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National cultural dimensions in finance and accounting scholarship: An important gap in the literatures?

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ABSTRACT

In spite of cultural dimensions being included in hundreds of business and management research studies, there have been relatively few studies in finance and accounting that include the use of cultural dimensions. We note the need for such studies in accounting and finance and review published studies in these areas that use cultural dimensions. We conclude that both the accounting and finance fields make sparse use of cultural dimensions in scholarship. However, the field of accounting has made greater use of cultural dimensions than the field of finance. We note that this is in part due to particular seminal theories regarding the connection of national culture with the behavior of individuals in accounting. Finance, on the other hand, has been more focused on effects of larger market aggregates. Finance just recently seems to have discovered the impact of national culture, particularly via the impact of individualism on market momentum and the impact of uncertainty avoidance on transaction costs. We conclude that there is much opportunity for further investigation of the impact of national culture on finance. Thus, the field of finance is being well served by the *Journal of Behavioral and Experimental Finance* championing research on cultural finance.

1. Introduction

It is well-recognized in business scholarship that nations differ along many dimensions. However, the various subfields of business scholarship vary considerably in their recognition of such international differences. Indeed, the fields of management and strategy seem to have a rich understanding of international differences and scholarship in these areas note and account for national differences along linguistic, cultural, and institutional dimensions. Somewhat surprisingly, the fields of accounting and finance do not seem to share this deeper understanding of international differences. In this paper we explain the need for the inclusion of international differences in cultural dimensions in the accounting and finance literatures and investigate the empirical bases of the contention that these literatures can benefit for a greater inclusion on international cultural dimensions in their scholarships.

Our investigation of the literatures in accounting and finance leads us to some firm conclusions. We conclude that both the accounting and finance fields make sparse use of cultural dimensions in scholarship. However, the field of accounting has made greater use of cultural dimensions than the field of finance. We note that this is in part due to particular seminal theories regarding the connection of national culture with the behavior of individuals in accounting. Finance, on the other hand, has been more focused on effects of larger market aggregates. Finance just recently seems to have discovered the impact of national culture, particularly via the impact of individualism on market momentum and the impact of uncertainty avoidance on transaction costs. We conclude that there is much opportunity for further investigation of the impact of national culture especially in the field of finance.

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The rest of the paper is organized as follows. We start by making the case for the inclusion of cultural dimensions in finance and accounting scholarship. In doing so, we first examine the importance of culture and its relationship with the institutional structure in a country. Next, we explore the importance of culture in determining social trust and transaction costs in finance. Having established the need for including culture in international financial and accounting scholarship, we examine the extent to which papers published in the top ranked journals in finance and accounting account for the cultural dimensions. The last part draws some conclusions based on our research.

2. National culture, institutions, and finance: theory

National culture can shape the manner in which entities influence social trust and financial transaction costs especially as it shapes the institutional environment in a country. In addition, national culture can also shape the way individuals react to the institutions that are in place or are being shaped around them. Therefore, the role and importance of national culture in finance is closely linked to the importance of institutions. Alternatively, one can see national culture as an important underlying institution in itself. As noted by Greif (2006), institutions arise from: "a system of rules, beliefs, norms, and organizations that together generate regular social behavior". As noted by Hofstede (1980), "Culture is the collective programming of the mind distinguishing the members of one group or category of people from others". Looking jointly at the seminal views of Greif (2006) and Hofstede (1980), it is clear that the role of national culture in finance is closely linked to the role of institutions.

2.1. Institutions and financial economics

Interestingly, the field of economics has long recognized this importance of institutional structure in influencing behavior. For instance, the International Society for New Institutional Economics (ISNIE) as described by Joskow (2008) considers the role of institutions as very important. Joskow (2008) notes that the ISNIE considers that legal, political, social and economic institutions have important effects on economic performance. The effects of alternative public policies aimed at improving economic performance in various dimensions will vary along with the nature and quality of the institutions that are available. The ISNIE also posits that institutions can and should be analyzed using the same types of rigorous theoretical and empirical methods that have been developed in the neoclassical tradition while recognizing that additional tools may be useful to better understand the development and role of institutions in affecting economic performance (Joskow, 2008).

Joskow (2008) also suggests that theoretical and empirical analysis should be interactive and evolve over time. Theory identifies relationships that may be examined empirically, whereas empirical regularities and anomalies raise questions about existing theory. As noted by ISNIE, it is also the case that integrating institutions readily segues into interdisciplinary connections with economics and contributions from, among other disciplines, history, law, psychology, anthropology, and sociology. Consistent with the ISNIE we also contend that institutional analysis seeks to understand the role of government and political institutions in policy formation but it does not have a political agenda (Joskow, 2008).

The field of finance choices has traditionally focused on rational agents and rational models in frictionless, idealized settings. However, in recent years it has become clear that the role of institutions in finance must be included. The role of institutions in financial research is very important as they can and do, for example, influence the functioning of markets. As described by Nye (2008), following Coase (1960), market transactions are best undertaken in environments of well-defined property rights and enforceable contracts. While markets ideally function in environments of unimpeded voluntary transactions, any entity that has the power to make laws or influence the enforceability of contracts will inevitably influence the financial market place. These changes can include deprecating or enhancing trust or simply applying an influencing another cultural predilection.

The qualities of specific institutions that are of particular interest here include, for example, the transparency of financial statements and financial disclosure by firms. These are important factors influencing the costs of resolving asymmetric information. After all, for example, if firms are more forthcoming and honest in the disclosure of their respective circumstances, investors will require less effort to ascertain the validity of contracts with such a firm. Highlighting the interconnectedness of various aspects of institutional quality, Bushman et al. (2004) find that across nations, corporate transparency is largely determined by judicial and legal regimes and by related political economic factors. Johnson et al. (2002) note that the capacity for firms to tunnel resources to insiders and other preferred entities is largely shaped by political institutions.

As an example, international variations in disclosure laws and regulations regarding corporate ownership can and is increasingly used advantageously by many multinational companies to provide anonymity and, for example, avoid taxes, and leverage control through holding companies. The lack of ownership disclosure is also at the heart of the pyramidal ownership structures used to control many large European and Asian conglomerates with small amounts of beneficial ownership in holding companies.

Similar to these lack of regulations requiring disclosure of beneficial corporate ownership, are surprisingly the lack of laws and regulations requiring the disclosure of self-dealing in business transactions. As noted by the extensive literature on transaction costs, such lack of self-dealing disclosure allows many instances of opportunistic behavior where a business or an individual may be a party on both sides of a transaction; giving them the ability to take unfair advantage of third parties who are often unaware of self-dealing by the other party. Often a country with poor self-dealing disclosure also has poor corporate ownership disclosure. Doing business can be very hazardous in such countries.

Poor disclosure regarding both self-dealing and corporate ownership can often also be a critical factor facilitating corruption and crony capitalism. The lack of laws and regulations regarding these disclosures has been a major factor in the failure of many formerly socialist countries to transition to capitalism successfully. Indeed, for capitalism to function efficiently there must be adequate laws and