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The impact of country-of-origin on the acceptance of foreign subsidiaries in host countries: An examination of the 'liability-of-foreignness'

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ABSTRACT

This paper examines the relationship between an organization's country-of-origin and the acceptance into a host country environment by constituents such as vendors, suppliers, and distributors. This study contributes to the literature by proposing the examination and ultimate measurement of various tangible and intangible sources of the 'liabilities of foreignness'. Additionally we show that are these sources are internal and external moderators of perceived acceptance in the host country. Manager must recognize the country-of-origin strategic options to address the negative overshadowing of the liability-of foreignness. We conclude that not doing so can create a stigma that may be attached to the overall organization, its image, products, brands, and to its employees. Further, negative attribution may be caste upon all the identifying characteristics of the foreign entity. The management of the firm must note the potential resistance to accept the organization and its products/services and must develop a proactive set of strategies to address the negativism of the host country constituents.

"Stigmatization, at its essence, is a challenge to one's humanity . . . both the stigmatized person and of the stigmatizer . . ."
(Dovidio, Major, & Crocker, 2000, p. 1)

1. Introduction

The accelerating rate of globalization has and will continue to increase the span of geographic involvement of organizations, potentially increasing the risk for overseas subsidiaries (Debebe, 2008; Douglas & Craig, 2011). For example, given the economic and cultural distance between western organizations and emerging countries environmental context this risk may be manifested in the establishment of subsidiaries in emerging markets. The tendency to expand business in these markets is rooted in a recent study conducted by IBM, suggesting that by the year 2050 roughly seven-eighths of the world's population will be living in emerging economies such as China, India, Russia, Mexico, Brazil, and so forth (IBM, 2008).

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Organizations that take advantage of these predictions will first of all require an immense shift in strategic perspective. In addition, global management has to develop the ability to predict and assess the implications of cultural stigmatization (i.e., a cultural/social regulatory tactic that judges certain groups as being deviated from the dominating or majority standard: Crocker, Major, & Steele, 1999; Pinel, 1999) on various characteristics of an organization when expanding into emerging markets (Ocampo, 2002).

The uncertainties faced by foreign entrants are extremely difficult to anticipate and or eventually to overcome given the lack of cultural understanding by both host and home country constituents (Craig, Greene, & Douglas, 2005); the extant literature identifies such cultural gaps in understanding as the liability-of-foreignness (LOF) (Meschi & Riccio, 2008; Moeller & Harvey, 2011; Yildiz & Fey, 2011). The liabilities-of-foreignness is viewed as the additional costs organizations face when operating abroad, these cost and: (1) costs directly associated with spatial distance between parent and subsidiaries; (2) specific costs incurred exclusively by foreign subsidiaries due to unfamiliarity with host-country environments; (3) costs resulting from economic nationalism and a lack of legitimacy in the host country; and (4) costs from sales restrictions imposed by the home country. While this list is not exhaustive, it identifies key sources of additional costs facing foreign organizations operating abroad. Similarly, researchers identify culture and language differences, economic and political regulations, and spatial difference between parent and subsidiary as the causes of the liability-of-foreignness (Griffith, 2006; Harvey & Novicevic, 2002a, 2002b; Matsuo, 2000; Zaheer, 1995).

Despite the recent economic downturn, organizations continue to globalize and do so at an increasing rate each consecutive year (GRTS, 2008). Globalizing, in essence, refers to the expansion of business across various countries/regions, some of which, depending on your country-of-origin, may be more or less economically, politically, and socially developed. Along with the expansion of physical locations comes the relocation of home/host country employees (i.e., expatriates, inpatriates, flexpatriates) (Konopaske, Robie, & Ivancevich, 2009; Scullion & Collings, 2006; Scullion, Collings, & Gunnigle, 2007).

While various works have addressed the issue of overcoming the 'liability-of-foreignness' of individuals, less attention has been paid to the organizational level of analysis concerning the a prolonged acceptance in a host country (Williamson, 2008). As subsidiaries continue to be built in emerging markets (or subsidiaries of emerging market firms in developed markets), mainly due to the economic feasibility of available organizational resources, such decisions do not always take into account the fact that the organization may not be welcomed by the local people and/or businesses. In other words, foreign organizations are disadvantages in comparison to native organizations by gaps in understanding caused by cultural variations present in the organization's external and internal environments (e.g., institutional practices, procedures, corruption, consumption, etc.) (Chen, Griffith, & Hu, 2006; Dwyer, Mesak, & Maxwell, 2003; Yildiz & Fey, 2011).

It is therefore imperative to an organization's long-term success to develop and be able to rely on a number of new external stakeholder relationships such as those with suppliers, vendors, and distributors in the host country (Calhoun, 2002; Hult, Cavusgil, Deligonul, Kiyak, & Lagerstrom, 2007). Based on the opportunities present in expanding globally, we want to investigate the impact of an organization's country-of-origin (COO) on the acceptance of the organization by home country constituents (i.e., vendors, suppliers, and distributors). The notion behind examining this relationship is to explore the factors that either diminish or enhance preconceived notions of 'liabilities of foreignness' (Dovidio, Major, & Crocker 2000; Roth & Romeo, 1992; Zaheer, 1995) of home country nationals based on the perceived economic classification of foreign organizations.

While the overall intention of this work is to expand on previous research efforts by examining the relationship between an organization's COO and ultimate acceptance of an organization in a host country, the specific purpose of this paper is two-fold. First, we are interested in analyzing the relationship between an organization's COO and a host country organization's predisposition towards entering into a contract with an organization from particular foreign countries (Lee, Chen, & Lu, 2009). Secondly, our intent is to investigate the impact of tangible and intangible sources of 'liabilities of foreignness' that mitigate the relationship between a host country organization and a foreign organization's acceptance in the host country environment (Johansson, Douglas, & Nonaka, 1985; Zaheer & Mosakowski, 1997). The importance of this work lies in the fact that globalization will continue to have an impact on individuals and organizations alike; therefore, increasing effort to understand and assess these dimensions of risk may provide insight into ways to decrease an organization's 'liability-of-foreignness' and aid in gaining a sustained global competitive advantage. The key concepts used in this paper are defined in Table 1.

The premise of this paper lies in what the literature defines as 'stigmatization', a bias expressed by individuals relative to the home country organization (Amine, 2008; Mascarenhas, 1995). This concept is important because as cultural distance increases, the potential for conflict due to stigmatization of foreign organizations rises (Riddle & Brinkerhoff, 2011; Wagner, 2004). Following the discussion of the purpose, this work will proceed as follows: first, we will address the notion of an organization's COO and how it may impact a constituent's predisposition towards the organization's headquarters location based on Stakeholder Theory. We will also address the impact of global awareness (from a clustered standpoint) on the proposed relationship. Secondly, we will examine the relationship between the predisposition and the acceptance of the organization in the host country. Based on status inconsistencies, we analyze the tangible and intangible sources that may or may not allow organizations to enter foreign markets with long-term success. In essence, we investigate means of avoiding and/or overcoming cultural and social barriers frequently referred to as the 'liability-of-foreignness'. Practical implications for global organizations are also presented.