This project is funded partly by the Wharton-SMU Research Center of Singapore Management University
The Political Spectrum

Witold J. Henisz and Bennet A. Zelner*

The Wharton School
University of Pennsylvania
Philadelphia, PA 19104-6370
henisz@wharton.upenn.edu
215-898-0788

and

McDonough School of Business
Georgetown University
Washington D.C. 20057-1147
zelnerb@georgetown.edu
202-687-6087

Proposal Submitted for Strategic Management Society Mini-Conference
Strategic Management in Emerging Economies: Challenging the Conventional Wisdom

* We thank the Mack Center for Technological Innovation, The Wharton-Singapore Management University Research Center, The McDonough School of Business and the Reginald H. Jones Center for Management Policy, Strategy, and Organization for their generous financial support. We also acknowledge the research assistance of Seth Abramowitz, Dan Fields, Indranil Guha, Hee Young Kim, Michele Konrad, Sarah Lewis, Dan Matisoff, Zhen Tao, Anna Yen and Paul Yoon.
In this paper we use a comparative analysis of investor experiences in 10 emerging market countries to extend the framework for identifying and managing political and regulatory risks in the infrastructure sector originally developed in Henisz and Zelner (2002). By examining an industry context characterized by rapid market growth and technological change we identify an alternate set of hazards to which firms are exposed and an expanded set of strategies that may mitigate those hazards as compared to the case of the relatively slowly growing and technologically stable sector of electricity generation. This generalization of the earlier theoretical framework remains broadly consistent with the underlying theoretical arguments of Henisz and Zelner’s (2002) augmented bargaining power framework but does challenge several common conceptions of the nature of competitive rivalry in rapidly growing industries as described by Porter (1980). The contrast between Porter’s (1980) analysis that focuses on purely market-based rivalry and an expanded set of strategies that includes political and regulatory actors provides substantial insight to managers in other rapidly growing industries particularly in emerging market settings regarding a key driver of performance: the ability to appeal to passive or disorganized interest groups in a manner that secures favorable intervention from the government and tilts the rapidly evolving strategic playing field in your favor during a period of rapid demand growth.

Henisz and Zelner (2002) used cross-national evidence from over 150 interviews with investors, regulators and others involved in the private electricity generation industry in 10 emerging market countries to augment the traditional bargaining power framework (Biersteker, 1980; Fagre & Wells, 1982; Kobrin, 1987; LeCraw, 1984; Poynter, 1985; Svejnar & Smith, 1984; Vernon, 1977) with a more sophisticated analysis of the institutional context of the ‘bargain’ between political actors and investors. The resulting analysis highlighted the importance for the evolution of relative bargaining power of such factors as the breadth of the process of institutional design, the length of time since that institutional design, the frequency and severity of macro- and micro-level economic shocks, and an organization’s own business practices. Henisz and Zelner (2002) posited that variation in these characteristics could aggravate or highlight misalignment between the distributional consequences of the formal institutional structures governing investment and those distributional outcomes preferred by key interest groups in society. Such misalignment could undermine the legitimacy of the formal institutional structures thereby triggering the mobilization of otherwise passive or marginal interest groups (Becker, 1983; Olson, 1965; Peltzman, 1976; Stigler, 1975) by political entrepreneurs (Cox & McCubbins, 1993; Jones, 1978; Schneider & Teske, 1992), such as incumbent politicians, opposition politicians and non-governmental organizations (NGOs) for the purpose of affecting institutional change (Greenwood & Hinings, 1996; Holm, 1995; Seo & Creed, 2002; Sjöstrand, 1995) inimical to investor interest. Broader country-level institutional structures that create a status quo bias mute political actors’ ability to respond to such interest group pressures (Dixit, 1996; Laffont, 1999; Levy & Spiller, 1994; North, 1990; North & Weingast, 1989; Spiller, 1993), while firm-level organizational characteristics that provide access to pivotal political actors or other useful knowledge and capabilities may moderate their firm-specific impact (Oliver, 1991).

The current paper extends the analysis using evidence using approximately 100 interviews with participants in the cellular service sector in 5 Asian, 3 Central European and 3
Latin American emerging market countries. Like electricity generation, cellular service provision exhibits several characteristics that render investors vulnerable to expropriation by political actors or regulators, in particular, large up-front capital costs, long payback periods and high political salience (Levy & Spiller, 1994; Spiller, 1993, 1996). The cellular industry, however, is considerably younger than the electricity generation industry and has exhibited much more rapid growth during the past decade. As a result, players in the cellular service industry face substantially different types of non-market hazards and pursue correspondingly different types of non-market strategies than their counterparts in the electricity generation industry do.

Despite these differences, the same underlying investors assessing market opportunities should still identify the tensions between the distributional outcomes generated by formal institutional structures and those supported by key interest groups as well as institutional structures at the country- and organization level that help moderate the impact of interest group pressures for government redistribution of rents on actual policy outcomes. This similarity in the analysis of the non-market hazards faced by these firms differs from that of conventional market strategy analysis where rapid market growth softens rivalry by reducing the incentives that firms face to lure their competitors’ customers away. Porter writes:

“Slow industry growth turns competition into a market share game for firms seeking expansion. Market share competition is a great deal more volatile than the situation where rapid industry growth means that firms can improve results just by keeping up with the industry, and in fact all their financial and managerial resources may be consumed by expanding with the industry” (Porter, 1980).

A comparison of non-market strategy in electricity generation and cellular service sectors illustrates this important difference. As discussed by Henisz and Zelner (2002), firms in the electricity generation sector typically adopt defensive non-market strategies aimed at upholding the terms of a contract with the state or maintaining the market structure that had been promised to them. Consistent with Porter’s analysis, firms in younger, fast-growing cellular markets do not face direct hazards emanating from the government but, in contrast with Porter’s logic and consistent with our claim of consistency in non-market analysis, they do exhibit greater rivalry with one another for the attention of the government. Specifically, firms in rapidly growing and politically salient industries recognize that they cannot expect to keep up with the market automatically or even by virtue of their product offerings and cost structure, as political actors may “level” or “tilt” the playing field to favor one firm or class of firms over another as the market expands. As a result, the hazards that firms in cellular markets face—and the non-market strategies that they adopt—are offensive rather than defensive in nature and revolve around the battle for future market share. A key question for non-market strategy analysis is therefore, what are the conditions under which political actors are more or less likely to initiate “asymmetric” policies that favor one firm or one class of firms over another? Accordingly, the policies of interest are neither a bilateral contract with the government nor an industry-wide market structure, as in Henisz and Zelner’s (2002) analysis of electricity generation, but rather policies that affect future market share of the various cellular operators.

1 The five Asian countries visited were South Korea, Taiwan, Thailand, the Philippines and Malaysia while the three Central European economies visited were Poland, the Czech Republic and Hungary and the three Latin American countries were Argentina, Brazil and Chile.
Following the structure of Henisz and Zelner (2002), we focus on three main factors that affect a firm’s success in lobbying for such asymmetric policies. First, we consider various misalignments between the distribution of rents produced by the existing institutional structure and the distribution that is seen as reasonable or desirable by the key interest groups in the polity. One common tension is the appeal by fixed-line operators with their universal service obligations and large government payrolls for a share of the rents from mobile telephony both through direct participation and through a tax on or transfer from mobile operators without similar obligations. Asymmetry in the existing levels of cellular market share can also trigger calls for redistribution of rents this time from the relatively small carriers who argue that the existing competitive landscape is inherently unfair and successfully taps into public or political undercurrents of suspicion against the dominant position of the largest or larger firms. Upstream suppliers and downstream consumers can also stake a claim to unexpectedly high rents earned either by a segment of the operators or by the sector as a whole. In each case, the two parties spar with each other for the moral high ground. They seek to tap into pre-existing “cultural preoccupations and political biases” (Hilgartner and Bosk, 1988: 63) about what constitutes a legitimate distributional outcome (McFarland, 1991). Despite tremendous heterogeneity in market, technological, cultural and political contexts across our 10 emerging market countries, we observed remarkably similar public appeals from firms based on their position in the industry.

Two institutional structures moderate the role of such incentives for government redistribution. One such moderator is the structure of political and regulatory institutions. As in Henisz and Zelner (2002), such institutions moderate the responsiveness of political actors to external pressures and thereby determine the likelihood of policy change. Where political and regulatory institutions make such change more difficult by empowering multiple veto players with divergent representation and formal processes, more pressure is necessary to secure a given policy change. Cellular investors, like electricity investors, must therefore consider both the level of pressure that politicians face from interest groups as well as the ability of politicians to respond to such pressure given the political and regulatory institutions that govern their behavior. Organization-level structures especially the direct and indirect linkages of various investors to political actors in the host country or internationally also moderate the impact of government incentives to redistribute rents on firm-level outcomes. Firms with ties to pivotal political actors or firms that possess other useful knowledge or resources expended relatively less effort to secure the same favorable institutional change or protect themselves against unfavorable institutional change than their counterparts.

The paper proceeds as follows. We begin by describing the incentives that the governments faced to privatize and deregulate the cellular service sector. We next consider the determinants of the timing of subsequent policy changes that “tilted” the playing field in favor of one firm or class of firms. As described above we include a discussion of misalignments between the existing market structure and that seen as reasonable or fair by the polity, country-level institutional moderators that minimize the impact of any government incentives to alter the market structure and organization-level structures that similarly moderate the impact of such pressures on individual firms or allow a firm to benefit from government policy change. We conclude with a discussion of the generalizability of the non-market strategy framework employed here and in Henisz and Zelner (2002) to sectors outside of basic infrastructure in emerging markets.
REFERENCES


