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A double-edged sword? The antipodal effects of institutional distance on partner selection in cross-border alliances

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ABSTRACT

Careful partner selection is a prerequisite for successful alliances. I posit that institutional distance will influence partner selection in international technological alliances negatively for exploitation, and positively for exploration alliances. A longitudinal dataset of firms in the global tire industry confirms firms' preference for similar cognitive, normative, and regulatory partners in exploitation alliances, and a preference for dissimilar partners in exploration alliances. However, the latter is true for differences across the regulative and cognitive pillars rather than for normative differences. These findings attest to the antipodal role of institutional differences in the selection of prospective partners for cross-border technological alliances.

1. Introduction

Technological alliances have become a popular strategy over the last decades (Anand & Khanna, 2000; Gulati, 1995a; Rothaermel & Boeker, 2008). Firms form explorative and exploitative alliances (Lavie & Rosenkopf, 2006; Sarala, Junni, Cooper, & Tarba, 2014) to access complementary technologies (Prahalad & Hamel, 1990), reduce uncertainty (Burgers, Hill, & Kim, 1993), enter new markets (García-Canal, Valdés-Llaneza, & Sánchez-Lorda, 2008), spur performance (Yamakawa, Yang, & Lin, 2011), or improve their strategic options (Weber & Tarba, 2014). However, as firms rush to leverage these benefits, they often ignore potential losses from alliance mismatches (Ireland, Hitt, & Vaidyanath, 2002) that ultimately result in high failure rates (Kale & Singh, 2002; Park & Ungson, 1997). To avoid such outcomes, firms must carefully select their partners (Shah & Swaminathan, 2008), especially in international settings (Dacin, Hitt, & Levitas, 1997; Dong & Glaister, 2006).

Employing elements from transaction costs economics (TCE) and resource-based theory (RBV), prior studies show that successful selection of alliance partners depends on the complementarity between them in terms of characteristics and resources (Hitt, Dacin, Levitas, Arregle, & Borza, 2000; Hitt, Ahlstrom, Dacin, Levitas, & Svobodina, 2004; Rothaermel & Boeker, 2008). Others suggest that, despite this need for complementarity, partners must share compatible skills, routines, and strategies for the alliance to function well (Dacin et al., 1997; Glaister, 1996). Besides the individual characteristics of partnering firms, alliances are also subject to agency problems arising from misalignment of partners' goals (Eisenhardt, 1989), separation of ownership and control mechanisms (Reuer & Ragozzino, 2006) and project-specific behavior of partners (Shah & Swaminathan, 2008). Thus, the uncertainty firms face (Beckman, Haunschild, & Phillips, 2004), level of mutual trust (Anand & Khanna, 2000; Gulati, 1995a), social and strategic interdependence (Gulati, 1995b), product and technological relatedness (Krammer, 2016), as well as prior commitments to the alliance (Mohr & Spekman, 1994) have all important implications for the selections of partners.

In addition to the above firm-specifics, the selection of alliance partners in an international context needs to overcome idiosyncratic differences between countries stemming from economic, political, legislative, and social factors (Hitt et al., 2000; Parkhe, 2003). Firm behavior does not occur in an organizational vacuum (Dacin, Ventresca, & Beal, 1999) but is rather nested in the institutional environment in which it operates (Ambos & Håkanson, 2014; Brouthers & Brouthers, 2000; Krammer, Strange, & Lashitew, 2018; Meyer, Estrin, Bhaumik, & Peng, 2009). As a result, institutional distance between home and host country plays an important role in determining different elements of MNE strategy, such as entry modes (Lu, 2002), staffing (Gaur, Delios, & Singh, 2007), inter-firm collaborations (Park & Ungson, 1997) or export activities (He, Brouthers, & Filatotchev, 2013).

Given the existing institutional heterogeneity worldwide (Meyer et al., 2009), it is important to understand how institutional distance affects MNE's selection of strategic partners (Hitt, Li, & Worthington, 2005). However, with few exceptions, this issue has yet to receive significant attention in the literature. For example, Hitt et al. (2000) identify significant differences in competences sought from foreign partners between firms from emerging (i.e., financial resources, assets,

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technologies) and developed economies (i.e., unique competences, local market knowledge). Moreover, Hitt et al. (2004) point out that institutional differences are important even among emerging economies themselves, and contrast their effects on the partnering preferences of Chinese versus Russian managers. These inherent differences are confirmed by more recent studies focusing on the Indian (Chand & Katou, 2012) and Chinese subnational contexts (Ahlstrom, Levitas, Hitt, Dacin, & Zhu, 2014). Finally, Roy and Oliver (2009) show that the selection of foreign partners is contingent on the host-countries' regulatory environments, such as the rule of law or control of corruption. While all these studies provide important foundations for understanding the role of institutions in the selection of alliance partners, they also exhibit important limitations in terms of generality and scope by being confined to few countries and/or single institutional dimensions that fail to capture compellingly the considerable institutional heterogeneity across the world (Hitt et al., 2004) and its subsequent effects on different types of inter-firm alliances (Kale & Singh, 2009).

In response to these challenges, I explore partner selection for alliances through the lens of TCE theory (Gulati & Singh, 1998), supplemented by institutional (Kostova, 1999) and learning (Grant & Baden-Fuller, 2004) rationales. Once a firm identifies a pool of possible international partners that are committed, compatible and complementary, it must decide which one(s) to actually partner with, and I content that, in addition to firm-specific factors, country-specific rationales will also play an important role in this process (Parkhe, 1991). Specifically, I propose that firms seeking exploitation will prefer partners from closer cognitive and normative environments and similar or superior regulatory ones, given coordination concerns, absorptive capacity issues, and appropriation risks that can affect the transfer of technologies and the potential for rents from these alliances (Belderbos, Jacob, & Lokshin, 2018; Delerue & Simon, 2009; Gulati & Singh, 1998; Michailova & Hutchings, 2006). In turn, I suggest that institutional distance will relate positively to selection of partners for exploration, given the increased opportunities for learning, cross-feeding, pooling of resources, institutional arbitrage, and lower risks of leakages (Gimeno, 2004; Noteboom et al., 2007; Nathan & Lee, 2013).

These hypotheses are tested using a hand-collected dataset that covers all firms in the global tire industry and their alliances between 1985 and 2003. Following previous studies in this area, I focus on horizontal agreements (Lavie & Rosenkopf, 2006; Mowery, Oxley, & Silverman, 2002) for both theoretical clarity (Phelps, 2010) and consistency with the particularities of this industry, in which technological alliances occur almost exclusively between tire producers (Acha & Brusoni, 2005). The results of the empirical analysis broadly support my conjectures regarding the antipodal effects of institutional distance on the selection of international alliance partners.

Accordingly, this work proposes several contributions. First, it advances the alliance literature by theorizing and testing the importance of environmental contingencies, in this case of institutional nature, in the process of partner selection. While most prior studies on the selection process have paid significant attention to the firm-specific contingencies (Shah & Swaminathan, 2008; Weber & Tarba, 2014; Yamakawa et al., 2011), our knowledge on the mechanisms through which external environments may affect these choices is still very limited, particularly in terms of generality and international scope (Ahlstrom et al., 2014). By examining how different institutional environments affect the selection of partners in a truly global context (i.e., numerous home and home countries), it offers more comprehensive explanations for this phenomenon that advance significantly this stream of literature (Hitt et al., 2000, 2004; Roy & Oliver, 2009).

The second contribution is to examine the process of partner selection by focusing on learning objectives of the alliance as an important inducement of this process. In doing so, I distinguish between exploitation alliances, which involve the use of technologies already known (March, 1991), and explorative ones that aim to develop new technologies or competences for securing new strategic opportunities (Koza & Levin, 1998). Given these fundamental differences, my theoretical arguments suggest that institutional distance will have antipodal effects on the appeal of partners for exploitative versus explorative interactions. Together these insights extend TCE theory by expounding mechanisms through which the institutional background of prospective partners may become either a benefit or a liability for a technological alliance, contingent on the latter's learning objectives.

Third, I differentiate the concomitant effects of several institutional pillars on partnering decisions, given their different, yet complementary, nature (Scott, 2001). Exploitation of technological assets via alliances involves unidirectional transfer of technology from one (focal) firm to its partner(s); as such, it is sensitive to normative (Steensma, Marino, Weaver, & Dickson, 2000), regulatory (Oxley, 1999) and cognitive (Kelly, Schaan, & Joncas, 2002) differences between partners, which may entail additional costs or opportunities for such alliance. In contrast, institutionally-distant partners will be more appealing for exploration given firms' need to diversify and complement each other's knowledge (Schildt, Maula, & Keil, 2005). The empirical results broadly support these antipodal effects of different institutional pillars on selection of partners for exploitation versus exploration alliances, with the exception of differences in terms normative institutions, which appear to hinder both types of endeavors. Consequently, these results support the idea of complex interactions between institutions and firm strategies across different institutional pillars, and advance our knowledge on these issues by proposing and testing the "double-edged sword" effect of institutional distance on partner selection for alliances.

2. Background and theory

A central issue for alliance formation is the quest for a suitable partner (Gulati, 1995a, 1995b; Hitt et al., 2000). Surveys confirm that most managers see partner selection as the most important factor for alliance success, one that firms should continuously perfect if they are to improve the outcome of their alliances (Glaister, 1996). Whereas a thorough selection procedure involves careful screening and a commitment of substantial resources, it pays major dividends in terms of improving the flow of knowledge, resource and skills into and within the alliance, thereby meaningfully increasing the ability of firms to meet their strategic objectives (Geringer, 1991).

While firm-specific factors (e.g., complementarity, compatibility, trust, strategic interdependence, relatedness) present important explanations for a successful selection of alliance partners, in international transactions, country-specific factors (e.g., differences in economic development, governmental policies) exacerbate the repercussions of a potential mismatch (Dacin et al., 1997; Dong & Glaister, 2006; Parkhe, 2003). Among them, institutional characteristics have been found to be particularly relevant for MNE strategies (Brouthers & Brouthers, 2000; Kostova & Zaheer, 1999; Meyer et al., 2009), however such factors have rarely been studied in conjunction with partner selection, let alone in relation to different alliance types in terms of objectives and underlying requirements.

2.1. Exploitation and exploration in alliances

Strategic alliances are often formed with the primary purpose of acquiring (i.e., learning and absorbing) or providing (e.g., licensing or exchanging) knowledge to partnering firms (Grant & Baden-Fuller, 2004). Following March (1991), I distinguish between explorative and exploitative knowledge quests and consider their respective alliance ramifications.

Explorative knowledge involves intense search, high risk, discovery, and the pursuit of novelty. It usually takes the organization away from its established and comfortable knowledge base, which is expressed in its structure and routines, into new domains and unchartered territory. For the firm, exploration holds the promise of long term survival and