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Market–political ambidexterity during institutional transitions

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Introduction

In 1996, Royal Dutch Shell struck an advantageous deal to obtain a 55% stake in the Sakhalin oil fields in Eastern Russia. This was a result of Shell's superior technological and market capabilities and Russia's need for revenue during difficult institutional transitions. By 2000, the picture had changed. Russia's power was considerably stronger, and Shell had mismanaged local stakeholders and governments by putting profits ahead of safety (Ray, 2008). Shell's inability to leverage previously good governmental relations would come back to haunt it. It was eventually forced to reduce its stake of the project in half (from 55% to 27.5%), and Gazprom, the Russian government-controlled oil giant, bought the remaining shares at less than market price.

This example illustrates how market capabilities are only part of the key success factors for doing business in emerging economies undergoing institutional transitions such as Russia (Puffer and McCarthy, 2011). Without strong capabilities to manage government relations, firms (particularly, foreign ones) can find themselves in vulnerable positions with little recourse, as Shell did.

The need to pay attention to political winds and develop corresponding political capabilities is not only relevant to foreign firms such as Shell in Russia but also important to domestic firms. Case in point: the Tata Nano, the much-hyped, cheapest car that presumably would allow many Indians to become first-time car owners and create thousands of jobs, could not be made in its originally planned factory in the Indian state of West Bengal. Thousands of farmers who lost their land used to build the Nano factory protested. Pressures from angry politicians forced Tata to abandon the plant and start another plant in another state, Gujarat, at a great cost. The fact that such an influential and otherwise-respected firm can mess up its political relationships *domestically* underscores the importance of managing political calculations during institutional

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transitions in emerging economies—in addition to the obvious necessity to have competitive, market-based products.

Institutional transitions are "fundamental and comprehensive changes introduced to the formal and informal rules of the game that affect organizations as players" (Peng, 2003: 275). The hallmark of the great institutional transitions unfolding in emerging economies is often believed to be the transitions from government control to market competition (Wright et al., 2005).

Examples such as Shell in Russia and Tata in India have led us to believe that such "transition to market" arguments have only captured part of the essence of institutional transitions. We argue that during institutional transitions, while market forces have certainly become more important, government influences are not necessarily in decline (Khanna and Yafeh, 2007; Puffer and McCarthy, 2011). Numerous foreign and domestic firms active in emerging economies have realized that their superb market capabilities may not be enough to carry the day. Many firms thus have assimilated the pervasive aspect of institutional transitions by devoting considerable resources to nurture government relations.[1]

How do firms grow during institutional transitions when forces of both governments and markets are strong? Our central argument is that firms grow by developing capabilities to embrace *both* markets and governments—specifically, market–political ambidexterity. Viewing market–political ambidexterity as a bundle of dynamic capabilities, we contribute to the literature by articulating this important but previously underexplored construct.

Institutional transitions, nonmarket strategies, and dynamic capabilities

"Ambidexterity" literally means the ability to use one's hands equally well. Management scholars have leveraged this metaphor to deal with paradoxes, such as exploitation versus exploration (March, 1991) and efficiency versus innovation (O'Reilly and Tushman, 2008). Extending the ambidexterity literature, we develop the concept of "market–political ambidexterity" in the context of institutional transitions—defined as firms' dynamic capabilities to manage influences from both markets and governments simultaneously. Most individuals are either right- or left-handed, and only a small percentage of individuals are truly ambidextrous. Likewise, while most firms understand the importance of developing dynamic capabilities to manage markets and governments, few are truly good at both—this is where the tension lies. Because such market–political ambidexterity is valuable, rare, and hard to imitate, we argue that these important dynamic capabilities are central to a firm's success in an environment where both markets and governments play a pivotal role.

A focus on market–political ambidexterity enables us to draw on and contribute to three streams of the literature. First, this article continues the line of research on institutional transitions and strategic choices (Hoskisson et al., in press; Li and Peng, 2008; Meyer et al., 2009; Peng, 2003; Peng and Heath, 1996; Wright et al., 2005). Treating governments and markets as twin forces of a paradox, we follow Lado et al. (2008) and Smith and Lewis (2011) by leveraging the tension between these two forces. Specifically, we move beyond traditional either/or thinking and embrace both/and reasoning by articulating the strategic ambidexterity concept. We challenge the traditional view of government and market forces being at opposite ends of a scale. More influence of market forces does not necessarily mean less of government forces. Therefore, a view that gives equal weight to market and government capabilities will have greater explanatory power when examining this phenomenon than the alternative view, which focuses solely on one or the other.

Second, this article draws on the literature on political and nonmarket strategies (Lux et al., 2011). Much of this research focuses on developed economies,[2] thus necessitating more attention on how political and nonmarket strategies play out in emerging economies undergoing institutional transitions.

Third, we follow Oliver and Holzinger (2008) to position this article within the broader literature on resources and capabilities (Teece, 2007). Extending O'Reilly and Tushman (2008), we argue that strategic ambidexterity during institutional transitions represents a bundle of dynamic capabilities that can differentiate the winning firms from the mediocre and losing ones.

The government–market paradox

A paradox represents dynamic tensions and contradictions (Smith and Lewis, 2011). Institutional transitions in emerging economies represent a paradox full of tensions and contradictions. For example, in China, while market competition becomes more intense, firms have to pay more attention on market environment change when they make strategic decisions (Sheng et al., 2011). Meanwhile, heavy government involvement is still common (Li and Peng, 2008). Thus, firms in emerging economies such as China have to face the high uncertainties that often come from both imperfect market mechanisms and powerful but unstable governments (Peng, 2003; Wright et al., 2005). In this case, both institutional factors from government factors and market factors from industry competition may influence firm performance (Oliver, 1997; Peng, 2003). Thus, rather than attempting to resolve paradoxes by making either/or assertions (either "governments are in decline" or "not" while markets are clearly on the rise), researchers and managers may "be better off accepting these paradoxes and using them constructively" (Lado et al., 2008: 405).

For at least three reasons, governments have continued to assert their importance. First, institutional transitions calling for more formal market institutions need to be supported by strong (as opposed to weak) governments (Peng et al., 2009). Second, from a cultural and historical standpoint, governments in what we call emerging economies today (such as Brazil, China, India, and Russia) have usually been heavy handed in their intervention in many fields. While there is some reduction in government intervention during institutional transitions, governments still possess considerable power in approving projects and allocating resources (Hitt et al., 2004). Finally, stimulus packages issued by governments since the 2008 economic crisis have strengthened government influences. The decisions made by governments in developed economies to bail out troubled firms have emboldened governments in emerging economies not to "withdraw" but to advance government influences.

Overall, there is no doubt that firms need to strengthen market capabilities during institutional transitions. Relatively underexplored is firms' necessity to develop and nurture capabilities to leverage government relations during transitions when the rules of the game are changing (Peng et al., 2009). The fundamental incompatibility lies in the lack of specific demarcation that separate market influences and government influences, triggering firms to continuously search for the best way to manage both areas in the absence of clear guidance either from markets or from governments.[3]

Market–political ambidexterity to embrace both governments and markets

Most existing research on ambidexterity has focused on firms in developed economies. The emphasis is on organizational ambidexterity associated with the *internal* structures such as business units, processes, and systems—some focus on exploitation and others on exploration (March, 1991; O'Reilly and Tushman, 2008). Other work on ambidexterity has focused on multinationals from emerging economies (Luo and Rui, 2009), but it has not focused on the need for competencies in managing government relations. Essentially, none of the previous work has focused on the *externally*-oriented ambidexterity capabilities to embrace both governments and markets during institutional transitions in emerging economies. Therefore, we label this new dimension of ambidexterity "market–political ambidexterity."

The concept of market–political ambidexterity builds on three underlying streams of the literature. First, although the earlier literature on institutional transitions and strategic choices has focused on the march toward markets (Peng, 2003), recent work has documented the persistent influence of governments on firms' various strategic responses (Puffer and McCarthy, 2011; Zhou and Peng, 2010, 2012). A new generation of research in this area cannot ignore this phenomenon.

Second, research has documented the importance of political and nonmarket strategies. The thrust of this research is that firms need to outcompete rivals not only in product markets but also in political markets. While most of this research focuses on developed economies whose rules of the game—even for political rules of the game (such as lobbying)—are relatively transparent and stable (Lux et al., 2011), its extension to emerging economies undergoing institutional transitions is particularly important because political and nonmarket strategies are more opaque, and thus offer potentially more attractive rewards to successful firms (Li et al., 2012; Sun et al., 2011; Xu et al., 2012).

Finally, market–political ambidexterity can be viewed as a bundle of dynamic capabilities (O'Reilly and Tushman, 2008). Peng (2003) outlines a leading strategic question during institutional transitions: "How do firms play the new game when the new rules are not completely known?" We can push this question further: "How do firms simultaneously play the market competition game and the political/nonmarket game when the new rules for both sets of competition are not completely known?" It is plausible to argue that market–political ambidexterity enables firms to exploit and explore in their dealings with governments and in their competition with market rivals. We suggest that market–political ambidexterity, as a bundle of dynamic capabilities, enables firms to achieve new resource configurations as political markets and product markets emerge, collide, and evolve. Research on corporate political strategy suggests that firms can undertake effective political strategies such as influencing governments or government officials when they realize that governments have significant effects on the competitive environment (Oliver, 1997). Oliver and Holzinger (2008) further regard political strategy of influencing governments as one crucial type of firms' external capabilities. In this regard, we view the capabilities to influence governments and to influence markets as dual capabilities, which represent some of the most important capabilities for navigating the external environment of institutional transitions in emerging economies. Here, capabilities to influence governments are referred to as external dynamic capabilities that can influence firms' political environment for the purposes of generating future value or protecting the present value of the firm from future loss or erosion, and capabilities to influence markets are defined as a firm's market or bargaining power in the industry.

Specifically, we argue that Teece's (2007) explication of the microfoundations of dynamic capabilities is useful. Teece argues that dynamic capabilities have three components: (1) sensing, (2) seizing, and (3) reconfiguring. Teece (2007) suggests that sensing refers to firms' efforts to "scan, search, and explore across technologies and markets, both local and distant"—obviously related to exploration. Seizing refers to firms' decisive moves to seize opportunities—clearly related to exploitation. Reconfiguring involves business model redesign, asset realignment, and revamping of routines (Teece, 2007). While Teece (2007) focuses on technological innovations, we leverage these insights to enrich the concept of market–political ambidexterity. By linking dual capabilities with three components of dynamic capabilities, we can enhance our understanding of dynamic capabilities as a driver behind firm performance during institutional transitions.

The existing literature has paid more attention to the effect of capabilities to influence markets in Western countries. There remains a gap about the effect of capabilities to influence governments, especially in emerging economies. We argue that in emerging economies undergoing institutional transitions, firms (especially those in politically important industries) may be better prepared by paying more attention to emerging government policies, interests, and preferences—in short, *sensing* (Teece, 2007). For example, Russia is known for having a large number of privatized firms controlled by oligarchs, who until recently had preferred to be "left alone" and mind their own business. However, the government in the early 2000s expressed a strong interest in (re)asserting its control of the strategically crucial energy sector. Anyone who did not sense this had a rude awakening in 2005 when Russia's then largest and most successful privatized oil company Yukos was broken up and its owner Mikhail Khodorkovsky jailed. The message was clear: resistance would be futile. Consequently, several oligarchs sold valuable assets to the state. A leading lesson from the Yukos affair is that Khodorkovsky failed to sense the need to acquiesce. Our opening example of Shell is also indicative of similar failure in sensing.

Seizing refers firms' efforts to reach out to work with governments even when confronting unfavorable political winds. For example, in the Brazilian state of Rio Grande do Sul, the late 1998 election success of a leftist PT Party (Workers Party) created a problem for Dell (Nelson, 2007). In early 1998, Dell signed a US $100 million investment deal with the previous state government that was more friendly to multinationals, obtaining a lucrative deal consisting of a 75% tax reduction for 12 years and a US $16 million loan at a favorable rate. During the next election campaign, the PT Party candidate, who would eventually win and become the new governor, attacked such "excessive" concessions granted to Dell (and also to Ford in a similar deal). Once the new governor was in power, Ford chose to go to another Brazilian state.

Sensing that the new governor was criticized for the loss of jobs associated with Ford's departure, Dell seized the opportunity by reaching out to renegotiate with the new governor. Dell argued that unlike Ford, Dell's operations would not pollute the environment; instead, Dell would facilitate access to the Internet—a precondition for a more just and egalitarian social order promoted by the new governor. Not wanting to lose another major investor, the new governor in the end agreed to let Dell keep its lucrative incentive package intact. Through self-selection, Dell chose to reach out to work with the new state government that was known to be hostile to multinationals, underscoring the necessity to embrace governments during institutional transitions when rules may change unpredictably.

Finally, reconfiguration refers to "the sharing of capability between the old and the new and the geographic transfer of capability from one market to another" (Teece, 2007). An example of adroit leveraging of both market and government capabilities is provided by Infosys in India, formed in 1981. After some early challenges, Infosys maneuvered itself to be well positioned to take advantage of incentives created by the Indian government in the 1990s with respect to India's budding software industry (Abdelal et al., 2007).

Infosys grew to become one of the most respected companies in India for its exemplary corporate governance. At the same time, the Indian government was interested in creating market-friendly institutions and rules. Instead of having bureaucrats inexperienced in business competition (especially in new industries such as software) craft regulations, the government was interested in inviting experienced executives to participate in the new rule making. Leveraging both market prowess and political shrewdness, Infosys rose to the challenge to fill this new role by participating in the new rule making. Infosys adeptly managed the market to become one of the largest and most prominent companies in India, and simultaneously used its competencies in government relations to lobby successfully for itself and to help strengthen government institutions. In other words, Infosys reconfigured itself by embracing both the market and the government.

Discussion

Contributions

By articulating the important but previously underexplored construct of market–political ambidexterity, we make at least three contributions. First, this article deepens research on strategic choices during institutional transitions by highlighting the relatively underexplored dimension of government influences. This contrasts with the relatively one-sided emphasis on market competition at the expense of government influences (Peng, 2003; Whittington, 2012). By viewing governments and markets as a paradox, we move beyond the traditional either/or thinking and articulate the both/and nature embodied in market–political ambidexterity. Overall, long-term success during institutional transitions seems to "require continuous efforts to meet multiple, divergent demands" (Smith and Lewis, 2011). Why is market–political ambidexterity important during institutional transitions? In a nutshell, because most firms do not possess such ambidexterity in their repertoire of capabilities—in other words, being equally good at managing markets and managing governments—but successfully navigating the uncertain waters of institutional transitions calls for such dynamic capabilities.

Second, this article extends the literature on political and nonmarket strategies from a focus on developed economies to the context of emerging economies. Clearly, some of the arguments on the importance of political strategies are not entirely unique. Relationships with governments are obviously still important in developed economies. However, considering that the bulk of our knowledge on corporate political strategy—as meta-analyzed by Lux et al. (2011)—is from developed economies, extending this literature to institutional transitions in emerging economies is crucial.

Finally, our identification and articulation of the market–political ambidexterity construct directly enriches the ambidexterity literature, which so far has largely focused on the internal, organizational side. Market–political ambidexterity focuses more on the external side, emphasizing the strategic nature of firms' dealings with both governments and markets simultaneously. This article also enriches the resources and capabilities literature, by arguing that as a bundle of dynamic capabilities, market–political ambidexterity centers on the three components articulated by Teece (2007): (1) sensing, (2) seizing, and (3) reconfiguration.

Future research directions

In terms of future research directions, as much as the concept of ambidexterity (March, 1991) has generated significant enthusiasm in the literature, a market–political ambidexterity lens may be a new way of looking at the growth of the firm during institutional transitions (Li and Peng, 2008; Peng, 2003; Peng and Heath, 1996; Zhou and Peng, 2010, 2012). The boundary conditions of the market–political ambidexterity remain to be specified (Li et al., 2012; Sun et al., 2011; Xu et al., 2012). As much as many of us would wish that we can use both hands equally well, most of us are either right-handed or left-handed. Likewise, most firms (or at least most units and most individuals) can only do one task well (such as exploitation or exploration) but cannot be equally good at both, and an emphasis on one task at one point in time may be entirely viable (March, 1991). Overall, the question remains: Under what conditions is market–political ambidexterity most desirable (value enhancing)?

A new area that awaits future research is how some emerging multinationals from emerging economies develop and strengthen market–political ambidexterity when venturing out of their home countries (Luo and Rui, 2009). For such emerging multinationals, market competition abroad is likely to be intense. However, political resistance in host countries, fueled by unfriendly media and politicians, is also likely to pose more significant challenges. This clearly suggests a necessity for such emerging multinationals to pay more attention to managing government and media relations in host countries—in addition to the obvious necessity to strengthen market capabilities (Globerman and Shapiro, 2009; Peng, 2012). Recently, two technologically capable and successful Chinese telecom equipment firms Huawei and ZTE were labeled by a US Congressional report as "national security threats" (US Congress, 2012). Why did they get themselves into such political trouble in the host country? Our answer is because of their failure to appreciate the importance of market–political ambidexterity. In other words, their single-minded focus on their market capabilities (which of course is important) resulted in their lack of awareness or willingness to develop political capabilities, which would have avoided such a fiasco.

Conclusion

Why were foreign firms such as Shell in Russia, Ford in Brazil, and Huawei and ZTE in the United States frustrated? Why were domestic firms such as Tata in India also frustrated? Why were foreign firms such as Dell in Brazil and domestic firms such as Infosys in India maneuvered successfully during institutional transitions? While numerous answers can be entertained, we believe that market–political ambidexterity holds a key to answer these intriguing questions. Overall, the concept of market–political ambidexterity serves to counterbalance the impression—implicit or explicit—that "markets have triumphed" during institutional transitions. In conclusion, if this article can contain only one message, we would like it to be a sense of the staggering power of the forces associated with both market competition and government influences during institutional transitions, and of firms' necessity to master skills in managing both sets of market-based and nonmarket-based competition simultaneously.

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Notes

1. Certain aspects of government relations may be related to corruption (Zhou and Peng, 2012). In this article, we focus on *legitimate* relations with governments.
2. A recent meta-analysis on the antecedents and outcomes of corporate political activity (Lux et al., 2011) samples 78 studies, but all of these studies use data from the United States.
3. In developed economies, this incompatibility is often experienced by firms in regulated industries (Armstrong and Sappington, 2006). Such firms have to simultaneously deal with markets and with

governments, but the lines of demarcation separating them are often blurred, especially during periods of institutional transitions such as deregulation.

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