated by strategy theorists as a means to enhance our understanding of the strategic relevance of contemporary nonmarket phenomena such as corruption (Doh, Lawton, & Rajwani, 2012). This research also offered important insights for policy makers. Two key assumptions have traditionally underpinned the policy recommendations of anti-corruption scholars (first, corruption primarily occurs within firm-government transactions; second, engaging a partner is a key strategy employed by firms to manage the increased uncertainty precipitated by public corruption). My research suggests that policy prescriptions designed to curb MNE engagement in foreign market corruption must consider the multidimensional nature of the construct in order to ensure that policy efforts are not misguided. To date, scholars have focused on formulating policy recommendations that are designed to reduce the efficacy of the transaction cost-reducing strategies employed by firms to facilitate corrupt transactions (Lambsdorff, 2002; Svensson, 2003). My findings that *public corruption* and *private corruption* each exert a distinct impact upon the foreign-investment decisions of MNEs, coupled with my

findings pertaining to the interaction effect between both types of corruption upon these foreign entry strategies, suggests the need for more nuanced anti-corruption initiatives.

Finally, in *Essay 3*, by elaborating two distinct approaches towards facilitating a subsidiary's localization into the host country market (*proximal* versus *distal*), I have enhanced our comprehension of the veiled relationship between corruption pervasiveness, MNE strategy and host market exit. In doing so, my work provides theoretically-grounded and empirically-validated guidance to MNEs that seek insights with respect to the relative efficacy of various localization strategies that can be implemented in host markets characterized by heightened corruption. Testing this theory revealed that the direct effects of corruption on market exit, as well as the moderating impact of an MNE's subsidiary localization strategies, are dependent upon both the dimension of corruption being considered (*public* or *private*) and the host market context (developed market or, emerging market).

### **Limitations**

As is often true of most research endeavors, my work is not without limitations. The most significant limitation to my work has been the challenge associated with engaging in qualitative analysis that could either confirm or contradict my theory and quantitative analysis. In this regard, my research experience indirectly provides support for Klitgaard's (1991: 30) seemingly timeless observation that corruption is so difficult to study because "...the parties involved have every reason to keep the data hidden." Closely related to this challenge has been the limitation posed by the availability of quantitative data. While non-governmental agencies such as Transparency International (TI) have made significant advances in developing and collecting data (such as TI's *Corruption Perceptions Index*) that help us to broadly understand public sector- or, government-oriented corruption over time in foreign markets, longitudinal data with respect to the multiple, more fine-grained dimensions of host market corruption that I theorize in this dissertation is lacking. As one example, an important limitation in my research has been the absence of a comprehensive index to operationalize the *private corruption pervasiveness* construct (Faria, Morales, Pineda, & Montesinos, 2012), akin to the *Corruption Perceptions Index* that is available to measure *public corruption*. I hope

that my research will either stimulate an agency's efforts to collect the data needed to develop and maintain such an index or, provide me with an opportunity to pursue the development and maintenance of such as index.

### **Future Research**

This dissertation enhances our understanding of how host market corruption affects the subsidiary-level strategic behavior of multinational enterprises (MNEs) in foreign markets. Further, it equips scholars and managers to formulate theoretically-grounded predictions with respect to the strategic behavior of MNEs under conditions of heightened host market corruption. However, the theory and constructs that I have developed also open up new lines of inquiry that promise to further extend our comprehension with respect to the phenomenon of corruption and its relationship with MNE strategy, as well as exposing new research opportunities outside the domain of corruption-oriented international business strategy research.

At the very least, my dissertation provides a point of departure for what I believe are two important areas for future research inquiry. First, my research collectively suggests that in the context of corruption-oriented research, the distinction between developed market-based and emerging market-based investments may be highly pertinent to efforts to secure a more nuanced understanding of the relationship between host market corruption and MNE activity. Second, while my work has sought to build upon and extend prior work in economics that has focused extensively on the country as the unit of analysis (i.e., the relationship between corruption and dependent variables such as foreign direct investments flows, economic growth, etc.), my research has concentrated on firm-level strategic analysis. An opportunity exists for behavioral scholars to leverage my theory and empirical findings to explore unanswered research questions pertaining to increasingly more micro levels of analysis and to better comprehend how decisions pertaining to the strategy and structure of subsidiary investments unfold under conditions of more pervasive host market corruption. Just as my research promises to inform the work of scholars whose research focuses on these more micro levels of analysis, I expect that their findings will reverberate back and generate insights that are relevant to scholars working at the firm-level.

Both of these research undertakings are imperative. As I noted in Chapter 1 of this dissertation, without a theoretically-based understanding of the interrelationship between host market corruption and subsidiary-level strategy in foreign markets, it becomes more difficult to prescribe how MNEs can effectively integrate the Global Compact's tenth principle (*Businesses should work against corruption in all its forms, including extortion and bribery*) into the business strategies, operations and structures of their foreign subsidiaries. In developing a framework designed to secure corporate commitment to the Global Compact's principles, the United Nations has suggested that the engagement of worldwide subsidiary operations is one of the most important avenues through which MNEs can scale-up corporate responsibility efforts (Kell, 2012). It's my sincere hope that this dissertation makes a contribution to this timely and important endeavor.



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## MICHAEL A. SARTOR

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### **EDUCATION:**

Ivey Business School, Western University	2014
Doctor of Philosophy (PhD) in General Management	
Ivey Business School, Western University	2004
Master of Business Administration (MBA)	
Osgoode Hall Law School, York University	1995
Juris Doctor (JD)	
Queen's University	1992
Bachelor of Arts (Honors)	

### **RESEARCH PUBLICATIONS:**

#### Refereed Journal Publication:

- Sartor, Michael A. & Beamish, Paul W. (forthcoming). Offshoring innovation to emerging markets: Organizational control and informal institutional distance. *Journal of International Business Studies*.

#### Published Book:

- Mu, Fengli & Sartor, Michael A. (eds.) (2012). *Legal-Business Management*. Beijing, China: Economy & Management Publishing House, (in Simplified Chinese and English, 278 pp.). ISBN 978-7-5096-1905-6.

#### Published Book Chapter:

- Sartor, Michael A. (2013). Organizing and executing a longitudinally based research program. In Paavilainen-Mäntymäki, E. & Hassett, M. (eds.), *Handbook of longitudinal research methods in organisation and business studies*, 318-350. London: Edward Elgar Publishing Limited. ISBN 978-0-85793-678-3.

#### Peer-Reviewed Conference Proceedings:

- Sartor, Michael A. (2013). *Host markets, informal institutions and strategy formulation*. Administrative Sciences Association of Canada, International Business Division Proceedings, 34(10): 47-52.
- Sartor, Michael A. (2012). *Latent transaction costs: Evidence from an internationalizing SME*. Administrative Sciences Association of Canada, International Business Division Proceedings, 33.

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- Sartor, Michael A. (2010). *Intellectual property-intensive MNEs' entry into China*. Administrative Sciences Association of Canada, International Business Division Proceedings, 31(8): 95-113.

### **RESEARCH PRESENTATIONS:**

#### **Refereed Conference Presentations:**

- Sartor, Michael A. (2014). *Corruption, multinational enterprise strategy and foreign subsidiary survival*. Academy of Management Annual Meeting (International Management Division - Divisional Paper Session). Philadelphia, USA.
- Sartor, Michael A. (2013). *Government corruption and multinational enterprise strategy*. Strategic Management Society Annual International Conference (Global Strategy Track). Atlanta, USA.
  - Nominee: *Best Conference Paper*.
  - Nominee: *Best Paper for Practice Implications*.
- Sartor, Michael A. (2013). *The impact of informal institutions on MNE strategy*. Academy of Management Annual Meeting (International Management Division - Divisional Paper Session). Orlando, USA.
  - Winner: *GWU-CIBER Best Paper on Emerging Markets*.
  - Finalist: *Douglas Nigh Award for Cross-Disciplinary Research*.
- Sartor, Michael A. (2013). *Multilevel normative institutions: Host market bribery and multinational enterprise strategy*. Academy of International Business Annual Meeting (Institutions, Governance and Corporate Social Responsibility Division - Competitive Session). Istanbul, Turkey.
- Sartor, Michael A. (2013). *Host markets, informal institutions and strategy formulation*. Administrative Sciences Association of Canada (International Business Division). Calgary, Canada.
  - Winner: *Best Student Paper Award*.
- Sartor, Michael A. (2012). *The structure and performance of reverse-innovating subsidiaries in emerging markets*. Academy of International Business Annual Meeting (Emerging Markets Division - Competitive Session). Washington, D.C.
- Sartor, Michael A. (2012). *Latent transaction costs: Evidence from an internationalizing SME*. Administrative Sciences Association of Canada (International Business Division). St. John's, Canada.
- Sartor, Michael A. (2011). *Corruption and firm strategy: A multilevel analysis of theory and evidence*. Academy of International Business Annual Meeting (Institutions, Governance and Corporate Social Responsibility Division - Competitive Session). Nagoya, Japan.

- Sartor, Michael A. (2011). *The entry strategies of reverse-innovating MNEs in emerging markets: The effects of regulative and normative institutional distances*. Administrative Sciences Association of Canada (International Business Division). Montreal, Canada.
  - Winner: *Best Student Paper Award*.
- Sartor, Michael A. (2010). *Intellectual property-intensive MNEs' entry into China*. Administrative Sciences Association of Canada (International Business Division). Regina, Canada.

#### Invited Research Presentations:

- University of South Carolina Moore School of Business and School of Law Corruption Symposium (*Institutional Capacity, Corruption and Development*). Columbia, South Carolina, USA (2014).
  - Invited presenter: *Anti-corruption efforts in the private sector* panel.
- Strategic Management Society (SMS) Global Strategy Division Paper Development Workshop. Atlanta, USA (2013).
  - Invited participant: *Government corruption and multinational enterprise strategy*.
- Academy of Management (AOM) Doctoral Consortium (International Management Division). Orlando, USA (2013).
- Academy of International Business (AIB) Doctoral Consortium. Istanbul, Turkey (2013).
  - Winner: *AIB-Sheth Doctoral Dissertation Proposal Award*.
- Canadian Business Ethics Research Network (CBERN) Winter Research Meeting. York University, Toronto, Canada (2013).
  - Invited presenter: *Multinational enterprise strategy and foreign market corruption*.

#### **RESEARCH-BASED SCHOLARSHIPS:**

##### Externally-Funded, Research-Based Competitive Scholarships:

- Ontario Graduate Scholarship (with Distinction): (2013-2014).
- Social Sciences and Humanities Research Council of Canada (SSHRC) Doctoral Fellowship: (2012-2013).
- Ontario Graduate Scholarship: (2011-2012).

#### **PROFESSIONAL AFFILIATION AND ACADEMIC MEMBERSHIPS:**

- The Law Society of Upper Canada.
- Academy of International Business.
- Academy of Management.
- Strategic Management Society.