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Retailers' foreign market entry decisions: An institutional perspective

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Abstract

Institutional theory emphasizes the relationship between organizations and the environment. Institutions consist of political, cognitive and sociological elements that form the external and internal environment of a firm. Both external and internal environments affect firm decisions and behaviors. This paper introduces institutional theory as a complementary framework to explain international retailers' foreign market entry choices and suggests propositions for further research. We also consider managerial implications in relation to this theoretical perspective as an explanation for retailers' internationalization.
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Keywords: Entry location; Entry mode; Entry timing; Foreign market entry; Internationalization; International expansion; Institutional theory; Retailer

1. Introduction

About two centuries ago, the industrial revolution transformed small, rudimentary family-centered manufacturing into mass production activities, and the subsequently available economies of scale and scope made it possible for national firms to further become multinational corporations by expanding into other countries and developing global markets (Kleindorfer, Kunreuther, & Schoemaker, 1993). Consequently, entry location (whether to enter a market or not), entry mode (how to enter a market), and entry

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timing (when to enter a market) are among the dilemmas that challenge firms who are concerned with international expansion in the face of an uncertain and complex world. These foreign market entry choices are important strategic decisions for a firm: the appropriateness of foreign entry decisions not only accounts for the parent company's competitiveness in the global arena (Root, 1987), but also for foreign subsidiaries' performance in overseas markets (Gielens & Dekimpe, 2001; Pan & Li, 1998).

Previous studies have focused on explaining international expansion using Dunning's eclectic theory (Agarwal & Ramaswami, 1992; Kim & Hwang, 1992) and/or transaction cost analysis (Gatignon & Anderson, 1988), and researchers have gathered considerable evidence regarding determinants of entry decisions. However, concerns have been raised about the explanatory limits of these theories. For example, why do firms avoid investing in certain countries where property rights are not well protected? Why are there so many commonalties across firms in entry decisions? Why do foreign subsidiaries resemble their parent corporations? Correspondingly, scholars began challenging the importance given to prevalent theories such as transaction cost theory. For example, Davis, Desai, and Francis (2000, p. 241) suggest, "existing frameworks are ambiguous and could offer contradictory explanations for the patterns of entry-mode choices." Therefore, they propose institutional theory as an effective complementary explanation for foreign entry decision-making.

Institutional theory emphasizes the relationship between organizations and the environment. A key insight from this theory is an acknowledgment of the institutional environment—the environment consisting of political, cognitive, and sociological elements such as laws, rules, norms, cultural beliefs, and habits shared by relevant members (Handelman & Arnold, 1999). It focuses on the roles of the institutional environment in affecting organizational behavior and the fact that a firm has to follow the institutional rules in order to gain legitimacy (DiMaggio & Powell, 1983). The institutional environment influences not only an organization's growth (see Arnold, Kozinets, & Handelman, 2001) but also inter-organizational relationships (see Grewal & Dharwadkar, 2002). From both an economic orientation (North, 1990) and a sociological orientation (DiMaggio & Powell, 1983), scholars agree that institutional forces affect organizational decision making from both a macro and micro perspective. Applying these concepts to an international context, pressures from both the macroenvironment (the home and the host countries) and microenvironment (the firm itself) exert influences on a firm's foreign expansion choices (Davis, et al., 2000).

Extant studies on internationalization have mainly focused on manufacturers (Doherty, 1999). Meanwhile, retailers are expanding dramatically overseas. In 2005, 39 of the Top 50 retailers had foreign operations and these retailers accounted for 65.3% of Top 100 sales, up substantially from 55.5% in 2002, 45.1% in 1996 and 29.3% in 1986. In 2005, the Top 10 retailers in the world generated on average 25.9% of their sales volume outside their home countries (Badillo & Kidder, 2007). Blindly applying international business paradigms to retail internationalization without considering organizational differences between manufacturers and retailers could be dangerous, as cautioned by Dawson (1994).

Retailers are different from manufacturers in international expansions. For example, retailers must have physical presences in foreign countries while manufacturers can use export as one means of internationalization. Further, retailers have direct contact with consumers in foreign countries, which makes retailing highly culture specific

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