Risky Business: A Contingency Approach to Political Strategies and Political Risk Exposure in Emerging Markets

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Abstract

Emerging markets are of growing importance in global economies. However, firms in those markets are exposed to a relatively high level of political risk. We specifically focus on the political risk that is faced by subsidiaries of MNCs in these markets and seek to determine how it is managed. We develop a set of hypotheses to analyze effects of non-market strategies on political risk exposure that are subsequently quantitatively tested in BRICS-country subsidiaries. Applying a contingency approach, we specifically analyze the role of B2B vs. B2C contexts as situational conditions. The results challenge existing thought on the effectiveness of political risk and non-market strategies in these markets. In particular, they show that intense non-market strategies may even enhance the risk exposure of subsidiaries in emerging markets. They are thus useful to practitioners in helping them select appropriate political strategies for their subsidiaries and to academics in providing strong implications for future research.

Introduction

Emerging markets now play a critical role in global economies. The high GDP growth rates, combined with a developing infrastructure, relatively low labor costs and a liberalization of the trade and investment policies are among the main reasons for increasing the influx of FDI into these markets. However, subsidiaries in emerging markets face a particularly high level of political risk, especially as the regulatory framework of emerging markets is still developing and often not fully defined. Social conflicts are also more likely and foreign firms can often find themselves confronted with discriminatory action. As a result of this comparatively high-risk political environment, the success of investments in emerging markets is not solely influenced by market actors such as shareholders, customers and suppliers, but is also (at ever greater levels) dependent on a company's interaction with socio-political stakeholders as a means of reducing the political risk exposure (e.g. Hillman and Wan 2005; Shaffer 1995; Wartick and Wood 1998). As a number of authors argue, the inadequate integration of governments, non-governmental organizations (NGOs) and the media into the overall strategy can cause major business-critical problems (e.g., Baron 1995a; Baron 1995b). For example Holtbrügge et al. (2007, p. 48) state: "The insufficient consideration or ignorance of these stakeholders may not only cause severe conflicts and moral condemnation but may also lead to financial losses." However, even though emerging economies are now important, they have been largely neglected by scholars in this research area. Existing research has instead mainly focused on political strategies in the United States (Baysinger and Woodman 1982; Mattingly 2007) or European countries (Hillman and Wan 2005; Taminiau and Wilts 2006; Tenbücken 2002), with some recent exceptions (Elg et al. 2008; Holtbrügge et al. 2007; Yongqiang 2006). It is important to note, however, that the effects of political strategies may differ significantly between emerging and established markets due to their specific institutional environments (Brewer, 1983; Kostova et al. 2008).

An illustrative example of the relevance of political stakeholders in emerging markets is the failed investment of the German tire company Continental. After three years of negotiations, Moscow City Council finally refused the company's application to establish a production site in the city of Moscow. Consequently, Continental decided to end its cooperation with the Moscow Tire Plant in 2004. According to Continental's CEO, this withdrawal from the attractive Russian market cost the company nearly € 30 million. At the same time, Michelin, Continental's main European competitor, was allowed to establish a similar factory in a

Moscow suburb. One reason for this success was apparently Michelin's close relations with the local authorities (Moscow News, 17.11.2004).

Alongside this case-based evidence, the relevance of non-market forces has been widely discussed in the academic literature (Baysinger 1984; Blumentritt and Nigh 2002; Meznar and Nigh 1995; Rodriguez et al. 2006; Scherer and Smid 2000; Shaffer 1995; van Tulder and van der Zwart 2006). The majority of empirical studies on this subject are, however, limited to the discussion of non-market forces and their effect on strategy design. An empirical understanding of the relationship between political strategies and its consequences for subsidiaries in emerging markets has been very much under-researched (see Bonardi et al. 2006; Hillman et al. 1999, Keim and Baysinger 1988 or Elg et al. 2008 for exceptions). In addition, the few existing studies that analyze this relationship do not apply an integrative approach of different strategies but are instead limited in the types of political strategies studied (Hillman et al. 2004). As stated by Getz (1997): "If political action is ever to be fully integrated with strategic planning and organizational behavior (intellectually or practically - see Shaffer, 1995), much more empirical work on effectiveness will need to be done." Thus, the first aim of this paper is to empirically analyze the effect of non-market strategies on the political risk exposure of subsidiaries in emerging markets based on a taxonomy of political strategies.

In addition to the missing "performance" link, existing research has merely analysed how different socio-political stakeholders influence the activities of MNCs and in how far certain conditions have an impact on stakeholder exposure and non-market strategy formulation. These studies, however, fail to specify to what extent political strategies should be used and under which situational conditions. Furthermore, many studies limit themselves only to business-government relations (Keim and Zeithaml 1986; Schuler 1996) or fail to analyze possible interaction effects of contextual surroundings. While there have been calls for a stronger consideration of contingencies and their possible moderating role, this continues to be a gap in the literature (Buehler and Shetty 1976; Kostova and Zaheer 1999). Therefore, the second aim of this paper is to analyze situational conditions as moderating effects. We apply thoughts from social network theory and integrate the international marketing literature and the political strategies literature and argue that the percentage of B2B vs. B2C transactions pursued by a subsidiary in a host country is a critical contingency for the efficiency of political strategies. This assumption is generally based on two arguments: first, that firms in B2C markets are confronted with a significantly higher number of (more diffused) stakeholders, thus affecting the efficiency of political strategies. Second, we believe that political stakeholders play a much stronger role in B2B as compared to B2C markets, once again affecting the efficiency of political strategies.

Overall, the main intention of this paper is to thus extend theory by, first, testing the effects of political strategies on political risk exposure in emerging markets. Second, we aim to extend theory on the role of B2B vs. B2C industry affiliation in this context. In summary, we aim to provide a more detailed analysis on the effectiveness of political strategies in emerging markets. The findings may be particularly useful to practitioners by helping them to select appropriate strategies for their subsidiaries.

In order to close the above-mentioned gaps, this study is organised as follows. First, the theoretical framework is discussed and research hypotheses proposed. We then present our sample and measures, followed by the results, discussion and directions for future research on political strategies as well as implications for practitioners.

Political Risk Exposure and Political Strategies in Emerging Markets

Political risk can be referred to as the volatility of returns against events in a given country (Clark and Marois 1996). Traditional sources of political risk include expropriation and nationalization, war, civil disturbance and ethnic or religious tension. While expropriation and nationalization have dominated in the past, today the focus is more on new, often rather subtle sources such as discriminatory action against foreign companies (owing to competing interests of local firms), corruption, organized crime and sanctions in foreign policy (Hood and Nawaz 2004; Moran 1998). Political risk exposure is thus defined as the sensitivity of a firm's projected profitability and operationality in a host country to changes in investment climate (Brink 2004).

Subsidiaries in emerging markets face a particularly high level of political risk, as the regulatory framework of emerging markets can be still developing and often not fully defined. Social conflicts also arise more frequently and foreign firms are often confronted with discriminatory actions (Yongqiang 2006). Thus, risk management plays a major role in emerging economies. Risk management can be described as the outcome of plans or strategies implemented to maintain an accepted level of associated risk and to reduce risk exposure (Brink 2004). According to this definition, political risk and political risk exposure are at least manageable to some degree.

An organization's strategic choices determine the size of exposure to uncertain environmental and organizational components. In the broadest sense, a firm has three options when exposed to political risk: 1) adaptation to the wishes and policies of the host government, 2) not entering the market or withdrawing from the market when already present, or, 3) trying to make a move to gain a competitive advantage based on the company's strengths and the needs of the host government (Jain 1990). The latter is referred to as a "counteractive response", meaning that the company uses its bargaining power to alter its position relative to other subsidiaries and thus gain a competitive advantage by reducing its risk exposure (Mortanges and Allers 1996). To do so, firms apply specific political strategies.

Political strategies are defined as the design of all relations with non-market stakeholders that may affect the operations of a company in a positive or negative way in order to achieve competitive advantages by reducing its risk exposure (Holtbrügge et al. 2007). Although research has been undertaken to analyze the measures that influence a MNC's non-market environment, few scholars have focused on formulating comprehensive theoretical taxonomies of generic political strategies (Hillman and Hitt 1999; Boddewyn and Brewer 1994). For the following three main reasons, this study builds on a classification developed by Hillman and Hitt (1999): First, the taxonomy takes a proactive approach and so supports the assumption that socio-political stakeholders can be influenced by firms directly. Strategies that imply that firms use their bargaining power seem to be more suitable for applied empirical research design than reactive measures (such as avoidance or compliance) as avoidance often means disinvestment and compliance is often impossible due to home-country or MNC-wide policies (Boddewyn and Brewer 1994). Second, the classification was originally created to provide cross-cultural strategies and therefore is more appropriate when analysing subsidiary strategies (Hillman and Wan 2005). Third, this typology seems to be generally accepted and is pre-tested (Yongqiang 2006; Taminiau and Wilts 2006). As a consequence, the three non-market strategies, as defined by Hillman and Hitt (1999), provide the starting point of this study's argumentation; the financial incentive, the information and the constituency-building strategy.

The financial incentive strategy seeks to reduce risk exposure by influencing policy-makers using financial incentives. Besides the most commonly known tactic; bribery, companies provide financial support or honoraria for speeches, or hire personnel with political experience when applying this strategy. By applying this strategy, firms therefore try to align the incentives of policy makers with the interest of the firm through financial inducements (Hillman and Hitt 1999). The information strategy is a measure that also targets policy-makers directly by communicating preferences on policy and political positions, or decisions on relocation and investment to policy makers. Relevant tactics include lobbying, supplying survey results and reports on research projects, or providing expertise and knowledge for dealing with critical issues, such as environmental problems. Thus, the good provided in this strategy is information. The constituency-building strategy impacts social actors in the socio-political stakeholder population. This strategy covers activities such as grassroots mobilization, public relations, communicating political positions in press conferences or implementing codes of conduct (Hillman and Hitt 1999, Hillman and Wan 2005, Taminiau and Wilts 2006,). Originally, Hillman and Hitt (1999) focused on a company's interaction with governments, so 'constituency-building' was not primarily defined to target individual citizens but rather to influence voters and therefore develop certain leverage on political decision makers. As our approach is more inclusive, involving both political and social stakeholders (Meznar and Nigh 1995) such as NGOs, resident initiatives and labour unions, the term does not seem appropriate here. 'Reputation-building' is used instead as it conveys the efforts of MNCs to shape socio-political stakeholder relations (Dowling 2001; Fombrun and Shanley 1990; Holtbrügge et al. 2007). All three strategies are conducted to compete in the public policy process and therefore to affect actual and future policy decisions in favour of the firm. In other words, the pursuing of each strategy in the past is expected to reduce the current political risk exposure of subsidiaries. Therefore, we propose the following three hypotheses:

> <u>Hypotheses 1a):</u> *The more intensely a financial incentives strategy is conducted, the lower the risk exposure of a subsidiary.*
> <u>Hypotheses 1b):</u> *The more intensely an information strategy is conducted, the lower the risk exposure of a subsidiary.*
> <u>Hypotheses 1c):</u> *The more intensely a reputation-building strategy is conducted, the lower the risk exposure of a subsidiary.*

Effects of B2C vs. B2B Industry Affiliation on the Political Strategy-Political Risk Exposure Link

Political strategies are implemented by firms to cope with differing stakeholder interests. Baron (1995b) for example notes that "a nonmarket strategy must (..) be tailored to the firm's nonmarket competencies and the characteristics of its market and nonmarket environments." Only recently have scholars focused on identifying determinants of political strategy design, such as host-country variables (e.g., economic integration or market orientation) and firm variables, such as company/subsidiary size and subsidiary integration (Hillman and Wan 2005; Holtbrügge et al. 2007). However, the challenge non-market research faces is to define comprehensive strategies that entail a favourable effect for a company and thus provide businesses with recommendations on how to act under various conditions. Subsidiaries are exposed to a certain environmental context and are vulnerable to effects resulting from these specifics but also have to develop strategies according to these conditions in order to increase success. In addition, the few existing studies on the efficiency of political strategies show inconsistent results, ranging from a negative to a positive effect on performance, including no effect at all (e.g., Elg et al. 2008; Li et al. 2008; Rodriguez et al. 2006, Rogers, et al, 2005). This confirms the suspicion that some contextual surroundings may have a moderating effect and alter the non-market strategy-success relationship. Consequently, the model developed here draws on contingency theory.

The contingency approach is defined as "identifying and developing functional relationships between environmental (e.g. culture, technology, raw materials), management (e.g. planning, leadership) and performance variables" (Salzmann 2006). Following this argumentation, the success of a company is subject to its management approach, e.g. political strategies, as well as to certain situational conditions. Therefore, contingencies need to be taken into consideration when designing structures, strategies and practices (Luthans and Stewart 1977; Salzmann 2006).

Following this contingency theory approach, the efficiency of non-market strategies is therefore dependent on contextual conditions. We argue that the relationship between non-market strategies and the risk exposure of subsidiaries is strongly influenced by the proportion of B2C transactions a company's subsidiary carries out within the host country. B2C is defined as business transactions involving consumer goods, including retail and wholesale activities, as opposed to business-to-business (B2B) transactions that provide goods or services to other companies or the government. The basic assumption derived is that the types of end consumers (i.e. companies and governments vs. individuals) differ in the way that they can be addressed by specific political strategies and that this, therefore, affects the risk exposure of subsidiaries stemming from these political strategies. We draw on social network theory and empirical findings from the industrial marketing and the political strategies literature to support this argument.

Social network theory argues that economic activities are deeply embedded in networks of interpersonal relations, and that managers can use the social capital inherent in those networks to influence the allocation of resources and shape economic actions (Batjargal 2003; Granovetter, 1985; Li et al. 2008; Uzzi 1997). Those ties are even more important in emerging (as compared to established) markets and may substitute for reliable government decision making and the established rule of law (Xin and Pearce 1996; Peng and Luo 2000). In addition, existing literature shows that strong ties and networks are much more important and relevant in B2B, as compared to B2C markets for at least two reasons. First, the state – as the most relevant policy maker – frequently acts not only as a policy maker but also as a market actor, as state-owned or state-financed firms are much more common in emerging markets (Luo 2001; Salancik 1979). Through constant contact with political decision makers, companies focusing on B2B transactions are thus better able to benefit from utilizing a relational approach (Yongqiang 2006) and to gain access to politicians (Tian and Deng 2007) than firms that solely supply products to individual end customers. Second, the boundaries of state jurisdiction are much wider in emerging, than in established markets, leading to market interventions being much more commonplace in emerging markets (Luo 2004; Wright et al. 2005). As described above, the financial incentives strategy and the information strategy are pursued to develop and manage ties with policy makers. Combining those aspects, we therefore argue that these strategies are more efficient in B2B markets as compared to B2C markets, which leads to the following hypothesis.

> Hypothesis 2a): *Information and financial incentive strategies are more effective with regard to managing risk exposure in B2B than in B2C markets.*

While the information and financial incentive strategies are aimed directly towards policy makers, the reputation building strategy impacts social actors in the socio-political stakeholder population.. Companies in B2C industries are more exposed to political actors such as NGOs and activists than firms in the B2B sector. As one participant in a former study explained: “We sell our products mainly to a handful of industrial buyers. Although we are quite large, nobody knows us here. We had never Greenpeace or any other NGO demonstrating in front of our doors” (Holtbrügge et al. 2007, p. 59). This statement proves that visibility plays an important role in political strategies (Pfeffer and Salancik 2003; Tian and Deng 2007) and that retail and wholesale activities are likely to increase visibility. Argenti (2004), for example, notes that NGOs often try to generate pressure through building market intelligence, as was the case with the agricultural company Monsanto. NGOs tried to stop Monsanto from marketing genetically-altered products by focusing not on the company itself but on supermarkets offering the products to consumers. As Meznar and Nigh (1995, p. 980) state: “Actors in the general environment are likely to take a greater interest in organizations that directly affect them, or at least in organizations of which they are aware.”

Consequently, companies dealing with consumer goods are particularly visible and confronted with much more diverse stakeholders that cannot easily be directly addressed via informational or financial incentive strategies (Salancik 1979; Tian and Deng 2007). These companies therefore need to implement strategies that safeguard their reputation (van Tulder and van der Zwart 2006). The reputation-building strategy is particularly appropriate to improve corporate image in the public eye, as it targets individual citizens directly (Hillman and Hitt 1999). Accordingly, we derive the following hypothesis:

> *Hypothesis 2b):* *Reputation-building strategies are more effective with regard to managing risk exposure in B2C than in B2B markets.*

Methods

The data analyzed in this study was gathered with an online survey from a sample of branch managers heading MNCs’ foreign subsidiaries in the BRICS countries and Turkey. The data was collected in early 2007. 1.437 managers of foreign subsidiaries were contacted according to information provided by the Chambers of Foreign Trade (or equivalent organizations) and asked to participate in the survey. The questionnaire was offered in German and English, allowing the respondents to decide which language to choose. A translate-retranslate technique was use to ensure the equivalence of both questionnaires. Data was processed and analyzed using SPSS 17.

From a total of 565 managers that agreed to participate in the survey, 173 fully filled questionnaires could be used for the present study, which equates to a percentage of 30.62. All cases with missing information, or answers that were not possible from a logical point of view were eliminated prior to any further analysis. Furthermore, we removed all firms that operated more than one subsidiary in the host country from the sample, as the risk exposure of a subsidiary may depend upon the political activities of other subsidiaries in a host country. The respondents qualifying for this research mainly consisted of expatriates (63.95%), while 21.51% were locals and 14.54% were managers from third countries. All respondents were among the top management team of the subsidiary.

Of all 173 companies represented in this analysis, 107 headquarters were located in European countries, e.g. Austria, Germany, France and Italy, 32 were based in Asia (mostly in Japan, India and Hong Kong SAR), while 18 were North or South American and 16 had their headquarters in Africa. On a subsidiary level, most firms were located in China, India and South Africa, accounting for about 80% of the responses. 38.15% of the represented companies were above-average dependent on the parent company in their decision making process, with only 3.47% being fully controlled. Subsidiaries operated in all three economic sectors, with the majority of them based in the secondary sector (50.29%), closely followed by the tertiary sector (47.98%).

Measures

Dependent Variable

The dependent variable in this study is the perceived political risk exposure of subsidiaries. For many years authors have discussed how to develop a sophisticated measure of political risk exposure (e.g. Aharoni, 1966; Robock 1971; Root, 1972). Following Kobrins (1979) suggestions we used a measure of exposure that consists of three specific types of political hazard: legal, political, and economic events stemming from the political environment. Legal risks are included, as political risk is associated with the legal jurisdictions in which assets are issued (e.g. Aliber, 1973) and emerge, for example, due to differences in legal systems, insufficient legal security or discrimination against foreign companies. Political risks are those that are traditionally assumed when analyzing political issues and include domestic problems or military conflicts that can lead to losses, ranging from destroyed property to expropriation. As a third item, we included economic risks stemming from the political environment, e.g. state-initiated changes in exchange rates, changes in market barriers in specific industries or even changes in buyer-supplier-relationships with the state.

In a first step, each type of political risk exposure was explained to the survey participants. In a second step, each type of risk exposure was measured independently on a 7-point Likert scale. The overall political risk perceived by a subsidiary was calculated as the arithmetical mean across all three types of risk. Cronbach's α was .735, thus showing a sufficient result.

Independent Variable and Contingency

As explained earlier in this paper, the different strategies developed by Hillman and Hitt (1999) serve as independent variables. Managers were requested to assess how frequently they applied each of eighteen different tactics, such as mobilising grassroots political campaigns or providing financial contributions to candidates or parties, within the past three years. In line with previous research, respondents had to answer this question on a 5-point Likert-type scale (Hillman and Wan 2005), with 1 = never, 2 = once per year, 3 = once per month, 4 = once per week and 5 = once per day. The results were then sorted into the three different non-market strategies: the information strategy (Cronbach's α = .750), the financial incentive strategy (Cronbach's α = .780) and the reputation-building strategy (Cronbach's α = .822). The coding of the replies made it possible to measure the usage of each non-market strategy by computing the arithmetical mean.

The proportion of B2C transactions was calculated as a percentage. Participants had to evaluate on a ratio scale the question: 'How much of your subsidiary's overall turnover could be accounted for by transactions with individual end consumers?'

Control Variables

Three control variables were added. First, we included the amount of value activities that were operated in a subsidiary. We expect, that the more value-added activities (VAA) exist in a subsidiary, the higher the exposure of assets and therefore the higher the risk exposure of subsidiaries. The managers had to specify on a dummy-coded scale whether one of the following activities was employed or not: R&D, procurement, production, and sales & marketing. The amount of value-added activities was then measured as the percentage of activities performed in the host-country. We additionally included the cultural distance (CD) between the home- and host-country as a second control variable. *Cultural distance* between the home and host country was measured using the index of Kogut and Singh (1988). They suggest employing the results of Hofstede's (1980; 2001) study to calculate a single composite index of cultural distance for each country pair using the following formula:

$$KD_{jk} = \sum \left\{ \left(D_{ij} - D_{ik} \right)^2 / V_i \right\} / 4$$

KD_{jk} reflects the cultural distance between country j and China (k). D_{ij} reflects the value of the country j and D_{ik} the value of China on the cultural dimension i. V_i indicates the variance of the index of the cultural dimension i based on the data of Hofstede (1980; 2001). We expect that with growing distance, the perceived risk exposure of subsidiaries rises, as cultural differences may lead to unexpected behavior or errors in interpretation. Lastly, we added the Economic Freedom Index (EFI) of the Host Country. The EFI is published by the Heritage Foundation and represents the economic freedom in a country, measured by ten items. Maximum score is 100, representing full economic freedom. Logically, we expect a negative effect of high economic freedom on risk exposure. Figure 1 presents our overall research model:

==== INSERT FIGURE 1 ABOUT HERE =======

Results and Discussion

Descriptive Results

Regarding risk exposure, all subsidiaries stated that they are exposed to a certain level of legal, political, and economic risk, with a mean of 3.84 (SD = 1.48; see Table 1). With regard to specific political strategies, 18 respondents noted that the information strategy has not been used within the previous year, 30 subsidiaries did not make use of the reputation-building strategy and 86 managers claimed that they did not implement the financial incentive strategy at all. The reason for this might be that especially 'Western-oriented' MNCs tend to prohibit bribes in order to comply with jurisdictions in the home country as well as demands from INGOs and supranational organisations. All companies that have implemented public affairs management – defined as the use of at least one strategy once a year within the last three years – executed non-market strategies around once a year (Mean = 1.78; SD = .452). Thus, political strategies were used but only on a very low level. Table 1 presents the means and standard deviations (SD) of all variables relevant for the present study.

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Testing of Hypotheses

As the theoretical framework of the present study is based on a contingency approach, hierarchical moderated multiple regression procedures have been applied to test the hypotheses developed as a first step. This procedure can be used to analyse research models when variables have to be entered according to a specific order (Newton and Rudestam 1999). This method seems to be appropriate in order to interpret interaction effects correctly (Aguinis 1995; Weinberg and Abramowitz 2002).

In order to test for multicollinearity, the bivariate Pearson correlations among all relevant variables were consulted. The results are shown in Table 1. The three types of political strategies, in particular, are highly correlated, with all of them having values greater than .500. Previous studies that reported a similar matrix obtained comparable scores (e.g., Holtbrügge et al. 2007). Due to the high inter-variable correlations observed, we decided to run three distinct regressions in the first place to analyze the effects of each single political strategy in the contingency framework.

Apart from the independent variables, further multicollinearity has to be considered when conducting regression analysis with moderating effects. Prior to running the regression, interaction terms have to be created by multiplying the independent variable with the moderator and including the new term into the regression equation as an additional independent variable. Thus, predictor and moderator variables are normally correlated to a very high level. Therefore, variables were standardised before creating the interaction term. Some scholars recommend centring variables and aligning their mean to 0 in order to reduce unwanted effects caused by multicollinearity (Cohen et al. 2003; Frazier et al. 2004). However, the method chosen for this study was standardisation. While having the same effect in terms of multicollinearity as centring, standardised variables offer some other advantages: With a SD equal to 1 and a mean equal to 0, the plotting and the interpretation of the interaction are easier (Frazier et al. 2004). Also, standardization helps to draw comparisons between different models, as non-standardized variables are dependent on their unique unit of measurement.

Each hierarchical multiple regression consisted of three steps: First, the control variables were entered. In a second step, independent as well as the moderator variables were entered to control the main effects. Third, the interaction terms were entered in the regression model. Moderator effects are existent if the interaction term turns out to be significant (Baron and Kenny 1986). In hierarchical multiple regression, the effect size of an interaction is illuminated by the R^2 change statistics and the significance of this change (Field 2005). Table 2 shows the results of the regression analyses.

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As a next step, we applied a heuristic method for estimating the relative weight of each variable in a combined model that includes all independent, moderating and control variables. Although multicollinearity issues prohibit the inclusion of all three political strategies in a combined regression model, Johnson (2000) developed a heuristic method to estimate the proportional contribution that each variable makes to R^2, thus reflecting the importance of each variable in the regression model. This approach addresses the issue of variable collinearity, using a variable transformation approach. First, a new set of uncorrelated predictor variables that are maximally correlated with the (intercorrelated) predictor variables are calculated. In a second step, the dependent variable is regressed on the new uncorrelated predictor variables, yielding standardized regression coefficients. To derive estimates of relative weight, these coefficients are then squared and combined with the standardized regression coefficients obtained by regressing the original predictors on the new uncorrelated terms. As discussed by LeBreton et al. (2007), this approach yields estimates that are highly consistent and leads to meaningful estimates in the presence of multicollinearity. These results are reported in Table 3.

===== INSERT TABLE 3 ABOUT HERE =======

Before discussing the results in detail, we turn our attention to the percentage of variation in the dependent variable accounted for by the predictors, which is indicated by R^2. While these values do not seem be very high (ranging from .078 to .11, see Tables 2 and 3), this is not unusual in interaction analysis (Frazier et al. 2004). In addition, the nature of the dependent variable itself is responsible for the low R^2 values. Several factors influence risk exposure, especially when contemplating different aspects of political risk together. While it is necessary for firms to implement an effective risk management, some hazards such as terrorist attacks or environmental disasters, cannot be controlled at all (Ghoshal 1987). In summary, the low levels of R^2 obtained in this empirical research does not seem to be exceptional and is mainly caused by the nature and definition of risk.

Hypothesis 1a), 1b), and 1c) proposed a reduction of risk exposure as a consequence of pursued political strategies. As can be seen from Table 2, none of the three hypotheses can be confirmed by our data in the full sample. Direct effects of political strategies on risk exposure are very low and non-significant in all models. Furthermore, coefficients are positive with one exception, thus indicating an enhancement of risk exposure as a consequence of pursued political strategies. Furthermore, all three political strategies contribute to R^2 but only on a very low level (Table 3). This finding is highly surprising, as previous research generally assumed that the utilization of political strategies has a positive outcome for MNCs (Hillman et al. 1999).

One explanation might be that many stakeholders in emerging markets see MNCs subsidiaries as their main adversaries (Mattingly 2007) and NGOs, in particular, often doubt the information provided by companies. This is at least partly caused by stereotypical judgements based on negative legitimacy spillover effects (Kostova and Zaheer 1999). NGOs and their supporters claim that the achievements of MNCs are solely brought about for image reasons and not based on goodwill (Loew 2006). Thus, companies are under pressure from stakeholders regardless of their efforts (Kostova and Zaheer 1999). This might be especially important if subsidiaries are perceived to not contribute positively to the local economy (Luo 2001), as the public expects subsidiaries of foreign subsidiaries to respond more proactively to the social needs of the host-country than local firms (Kostova and Zaheer 1999). In the view of stakeholders, many subsidiaries try to press home advantages such as low labor costs, and thus face criticism as an “exploiting consortium” (Luo 2001). Foreign MNCs are thus often seen as a threat, as they can cause detrimental effects for local companies. For example, they can result in sales difficulties for domestic products (Kostova and Zaheer 1999) - an effect that is only weakly counteracted by political strategies.

Finally, the results may be explained by the fact that the political strategies formulated by previous research seem to be only partially applicable to investigating the current socio-political environment. Originally developed to deal with political stakeholders, the increasing importance of social actors such as NGOs may make it necessary to broaden this approach and re-evaluate available measures in order to cover all relevant socio-political stakeholders, as well as new techniques of stakeholder management.

With regard to hypotheses 2a and 2b, the results are positive and highly significant in all models. In addition, the interaction effects contribute to over 60 percent of R^2 (see Table 3), thus lending strong support for our contingency approach. In order to gain a better understanding of those effects, all interactions were plotted with one SD above and below the mean (Aiken and West 1991; Weinberg and Abramowitz 2002). Figure 2 visualises the interaction effects.

==== INSERT FIGURE 2 ABOUT HERE ====

Hypothesis 2a) proposed that information and financial incentive strategies can be used more effectively to manage and hence reduce risk exposure in B2B than B2C markets. The data revealed significant interaction effects at the .01 level in all models and significant changes in R^2 as indicated by the F-change statistics. Therefore, all regressions lend strong support for our contingency approach. However, the results go beyond our expectations, as they show that the intense use of both strategies actually leads to a higher risk exposure in firms with high levels of B2C transactions. This is shown in Figure 2.

With regard to the information and financial incentives strategy, the results are less clear cut. An explanation of this interaction may be that, as outlined above, subsidiaries in emerging markets were in some cases forced to use financial incentives to achieve or maintain market power. However, the legal environment in most emerging markets is changing rapidly and many countries have now implemented regulations against corruption. Some of them include legal responsibility for illegal transactions in the past. Thus, if a subsidiary engaged in illegal transactions in the past, they may find themselves exposed to higher risks today. Owing to the customer-facing nature of B2C subsidiaries, the effect is likely to be greater for them, as they are more exposed to public opinion.

Hypothesis 2b) proposed that the reputation building strategy can be used more effectively to manage and hence reduce risk exposure in B2C than B2B markets. Again, the data revealed significant interaction effects at the .01 level in all models and significant changes in R^2 as indicated by the F-change statistics. However, the direction of the effect is contrary to the one expected, thus delivering no support for our hypothesis. In addition, Figure 2 shows that the intense use of the reputation building strategy actually leads to a higher risk exposure in firms with high levels of B2C transactions.

A case from Starbucks provides an interesting interpretation for this finding. Political stakeholders attacked the firm, as it did not offer Fair trade Coffee. As a consequence, Starbucks included Fair Trade coffee in its product line and communicated this to the media. However, the NGO Global Exchange was not satisfied and continued to pressure Starbucks, asking for a higher percentage of Fair Trade Coffee (Argenti 2004). This indicates that an intensive utilisation of the reputation-building strategy may add to the risk of firms, as it draws attention to the company and may therefore even increase negative perceptions. A second possible explanation is that firms are expected to communicate openly and honestly about their operations in developed markets. Many authors have claimed that transparency and accountability are the key factors for efficient public affairs management (Florini 2000). Recent research has, however, discovered that too much transparency can cause a white noise effect and thus lead to 'intransparency'. This may be especially important in emerging markets with controlled media and a lower level of customer information. Subsidiaries that communicate often or too openly about their efforts, for example in the supply chain, may uncover issues that the majority of the stakeholder population might not have known about. Too much detail may also cloud the main achievements of MNCs and leave a negative overall impression (Florini 2000). An intensive use of the reputation strategy, especially in terms of public relations and NGO engagement, may thus cause an opposite effect and accusations of "greenwashing" (Argenti 2004) and outweigh the advantages of transparency (Jahansoozi 2006).

Limitations and Implications

Although the present study revealed some strong and significant effects, some limitations have to be considered. One limitation was the relatively small sample size. Future studies should analyze possible moderating effects using a larger sample. Moreover, this paper only analyzed the political situation in emerging markets, which implies that country-specific conditions such as economic growth and the level of corruption turn out to be similar. This focus limited the research to mainly firm-specific contingencies. However, besides the B2B/B2C contingency analyzed, other situational conditions may influence the effectiveness of political strategies and should be tested in future studies. Examples include the economic sector in which a MNC operates or its capacity for innovation. Additionally, little research has been carried out to date on the relationship between political strategies and performance indicators. While this study focuses on the generic (but important) factor of political risk exposure, other dependent variables such as target achievement, subsidiary turnover or reduction of uncertainty should also be considered. In this way, empirical research may be able to provide more comprehensive recommendations to firms in the future. Also, only the situation of the MNCs' subsidiaries was analyzed, as data was not collected at headquarters level. It would therefore be advantageous to examine political strategies from both the headquarters and the subsidiary point of view, as suggested by previous studies (Holtbrügge et al. 2007; Hillman and Wan 2005). Furthermore, the static nature of this research narrowed the applicability of the results. In reality relations can change, for example, with increasing subsidiary tenure. Future research should take a broader approach and analyze interdependencies between MNCs and socio-political stakeholders over an extended period of time. In addition, this study focused on political strategies that were originally developed to interact only with political stakeholders. However, one could argue that these strategies do not satisfactorily address the increasing importance of social interest groups (Yongqiang 2007). Future research should seek to alter past taxonomies and include further tactics that are directly targeting social actors, in order fully consider the needs of both social and political stakeholders. One example is a MNC's non-financial reporting.

In addition to the implications for future research, the results provide strong implications for practitioners. First, the results challenge existing thought on the effectiveness of political strategies. Thus, firms need to be aware that those strategies may have no effect at all if implemented in emerging markets. Furthermore, a number of firms within our sample that conducted political strategies actually increased their risk exposure. This is especially the case for firms in markets with high amounts of B2C transactions. Firms should therefore be very careful about the implementation of such strategies, especially when active in B2C markets in emerging economies.

Conclusions

The purpose of this study was to investigate the performance and effectiveness of political strategies, i.e. the information, the financial incentive and the reputation-building strategy, using the B2B vs. B2C context as a possible contingency. To achieve this, 173 questionnaires submitted by branch managers of MNCs' foreign subsidiaries in the BRICS countries and Turkey were analysed. At least three important conclusions can be drawn:

First, the political strategies formulated by previous research seem to be only partially applicable in investigating the current socio-political environment. Originally developed to deal with political stakeholders, the increasing importance of social actors such as NGOs makes it necessary to broaden this approach and re-evaluate available measures in order to cover all relevant socio-political stakeholders. Second, the results show that the affiliation to B2B or B2C markets strongly moderates the efficiency of political strategies. Furthermore, the effects of political strategies differ significantly between B2B and B2C markets. The third conclusion is that unlike earlier assumptions, political strategy implementation can also be detrimental to firms, if carried out without sufficient consideration of the possible contingencies. The analysed data revealed that the contextual setting impacts the effectiveness of public affairs management to such an extent that even negative effects could occur for MNCs. While it has previously been accepted that more political strategies lead to more success, the findings illustrate that an intensive use of the reputation-building strategy can indeed be risky business for MNCs' subsidiaries, especially when there is a high proportion of B2C transactions involved.

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TABLES

Table 1: Means, standard deviations and correlations

Variables	Mean	SD	1	2	3	4	5	6	7	8
1. RE	3.84	1.48	-							
2. INF	1.83	.64	.040	-						
3. FIN	1.27	.47	-.029	.536**	-					
4. REP	1.57	.54	.079	.550**	.650**	-				
5. B2C	45.55	42.06	-.043	-.027	-.083	-.071	-			
6. VAA	0.58	0.29	.066	.096	.121	.101	-.022	-		
7. CD	1.48	1.30	.139†	-.138†	-.180*	-.128†	.010	.136†	-	
8. EFI	57.95	4.19	.133†	-.058	-.101	.030	.044	.035	.140†	-
N=173; **p < .01; *p < .05; †p < .1										
RE= Risk Exposure; INF = Information; FIN = Financial incentive; REP = Reputation-building Contingencies: B2C = Proportion of B2C transactions; ; VAA= Value-Added Activities; CD= Cultural Distance; EFI=Economic Freedom Index										

Table 2: Hierarchical Regression Analyses

Step 1: Controls									
Value-Added Activities	,046	,038	,040	,046	,045	,055	,046	,034	,060
Cultural Distance	,117	,126†	,109	,117	,116	,124	,117	,130†	,107
Economic Freedom Index	,115	,119	,143†	,115	,116	,139†	,115	,113	,116
					-				
Step 2: Main Effects									
Information		,060	,061						
Financial Incentives					-,006	,136			
Reputation								,086	,112
Combined									
B2C Percentage		-,047	-,048		-,048	-,009		-,042	-,020
Step 3: Interaction Effects									
Information*B2C			,261**						
Financial Inc.*B2C						,253**			
Reputation*B2C									,223**
Change in R^2		,006	,037		,002	,043		,009	,047
F Change		,501	6,716**		,201	7,783**		,825	8,661**
R^2	,034	0,40	,078	,034	,037	,080	,034	,044	,091
Adj. R^2	,017	,011	,044	,017	,008	,047	,017	,015	,058
F	2,012	1,400	2,326*	2,012	1,276	2,404*	2,012	1,535	2,781*

n=173; †p<.1; *p<.05; **p<.01

Table 3: Relative Weights as Percentage of R-Square

Variable	**Percentage of R^2**
Controls	
Value Added Activities	3.4
Cultural Distance	13.7
Economic Freedom Index	16.1
Main Effects	
Information	2.1
Financial Incentives	2.6
Reputation	9.5
B2C Percentage	0.7
Interaction Effects	
Information*B2C	17.2
Financial Inc.*B2C	14.9
Reputation*B2C	19.8
R^2	.110

FIGURES

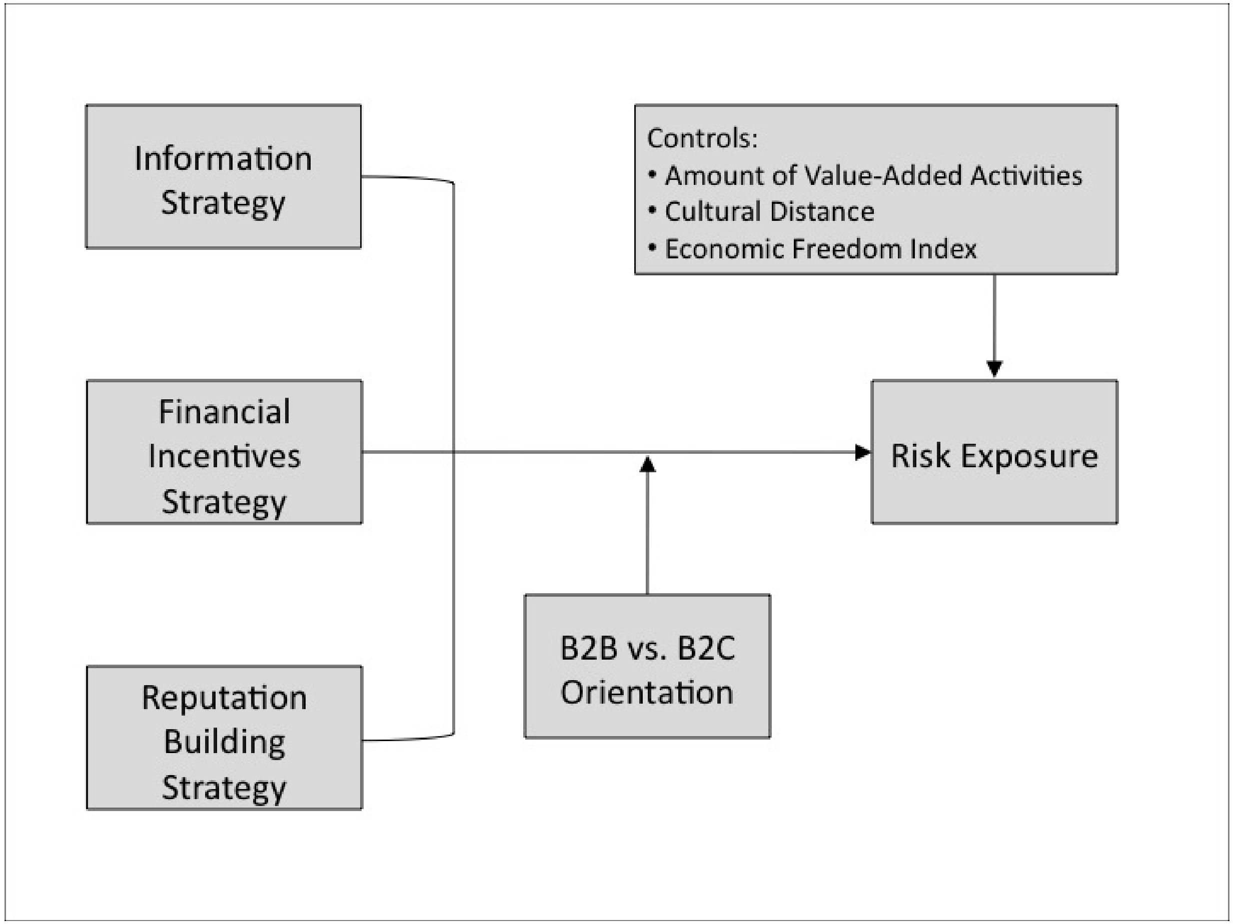

Figure 1: Research Model

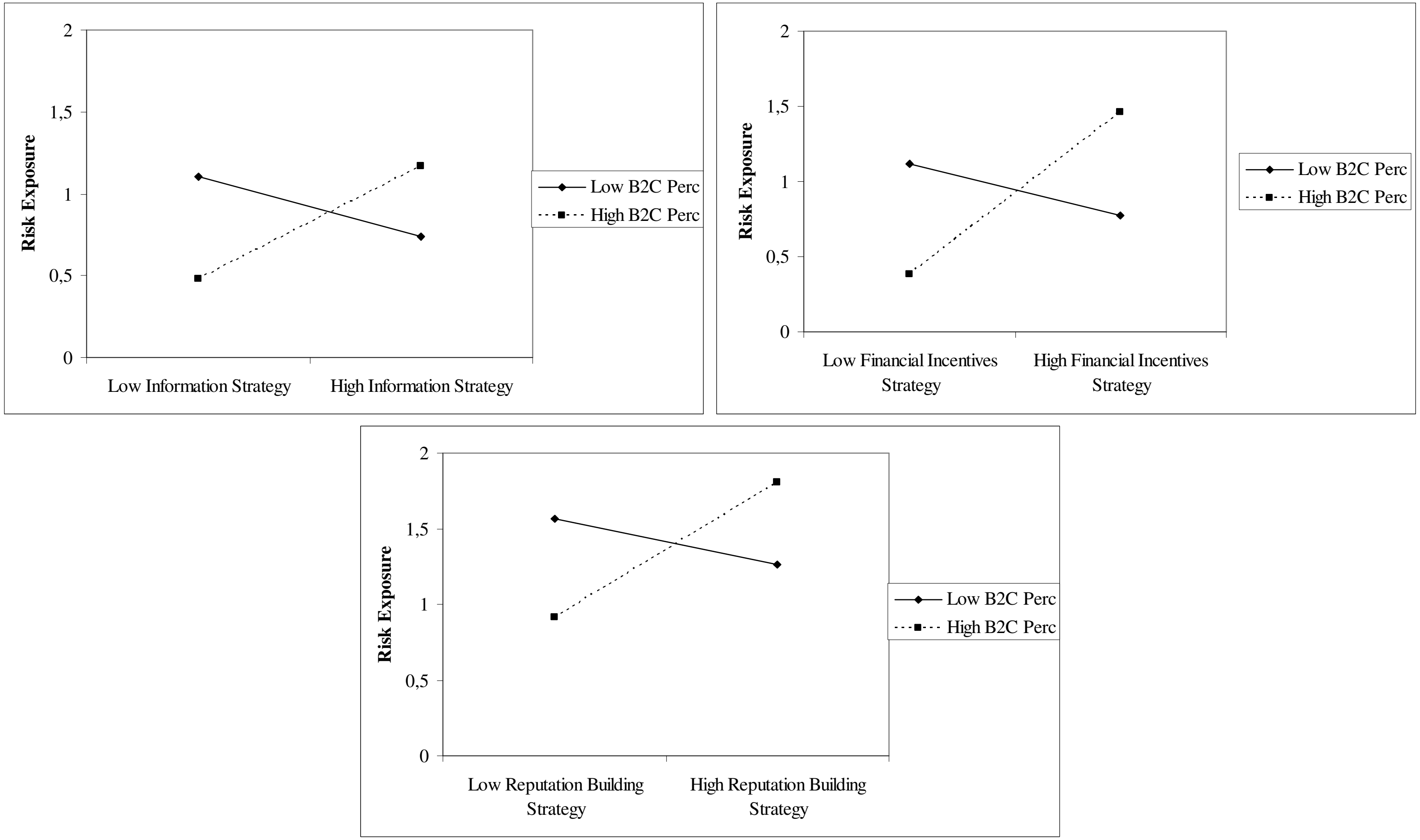

Figure 2: Plotted Interaction Effects