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EDITORIAL ESSAYS

The strategic organization of political risks and opportunities

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Firms compete for rents not only within the marketplace, but also through their efforts in the political arena to manipulate regulations, laws and other institutions that govern the marketplace. The field of strategic organization has traditionally focused on the first form of competition, leaving the latter, often distinguished as non-market strategy, largely to scholars from the field of political economy. This research primarily examines how a firm's political environment – the configuration of formal policymaking institutions, regulatory rules, partisan composition and interest group influence – determines the form and efficacy of its non-market behavior, such as lobbying and making donations to political actors.

We urge scholars of strategic organization to enter the field of non-market strategy. Because investigation of the process by which firms manage political opportunities and risks requires that the political environment be taken into account, strategic organization scholars who follow our suggestion will need to cross the disciplinary boundary of positive political economy (PPE). As adherents of multidisciplinary analysis, these scholars are better equipped and likely more willing to cross this boundary than their disciplinary counterparts in PPE are to venture into disciplines such as sociology and organization theory. Moreover, we believe that continued growth of the field of non-market strategy, including the development of managerially relevant knowledge, depends critically on the incorporation of constructs and insights from these disciplines. At the same time, scholars of strategic organization would benefit from the novel opportunities that non-market topics provide to ply their tools of trade.

We focus on two current growth areas. The first is the social context of policymaking. Political economy scholars take a rationalist, equilibrium approach to the policymaking process – and thus to non-market strategy – that focuses on economic influences to the neglect of cultural biases and beliefs that in reality play a critical role. Scholars of strategic organization possess the multidisciplinary skills necessary to analyze how firms' non-market strategies reflect and exploit these social institutions.

The second growth area is firm-level heterogeneity. Many scholars of strategic organization argue that firm-level differences in difficult-to-imitate knowledge and other resources are central to the conduct of market strategy. Analogous differences in knowledge and resources also affect the ability of individual firms to exploit opportunities and mitigate risks that arise in the specific type of political environment that they face.

The strategic importance of political risks and opportunities

The importance of firms' efforts to manage opportunities and risks in the political arena is evident from the level of resources that such organizations deploy for such efforts and the strength of the relationship between the policy environment and business behavior and performance. Recent estimates of total corporate spending on political lobbying activity in the United States exceed $30 billion per year, with notable concentrations of spending on such issues as the deregulation of telecommunications and electricity markets, including the aftermath of the California power crisis; the Microsoft antitrust case; tobacco advertising; agricultural policy; defense contracting; environmental regulation and trade policy (Ansolabehere et al., 2003). Sixteen thousand full-time lobbyists are employed in Washington, DC and another 10,000 now roam the halls of the European Union in Brussels, arguing varying perspectives on recent debates including the proposed merger of GE with Honeywell and Boeing with McDonnell Douglas, the Microsoft case and EU rulings on genetically-modified organisms and data privacy (Mitchener, 2002).

The strength of the link between the policy environment and business behavior and performance is evident in surveys of multinational managers, particularly in emerging markets (Kobrin et al., 1980; Root, 1968). For example, a survey of 3951 firms in 74 countries found that corruption and judicial unpredictability were the second and third most serious obstacles to doing business, following only taxation (Pfeffermann and Kisunko, 1999). A similar survey of the largest global multinational corporations found that non-conventional risks such as corruption, crony capitalism and political risk cost firms $24 billion in lost revenue in 1998 alone, leading 84% of subsidiaries in emerging markets to fall short of their financial targets and resulting in an 8–10% diminution in total corporate returns (Merchant International Group, 1999). Yet another recent report estimated that investors contemplating entry into countries with opaque governance (e.g. China, Russia, Indonesia, Turkey, South Korea, Romania and the Czech Republic) faced the equivalent of an increase in corporate income taxes of 33–46%, relative to the costs of entering a country with stronger governance (e.g. the United States or Chile) (Wei and Hall, 2001). In a similar analysis of portfolio flows, countries with opaque governance and the firms in them were penalized by 900–1316 basis points. All of these studies suggest the potential for firms that are able to manage the policymaking environment – even if in a limited way – to improve their performance.

The political economy perspective

PPE scholars have already recognized this potential and leveraged their knowledge of the policymaking process to make significant contributions to the study of non-market

strategy. Consistent with their disciplinary orientation, these scholars begin with the assumption that policymakers are rational actors who pursue their own self-interest and are capable of making complex, sophisticated calculations using all available data.

The interest group politics perspective in PPE (Baron, 1994, 2001; Denzau and Munger, 1986; Olson, 1965; Snyder, 1992; Wilson, 1980) focuses on the demand for policy. An interest group seeking a specific policy may 'purchase' that policy by supplying a policymaker with a greater level of electoral support in the form of campaign contributions and votes than do the interest groups that oppose the policy. More concentrated interest groups win out over less concentrated ones because members of the former receive higher net benefits per head from attaining their preferred policy and also suffer from a lower incidence of free-riding. As a result, business interests typically prevail over consumers, who are relatively diffuse and poorly organized (Peltzman, 1976; Stigler, 1971).

The literature on structure-induced equilibrium focuses on the supply of policy. Scholars working in this area accept the tenets of the interest group politics perspective but use game-theoretic analysis to add to it the role that political structures such as the executive, legislative and judicial branches of government play in the formal policymaking process. Specific features of these structures, such as voting rules, partisan composition, committee and agency jurisdiction, and veto thresholds, determine the range of feasible policy outcomes that can result from the process (Gilligan et al., 1989; McNollGast, 1987; Shepsle and Weingast, 1987; Tsebelis, 2003; Weingast and Marshall, 1988).

Together, this literature has shaped much of the existing thinking on non-market strategy. The outcome of non-market competition among interest groups, including firms, is viewed as depending exclusively on the configuration of economic interests and formal political institutions. That unorganized groups, the public at large, are impotent to affect policy on their own frequently assumes the status of a stylized fact (Denzau and Munger, 1986). But firms assess the range of feasible policy options, identify pivotal political actors to support (i.e. those with the greatest ability to influence policy outcomes) and determine optimal campaign donation levels (Holburn and Vanden Bergh, 2002), presumably by undertaking equilibrium analysis based on information about the derived policy preferences of individual policymakers and the structure of formal policymaking institutions.

A third body of literature builds on these insights to consider more traditional choices of interest in the study of organizational strategy. Specifically, this literature examines how cross-sectional variation in formal political institutions affects the location of investment (Henisz and Delios, 2001; Wei, 2000; Wei and Hall, 2001), entry mode (Henisz, 2000; Oxley, 1999) and investment sequencing (Delios and Henisz, 2003a). Even though this nascent body of work does not fall strictly into the field of non-market strategy under the definition that we have adopted above, it is clearly of rele vance to strategic organization scholars. Of particular interest is recent work examining the differential impact of formal political institutional configurations on firms possessing varying levels of experience with specific types of configurations (Delios and Henisz, 2003a, 2003b).

The social context of policymaking

Although the disciplinary perspective of political economy scholars is useful for isolating a firm's non-market responses to the configuration of economic interests and formal political institutions, it should not be confused with reality. In our own research on the politics of private infrastructure investment, for which we interviewed almost 400 market participants, policymakers and regulators in 13 countries, our informants repeatedly pointed to the influence of widely held beliefs and biases about issues such as the moral propriety of private infrastructure ownership and workers' rights (Henisz and Zelner, 2003a, 2003b). This influence did not manifest itself exclusively through the formal policymaking process, but rather shaped a series of ongoing interactions between investors and the government. We develop a model of policymaking and non-market strategy based on these insights elsewhere (Henisz and Zelner, 2003a, 2003b). Many of the specific attributes of this model appear to generalize beyond the infrastructure sector, having been addressed by scholars working in other contexts (Baumgartner, 2002; Baumgartner and Mahoney, 2002; Dowell et al., 2002; Guillén, 2000; Hoffman, 1999; Holm, 1995; Kingdon, 1984; Lounsbury et al., 2003; Seo and Creed, 2002).

Policymakers in this model still seek constituent support in the form of votes and campaign contributions, and firms, organized interest groups and other non-governmental organizations supply (or facilitate the supply of) these resources in exchange for political support of their desired objective. However, as in reality, the model portrays these actors as subject to cognitive limitations, in response to which they employ mental strategies that help them to organize and make sense of the vast amount of information that confronts them (Hilgartner and Bosk, 1988; Kahneman et al., 1986; Kingdon, 1984; McFarland, 1991; Zajac, 1995).

Under this view, an interest group's substantial concentration and economic resources do not guarantee success in obtaining a desired policy. In fact, because policymakers are unable to address, understand or even survey the entire range of potential issues that myriad particularistic interests routinely raise, they often choose to address issues that have captured widespread public attention, that is, the attention of large, diffuse interest groups in the polity whose aggregate support significantly affects a policymaker's chances of political survival. The members of these groups mobilize around specific issues that fit into a master frame that they use to organize and simplify political debate, irrespective of their economic interest in the issue and the depth of their understanding (Benford and Snow, 2000). Indeed, the most entrepreneurial politicians intentionally seek out issues that link to voters' master frames in order to boost their electoral prospects (Cox and McCubbins, 1993; Jones, 1978; Schneider and Teske, 1992).

Perhaps the most wide-ranging and powerful of these frames is a society's prevailing notion of legitimacy, defined as 'the generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs and definitions' (Suchman, 1995: 574). Firms that understand the determinants of legitimacy in a society are better able to assess which existing and potential policies are likely to survive – or be introduced in the first place – than they would through attention to the configuration of economic influences and for-

mal political institutions alone. These organizations are also less likely to engage in costly lobbying campaigns that turn out to be futile, or to depend on attractive investment policies that are socially unsustainable. Scholars of strategic organization possess the expertise to make headway in this area by identifying the mechanisms through which firms assess social institutions, both to identify political opportunities and to safeguard themselves against political risks.

Another opportunity lies in the analysis of firms' influence-seeking strategies. Parallel to the financially-oriented lobbying that constitutes influence-seeking in the traditional model, in this case influence-seeking involves the development of political arguments whose persuasiveness derives from their linkages to pre-existing cultural beliefs and biases. Social movement theorists have examined how interest groups use frames to enlist diffuse interests in support of a desired policy, for example, the use of national competitiveness frames by interest groups seeking to influence standards for high-definition television (Dowell et al., 2002) and the use of environmental justice frames by interest groups seeking to influence recycling policy (Lounsbury et al., 2003). Little work has been done, however, on firms' use of frames to enlist such interests.

Consider, for example, firms lobbying for policy changes that restrict entry, for example extending the life of intellectual property protection or a franchise's zone of exclusivity. These organizations may try to enlist support by arguing that such policies are necessary to support the right of inventors to receive a compensatory return; failure to enforce this right would presumably be illegitimate in a society whose members possess strong capitalist values. Opponent organizations, in contrast, may argue that entry restrictions limit competition, the flow of ideas and consumer choice, all of which are presumably illegitimate outcomes in such a society.

Persuasive techniques other than sheer force of principle may work as well. Drawing comparisons with reference points that reflect a prevailing standard of legitimacy (Gamson et al., 1982), for example, may influence the 'moral-based' (Suchman, 1995: 579–81) ascription of legitimacy to a policy outcome and thereby generate support for or mitigate opposition to the policy. Linking a proposed policy reform to deeply held values that a recent crisis or scandal has inflamed (for example, the moral impropriety of child labor) may also affect support for that reform regardless of its true purpose (for example, protection against foreign imports).

Organizational heterogeneity

In addition to examining the relationship between the social context of policymaking and non-market strategy, strategic organization scholars may also develop the study of non-market strategy by considering the role of organizational heterogeneity, whose significance also derives from the assumption of cognitively limited actors (this time, the strategic organizations themselves). The core insight is that 'the heterogeneity . . . of the productive services available or potentially available from its resources that . . . [give] each firm its unique character' (Penrose, 1959: 75).

Some resources that are of interest in the study of market strategy, such as technological assets or capabilities, may affect a firm's ability to influence policymakers'

decisions, for example, by generating spillovers that the government desires and so is unwilling to jeopardize through an adverse policy change (Poynter, 1985; Vernon, 1977). More squarely in the domain of non-market strategy are resources such as social network ties to political actors and other politically powerful players, which we have observed firms to exploit in our own research (Henisz and Zelner, 2003a, 2003b).

Equally important are intertemporal learning processes through which firms develop an understanding of the complex economic, political and social institutions that shape their policymaking environment. Firms may also develop skills in cultivating relationships, building and maintaining coalitions, framing debates in a manner that resonates with powerful external or internal constituencies, and enhancing the perceived legitimacy of their behavior (Boddewyn and Brewer, 1994; Henisz and Zelner, 2003a, 2003b; Henisz, 2003).

The evolutionary nature of firms' capabilities to manage political risks and opportunities creates resource heterogeneity that may shape industry structure and the distribution of rents among various players. An example comes from the work of Holburn (2001), who finds evidence that utilities that have previously operated under rate-of-return regulation are better equipped to manage regulatory rate reviews, while organizations with experience in wholesale market competition are better able to manipulate prices under complex market rules. Similarly, firms with experience in countries with a specific institutional profile (e.g. centralized political decision-making or a strong independent regulator) enjoy a comparative advantage in other countries with a similar institutional structure. Delios and Henisz (2003b) report analogous results on the effect of experience with 'high' or 'low' political hazards in a sample of Japanese multinational corporations.

Opportunities in empirical work

In addition to the conceptual progress that strategic organization scholars can make on the topics discussed above, solid empirical work will also play a significant role in moving the field of non-market strategy forward. However, whereas existing empirical work uses publicly available data on institutional structure and firm characteristics (Alt et al., 1999; Delios and Henisz, 2000, 2003a, 2003b; Henisz and Delios, 2001; Holburn, 2001; Oxley, 1999; Smarzynska and Wei, 2000), empirical examination of the proposed topics requires a multi-method research design. The salient dimensions of legitimacy vary by policy issue, and while suitable empirical proxies may exist in the public domain or be developed using text analysis, their identification and isolation will first require careful qualitative research, including field interviews with a range of relevant political actors. Subsequent analysis can use press accounts or publicly disclosed lobbying data to unpack the strategic interactions between firms and political actors to influence policy change. Formal policy outcomes can then be compared with lobbying efforts to ascertain the efficacy of a given organization in achieving its desired policy outcomes. Various environmental contingencies may also be incorporated into such an analysis to assess the extent to which they mediate or moderate the success of lobbying efforts. Finally, organizational performance may be linked to strategic lobbying and its success.

Conclusion

The path that we urge scholars from the field of strategic organization to follow here promotes one of the field's overarching objectives: to identify the organizational characteristics associated with the adoption of various strategies conjectured to improve organizational performance, irrespective of the disciplinary boundaries that often separate scholars seeking to understand strategic organization. The incorporation of an additional discipline into the analysis, that of PPE, clearly places a burden on researchers seeking to follow this path. The intellectual payoff of accepting this burden will be a richer, more accurate model of the risks and opportunities that firms face when devising their strategy. *Strategic Organization!*, with its interdisciplinary orientation and mission to draw attention to 'compelling practical strategic organization' issues and 'strong theoretical framework[s]' for addressing them, is an outlet that should embrace such work.

Note

Both authors contributed equally and list their names alphabetically on joint work.

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