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Business group reputation and affiliates' internationalization strategies

Debmalya Mukherjee[a,*], Erin E. Makarius[a], Charles E. Stevens[b]

[a] The University of Akron, Department of Management, College of Business Administration, 259 South Broadway, Akron, OH 44325, United States
[b] Lehigh University, Department of Management, College of Business and Economics, 621 Taylor Street, Bethlehem, PA 18015, United States

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ABSTRACT

The literature on business groups (BGs) has identified reputation as a critical factor in their success and survival. However, most studies have assumed that BGs are well-known and well-regarded—an assumption that may not be tenable in the context of international expansion. We use signaling theory to explore the causes of an unacknowledged source of BG heterogeneity—variance in their reputation prominence (whether they are well-known or not) and reputation quality (whether they are regarded favorably or unfavorably)—and seek to understand how this heterogeneity may result in differences in BG affiliates' geographic scope and location choices as they internationalize.

1. Introduction

Business groups (BGs) are collections of interconnected yet legally independent businesses, and have several attributes that make them a unique organizational form (Elango, Pattnaik, & Wieland, 2016; Jones & Khanna, 2006; Khanna and Palepu, 1997, 2000). A growing body of research delving into the dynamics of BGs and BG-affiliated firms (henceforth, "affiliates") has identified reputation as critical to their success (Holmes, Hoskisson, Kim, Wan, & Holcomb, 2016). BGs are often well-known and perceived favorably at home, making them the most dominant organizational form in many emerging economies[1] (Khanna & Palepu, 1997; Manikandan & Ramachandran, 2015). A positive reputation helps BGs gain greater access to foreign capital and technological resources (Khanna & Palepu, 2000), and Lamin (2013) argued that "business group affiliation … confers additional information-based advantages, such as third-party referrals and general reputation, that enable group-affiliated firms to then capitalize on these opportunities." This research on BG reputation is based on the literature on 'reputation borrowing' (Petkova, Rindova, & Gupta, 2013; Stuart, Hoang, & Hybels, 1999; Vanacker & Forbes, 2016) and assumes that the BG an affiliate is associated with is both well-known and well-regarded. Consequently, BG reputation has been suggested to be a positive factor for affiliates as they internationalize beyond their home market (Lamin, 2013).

In this paper, we challenge the assumptions that (1) BGs are always well-known and well-regarded and that (2) reputation is always a positive factor for affiliates as they go abroad. Instead, the organizational reputation literature finds systematic variance in firms' *reputation prominence* (how well it is known) and their *reputation quality* (whether it is viewed positively or negatively) (Gao, Zuzul, Jones, & Khanna, 2017; Lange, Lee, & Dai, 2011; Vanacker & Forbes, 2016; Wei, Ouyang, & Chen, 2017). The BG literature has not yet adequately acknowledged this inherent variance in firm reputation, however. Thus, it remains unclear as to what specific factors may cause differences to emerge with respect to BGs' reputation prominence and quality, or what consequences this variance in BGs' reputation may have for affiliates' international expansion. These limitations in the literature lead us to our research questions: What factors unique to BGs may lead to differences in their reputation? How may a BG's reputation impact its affiliates' internationalization strategy?

We believe that signaling theory (Spence, 1973, 2002) is uniquely suited to address these questions. Signaling theory treats reputation as an important 'signal' used by external stakeholders to evaluate a firm (Connelly, Certo, Ireland, & Reutzel, 2011). The theory argues that the actions and attributes of firms affect the observability and the reliability of the signals that they emit, meaning that unique aspects of BGs (e.g., their higher level of diversification, frequent reliance on social and political ties, and strong formal and informal horizontal intra-firm linkages) may result in variance in how well they are known and how favorably they are perceived. Additionally, the theory's fundamental tenets imply that BG reputation is a costly signal to build and can be difficult for affiliates to "take with them" when they internationalize (Bergh, Connelly, Ketchen, & Shannon, 2014). This is because no matter how the BG is perceived at home, it may or may not be perceived

* Corresponding author.
E-mail addresses: dmukher@uakron.edu (D. Mukherjee), makarius@uakron.edu (E.E. Makarius), ces213@lehigh.edu (C.E. Stevens).

[1] BGs are also present in developed markets; however, their presence in emerging markets is ubiquitous (Khanna & Yafeh, 2007; Yaprak & Karademir, 2010). As such, we focus specifically on emerging market BGs in this paper; when we use the term BGs, we are referring to emerging market BGs.

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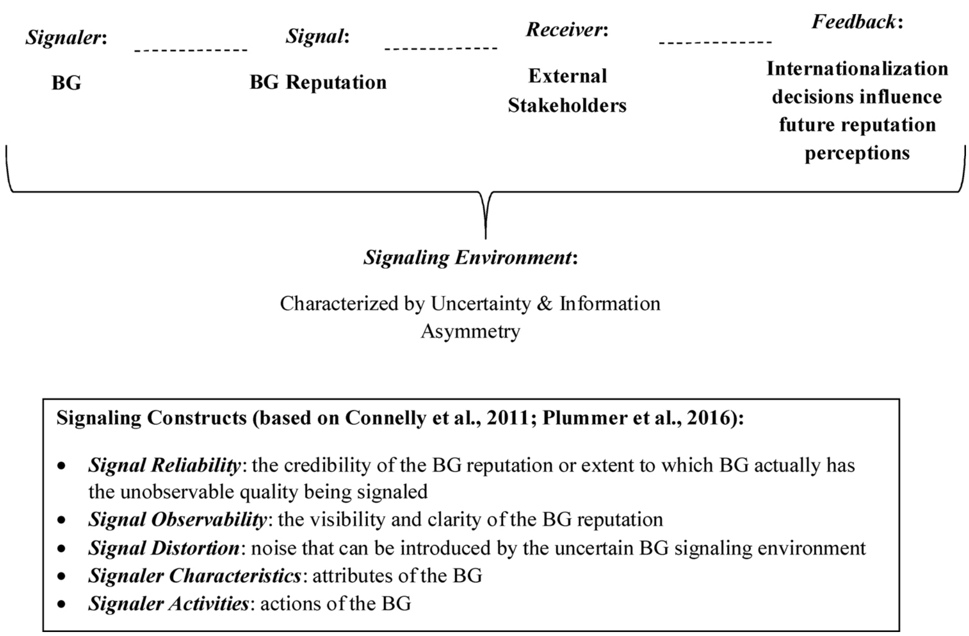

Fig. 1. BG Signaling Model.
Adapted from Connelly et al. (2011, p. 44).

favorably abroad, or it might not even be known at all. Taken together, this suggests that the attributes and actions of BGs create signals that form the basis of their reputation, which in turn can help or hinder affiliates as they internationalize.

This paper aims to contribute to the literature in three ways. First, in order to understand how BG reputation develops, we consider unique aspects of BGs that may influence their reputation. This addresses a gap in the BG literature, which has discussed the importance of having a positive reputation, but has not considered specific antecedents of reputation that are unique to BGs (Holmes et al., 2016). Second, in contrast to the literature that assumes BGs are both well-known and well-regarded (e.g., Gao et al., 2017; Lamin, 2013), we distinguish between BGs' reputation prominence and reputation quality. In doing so, we attend to increasing interest in and calls for research that explores the formation of different facets of reputation (Gao et al., 2017; Lange et al., 2011; Rindova, Petkova, & Kotha, 2007; Rindova, Williamson, Petkova, & Sever, 2005; Wei et al., 2017), and why each of these reputation dimensions matter in the emerging market context. Finally, despite the increased international expansion of BGs in recent years, inadequate attention has been paid to identifying sources of heterogeneity among BGs and the impact of such variation on their affiliates' internationalization strategies (Holmes et al., 2016; Singh & Gaur, 2013). We contribute to the literature by exploring how heterogeneity in BGs' reputation, or differences in the way BGs are perceived by others, may serve as a catalyst, hindrance, or blank slate for their affiliates as they make decisions about their geographic scope and location choice. We explore these reputational differences along with a country's economic development and the presence of diaspora population as key parts of the location choice decision.

We begin by systematically reviewing the literature (Gaur & Kumar, in this issue) on signaling theory and reputation. We use these conceptual premises to consider how unique aspects of BGs can result in systematic variance in the formation of BG reputation quality and prominence. Then, we consider the implications for this heterogeneity in BGs' reputation for their affiliates as they make choices about how widely to internationalize and the types of countries they might seek to enter. Using these ideas, we propose an integrative conceptual framework of BG reputation and affiliate internationalization. The final section discusses the implications of our study and suggests avenues for future research.

2. How BG reputation develops

A firm's reputation is based on public recognition about the quality of its activities and outputs (Lee, Pollock, & Jin, 2011; Rindova et al., 2005). A positive reputation is developed when firms demonstrate consistent behaviors that lead to positive outcomes and such outcomes are appreciated by various stakeholders (Pfarrer, Pollock, & Rindova, 2010). As such, the construct of reputation is often linked with signaling theory (Connelly et al., 2011; Spence, 1973, 2002), which focuses on how firms (as *signalers*) send information (*signals)* about themselves to other actors (*receivers*) who use this information to resolve information asymmetries about the firm's true nature. Much of signaling theory is then concerned with examining issues such as attributes (*signaler characteristics)* and actions (*signaler activities)* that influence the reliability and observability of signals, taking into consideration noise (*signal distortion)* and context (*signaling environment)* (Connelly et al., 2011; Plummer, Allison, & Connelly, 2016). This information may be sent actively by firms in an attempt to proactively build their reputation, or may be given off passively through the firms' actions or underlying characteristics (Herbig & Milewicz, 1996; Stevens, Makarius, & Mukherjee, 2015). As Wei et al. (2017, p. 1) noted, "when information is scarce and uncertainty is high, the information asymmetry between firms and their external stakeholders creates a context wherein reputation is an important consideration in stakeholders' evaluation." This accurately describes the emerging market context that is home for many BGs (Gao et al., 2017), underscoring the importance of reputation as a signal for BGs and their affiliates. Fig. 1 indicates how the signaling theory model and constructs apply to the BG context.

Moreover, prior literature on signaling and reputation has looked at the role of third parties such as associations with credentialing bodies and high-status actors (Gulati & Higgins, 2003; Rindova, Pollock, & Hayward, 2006; Rindova et al., 2005). Yet, the BG affiliate represents a unique entity relative to other emerging market firms and standalone companies because they have legal independence and strategic autonomy and yet are affected by the reputation of their parent BG (Guillen, 2000; Khanna & Palepu, 1997; Lamin, 2013; Manikandan & Ramachandran, 2015). Although many BGs have a positive reputation, BGs as a broad organizational class generally tend to be viewed negatively, due to perceptions that they can perpetuate market imperfections (Lee, Lee, & Gaur, 2017; Ricart, Enright, Ghemawat, Hart, &