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Bridging the institutional divide: Partnerships in subsistence markets

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ABSTRACT

This study analyzes the impact of institutions on the structure of partnerships in subsistence markets (SMs). Grounded in institutional theory and transaction cost economics, the reasoning suggests that partnerships will adapt to the co-existence of SM-specific and external institutions in SMs. SM partnerships will include multiple partners from multiple sectors, each compensating for different institutional gaps in SMs. They will replace governance mechanisms discussed in the literature, such as formal contracts and equity, with substitutes better suited to SM contexts, including informal contracts, in-kind contributions, and gifts. The importance of these mechanisms will depend on the institutional distance between SM-specific and external institutions. Finally, different governance mechanisms will co-exist within the same partnership, as partners originating in the SM will rely on SM-specific institutions, while partners originating outside the SM will prefer to rely on external institutions where possible.

1. Introduction

As an important strand of the literature explores the potential for business to alleviate poverty, the subsistence market (SM) literature is growing rapidly. Among its main findings, SM scholarship emphasizes the importance of cross-sector partnerships, defined as partnerships between firms, non-profits and/or public actors, for businesses seeking to establish a presence and have a positive impact in subsistence markets (e.g., Crawford-Mathis, Darr, & Farmer, 2010; Dahan, Doh, Oetzel, & Yaziji, 2010; Johnson, 2007; London, Rondinelli, & O'Neill, 2006; Seelos & Mair, 2007; Simanis & Hart, 2008). In parallel, many SM scholars highlight the uniqueness of the institutional environment in SMs, typically emphasizing the importance of normative and cognitive, rather than regulative, institutions in these markets (e.g., De Soto, 2000; Rivera-Santos & Rufín, 2010; Webb, Kistruck, Ireland, & Ketchen, 2010), amid calls for greater scholarly attention to the role of institutions in emerging economies (Teegen, Doh, & Vachani, 2004).

Despite the recognition of uniqueness of institutions in SMs, and the established link between interorganizational relationships and their institutional environment (e.g., Williamson, 1985), no study heretofore systematically explores the potential impact of SM institutions on the structure of SM partnerships. This analysis seems particularly important, as mismatches between the local environment and the structure of SM ventures seem to represent a major challenge for practitioners and may actually lead companies to abandon SM partnerships (Karamchandani, Kubzansky, & Lalwani, 2011).

The purpose of this paper is to start filling this gap by answering the following research question: How do SM-specific and external institutions impact partnership structures in subsistence markets? Grounded in institutional theory and transaction cost economics (TCE), the paper develops propositions regarding the impact of the co-existence of different sets of institutions on the structure of partnerships in SMs. While the paper's approach is conceptual, examples from the literature serve to illustrate the paper's propositions. The analysis suggests that, in response to the co-existence of potentially conflicting institutions in SMs, partnerships will typically include multiple partners from multiple sectors, to compensate for institutional gaps and substitute for missing market actors. To mitigate opportunism risks, they will replace the governance mechanisms typically discussed in the literature, particularly equity and contracts, with substitutes that are better suited to SM-specific institutions, including in-kind contributions, gifts, and informal contracts. The importance of these substitutes will depend on the institutional distance between the institutions prevailing in a given SM and the institutions prevailing outside the SM. Finally, different governance mechanisms will co-exist within the same partnership, as partners originating in the SM will rely on SM-specific institutions,

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while partners originating outside the SM will prefer to rely on external institutions where possible.

The paper makes three main contributions. First, the study contributes to the Subsistence Market and Base-of-the-Pyramid (BoP) literatures, by developing a framework of SM partnership structures that recognizes both the uniqueness of SM-specific institutions and their relationship to external institutions. Second, the paper contributes to the broader partnership and alliance literatures, by exploring the role of normative and cognitive institutions in settings where regulative institutions are weak, and by analyzing the implications of the co-existence of several institutional environments for interorganizational relations. Third, the framework can help practitioners overcome the mismatch between local environments and governance choices, which often hinders the effectiveness of SM partnerships (Karamchandani et al., 2011).

The next section analyzes SM institutions, highlighting the prevalence of normative and cognitive institutions and the typical co-existence of SM-specific and external institutions in SMs. Building on these insights and on findings from the SM partnership literature, a subsequent section develops propositions and proposes a framework analyzing the impact of SM institutions on the structure of partnerships, including the partners and their activities, and the governance mechanisms set up in SM partnerships. The paper concludes with a discussion of the implications of the analysis for future research.

2. Institutions in subsistence markets

Both the alliance and the broader management literatures have emphasized the impact of institutions on alliance and partnership structures (Williamson, 1985). Understanding the uniqueness of the institutional environment in subsistence markets, defined as markets in which consumers barely have sufficient resources for day-to-day living (Viswanathan, Sridharan, & Ritchie, 2010), is therefore a necessary step before exploring the structure of SM partnerships. Table 1 summarizes the main differences between SM and non-SM institutions, highlighting the uniqueness and the complexity of SM contexts.

Institutional theorists distinguish between three main (sub)types or "pillars" of institutions (Scott, 2001): regulative, which comprise "rule-setting, monitoring, and sanctioning activities" (p.52); normative, which "introduce a prescriptive, evaluative, and obligatory dimension" (p.54); and cognitive, defined as the "shared conceptions that constitute the nature of social reality and the frames through which meaning is made" (p.57). Regulative institutions largely correspond to what other scholars have called formal institutions, while normative and cognitive institutions are closely associated with informal institutions (De Soto, 2000; North, 1990). Normative and cognitive institutions prevail in subsistence markets (De Soto, 2000; Rivera-Santos & Rufín, 2010), while regulative institutions play a much smaller (or negligible) role, which typically grows as part of the process of economic and political development from subsistence markets to more developed markets (Cheater, 2003; Mair, 1962). This prevalence of normative and cognitive institutions in SMs results from a combination of weak regulative institutions and strong normative and cognitive institutions. Severe institutional gaps, defined as the lack of regulative institutions to support economic activities (Khanna & Palepu, 1997), low enforceability of formal laws and regulations (Ricart, Enright, Ghemawat, Hart, & Khanna, 2004; Viswanathan et al., 2010) and little legal protection (World Bank, 2000) characterize SMs. By contrast, SM-specific normative and cognitive institutions are particularly strong and substitute for the weakness of regulative institutions to a certain extent (De Soto, 2000), although they often contradict regulative institutions (Arnould & Mohr, 2005; Johnson, 2007; Scott, 2005). Operating through the traditional ties, such as non-specialized kinship, age-group, religious, or other intra-group ties, which bind communities in SMs (De Soto, 2000; London & Hart, 2004; Rivera-Santos & Rufín, 2010), these normative and cognitive institutions are significantly stronger within the community than between communities, leading to localized structures with few bridges across communities (Arnould & Mohr, 2005).

The prevalence of normative and cognitive institutions leads to business transactions governed by informal, rather than formal, mechanisms, and to business ecosystems characterized by a higher prevalence of structural holes, as regulative institutional gaps prevent the development of supporting industries, such as finance or distribution (Rivera-Santos & Rufín, 2010; Viswanathan et al., 2010; Wheeler et al., 2005). In turn, the government, non-profit, and community sectors take on a particular importance in business ecosystems, as they replace missing actors or supporting industries in SMs.

To summarize, normative and cognitive institutions prevail over regulative institutions in SMs, with important implications for business transactions. At the same time, subsistence markets do not exist in a vacuum and are affected, at least to a certain extent, by the broader set of regulative institutions prevailing outside SMs, particularly at the national level. The co-existence of SM-specific normative and cognitive institutions and external regulative institutions thus characterizes SM institutional environments. In turn, the degree of institutional distance, defined as "the extent of similarity or dissimilarity between the regulatory, cognitive, and normative institutions" (Xu & Shenkar, 2002: 508), between SM-specific and external institutions determines the potential for conflict that may arise between these two sets of institutions (Arnould & Mohr, 2005; Rivera-Santos & Rufín, 2010; Scott, 2005). This divide between SM-specific and external institutions will influence the structure of SM partnerships, since governance mechanisms rely on, and adapt to, their surrounding institutions (Rivera-Santos & Rufín, 2010).

3. Institutions and partnership structures in SMs

Building on the previous analysis of institutions in SMs and on insights from institutional theory and transaction cost economics, this section develops propositions on the impact of SM institutions on partnership structures. The SM literature has highlighted the role of cross-sector partnerships in subsistence markets. Prahalad (2005), for instance, explains that partnering with a non-governmental

Table 1
Main differences between SM and non-SM institutions.

Non-SM institutions (external environment of SMs)	SM-specific institutions
Institutional characteristics:	*Institutional characteristics:*
– Primacy of regulative institutions, with few gaps in the range of activities under their control	– Prevalence of normative and cognitive institutions, with severe gaps in the scope of regulative institutions
– Specialization of institutions	– Lack of specialization of institutions
– Impersonal and transactional relationships	– Personal relationships
Source of authority:	*Source of authority:*
– Based on the authority of the state	– Based on social capital, with no well-defined authority structures, or on the authority of a single person or small group of persons (e.g. council of elders)
– Punishment for misbehavior through courts	– Punishment for misbehavior through exclusion from the community or through the judicial power of the central authority

Subsistence markets can vary substantially in terms of the institutional distance between SM-specific institutions and external institutions.