HOW MULTINATIONAL ENTERPRISES NAVIGATE THE INSTITUTIONAL LANDSCAPE IN EMERGING MARKETS & DEVELOPING ECONOMIES

GORIOLA G. OLUSINA DANIEL

Propositions

1. The term ‘institutional voids’, as it relates to developing economies, is a misnomer.
   (This thesis, chapter 3)
2. Understanding the institutional differences observed in developing economies requires an appreciation of their unique political and cultural history.
   (This thesis, chapter 4)
3. The value of business research is proportional to the degree to which it addresses real-world business problems.
4. Completing a PhD is as much a triumph of resilience, as it is a disciplined intellectual expedition.
5. The current global financial architecture is designed to systematically lead resource-rich nations into debt traps.
6. Developments in Artificial Intelligence have elevated the risk of a machine-led revolt against the supremacy of the human race.

Propositions belonging to the thesis, entitled “How Multinational Enterprises Navigate the Institutional Landscape in Emerging Markets and Developing Economies.”

Goriola G. Olusina Daniel

Wageningen, 24 May 2024

HOW MULTINATIONAL ENTERPRISES NAVIGATE THE INSTITUTIONAL LANDSCAPE IN EMERGING MARKETS & DEVELOPING ECONOMIES

ESSAYS ON THE STUDY OF THE INTERPLAY BETWEEN FORMAL AND INFORMAL INSTITUTIONS IN EMERGING MARKETS

GORIOLA G. OLUSINA DANIEL

WAGENINGEN
UNIVERSITY & RESEARCH

Thesis committee

Promotor

Prof. Dr W. A. Dolfsma
Professor of Business Management & Organisation
Wageningen University & Research

Co-Promotors

Prof. Dr H. L. Aalbers
Professor, Strategy and Innovation
Radboud University, Nijmegen

Dr K. Fu
Senior Lecturer, Entrepreneurship and Innovation Management
Loughborough University London, United Kingdom

Dr V. C. Materia
Associate Professor, Innovation and Entrepreneurship in Chains and Networks
Wageningen University & Research

Other members

Prof. Dr. J H. H. Wesseler, Wageningen University & Research

Prof. Dr K. Amaeshi, University of Edinburgh Business School, United Kingdom

Prof. Dr T. Halaszovich, Constructor University, Bremen, Germany

Prof. Dr R. J. Blomme, Nyenrode Business University, The Netherlands

This research was conducted under the auspices of the Graduate School Wageningen School of Social Sciences

HOW MULTINATIONAL ENTERPRISES NAVIGATE THE INSTITUTIONAL LANDSCAPE IN EMERGING MARKETS & DEVELOPING ECONOMIES

ESSAYS ON THE STUDY OF THE INTERPLAY BETWEEN FORMAL AND INFORMAL INSTITUTIONS IN EMERGING MARKETS

GORIOLA G. OLUSINA DANIEL

Thesis

Submitted in fulfilment of the requirements for the degree of Doctor

at Wageningen University

by the authority of the Rector Magnificus

Prof. Dr C. Kroeze

in the presence of the

Thesis Committee appointed by the Academic Board to be defended in public on

Friday 24 May 2024

At 1:30pm in the Omnia Auditorium

Goriola G. Olusina Daniel
How Multinational Enterprises Navigate the Institutional Landscape in Emerging Markets & Developing Economies

194 Pages

PhD thesis, Wageningen University, Wageningen, the Netherlands (2024)
With references, with summary in English

ISBN: 978-94-6469-990-6

DOI: https://doi.org/10.18174/658459

DEDICATION

My father was orphaned at 12. He managed to escape abject poverty, as his life trajectory was transformed by the pursuit of academic excellence. This was possible through scholarships and the kindness of a village of aunties, uncles and strangers-turned-family. He was my inspiration for this achievement, which I dedicate to Demi and Joelah – my amazing daughters, who inspire me to be the best version of myself through their unwavering commitment to their own self-actualisation.

Table of Contents

LIST OF FIGURES

LIST OF TABLES

Chapter 1

GENERAL INTRODUCTION

01. GENERAL INTRODUCTION

1

1.1 Introduction

Over the last twenty-five years the International Business (IB) literature on emerging market institutions has been dominated by the institutional voids' perspective, which explores the implications of the absence or underdevelopment of market-supporting institutions (Khanna & Palepu, 1997; Doh et al., 2017; Barasa et al., 2017).

Firms operating in emerging markets and developing economies (EMDEs) typically encounter institutional factors such as weak legal and regulatory systems, indiscriminate enforcement of rules, corrupt government officials and volatile political environments, which can pose significant risks to firms, leading to increased uncertainty and relatively higher transaction costs (Peng et al., 2009; Khanna & Palepu, 2010).

There are some, however, who hold the contrarian view that while EMDEs have institutions that are distinctively different from developed country institutional environments (Mbalyohere, 2015; Olthaar et al., 2017, Bothello et al., 2019) and often tend to be weak or ineffective by comparison (Rottig, 2016), the characterisation conveyed by the term 'institutional voids' does not accurately reflect the reality of the different kinds of institutional configurations in EMDEs (Olthaar et al., 2017:). The main proponents challenge the notion of an absence of institutions altogether and emphasise the relative importance of informal institutions where so-called (formal) institutional voids exist in EMDEs (Doh et al., 2017; Olthaar et al., 2017).

Bothello et al., (2019), in their critique of the institutional voids thesis, highlight the implications of branding non-western institutional configurations as inferior and add to the call for a more nuanced approach to the study of firm performance in EMDEs (Doh et al., 2017; Olthaar et al., 2017. This has the potential to increase our understanding of how these distinctly different institutional constructs (Dieleman et al., 2022), which emanate from the unique and rich history of these countries (Mbalyohere, 2016), impact or are impacted by firm strategy (Hillman et al., 2004; Olthaar et al., 2017).

This thesis a collection of four articles on how formal and informal institutions interact to establish the institutional configuration of EMDEs seeks to contribute to this ongoing debate and calls for a more nuanced approach to the study of firm performance in EMDEs.

The remainder of this chapter briefly describes the extant literature on the institutional configuration of EMDEs and their relevance for research on how formal and informal institutions impact the strategy and performance of multinational enterprises (MNEs). It then lays out the specific research questions addressed in the main body of the thesis. And concludes with a description of the conceptual and methodological approach taken.

1.2 EMDEs as a laboratory for research on institutions

The term "emerging markets" was coined in 1981 by Antoine van Agtmael of the International Financial Corporation (IFC) – part of the World Bank Group and the largest global development institution focused on the private sector in EMDEs. It was an attempt to replace the terms – "Third World" or "Developing Countries", which he believed could limit the support IFC was seeking from Wall Street for a new global investment fund for stock markets in developing countries, given that many people at the time, associated the terms with extreme poverty, inferior standards and goods, and hopelessness. It has since been widely adopted in practice and academia.

Hoskinsson et al. (2000, p. 249) initially described emerging markets as "low-income, rapid growth countries using liberalisation as their primary engine of growth" and identified 64 countries that match this description. In later work, Hoskinsson et al. (2013), in recognition of the significant heterogeneity in this group, which at the time included China and India – the two largest emerging markets (Rottig, 2016), describe emerging markets as countries in the process of developing market-supporting political, legal and economic institutions. They proposed three sub-groupings – traditional emerging markets, mid-range emerging economies, and newly developed economies – to reflect the dynamic and progressive nature of emerging economies as observed over the last three decades.

In practice, IB papers use both terms – “developing economies” and “emerging markets”; often interchangeably. In this thesis, we adopt the nomenclature in Doh et al. (2017) and refer to the diverse group of countries captured in this definition as emerging markets and developing economies (EMDEs), as this more accurately signals the differences in institutional quality and construct across the range of countries undergoing the process of developing market-supporting political, legal and economic institutions.

Notably, the economic liberalisation that serves as a boundary condition for emerging markets in this definition contrasts with the so-called 'guarded globalisation' now common in China and India – the two largest emerging markets today (Rottig, 2016). This typifies the dynamism of emerging markets. It also points to an evolutionary pathway in market orientation where "governments of developing nations… *[eventually]* become wary of opening more industries to multinational companies and zealously protect local interests…" (Bremmer, 2014).

EMDEs are distinctively different from developed country institutional environments (Rottig, 2016), and are characterised by several unique institutional features that do not exist in developed countries. These 'differences' include the absence or underdevelopment of key market-supporting institutions – often referred to as 'institutional voids' (Khanna & Palepu, 1997), the relative importance of informal rules, norms and practices over formal institutions, distinct and perhaps conflicting institutional pressures by host governments, as well as more frequent and often unpredictable institutional change and transitions.

The consequences of such missing (Khanna & Palepu, 1997) or different (Olthaar et al., 2017) institutional arrangements can profoundly affect how firms respond or navigate institutional environments in EMDEs (Doh et al., 2017). For example, in some EMDEs, it is possible to find private firms absorbing the costs of absent or weak institutions by substituting for government agencies in building infrastructure or providing education (Banerjee et al., 2016; Khanna & Palepu, 2010; Rivera-Santos et al., 2012; Boddewyn & Doh, 2011).

Similarly, Chinese investments in Africa have included the need to develop infrastructure and education programs for employees, the costs primarily absorbed by the Chinese government (Van Dijk, 2009). Even attempts to transplant formal institutions into emerging markets where they are missing or deficient may exert upward pressure on business operating costs due to their inconsistency with local modes of conduct (Hah & Freeman, 2014).

Growing Importance of EMDEs as a laboratory for institutional research.

The dynamic nature of EMDEs, their increasing share of FDI and contributions to global GDP growth, and their observed distinct features make this category of countries an important and unique laboratory for examining MNE responses to different institutional configurations – for academics and practitioners alike.

In comparison, developed countries are commonly characterised by stable or "mature" market-supporting institutions that regulate markets and encourage economic activity in predictable, reliable and transparent ways. Institutional change or development in this context is generally incremental, predictable and consequently manageable for companies operating in these markets (North, 1990). In EMDEs, however, institutional change is typically unpredictable and calls for specific capabilities for MNEs to manage (Rottig, 2016).

Institutional voids

Khanna & Palepu (1997) advanced the concept of institutional voids as the absence or underdevelopment of market-supporting institutions that reflect institutional conditions that hinder the ease with which economic actors – buyers and sellers can interact (Doh et al., 2017). As defined, institutional voids can include the absence or weakness of regulatory systems, under-development of products, capital and labour markets, and inadequate mechanisms for enforcing contracts. The result; "institutional voids increase transaction costs significantly and lead to massive inefficiencies in the long run" (Palepu & Khanna, 1998), as companies operating in emerging markets must adapt their strategies to 'fill' these institutional 'voids'.

According to Doh (2017), the concept of institutional voids, which has since been widely discussed in IB, motivated a new way to understand firm strategy in emerging markets. Rather than considering institutions as ''givens'' that constrain interactions (e.g. Meyer & Rowan, 1977; DiMaggio & Powell, 1983), an institutional voids lens encourages a more dynamic approach for examining how firms strategise – alone or in conjunction with other actors – to avoid, remedy (Regne´r & Edman, 2014), compensate, substitute (Boddewyn & Doh, 2011), shape or even take advantage of institutional weaknesses (Khanna & Palepu, 2010).

Some scholars have, however, criticized the usage of the term "institutional voids" as not reflective of the reality of the dominance of informal institutions in EMDEs (Olthaar et al., 2017). Bothello et al., (2019) suggest that having been built on a narrow transaction cost conceptualisation of institutions as regulatory rules, this privileges western institutions as superior; while ignoring a more holistic treatment as 'regulative, normative and cultural-cognitive elements that, together with associated activities and resources, provides stability and meaning to social life' (Scott, 2004). It also limits the usefulness of the construct and may have prevented scholars from answering pertinent questions about the role of institutions for IB. For example, when formal market-supporting institutions are inadequate, what other informal or formal institutions or actors can fill this void (Dieleman et al,, 2022).

Formal and informal institutions

Institutions are the socially constructed rules that enable and constrain human interaction (North 1990). Institutional theory suggests that formal and informal institutions coexist and interact to establish the institutional framework of a country. Formal institutions represent state-enforced structures of codified and explicit rules, regulations, policies and standards that shape interaction among societal members (North, 1990). Informal institutions are unwritten rules, norms, customs, and traditions that shape behaviour and interactions among individuals and organization (North, 1990; Sartor & Beamish, 2014; Sauerwald & Peng, 2012). They are created and enforced outside official channels and governed by socially shared rules; or more specifically, expectations for social interactions and behaviour (Helmke & Levitsky, 2004; Helmke, 2006).

Collectively, formal and informal institutions promote order and stability by providing authoritative guidelines and enabling the formation of expectations regarding conduct and behaviour (Scott, 1995). They are, therefore, both important in shaping the behaviour of individuals and organizations, as well as the interaction of participants in the development process.

Institutional Quality

Institutional quality refers to the overall effectiveness and efficiency of formal institutions in helping firms to engage in and gain from market transactions (North, 1991).

Formal institutions affect the enforcement of laws and the protection of property rights that can help firms rely on market transactions and enable widespread impersonal exchange (Dixit, 2004; North, 1991). The fundamental quality of formal institutions is therefore reflected in how they regulate the behaviour of persons subject to it, regularising and thus stabilising expectations and outcomes; and specifically, how effectively they protect property rights, the level of corruption, execution of undue influence by government officials, government efficiency, security, and corporate ethics and accountability (Kafouros et al., 2022).

Barbalet (2022) argues that to be effective, institutional rules must operate in concert with shared beliefs about the rules and also about the consequences of following—and not following—them, so that in essence, institutional rules must be supported by social norms. Thereby establishing the premise for the identified heterogeneity of the institutional configuration, quality and evolution path observed in different countries and regions.

1.3 Problem Statement and Research Questions

Problem Statement

Market exchanges are the cornerstone of economic activity and inherently involve actors who transact with one another while having competing interests. These exchanges occur within the ambit of the prevailing institutional framework or furniture (Veblen, 1961) consisting of both formal and informal institutions. Formal institutions define what is acceptable and wield the authority of the State to sanction nonconforming behaviour, they allow individuals to form expectations about the actions and commitments of exchange partners, enable equilibrium practices to emerge (Greif, 1994), and support the conduct of exchanges (Redding, 2005). They thus provide a framework for economic and social activities, while informal institutions provide the prevailing norms and values that guide the behaviour of all actors within that framework (Holmes et al., 2013).

The literature has devoted considerably less attention to informal institutions than to formal institutions (Estrin & Prevezer, 2011; Sauerwald & Peng, 2013; Sartor & Beamish, 2014). This is thought to be due to the challenge researchers have faced in terms of the conceptualization and measurement of informal institutions (Dau et al., 2022). And consequently, serves as a research gap this thesis seeks to address in chapter 4.

There is also growing interest in how formal and informal institutions coexist to impact the performance of firms operating in emerging markets (Helmke & Levitsky (2004); Holmes et al., 2013; Dau et al., 2022). This informs the central motivation for this thesis and is addressed in chapters 2, 3 and 4.

Overall, the coexistence and interaction of formal and informal institutions are critical in establishing the institutional framework of a country. They shape the behaviour of individuals and organizations, as well as the interaction of participants in the development process.

In some cases, informal institutions can substitute for ineffective formal institutions (Dau et al., 2022). For example, substitutive informal institutions refer to unwritten rules that are convergent with ineffective formal rules, such as the general expectation that facilitating payments or bribes could speed up access to licenses and permits firms need to operate (Krammer, 2017). As the formal rules are ineffective, the informal rules take over and become the dominant rules (Olthaar et al., 2017).

In other cases, formal institutions can reinforce informal institutions. For example, the legal system can reinforce cultural norms and values by providing a framework for their enforcement.

Understanding the interplay between formal and informal institutions is therefore important for policymakers and researchers seeking to understand the impact and implications for the unique institutional configuration of EMDEs. This impacts MNEs performance, strategy, as well as entry and exit choices – and was the subject of a recent JIBS Special Issue, which included calls for a more nuanced approach to the study of how formal and informal institutions interact to establish the institutional construct or configuration in EMDEs (Doh et. al., 2017).

Research Questions

This thesis – a collection of four articles, is a response to this call to adopt a more nuanced approach to the study of how multinational enterprises navigate different institutional environments in EMDEs.

Table 1.1 Overview of Research Chapters

	Research Question	**Methodology**	**Results**
2	Can Management Effort and Bribes Compensate for low-quality institutions in Africa?	Quantitative analysis	The expectation that TMT and informal payments can be used as substitutes for high-quality institutions only holds for the former. Informal payments or bribes are not a substitute for low-quality institutional environments in Africa.
3	To what extent does the experience of MNEs operating in Africa equate the existence of different institutional environments across Africa, with the notion of 'institutional voids'?	Qualitative analysis	What MNEs respond to, are not institutional voids, but rather a constellation of institutions with rules that are different to what advanced country MNEs are familiar with. Also, the lack of effective formal institutions, does not necessarily translate into a universal competitive disadvantage for MNEs.

4	How do formal and informal institutions interact to impact the performance of foreign and domestic firms in EMDEs?	Quantitative analysis	Informal institutions often enhance or complement the positive effect of formal institutions, but with some intriguing regional variations.
5	What are the policy imperatives for attracting FDI for agro-industrial processing in Africa?	Qualitative analysis	Evidenced-based seven-point framework public policy makers working collaboratively with other stakeholders can use to implement tailored policy frameworks to address challenges, leverage opportunities, and promote sustainable agro-industrial development in Africa.

In addressing the main research objective, this thesis examines the following four sub-research questions:

Research Question 1: Can Management Effort and Bribes Compensate for low-quality institutions in Africa?

This research question is the focus of Chapter 2 and was published in the June 2018 issue of the Journal of Economic Issues[1] with my supervisors: Prof dr. Wilfred Dolfsma and Dr Kun Fu as coauthors. This early article, sequenced as the first of four papers in the thesis, explores options firms operating in sub-Saharan Africa (SSA) have to obtain what they need for their firms to operate.

Without high-quality formal institutions, we theorise that senior management teams (TMT) are faced with one of two options – either spending a lot of time and effort monitoring and responding to inefficient bureaucratic processes; or, alternatively, they may pay bribes to grease the wheels of progress (Krammer, 2017), to access key services and permits they need for their businesses to operate efficiently and legitimately.

This is tested empirically by drawing on a sample of firms surveyed from 35 African countries over a ten-year period (2005 – 2015). We find that our expectation that TMT and informal payments can be used as substitutes for high-quality institutions only holds for the former. And that informal payments or bribes are not a substitute for low-quality institutional environments.

[1] See Olusina Daniel, Fu & Dolfsma (2018). Available online at https://www.tandfonline.com/doi/full/10.1080/00213624.2018.1469920

Research Question 2: To what extent does the experience of MNEs operating in Africa equate the existence of different institutional environments, with the notion of 'institutional voids' across Africa?

This research question is the focus of Chapter 3. It reflects the key output of the 2018 Association of International Business Africa Chapter (AIB Africa) Panel on "How MNEs navigate different institutional environments in Africa", which was developed around this thesis' main research question. The paper was drafted by the candidate as corresponding author with input from Dr Theresa Onaji Benson and Dr Charles Mbalyohere – who served as panellists on the 2018 AIB Africa Panel of the same topic, and are named as co-authors.

The chapter critically examines the institutional voids perspective from the lens of MNEs operating across Africa. It draws on case study evidence from advanced economy (AMNEs) and emerging economy MNEs (EMNEs) operating across Africa. The findings suggest that what the MNEs in our reference study respond to are not institutional voids but rather a constellation of institutions with generally different rules than those AMNEs from highly formally institutionalized contexts are familiar with. And interestingly that the lack of effective formal institutions, does not necessarily translate into a universal competitive disadvantage for MNEs.

In reality MNEs operating in Africa respond to a mix of informal and formal institutions that have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that is distinctively different from other regions. Given this difference, MNEs need to consider what strategies can be transferred from institutionally different contexts; and what new capabilities are required to successfully operate across Africa.

Research Question 3: How do formal and informal institutions interact to impact the performance of foreign and domestic firms?

This research question is the subject of Chapter 4. It is now in the second round of reviews for the International Business Review (IBR), and was developed with support from my academic supervision team, which includes Prof dr. Wilfred Dolfsma, Prof dr. Rick Aalbers, Dr Kun Fu, and Dr Valentina Materia.

The chapter seeks to empirically test how the institutional mix of different countries affects the performance of foreign and domestic firms. Drawing on firm-level data using the World Bank

Enterprise Survey (WBES) of firms operating across 128 countries over 11 years, the notion of institutional voids is tested empirically, by examining how informal and formal institutions impacts the comparative performance of MNEs. Addressing the need for measures for informal institutions, we propose and operationalise measures for three widely practiced norms which we identify in this paper as proxies for informal institutions as exemplified by time spent by senior managers on regulations (TMT), informal payments or bribes, and local sourcing – and test to see if they complement or substitute formal institutions across our sample.

Generally, we find that informal institutions often enhance or complement the positive effect of formal institutions, but with some intriguing regional variations. We conclude that the intriguing findings captured in our study underline the heterogeneity and distinct differences in our full sample, and emerging markets and sub-Saharan African sub-samples.

Research Question 4: What are the policy imperatives for attracting FDI for agro-industrial processing in Africa?

This research question is the focus of Chapter 5. As a policy paper, it is included in this thesis in line with Wageningen University Research ethos to bridge theory with practice. It draws on Dunning's OLI paradigm and Institutional theory to examine how governments particularly in Africa, in light of what is often described as the under-development of their market-supporting institutions can adopt policies that facilitate foreign direct investment and private capital for specific sectors where they identify the potential for developing a competitive or comparative advantage.

While not attempting to be exhaustive, the paper draws from the extant literature on SEZs, and case study evidence of successful agro-industrial processing zones to identify seven policy imperatives for the establishment of an integrated policy framework to support the implementation of successful agro-industrial processing zones in the region.

Findings include the central role governments can and must play in coordinating the wide range of stakeholders and market interventions required to attract and sustain the benefits from increased FDI and private sector participation in agro-industrial zones. By adapting and contextualizing the successful implementations of Agro-industrial Processing Zones (AIPZs) in several comparator countries, we provide a seven-point framework that African governments can use to implement tailored policies to address challenges, leverage opportunities, and promote sustainable agro-industrial development.

1

1.4 Theoretical Framework

Table 1.2 provides a summary of the key theories reference in this thesis.

Table 1.2 Key Theories Used

#	Theory	Chapters	Key concepts/Authors cited
1	Institutional Theory	2, 3, 4, 5	*Formal and informal institutions* (North, 1990; Scott, 1995)
			Institutions, institutional change (North, 1990)
			Institutional Quality (World Bank, 1998)
			Institutional voids (Khanna & Palepu, 2000; Mair et al., 2012)
			Institutional mix (Helmke & Levitsky, 2004; Helmke, 2006; Pejovich, 2006; Olthaar et al., 2017)
			Institution Based View of Strategy (Peng, 2002)
			Transactional vs Non-market strategies (Hilman & Hitt, 1999; Hilman et. al, 2004; Rajwani & Liedong, 2015; Mbalyohere, 2015)
2	Theory of Multinationals	2,3,4,5	*Internalisation* (Buckley & Casson, 1976)
			OLI Paradigm (Dunning, 1980)
			AMNEs and EMNEs (Mbalyohere, 2016)
3	Industrial Policy	5	*Structural Change* (Lewis, 1954; Kuznets & Murphy, 1966; Rodrik, 2004)
			Value Chain Analysis (Dunning, 1980)

Institutional Theory

Used throughout this thesis, Institutional theory is a broad interdisciplinary field that examines the role of institutions in shaping human behaviour and social outcomes. It encompasses a variety of perspectives and approaches that seek to understand how institutions, broadly defined as the rules, norms, and values that govern social interactions, influence individual and organizational choices. By recognizing the pervasive influence of institutions, institutional theory offers insights into how individuals, organizations, and societies are shaped and constrained by the rules, norms, and values that govern their interactions.

Key concepts in Institutional Theory include:

- *Institutions*: Institutions are often defined as the formal and informal rules, norms, and practices that structure social life and market exchanges (North, 1990; Scott, 1995). They can be formal, such as laws and regulations, or informal, such as social conventions and cultural values. And represent social structures that provide stability and order by constraining and enabling human behaviour.

- Formal institutions: Explicitly defined rules and regulations, such as laws, constitutions, and contracts, typically enforced by the authority of the state.
- Informal institutions: Unwritten norms, customs, and traditions that shape social interactions and expectations.
- Path dependence: The tendency of historical events and decisions to shape future outcomes, creating a trajectory that is difficult to change.
- Institutional isomorphism: The tendency of organizations to adopt similar structures and practices in response to similar institutional pressures.
- Institutional change: Despite their tendency to persist, institutions can also change over time. Institutional change can be driven by factors such as exogenous shocks, internal conflicts, and purposeful interventions.

Theory of multinational enterprise (MNE)

The theory of the multinational enterprise (MNE) is a foundational theory in IB that seeks to explain why and how firms expand their operations across national borders. It encompasses a variety of perspectives and frameworks that aim to understand the factors that drive MNEs to engage in foreign direct investment (FDI) and the strategies they employ to succeed in international markets.

The theory of the MNE continues to evolve as the global business landscape changes. Understanding the factors that drive MNE behaviour and the strategies they employ is crucial for policymakers, business leaders, and researchers seeking to navigate the complexities of international commerce and investment.

Key Concepts in MNE Theory used in this thesis (see chapters 2 and 5) are as summarised in Table 1.3 below:

Table 1.3 Key Concepts in MNE Theories Used

Theory	**Author(s)**	**Key concepts/Authors cited**
Ownership advantages:	*Dunning (1980)*	*Unique assets MNEs possess, such as proprietary technology, brand name recognition, or management expertise, that give them a competitive edge in foreign markets.*

Location advantages:	*Hymer (1960)*	*Specific benefits countries or regions offer that attract MNEs, such as access to raw materials, a skilled labor force, or favourable tax regimes.*
Internalization advantages:	*Buckley & Casson (1976)*	*Certain aspects of their operations MNEs internalize, such as production or distribution, to gain control over the value chain and protect their proprietary knowledge.*
Eclectic or OLI paradigm:	*Dunning (1993)*	*A unifying framework that integrates the concepts of ownership, location, and internalization advantages to explain MNE behaviour*
Transaction cost theory:	*Williamson (1985)*	*MNEs engage in FDI when the costs of managing transactions across borders are lower than conducting those transactions through market mechanisms.*
Network theory:	*Granovetter (1985)*	*Examines the complex networks of interfirm relationships, suppliers, and partners, that shape MNEs international operating models and strategies*
Global value chains (GVCs):	*Gereffi at al., (2005)*	*MNEs orchestrate GVCs, coordinating the production and distribution of goods and services across multiple countries*
Emerging market multinationals (EMNEs):	*Rugman & Verbeke (2009)*	*Firms from emerging economies are expanding their global presence, challenging traditional MNEs (or advanced MNEs) and bringing new dynamics to international business*

Industrial Policy

Adopted in Chapter 5 as a mechanism to facilitate the practical application of the evidence-based analysis in prior chapters in recommendations that can be adopted by governments across Africa, Industrial Policy is a government intervention aimed at improving the competitiveness and capabilities of domestic firms and promoting structural transformation (Rodrik, 2004). It involves a range of measures, including subsidies, tax breaks, trade protection, and government procurement, to encourage the development of specific industries or technologies. It is typically implemented in countries seeking to accelerate economic growth, diversify their economies, or catch up with more developed nations.

Key elements of Industrial Policy include:

- *Selectivity*: Industrial policy targets specific industries or technologies, rather than providing broad-based support to all industries.
- *Strategic focus:* Industrial policy is guided by a long-term vision of the desired economic structure and technological capabilities.
- *Coordination*: Industrial policy requires coordination across different government agencies and stakeholders.

- *Adaptability*: Industrial policy should be adaptable to changing economic conditions and technological advancements.

Industrial policy is a controversial tool, as it can lead to market distortions as certain industries or technologies are favoured over others. It also requires the government to make subjective decisions about which industries to support which can lead to inefficient allocation of resource, as well as encourage rent-seeking behaviours as firms may lobby for government support rather than focusing on innovation and efficiency. It nonetheless has the potential to be an effective means of promoting economic development and industrial transformation, within the context of scarce or limited government resources or capacity to deliver public services or outcomes firms rely on, more broadly. It is therefore important to design and implement industrial policy carefully to avoid unintended consequences and market distortions.

1.5 Methodology

Research Design

The dynamic interplay between MNEs and the institutional environments of emerging markets (EMs) has emerged as a critical area of inquiry in IB research. MNEs must navigate complex and often fluid institutional landscapes in EMDEs, characterized by a blend of formal and informal institutions (Khanna & Palepu, 1997; North, 1990).

Traditional monomethod approaches, relying solely on quantitative or qualitative data, often fail to capture the nuances and complexities inherent in this dynamic interplay (Creswell & Plano Clark, 2018). Mixed methods methodology, on the other hand, offers a comprehensive and nuanced approach to understanding the multifaceted relationship between MNEs and institutional environments in EMDE contexts (Creswell, 2014).

This thesis employs a mixed methods approach, combining qualitative and quantitative methodologies to address the need for a more nuanced approach to the study of the interplay between formal and informal institutions in emerging markets, and how this shapes MNE responses (Doh et al, 2017).

Table 1.4 Methodological approaches used

Ch.	Research Question	Methodology	Variables /Data Sources
2	Can Management Effort and Bribes Compensate for low-quality institutions in Africa?	Quantitative analysis	*Dependent variable:* Firm Performance *Explanatory variable:* Institutional effectiveness (EFW Index), Top

			Management Effort, Informal Payments (WBES) *Control variables:* Age, Size, no. of employees, industrial sector, ownership, managers experience, GDP per capita (USD/PPP), population size, year effect (WBES) *WBES Sample:* 17,757 firms, 35 countries, over 10-year period (2006 – 2015).
3	To what extent does the experience of MNEs operating in Africa equate the existence of different institutional environments across Africa, with the notion of 'institutional voids'?	Qualitative analysis	Qualitative multi-case study sample consisting of 3 EMNEs and 3 AMNEs operating in Uganda's electricity industry (Mbalyohere, 2016)
4	How do formal and informal institutions interact to impact the performance of foreign and domestic firms?	Quantitative analysis	*Dependent variable:* Firm Performance *Explanatory variable:* Institutional quality (EFW Index), Top Management Effort, Informal Payments, Local sourcing, Ownership (WBES) *Control variables:* Age, Size, no. of employees, industrial sector, ownership, managers experience, GDP per capita (USD/PPP), population size, year effect (WBES) *WBES Sample:* 96,320 firms, 128 countries, over an 11-year period (2006 – 2016).
5	What are the policy imperatives for attracting FDI for agro-industrial processing in Africa?	Qualitative analysis	Qualitative multi-country case studies of successful SEZ interventions in emerging markets (Various)

The thesis includes two qualitative (Chapters 3 and 5) and quantitative studies (Chapters 2 and 4), each. It was designed as such to provide a more comprehensive understanding by combining the depth of qualitative methods with the breadth of quantitative methods (Eisenhardt, 1989; Creswell, 2014).

Used extensively in chapters 3 and 5, case studies allow for the capture of nuanced aspects of informal institutions often overlooked in quantitative analysis (Patton, 2002). Where these can be validated with quantitative analysis, which is the approach adopted in this thesis, it makes for more robust analysis (Creswell and Plano Clark, 2018). Case studies (as in Chapter 3) are used to identify key themes from the experience of AMNEs and DMNEs operating in Africa, which were then tested empirically in chapters 2 and 4.

Reflecting on some of the findings from the quantitative analysis in chapter 4, as suggested by Johnson and Onwuegbuzie (2004), the integration of qualitative insights into quantitative analysis supports the formulation of a seven-point policy framework developed in chapter 5, which as proposed, African governments can use to implement tailored policy frameworks to address challenges, leverage opportunities, and promote sustainable agro-industrial development.

Data

World Bank Enterprise Survey (WBES): As used successfully in Halaszovich & Lundan (2016), the thesis draws on firm-level data using the World Bank Enterprise Surveys (WBES), which contains information about private firms from key manufacturing and service sectors for 139 countries across the world. Applying a uniform sampling frame and standardized survey, the WBES produces a representative sample and harmonized data that are comparable across a wide range of economies across the globe. It enables researchers to understand how and which factors and institutions in the business environment affect firm performance over time and across countries.

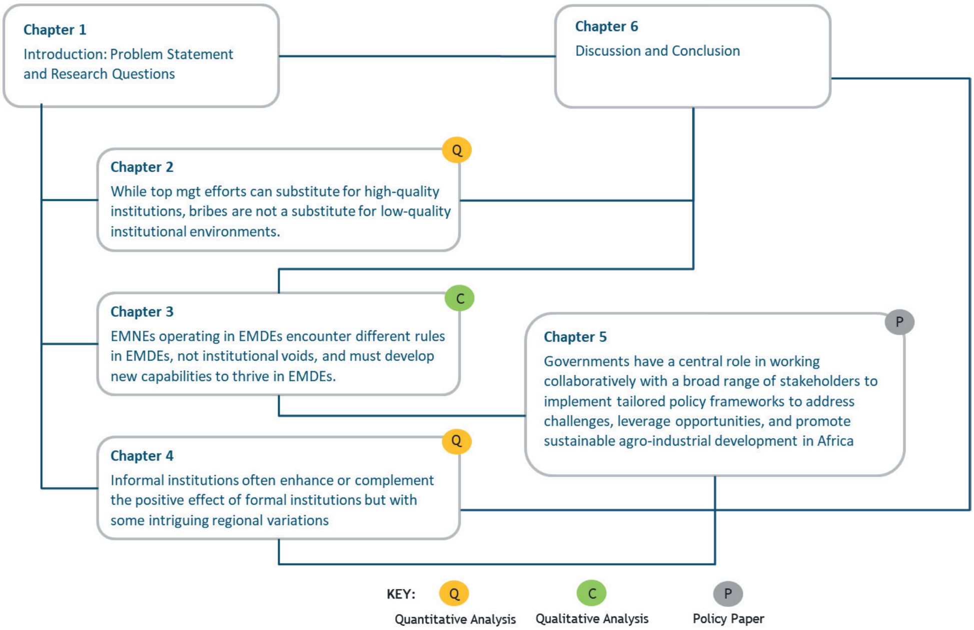
Economic Freedom (EFW) Index: Data from the WBES is combined with country-level variables from the Economic Freedom Index of the Fraser Institute. The Economic Freedom index draws on 42 distinct variables from third party sources, such as the International Country Risk Guide, the Global Competitiveness Report and the World Banks Doing Business Reports. It measures the degree to which the policies and institutions of countries are supportive of economic freedom; the cornerstone of which are personal choice, voluntary exchange, freedom to enter markets and compete, and security of the person and privately owned property. And captures the degree of economic freedom present in five major areas (1) Size of Government; (2) Legal System and Security of Property Rights; (3) Sound Money (4) Freedom to Trade Internationally (5) Regulation.

In order to receive a high EFW rating, a country must provide secure protection of privately owned property, a legal system that treats all equally, even-handed enforcement of contracts, and a stable monetary environment. It also must keep taxes low, refrain from creating barriers to both domestic and international trade and rely more fully on markets rather than government spending and regulation to allocate goods and resources.

Other: We use statistics regarding countries' overall socioeconomic conditions from the World Bank, AfDB, IMF and other sources.

1.6 Overview of the thesis

Figure 1.1 Overview of the thesis



This thesis is composed of a general introduction, four themed chapters and a general discussion and conclusion.

This section, the general introduction, sets out key concepts we reference in exploring how EMDE institutions impact and are impacted by foreign (as well as domestic) firms.

Chapter 2, examines empirically, a previously untested view underlying the institutional void thesis: the idea that entrepreneurs and managers of firms need to seek alternative routes to obtain what their firm needs to function when confronted by low quality institutions (Veblen 1961, p.236). We draw our sample from the World Bank Enterprise Survey - a population of firms surveyed from 35 African countries over a 10-year period of time between 2006 and 2015. And examine the impact of management effort and bribes - two common responses for firms operating in low quality institutional environments in sub-Saharan Africa.

Chapter 3 contributes to the debate on "How MNEs navigate different institutional environments across Africa" inspired by panel discussions at the AIB Africa Panel hosted by the University of Kigali, Rwanda in July 2018, by examining the institutional landscape in Africa from the perspective of MNEs operating across the continent. It draws on case study evidence from advanced economy and emerging economy MNEs operating across Africa (Mbalyohere, 2016) to argue that the wide-scale reality of institutions that significantly differ from what some MNEs are familiar with, should not necessarily imply institutional voids. It begins with a brief discussion on the relevance of institutions and the conceptual basis of our critique of the institutional void thesis. It then examines evidence from six in-depth case-studies that outline how six MNEs developed strategies to participate in the liberalisation of Uganda's electricity sector. These insights are then complimented with further evidence from across the continent on the influence of transactional political strategies on the performance of South African MNEs operating in Africa.

A large WBES dataset is used in Chapter 4, to empirically test the notion of institutional voids, based on the transaction costs perspective (Williamson, 1981) that chapter examines how informal and formal institutions interrelate, and how this impacts firm performance. Adopting Helmke & Levitsky's (2004) typology of informal institutions, three widely observed and established norms or firm responses to formal institutions are identified and drawn from the WBES data and are proposed as proxies for informal institutions (i.e. *a) senior management time spent of formal institutions b) informal payments* and *c) local sourcing*). We then theorise and empirically test how these informal institutions, interplay with formal institutions as captured by the Economic Freedom Index[2] – a comprehensive measure of the institutional quality of the host country's formal institutions, to constitute the institutional configuration of host-country environments, and how this combines to impact the performance of multinational enterprises.

Chapter 5, in an attempt to cement the practical relevance of this thesis, proceeds to establish the policy imperatives for attracting private sector investment for deepening agro-processing capabilities across the African region, in view of renewed interest in enhancing agri-food

[2] The Economic Freedom index draws on 42 distinct variables from third party sources, such as the International Country Risk Guide, the Global Competitiveness Report and the World Banks Doing Business Reports. And measures the degree of economic freedom present in five major areas (1) Size of Government; (2) Legal System and Security of Property Rights; (3) Sound Money (4) Freedom to Trade Internationally (5) Regulation

systems as a strategy to accelerate the goal of food security, creation of sustainable jobs, and harnessing the potential benefits of what the World Bank projects could become a $1 trillion market by 2030.

REFERENCES

Banerjee, S. B., Oetzel, J., & Ranganathan, J. (2016) Multinational enterprises and the challenge of sustainable development. California Management Review, 58(2), 58-82

Barasa. L., Knoben J., Vermeulen P., Kimuyu P., Kinyanjui B. (2017). Institutions, resources and innovation in East Africa: A firm level approach. Research Policy, 46, 280–291.

Barbalet J., 2022 Conceptualising informal institutions: Drawing on the case of guanxi. British Journal of Sociology, 74 (1):70-82.

Boddewyn, J. J., & Doh, J. P. (2011) Global Strategy and the collaboration of MNEs, NGOs, and governments for the provision of public goods: A conceptual review. Management International Review, 51(6), 899-924.

Bothello, J., Nason, R. S., & Schnyder, G. (2019). Institutional Voids and Organization Studies: Towards an epistemological rupture. Organization Studies, 40(10), 1499–1512.

Bremmer, I. (2014) The New Rules of Globalisation. Harvard Business review 92 (1-2)

Buckley, P. J., & Casson, M. (2016). *The future of the multinational enterprise*. Springer.

Creswell, J. W. (2014). A concise introduction to mixed methods research. SAGE Publications.

Creswell, J. W., & Plano Clark, V. L. (2018). Designing and Conducting Mixed Methods Research (3rd ed.). Thousand Oaks, CA: SAGE.

Dar S. (2017). De-colonizing the boundary-object. Organization Studies, 39, 565–584.

Dau, L. A., Chacar, A. S., Lyles, M. A., & Li, J. (2022). Informal institutions and international business: toward an integrative research agenda. Journal of International Business Studies, 53(6), 985-1010.

Dieleman, M., Markus, S., Rajwani, T., & White, G. O. (2022). Revisiting Institutional Voids: Advancing the International Business Literature by Leveraging Social Sciences. Journal of International Management, 28(3), 100935.

DiMaggio, P.J. and Powell, W.W. (1983) The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields. American Sociological Review, 48, 147-160.

Dixiit, A. (2004) "Two-Tier Market Institutions," Chicago Journal of International Law: Vol. 5: No. 1, Article 11.

Doh, S. Rodrigues, Saka-Helmhout, M. Makhija (2017) International business responses to institutional voids. J. Int. Bus. Stud., 48 (2017), pp. 293-307

Dunning, J.H, (1993*) Multinational Enterprises and the Global Economy.* Edward Elgar Publishing

Dunning, J. H. (1980). The eclectic paradigm as an envelope for economic and business theories of MNE activity. In *International business strategy* (pp. 60-84). Routledge.

Eisenhardt, K. M. (1989). Building Theories from Case Study Research. The Academy of Management Review, 14(4), 532–550.

Estrin, S. and Prevezer, M. (2010). The role of informal institutions in corporate governance: brazil, russia, india, and china compared. Asia Pacific Journal of Management, 28(1), 41-67.

Gereffi, G., Humphrey, J., & Sturgeon, T. (2005). The governance of global value chains. *Review of international political economy*, *12*(1), 78-104.

Granovetter, M. (1985). Economic action and social structure: The problem of embeddedness. *American Journal of Sociology, 91*(3), 481–510.

Greif, A. 1994. Cultural beliefs and the organization of society: A historical and theoretical reflection on collectivist and individualist societies. *Journal of Political Economy, 102:* 912-950.

Hah, K. and Freeman, S. (2014). Multinational enterprise subsidiaries and their CSR: A conceptual framework of the management of CSR in smaller emerging economies. Journal of Business Ethics, 122(1), 125-136.

Helmke, G. and Levitsky, S. (2004). Informal institutions and comparative politics: a research agenda. Perspectives on Politics, 2(04), 725-740.

Helmke, G. (2006). Informal institutions and democracy.

Hillman, A.; Hitt, M. (1999). Corporate political strategy formulation: A model of approach, participation, and strategy decisions. *Academy of Management Review, Number 24,* pp. 825–842.

Hillman, A. J., Keim, G. D., & Schuler, D. A. (2004). Corporate political activity: a review and research agenda. Journal of Management, 30(6), 837-857.

Holmes, R. M., Miller, T., Hitt, M. A., & Salmador, M. P. (2013). The Interrelationships Among Informal Institutions, Formal Institutions, and Inward Foreign Direct Investment. Journal of Management, 39(2), 531–566.

Hoskisson, R. E., Eden, L., Lau, C. M., & Wright, M. (2000). Strategy in emerging economies. *Academy of management journal, 43(3),* 249-267.

Hoskisson, R. E., Wright, M., Filatotchev, I., & Peng, M. W. (2012). Emerging multinationals from mid-range economies: the influence of institutions and factor markets. Journal of Management Studies, 50(7), 1295-1321.

Hymer, S (1960).,*The International Operations of National Firms: A Study of Direct Investment.* Cambridge, Mass.: MIT Press

Johnson, R.B. and Onwuegbuzie, A.J. (2004) Mixed Methods Research: A Research Paradigm Whose Time Has Come. Educational Researcher, 33, 14-26.

Kafouros, M., Aliyev, M., Piperopoulos, P., Au, A., Ho, J., & Wong, S. Y. N. (2023). The role of institutional quality and industry dynamism in explaining firm performance in emerging economies. Global Strategy Journal.

Kafouros, M., Chandrashekar, S. P., Aliyev, M., & Ming Au, A. K. (2022). How do formal and informal institutions influence firm profitability in emerging countries? Journal of International Management.

Khanna T. & Palepu K. G. (1997). Why Focussed Strategies May Be wrong for Emerging Markets. Harvard Business Review (July – August 1997). 28(1), 100890.

Khanna, Tarun, Krishna G. Palepu, and Richard Bullock (2010). Winning in Emerging Markets: A Road Map for Strategy and Execution. Boston: Harvard Business Press.

Krammer, S. (2017). Greasing the wheels of change: bribery, institutions, and new product introductions in emerging markets. Journal of Management, 45(5), 1889-1926.

Kuznets, S., & Murphy, J. T. (1966). *Modern economic growth: Rate, structure, and spread* (Vol. 2). New Haven: Yale University Press.

Lewis, W. A. (1954). Economic development with unlimited supplies of labour.

Mair, J., Martí, I., & Ventresca, M. J. (2012). Building inclusive markets in rural Bangladesh: How intermediaries work institutional voids. *Academy of Management Journal, 55(4),* 819- 850.

Mbalyohere, C. G. (2016). Corporate political activity in sub-Saharan Africa : the influence of multinational enterprises in the institutionalisation of Uganda's electricity industry. PhD thesis The Open University. DOI:

Meyer, J., & Rowan, B. (1977). Institutionalized Organizations: Formal Structure as Myth and Ceremony. American Journal of Sociology, 83, 340-363.

North, D. C. (1990). Institutions, institutional change and economic performance.

North, D. C. (1991). Institutions. Journal of Economic Perspectives, 5(1), 97-112.

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. (2016). Markets and institutional swamps: tensions confronting entrepreneurs in developing countries. Journal of Institutional Economics, 13(2), 243-269.

Palepu, K. G., & Khanna, T. (1998). Institutional Voids and Policy Challenges in Emerging Markets. The Brown Journal of World Affairs, 5(1), 71–78.

Patton, M. Q. (2002). Qualitative research and evaluation methods (3rd ed.). Thousand Oaks, CA: Sage Publications.

Pejovich, S. (2006). The effects of the interaction of formal and informal institutions on social stability and economic development. *Institutions, Globalisation and Empowerment, 56*.

Peng, M.W., Sun, S.L., Pinkham, B. and Chen, H. (2009) The Institution-Based View as a Third Leg for a Strategy Tripod. Academy of Management Perspective, 23, 63-81.

Peng, M. W. (2002). Towards an institution-based view of business strategy. *Asia Pacific journal of management*, *19*, 251-267.

Rajwani, T., & Liedong, T. A. (2015). Political activity and firm performance within nonmarket research: A review and international comparative assessment. *Journal of World Business*, *50*(2), 273-283.

Redding, G. (2005) The Thick description and comparison of societal systems of capitalism. Journal of international Business Studies 36(2), 123-155

Regnér, P. and Edman, J. (2013). MNE institutional advantage: how subunits shape, transpose and evade host country institutions. Journal of International Business Studies, 45(3), 275-302.

Rivera-Santos, M., Rufi'n C. R., & Kolk, A. (2012). Bridging the institutional divide: partnerships in subsistence markets. Journal of Business Research, 2012, 65(1), 1721-1727.

Rottig, D. (2016). Institutions and emerging markets: effects and implications for multinational corporations. International Journal of Emerging Markets, 11(1), 2-17.

Rugman, A. M., and Verbeke, A. 2003. "Extending the Theory of the Multinational Enterprise: Internalization and Strategic Management Perspectives," *Journal of International Business Studies 34:* 125–137.

Sartor, M. A., & Beamish, P. W., (2014). "Offshoring innovation to emerging markets: Organizational control and informal institutional distance," Journal of International Business Studies, Palgrave Macmillan; Academy of International Business, vol. 45(9), 1072-1095,

Sauerwald, S. and Peng, M. W. (2012). Informal institutions, shareholder coalitions, and principal–principal conflicts. Asia Pacific Journal of Management, 30(3), 853-870.

Scott, W. R. (1995), Institutions and Organizations. Ideas, Interests and Identities. Sage ISBN: 978-142242224

Scott, W. R. (2004). Institutional theory: Contributing to a theoretical research program. In K. G. Smith, & M. A. Hitt, (Eds.), Great minds in management: The process of theory development (pp. 460-484). Oxford: Oxford University Press.

Van Dijk M. P. (2009). The new presence of China in Africa.

Veblen, Thorstein. "The Limitations of Marginal Utility." In The Place of Science in Modern Civilization, by Thorstein Veblen, pp. 231-51. New York, NY: Russell and Russell, 1961.

Williamson, O. E. (1985). The economic institutions of capitalism. New York: Free Press.

Williamson, O. E. (1981). The economics of organization: The transaction cost approach. American journal of sociology, 87(3), 548-577.

World Bank. (1998). World development report 1998/1999: Knowledge for development. The World Bank.

Chapter 2

INSTITUTIONAL QUALITY AND INDUSTRIAL DEVELOPMENT IN SUB-SAHARAN AFRICA:

CAN MANAGEMENT EFFORT AND BRIBES COMPENSATE FOR LOW-QUALITY INSTITUTIONS?

PUBLISHED IN **JOURNAL OF ECONOMIC ISSUES**

Gori Olusina Daniel, Kun Fu and Wilfred Dolfsma (2018)

Institutional Quality and Economic Development in Sub-Saharan Africa: Can Management Effort and Bribes Compensate for Low-Quality Institutions? Journal of Economic Issues Vol. LII No. 2 June 2018.

ABSTRACT

The industrial development in sub-Saharan Africa is perhaps more affected by the quality of institutions than that of other regions. We investigate what alternatives managers have to secure what their firms need to function in case the institutional furniture they are confronted with is of low quality. We find that in high quality institutional environments management spending effort dealing with authorities and navigating regulations negates the effect of the institutional environment. Managers do not need to spend these efforts. Perhaps surprisingly, we find that the positive effect of high-quality institutional environments on firm performance is enhanced by making informal payments.

KEYWORDS

Firm performance, informal payments, institutional quality, institutions, sub-Saharan Africa

02. INSTITUTIONAL QUALITY AND INDUSTRIAL DEVELOPMENT IN SUB-SAHARAN AFRICA:

CAN MANAGEMENT EFFORT AND BRIBES COMPENSATE FOR LOW-QUALITY INSTITUTIONS?

2.1. Introduction: Institutions and Firms

Harry Trebing (1987) convincingly argued against a then mainstream consensus in economics that industry should face as little regulation as possible. The implicit assumption driving this view was that government failure was more likely or more detrimental than the market failures that were recognized. Trebing and others, prominent among them institutional economists, have since been able to demonstrate that the proper functioning of markets is dependent on appropriate institutions being in place as markets are necessarily embedded in society (see Dolfsma, 2013).

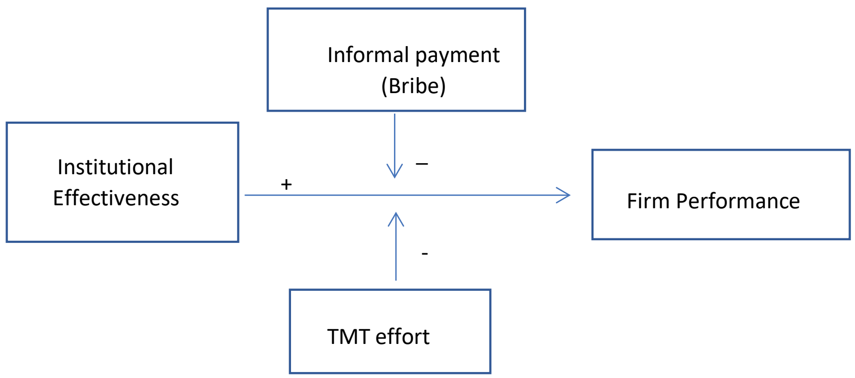
Mainstream economists and policymakers have, after North (1990), also embraced the idea that institutions affect the economy and firm performance. The World Bank (1998) and others, have since followed suit. A view has taken hold that if and when developing countries put in place the formal institutions that characterize western economies, private firms operating in their economies would benefit (Khanna and Palepu, 2000; Lee and Kim, 2009; Mair and Marti, 2009; Sutter et al., 2013). Without such institutions, an 'institutional void' is believed to exist that hampers firms' performance (Mair et al., 2012). Others have indicated, in contrast, that in such circumstances of absent formal institutions that regulate the economic domain, institutions still affect firms. These can be informal institutions, or formal institutions from a different, adjacent practice or domain (Olthaar et al., 2017).

In this brief article we address another potentially problematic untested view underlying the institutional void thesis: the idea that an inappropriate or unsatisfactory institutional 'furniture' (Veblen 1961, p.236) forces entrepreneurs and managers of firms (we will also refer to this as Top Management Team - TMT) to seek alternative routes to obtain what they need for their firm to function.

In this view, the preferred route is one where entrepreneurs and managers rely on clear, predictable and enforced rules that treat all equally; and equally efficiently. Consequently, in high-quality institutional environments, responses from public authorities and service providers become predictable in their nature and speed of delivery (World Bank 1998, p.15). Public authorities and service providers deliver a range of key services to firms such as licences, permits, access to electricity, tax administration, legal underpinning of contracts between parties, and certainty of property rights. When public institutions are of high quality, firms can focus their efforts and resources on production and other more directly value creating activities.

Without high quality institutions, entrepreneurs and managers must either spend a lot of effort navigating the inefficient regulatory system, or resort to other measures – such as informal payments (i.e. gifts or bribes[3]) to create an obligation (Darr, 2003; Dolfsma et al. 2008) – to try to ensure that the interests of individuals working in public authorities and service providers will be aligned with those of private citizens and TMT members alike.

Figure 2.1: Conceptual model



Low-quality institutions can therefore increase the transaction costs of dealing with public authorities as they give individuals at all levels in these government agencies the opportunity to have their own interests prevail over those of the agency or of society as a whole. In such circumstances of government failure (cf. Dolfsma, 2013), extra efforts may be required by non-principal individuals and TMT members in visiting authorities repeatedly, by monitoring

[3] On the difference between gifts and bribes, see Rose-Ackerman (1998). For a review of the literature on gift exchange see Dolfsma et al. (2008).

procedures, or by obtaining the resources from rogue agents. Under these conditions, informal payments as described, and TMT efforts, are thus perceived as substitutes for the quality of the institutional furniture; and can be thought to compensate for the strength or quality of a country's institutional furniture.

Figure 1 illustrates the conceptual model that characterises informal payments and TMT efforts as substitutes for the quality of the institutional furniture in a country.

We test this view directly in this short paper. Focusing on sub-Saharan Africa is appropriate as institutional quality varies substantially, following the differing pace and success of reforms to deepen democratic values and institutions, and adopt market liberating policies since the 1990s (UNCTAD & UNIDO, 2011); and that TMT efforts dealing with an inefficient regulatory system, as well as the prevalence of informal payments, are believed to be rife.

2.2. Methods

Data and Sample. We use the World Bank Enterprise Surveys (WBES) of firm-level data, which contains information about private firms from key manufacturing and service sectors across 139 countries in the world. The Enterprise Surveys adopt standardized survey instruments and a uniform sampling frame to produce a representative sample and harmonised data that are comparable across a wide range of economies, which enables understanding of how and which factors and institutions in the business environment affect firm performance over time and across countries (World Bank, 2007). We draw on other sources of data to compile the country-level variables such as the Economic Freedom Index provided by the Fraser Institute, the data on country's overall socioeconomic conditions from the World Bank and the IMF. We draw the sample from a population of firms surveyed from 35 African countries over a 10-year period of time between 2006 and 2015. A total of 17,757 observations are included in the sample.

Dependent variable: *Firm performance is* the dependent variable and is measured by a fiscal year's *total sales of a firm*. We convert the local currency into the internal dollar and factor in the purchasing power parity to ensure the comparability across countries over time.

Independent variables: *Institutional Effectiveness* is concerned with how well institutions relate with each other and are fit for purpose from the perspective of the wider society (Rodriguez-Pose, 2013). We measure this by the overall degree of economic freedom index provided by the Fraser Institute, which draws on a composite measure of 42 distinct variables across five major areas a) Size of Government; b) Legal system and security of property rights c) Sound money d) Freedom to trade internationally; and e) Regulation. *Top management effort* is the percent of senior management's time spent in dealing with regulations. We measure it by taking the difference between a firm's TMT effort and the sector-level average value of TMT effort within the country in which the firm is located. *Informal payment* is often seen that gifts or informal payments are paid to public officials to "get things done" with regard to customs, taxes, licenses, regulations, services etc. This is measured by the percent of a firm's total annual sales paid as informal payment.

Control variables: We control for a set of firm-level and country-level variables, which are associated with firms' performance and measured as follows. *Age* of a firm (see Johanson & Vahlne, 1990) is measured by the difference between the year of observation and the year in which the firm was formally registered. *Size* of a firm (see Schumpeter, 1947) is measured by the number of employees of the firm, and coded as a categorical variable taking the value '1' for small size firms with less than 20 employees, '2' for medium size firms with less than 100 employees, and '3' for large size firms with no less than 100 employees. The industrial *secto*[4]*r* in which a firm's primary business lies, which is measured by a categorical variable taking the value '1' for manufacturing industry, '2' for service industry, and '3' for other industries. *Ownership* of a firm (see McGahan & Victer, 2009) is measured by the percent of the firm owned by private foreign individuals, companies or organizations. It is measured by a dummy variable and we assign the value "1" for foreign firms with more than 50% of the firm is owned by foreigners, and "0" for domestic firms. *Manager's experience* (Ayyagari et al., 2011) is measured by the number of years a firm's top manager has been working in the sector. Because a country's wealth has been shown to influence firms' performance, we control for the country's *GDP per capita* (USD) adjusted for purchasing power parity (PPP). We control for *population* size of country as it captures the market size within the country. The *year effect* is controlled for as well.

Data Analyses: The WBES dataset is hierarchical in structure, which means that the firm-level observations are nested within the country-level observations. With this data structure, firm-

[4] The industrial *sector* is classified into manufacturing industry and service industry based on firms' primary business line.

level data are likely to be correlated within countries. Traditional multiple regressions such as the ordinary least square regressions with a pooled data could result in biased estimations due to ignoring the nested data structure, thus violating the assumption of data independence (Hofmann et al., 2000). We therefore apply multi-level modelling techniques to analyse the data while accounting for the hierarchical structure of the dataset. We specify a two-level model with random intercept to evaluate firms' performance by factoring in both the impact of institutional conditions at the country-level and the influence of informal payment and top management effort at the firm-level at the same time. The models are specified below.

2

Level-1 equation:

$$Y_{ij} = \beta_{0j+}\beta_{1j}X_{ij} + e_{ij}$$

Level-2 equations:

$$\beta_{0j} = \gamma_{00} + \gamma_{01}W_j + u_{0j}$$
$$\beta_{1j} = \gamma_{10} + u_{1j}$$

The level-1 equation predicts the direct effects (i.e. betas) of level-1 predictors on level-1 outcomes, where Y_{ij} is the dependent variable for an individual observation at level 1 (subscript i refers to a firm, subscript j refers to the country that the firm belongs to). X_{ij} is the firm-level (level-1) predictor. β_{0j} is the intercept of the dependent variable in country j (level-2). β_{1j} is the slope for the relationship in country j between the firm -level predictor and the dependent variable. e_{ij} is the firm -level residual. The level-2 equations predict the effects (i.e., gammas) of level-2 predictors on level-1 betas as well as on the level-1 intercept, where γ_{00} is the overall intercept, which is the mean of the intercepts across countries. W_j is the country-level predictor. γ_{01} is the slope or main effect of country-level predictor. γ_{10} is the slope or main effect of individual-level predictor. u_{0j} and u_{1j} are country-level residuals. Variance inflation factors (VIFs) of all variables in the model are between 1.04 and 2.9, indicating our analysis is unlikely to be influenced by multicollinearity between variables. The multilevel equation specified in this study is:

$$\begin{aligned} Y_{ij} = \gamma_{00+}\gamma_{01}InstitutionEffectiveness_j \; + \gamma_{02}GDPperCap_j + \gamma_{03}Population_j \\ + \gamma_{10}TopManagemnetEffort_{ij} + \gamma_{20}Size_{ij} + \gamma_{30}Age_{ij} + \gamma_{40}Ownership_{ij} \\ + \gamma_{50}ManagerExperience_{ij} + \gamma_{60}Sector_{ij} + \gamma_{70}Year_{ij} + u_{0j} + e_{ij} \end{aligned}$$

2.3. Results

Table 1 reports the descriptive statistics and correlations of all variables for the analysis.

Table 2 shows the regressions results, in which Model 1 is the baseline model including only control variables; Model 2 is the main effect model containing the key explanatory variables; Model 3 is the full model with interaction terms added to the model. The likelihood ratio tests show that adding institutional effectiveness, top management effort and informal payment as independent variables together in Model 2 and interaction terms in Model 3 both result in a statistically significant improvement in model fit (LR $chi^2(3)$ =237.5, $p<0.001$ and LR $chi^2(2)$= 28.21, $p<0.001$ respectively).

Table 2.1. Descriptive Statistics and Correlation of Variables

	1	2	3	4	5	6	7	8	9	10	11	12
Mean	23553.69	2.11	6.24	-0.14	1.48	15.54	0.10	13.49	1.57	3725.52	55.40	2009.70
Std. Dev.	2600197	6.55	0.69	14.38	0.68	13.32	0.30	9.48	0.59	3185.55	56.70	3.22
Min	0	0	4.79	-25.55	1	1	0	0	1	559.39	1.25	2006
Max	345000000	100	7.85	95.23	3	167	1	50	3	15306.39	176.00	2015
1 Sales (million)	1											
2 Institutional Effectiveness	0.13	1										
3 Top Management Efforts (%)	0.07	0.02^{d}	1									
4 Informal Payments (%)	0.01^{a}	-0.02^{d}	0.12	1								
5 Size	0.39	0.02^{d}	0.07	-0.04	1							
6 Age	0.17	0.02^{c}	0.04	-0.03	0.33	1						
7 Ownership (foreign =1)	0.21	0.03	0.02^{d}	-0.02^{c}	0.19	0.04	1					
8 Management Experience	0.11	-0.01^{a}	0.04	-0.04	0.20	0.53	0.05	1				
9 Sector	-0.04	-0.07	-0.003^{a}	0.004^{a}	-0.15	-0.13	-0.001^{a}	-0.08	1			
10 GDP per cap_PPP (USD)	-0.20	0.47	0.001^{a}	-0.03	-0.001^{a}	-0.01^{b}	-0.03	-0.04	-0.07	1		
11 Population (million)	-0.15	-0.06	0.01^{b}	0.04	0.01^{a}	0.02^{d}	-0.17	-0.06	-0.12	-0.004^{a}	1	
12 Year	-0.12	-0.05	0.09	-0.04	0.07	0.16	-0.04	0.14	0.002^{a}	-0.01^{b}	0.18	1

Notes: ^{a} indicates $p> 0.1$, ^{b} indicates $p<0.1$, ^{c} indicates $p<0.05$, ^{d} indicates $p<0.01$, all the rest $p<0.001$; n= 17,757.

Table 2.2. Estimation Results Using Multi-level Linear Regression Models

	Model 1	**Model 2**	**Model 3**
Institutional Effectiveness		0.808***	0.805***
		(0.054)	(0.054)
Top Management Effort		0.043***	0.039***
		(0.005)	(0.005)
Informal Payment		0.001	0.002
		(0.005)	(0.005)
Top Management Effort X Institutional Effectiveness			-0.024***
			(0.006)
Informal Payment X Institutional Effectiveness			0.021***
			(0.006)
Size (medium)	0.499***	0.498***	0.497***
	(0.013)	(0.012)	(0.012)
Size (small)	1.190***	1.180***	1.181***
	(0.019)	(0.019)	(0.019)
Age	0.082***	0.081***	0.081***
	(0.007)	(0.007)	(0.007)
Ownership	0.261***	0.263***	0.262***
	(0.018)	(0.018)	(0.018)
Management Experience	0.004	0.005	0.006

	(0.006)	(0.006)	(0.006)
Sector (service)	0.025*	0.019+	0.020+
	(0.011)	(0.011)	(0.011)
Sector (other)	-0.026	-0.016	-0.015
	(0.027)	(0.027)	(0.027)
GDP per cap PPP (USD)	-2.418***	-1.743***	-1.755***
	(0.132)	(0.128)	(0.128)
Population (million)	5.472***	0.898**	0.807*
	(0.544)	(0.332)	(0.328)
Year 2007	0.321***	0.159***	0.158***
	(0.031)	(0.034)	(0.034)
Year 2009	0.436***	0.091	0.100
	(0.081)	(0.084)	(0.083)
Year 2010	0.189**	0.201***	0.196***
	(0.065)	(0.054)	(0.053)
Year 2011	0.382***	-0.419***	-0.384**
	(0.106)	(0.120)	(0.120)
Year 2013	-0.445***	-0.054	-0.030
	(0.107)	(0.076)	(0.076)
Year 2014	-0.189+	0.068	0.084
	(0.107)	(0.078)	(0.077)
Year 2015	1.047***	-0.149	-0.105
	(0.169)	(0.184)	(0.184)
Constant	3.281**	0.442	0.365
	(1.193)	(0.459)	(0.451)
Random-effects Parameters			
Country-level variance	42.63	4.614	4.43
	(12.739)	(2.158)	(1.963)
Firm-level residual	0.474	0.47	0.469
	(0.005)	(0.005)	(0.005)
Likelihood-ratio test			
Degree of freedom	16	19	21
LR chi^2		237.5***	28.21***
Observations	17,757	17,757	17,757
Number of countries	35	35	35

Notes: Standard errors in parentheses; continuous variables all standardised; *** p<0.001, ** p<0.01, * p<0.05, + p<0.1.

Results in Table 2 show that our expectation that top management effort as well as informal payments can be used as substitutes for effective institutions only holds true for the former. Indeed, less top management effort is required to navigate regulations in high-quality institutional environments, typically characterised by clear, predictable, and properly enforced rules and regulations (World Bank, 1998). TMT efforts dealing with authorities and regulations also has a significant direct impact on firm performance. What is perhaps surprising, however, is that informal payments are not a substitute for low-quality institutional environments. The positive effect of high-quality institutions on firm performance is enhanced by a firm making informal payments. Informal payments do not have a direct effect themselves on firm performance, as expected. We graphically illustrate the interaction effects of top management effort and informal payments each matched against the overall institutional effectiveness of countries in Figures 2 and 3 respectively.

Figure 2.2. Interaction Effects Between Top Management Effort and Institutional Effectiveness

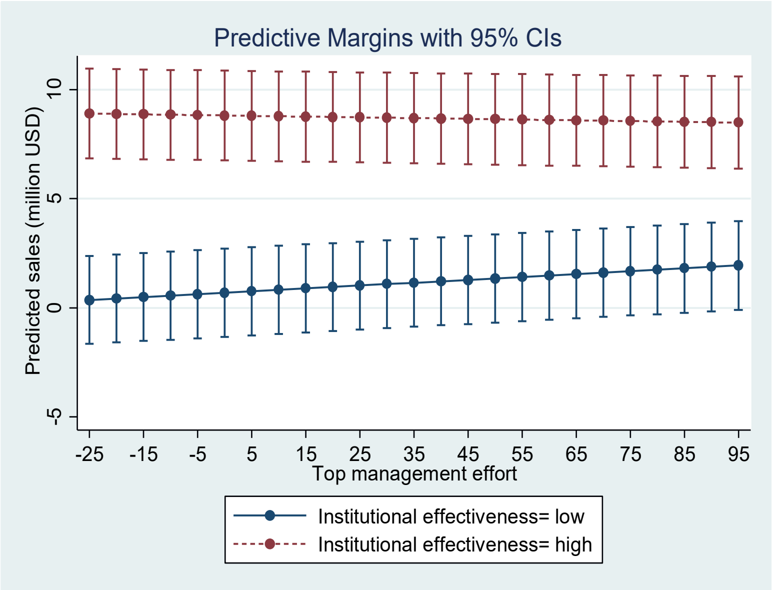
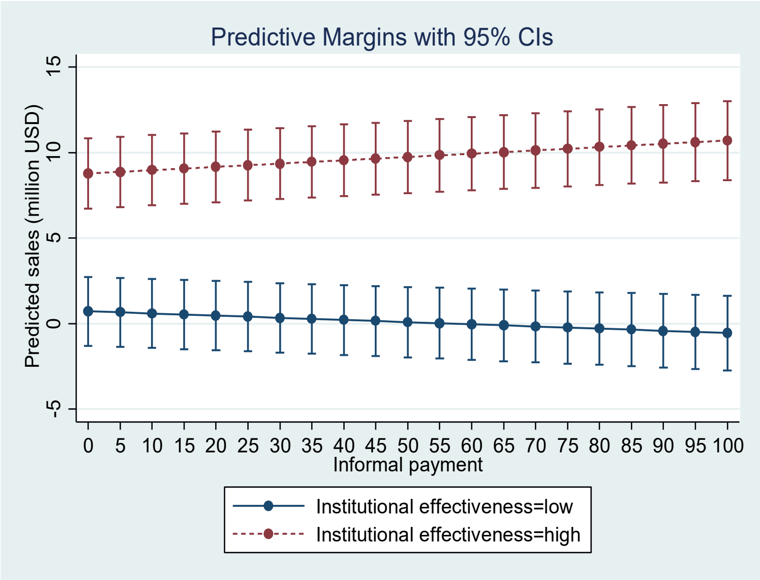


Figure 2.3. Interaction Effects Between Informal Payments and Institutional Effectiveness.



2.4. Discussion: Bribes and Institutional Quality

The finding that informal payments enhance institutional quality's positive impact on firm performance is an unexpected one. We can offer a number of possible explanations:

First, it might be that for a study that focuses on other regions, perhaps economically more developed, might return different results. Sub-Saharan Africa countries that have relatively high institutional quality might still not have high enough quality of institutions – that are free from political interference, treat all equally and, equally efficiently. Also, the practice of gift giving might be more culturally expected and accepted in sub-Saharan Africa. One should be aware, however, that anthropological studies have found the practice of gift giving rife across a range of countries. In developed countries there might be more regulation restricting the practice, and certainly the size of gifts, but gift giving happens nonetheless (Dolfsma et al. 2009; Offer 1997; Smart 1983).

We therefore believe that a second explanation for our remarkable finding is more plausible. Mauss (1954) has argued that there are three essential aspects of gift giving: giving, receiving and reciprocating. Reciprocation should not occur immediately, and what is reciprocated should not be predetermined in value. Gift giving thus creates and sustains relationships between concrete individuals. In a society that is characterized by low institutional quality, much uncertainty exists and the circumstances for relations to be stable may be absent. When giving a gift, the giver may not be sure that the givee is there to return a favour at some later stage. A givee will perhaps also be more inclined to treat an informal payment as a ransom payment rather than a gift to be reciprocated.

2.5. Conclusion

Institutional economists will not be surprised that high quality institutions in a society will make firms perform better. We find, as expected, that the efforts that a firm's top management spends on dealing with regulation are a substitute for high quality institutions. What is surprising to scholars who implicitly would claim that formal institutions are of paramount importance for the economy, is that informal payments actually enhance the positive contribution of high-quality institutions to firm performance. We submit that this is further support for the view that economists and policy makers need to adopt a more comprehensive understanding of how (and which) formal as well as informal institutions impact the economy in general, and firm performance in particular.

REFERENCES

Ayyagari, M., Demirgüç-Kunt, A., & Maksimovic, V. (2011). Firm innovation in emerging markets: the role of finance, governance, and competition. *Journal of Financial and*

Quantitative Analysis, 46(06), 1545–1580.

Bailey (2013), 'Entrepreneurs' Responses to Semi-Formal Illegitimate Institutional Arrangements', *Journal of Business Venturing*, 28(6): 743–758.

Burki, S. J. and Perry, G. E. (1998) *Beyond the Washington Consensus: institutions matter*. World Bank Latin American and Caribbean Studies, Viewpoints. ISBN: 0-8213-4282-7

Darr, A. (2003) Gifting Practices and Inter-Organisational Relations: Constructing Obligations Networks in Electronics Sector. *Sociological Forum* 18(1), p31-51.

Dolfsma, W. (2013) *Government Failure*. Cheltenham: Edward Elgar.

Dolfsma, W., R. Van der Eijk & A. Jolink (2008). On a Source of Social Capital: Gift Exchange.

Journal of Business Ethics 89: 315-329.

Hofmann, D. A., Griffin, M. A., and Gavin, M. B. (2000), 'The application of hierarchical linear

modeling to organizational research'. In K. J. Klein, & S. W. J. Kozlowski (Eds.), *Multilevel theory, research, and methods in organizations.* pp. 467-511. San Francisco, CA: Jossey-Bass.

Khanna, T. and K. Palepu (2000), 'The Future of Business Groups in Emerging Markets: Long-Run Evidence from Chile', *Academy of Management Journal*, 43(3): 268– 285.

Johanson, J., & Vahlne, J.-E. (1990). The mechanism of internationalisation. *International Marketing Review*, 7(4), 11–24.

Lee, K. and B.-Y. Kim (2009), 'Both Institutions and Policies Matter but Differently for Different Income Groups of Countries: Determinants of Long-Run Economic Growth Revisited', *World Development*, 37(3), 533–549.

Mair, J., Marti, I., and Ventresc M. J. (2012), 'Building Inclusive Markets in Rural Bangladesh:

How Intermediaries Work Institutional Voids', *Academy of Management Journal*, 55(4): 819–850.

Mauss, M. (1954 [2000]). *The Gift: Forms and Functions of Exchange in Archaic Societies*.

New York: Norton.

McGahan, A. M., & Victer, R. (2009). How much does home country matter to corporate profitability? *Journal of International Business Studies*, 41(1), 142–165.

North, D. C. (1990), *Institutions, Institutional Change, and Economic Performance*, Cambridge, UK: Cambridge University Press.

Offer, A. (1997). 'Between the Gift and the Market: The Economy of Regard', *Economic History Review* 50(3), 450–476.

Olthaar, M., Dolfsma, W., Lutz, C. and Noseleit, F. (2017), 'Markets and institutional swamps: tensions confronting entrepreneurs in developing *countries' Journal of Institutional Economics*, 13(2), 243-269.

Rodriguez-Pose, A. (2013). Do institutions matter for regional development? *Regional Studies*, 47, 1034–1047.

Rose-Ackerman, S.: 1998, 'Bribes and Gifts', in A. Ben-ner and L. Putterman (eds.), *Economics, Values and Organization* (Cambridge UP, Cambridge).

Schumpeter, J. (1947). The creative response in economic history. *Journal of Economic History*, 7(2), 149–159.

Smart, A. (1993). 'Gifts, Bribes, and Guanxi: A Reconsideration of Bourdieu's Social Capital', *Cultural Anthropology* 8(3), 388–408.

Trebing, Harry M. (1987) "Regulation of Industry: An Institutionalist Approach" *Journal of Economic Issues* 21(4).

UNIDO and UNCTAD (2011) "Economic Development in Africa Report: Fostering industrial development in Africa in the new global environment". Special Issue UNCTAD/ALDC/Africa/2011.

Veblen, Thorstein B. "The Limitations of Marginal Utility." In: *The Place of Science in Modern Civilization*, Thorstein Veblen , pp. 231-51. New York: Russell and Russell, 1961.

World Bank's Enterprise Survey: How to implement the survey (2007), World Bank Group [available at www.enterprisesurveys.org.]

2

Chapter 3

NAVIGATING INSTITUTIONAL DIFFERENCE IN AFRICA:

MOVING BEYOND THE INSTITUTIONAL VOIDS PERSPECTIVES

PUBLISHED IN **AIB INSIGHTS: SPECIAL ISSUE ON AFRICA**

Gori Olusina Daniel, Theresa Onaji-Benson and Charles Mbalyohere (2018)

Navigating Institutional Differences in Africa: Moving Beyond the Institutional Voids Perspective. AIB Insights, 18(4): 15-19.

ABSTRACT

MNEs operating across Africa need to develop distinct capabilities that enable them to navigate and respond to weak or non-existent formal institutions – often described as 'institutional voids'. Institutions play a critical role in the functioning of markets and society as a whole. There are however, observed differences in the characteristics, operations and maturity of institutions across emerging and developing economies. We draw on case study evidence from advanced economy and emerging economy MNEs operating in Africa to argue that the wide-scale reality of institutions that significantly differ from what some MNEs are familiar with, should not necessarily imply institutional voids.

KEYWORDS

Firm performance, informal payments, institutional quality, institutions, sub-Saharan Africa

03. NAVIGATING INSTITUTIONAL DIFFERENCE IN AFRICA:

MOVING BEYOND THE INSTITUTIONAL VOIDS PERSPECTIVES

3

3.1. Introduction

According to analysis from the McKinsey Global Institute, Africa has more than 400 companies with annual revenues exceeding US$1 billion. Many more are required to power the growth that will unlock the estimated US$5.6 trillion in Africa's business opportunities by 2025 (Bughin, Manyika & Woetzel, 2016). Despite the success of these noted exemplars, MNEs operating across Africa often need to develop distinct capabilities that enable them to navigate and respond to weak or non-existent formal institutions – what Khanna and Palepu (2005) describe as 'institutional voids'. This description ignores the reality that institutions across Africa have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that may be uniquely different from other regions, and worthy of closer examination. Especially as most studies examine the institutional environment in Africa and its implications for firm performance and strategy from a predominantly western perspective (Mair, Marti, & Ventresca, 2012; Khanna & Palepu, 2005).

We contribute to this debate by examining the institutional landscape in Africa from the perspective of MNEs operating across the continent. We draw on case study evidence from advanced economy and emerging economy MNEs operating across Africa to argue that the wide-scale reality of institutions that significantly differ from what some MNEs are familiar with, should not necessarily imply institutional voids. This was a critical point of debate at the 2018 AIB Africa Panel on "How MNEs navigate different institutional environments across Africa." We begin with a brief discussion on the relevance of institutions and the conceptual basis of our critique of the institutional void thesis. We then examine evidence from six in-depth case-studies that outline how six MNEs developed strategies to participate in the liberalisation of Uganda's electricity sector. We then build on these insights with further evidence from across the continent on the influence of transactional political strategies on the performance of South African MNEs operating in Africa; following which, we present our conclusions.

Institutions matter

Institutions matter and play a critical role in the functioning of markets and society as a whole, in developed economies, as well as in emerging and developing economies. There are however, observed differences in the characteristics, operations and maturity of institutions across economy-types.

Institutions, as distinct from the organizations that develop and enforce them, have been defined as "humanly devised constraints" or "rules of the game" (North, 1990) that shape the social and economic interactions between members of society. These so-called rule-based institutional environments have been shown to be conducive for firm performance, providing a predictable regulatory environment that reduces transaction costs and enables MNEs to plan ahead and focus on value-adding activities. By contrast, in emerging economies (Khanna & Palepu, 2005; Peng et al, 2008; Meyer et al., 2009), formal institutions are often weak or absent. Where they exist, they are poorly enforced, or not at all.

While the institutional voids thesis provides a useful framework from which to explore, anticipate and respond to the peculiarities of the institutional context firms operate in across emerging markets, some have questioned the accuracy of the term "institutional voids" and what it implies in describing the institutional make up of emerging markets. Olthaar, Dolfsma, Lutz, & Noseleit, (2017) for instance, challenge the idea of an institutional "*vacuum*" implied by the term "*voids*", and have suggested that even where formal institutions that regulate the proper functioning of markets and economic activity are absent, or do not function as expected, institutions still affect firms. And these can either be informal norms and practices or formal institutions from a different or adjacent practice or domain. Khanna and Palepu's (2005) arguments on institutional voids in emerging economies leans heavily on the new institutional economics view which pays little attention to the normative and cognitive expressions of institutions. They assert that emerging markets are different from western markets and are characterized by increasing transaction costs and an absence of (western-style formal) institutions. This position ignores the role of informal institutions, which provide the essential legitimacy for formal rules and assumes that institutions can be transferred across differing contexts. In African emerging economies, the influence of informal institutions cannot be ignored (Bagire & Namada, 2015; George, Corbishley, Khayesi, Haas, & Tihanyi, 2016; Zoogah, Peng, & Woldu 2015). Though their enforcements are not regulated in the strict western- style, they form a significant part of the rules of the game that guide operations within these contexts.

In reality, informal and formal institutions co-exist to establish the institutional mix of host countries, particularly in emerging markets. And depending on the context, can have a variety of configurations or interrelations, including, complementing and increasing their joint effectiveness, substituting informal institutions for non-functioning formal institutions, or informal institutions competing against ineffective formal institutions (Helmke & Levitsky, 2004). This is particularly true across Africa where distinctive economic, institutional and cultural systems and norms have emerged from a unique history and culture to evolve a business environment that is distinctively different from other regions in many ways. A phenomenon that is best examined with evidence from the experience of MNEs that operate across Africa, as detailed in the following sections.

3.2. Divergent MNE Experiences with Institutional Environments In Africa

In gathering evidence about heterogeneous responses to institutions in Africa, we draw on six MNEs that entered Uganda's electricity generation industry shortly before or after the implementation of pro-market reforms in the electricity sector in 2002. The qualitative, multi-case study sample consists of three emerging economy MNEs (EMNEs) and three advanced economy MNEs (AMNEs), thus offering insights into diverse MNE responses. The findings (established through exposing the qualitative data to a grounded analysis), suggest that some MNEs are most competitive at the early stages of pro-market reforms, when formal institutions are least developed and effective and informal institutions are most prevalent. EMNEs generally adapt best at this stage, indicating an above-average possession of capabilities that are suitable for responding to informal institutions. Conversely, AMNEs adapt more effectively at later stages, reflecting capabilities to effectively respond to more formal institutions. When they enter strategic partnerships, however, EMNEs and AMNEs appear to create synergies and complementarity in the capabilities to respond to both informal and formal institutions. They hence get positioned to adapt well at both early and late stages of reform, irrespective of the evolving institutional constellation. We conclude from these findings that the lack of effective formal institutions, something that characterizes the early stages of pro-market reforms in sub-

Saharan African and other emerging and emerging markets, does not necessarily translate into a universal competitive disadvantage. Since the MNEs that derive advantage here do so using explicit institutional responses, we further infer that the response is not to 'voids', but to a set of institutions that are not formal. The EMNEs in our study demonstrate extensive capabilities in responding to these informal institutions and understanding their dynamics. The capabilities are gathered in the host market and in other African markets that serve as incubators to nurture experience. In the end, some of the cases in the study acquired even more refined capabilities that positioned them well for entry into more challenging markets in the wider region. One of the cases, for example, leveraged its experiences in Uganda to win a new licence to develop a dam project at the border between Rwanda and the Democratic Republic of the Congo.

EMNEs are often better able to understand the rules governing informal institutions, and therefore develop the corresponding capabilities to respond competitively. Consequently, AMNEs that enter strategic partnerships with experienced EMNEs position themselves to fill the gaps they have in responding to these institutions (Mbalyohere et al., 2017). In such partnerships, there is a complementarity between the two partners. One partner adapts to local informal institutions while the other partner adapts to global formal institutions. In our cases, the informal institutions constituted the norms surrounding African traditional religious beliefs, expectations about gifts and favours, and relationships with diverse stakeholders at the grassroots of community. Global formal institutions, on the other hand, were typified by the regulatory demands of the World Bank, environmental protection agencies and similar bodies. The synergies that develop from such strategic partnerships are ultimately important, not only at the early stages in helping AMNEs adapt to informal institutions, but also at later stages of reform in assisting EMNEs in the partnership to respond better to emerging formal institutions.

More broadly, we propose that what the MNEs in our study respond to, are not institutional voids, but rather a constellation of institutions with generally different rules than those AMNEs from highly formally institutionalized contexts are familiar with. In light of the growing attractiveness of new frontier markets, like those in sub-Saharan Africa, for foreign direct investment, we suggest that these markets are increasingly emerging a more localized approach to institutions. Instead of seeking to further spend their meager resources to develop more sophisticated formal institutions after foreign templates, such countries have the strategic option to let institutions develop more organically, with a higher appreciation of informal institutions. This will, in turn, strengthen the strategic complementarity between informal and formal institutions. More importantly, it will provide a stronger context for the emergence and the nurturing of an African version of the free market economy. Since African economies are characterized by high rates of informality, informal institutions would be expected to have a significant influence under such circumstances.

Making the strategic institutional re-orientation in Africa even more intense is the growing entry of EMNEs from Asia, especially from China and India. Since these markets also have a strong history of informal institutions, experiences with these institutions in Africa are getting more complicated. We expect that hybrid experiences will emerge and influence what ultimately works or does not work in Africa. We also envisage that African countries will increasingly become more assertive in creating conditions in which local informal institutions get prioritized and are enabled to develop further.

The informal institutions at the bottom of the pyramid are particularly important, given that this accounts for the majority of Africa's population and it is here that efforts to help people escape poverty have most impact. Consequently, MNEs involved in major projects located in the communities at bottom of the pyramid can respond to informal institutions in ways that either strategically support or undermine anti-poverty programs.

3.3. Employing Non-Market Strategies in sub-Saharan Africa

The reality of weak or different institutional environments requires that MNEs operating in Africa, critically consider what strategies are being transferred from institutionally different contexts. In this section, we discuss the contradicting influence of transactional political strategies on subsidiary performance to what is obtainable in developed economies as indicated in previous research (Hadani & Schuler, 2013; Hillman, 2003).

Drawing on evidence from quantitative research surveys of senior executives of South African MNE operations across sub-Saharan Africa, we find that unlike in developed economies such as the United States, where transactional political strategies like lobbying and political action committee contributions are effectively part of the formally institutionalized system that requires that all firms declare their political expenditure policies, Africa has a different institutional environment. Our evidence suggests that transactional political strategies, employed as and when needed in Africa, do not necessarily provide competitive advantages for the firms (Hillman, Keim, & Schuler, 2004) in the long run. While they provide an entry point for the firm, to sustain performance, MNE subsidiaries need to develop relationships through constituency building, with stakeholders in the host environment. This may signal to MNEs to move away from such transactional political strategies to other relational-based ways of gaining influence, especially given the collectivist nature of sub-Sahara African societies. And is similar to the need to employ non-engaged approaches, like low visibility and rapid compliance to informal institutions in these environments.

Even though, the use of transactional political strategies signifies a firm's buffering mechanism to proactively influence their environment, the evidence suggests that this does not apply in all contexts. Hillman and Hitt (1999) argued that within weak institutional environments, such transactional political strategies are more effective, the evidence suggests differently. Premised on our findings and corroborated by the positions of a number of scholars (Rajwani and Liedong, 2015; Mbalyohere, 2015; White et al., 2014), it can be argued that a transactional approach to political strategies is not a precursor to increased subsidiary performance, but rather MNEs need to exploit other political strategies. For example, a relational strategy that thrives on a continuous maintenance of relationships, and constituency building may yield more positive results for MNEs. In Africa, where communal informal institutions abound, this remains important.

Though similar to the relational motive of engaging in corporate social responsibility (CSR), relational political strategies are different, in the sense that unlike firms' use of CSR which seeks to influence the social environment and improve their triple bottom line, the application of relational political strategies seeks to, in a myriad of ways, influence the political environment by building its legitimacy within that environment. Such socio-political legitimacy is necessary to be able to adequately harness the MNEs political strategy as it relates to embeddedness in the environment.

3.4. Conclusions

This article re-examines the institutional voids perspective from the lens of MNEs operating across Africa. Drawing on evidence from the experience of six AMNE and EMNEs operating in Africa, we propose that the conceptualization of institutional voids proposes a judgement on contexts that are institutionally different from Western developed economies, which may limit our inclinations to actively interrogate these contexts to understand and co-evolve with them.

In reality MNEs operating in Africa respond to a mix of informal and formal institutions that have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that is distinctively different from other regions. Given this difference, MNEs need to critically consider what strategies can be transferred from institutionally different contexts; and what new capabilities are required to successfully operate across Africa.

The institutional environment in many African countries is still evolving, yet informal institutions continue to play a significant part in the rules of the game. We propose that strategic partnerships that incorporate non-market relational strategies that thrive on a continuous maintenance of relationships, and constituency building may yield more positive results for MNEs operating in Africa.

REFERENCES

Bagire, V., & Namada, J. 2015. Management theory, research and practice for sustainable development in Africa: A commentary from a practitioner's perspective. Africa Journal of Management, 1(1): 99–108.

Bughin, J., Manyika, J., & Woetzel, J. 2016. Lions on the move II: Realising the potential of Africa's economies. McKinsey Global Institute.

De Villa, M. A., Rajwani, T., Lawton, T. C., & Mellahi, K., 2018. To engage or not to engage with host governments: Corporate political activity and host-country political risk. Global Strategy Journal. http://doi.org/10.1002/gsj.1205

George, G., Corbishley, C., Khayesi, J. N. O., Haas, M. R., & Tihanyi, L. 2016. Bringing Africa in: Promising directions for management research. Academy of Management Journal, 59(2): 377–393.

Hadani, M., & Schuler, D. 2013. In search of El Dorado: The elusive financial returns on corporate political investments. Strategic Management Journal, 34: 165–181.

Helmke, G., & Levitsky, S. 2004. Informal institutions and comparative politics: A research agenda. Perspectives on Politics, 2(4): 725–740.

Hillman, A., & Hitt, M. 1999. Corporate political strategy formulation: A model of approach, participation, and strategy decisions. Academy of Management Review, 24(4): 825–842.

Hillman, A., Keim, G., & Schuler, D. 2004. Corporate political activity: A review and research agenda. Journal of Management, 30(6): 837–857.

Hotho, J. J., & Pedersen, T. 2012. Beyond the rules of the game: Three institutional approaches and how they matter for international business. In M. Demirbag & G. Wood (Eds), Handbook of institutional approaches to international business. Cheltenham: Elgar.

Khanna, T., & Palepu K. 2005. Spotting institutional voids in emerging markets. Harvard Business School background note 9: 106-014.

Mair, J., Marti, I., & Ventresca, M. 2012. Building inclusive markets in rural Bangladesh: How intermediaries work institutional voids. Academy of Management Journal, 55(4): 819–850.

Mbalyohere, C., Lawton, T., Boojihawon, R., & Viney, H. 2017. Corporate political activity and location-based advantage: MNE responses to institutional transformation in Uganda's electricity industry. Journal of World Business, 52(6): 743–759.

Mbalyohere, C. G. 2015. Corporate political activity in sub-Saharan Africa: The influence of MNE enterprises in the institutionalisation of Uganda's electricity industry. PhD Thesis. Milton Keynes: The Open University Business School.

Meyer, K. E., Estrin, S., Bhaumik, S. K., & Peng, M. W. 2009. Institutions, resources, and entry strategies in emerging economies. Strategic Management Journal, 30(1): 61–80.

North, D.C. 1990. Institutions, institutional change and economic performance. Cambridge: Cambridge University Press.

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. 2017. Markets and institutional swamps: Tensions confronting entrepreneurs in developing countries. Journal of Institutional Economics, 13(2): 243–269.

Peng, M. W., Wang, D. Y., & Jiang, Y. 2008. An institution-based view of international business strategy: A focus on emerging economies. Journal of International Business Studies, 39(5): 920–936.

Rajwani, T., & Liedong, T. A. 2015. Political activity and firm performance within nonmarket research: A review and international comparative assessment. Journal of World Business, 50(2): 273–283.

White, G. O., Hemphill, T. A., Joplin, J. R. W., & Marsh, L. A. 2014. Wholly owned foreign subsidiary relation-based strategies in volatile environments. International Business Review, 23(1): 303–312.

Zoogah, D. B., & Peng, M. W. 2015. Effectiveness in Africa. Academy of Management Perspectives, 29(1): 7–31.

Chapter 4

DISENTANGLING INSTITUTIONAL VOIDS:

HOW INFORMAL INSTITUTIONS INTERACT WITH FORMAL INSTITUTIONS TO IMPACT FIRM PERFORMANCE IN EMERGING MARKETS

REVISE AND RESUBMIT AT **INTERNATIONAL BUSINESS REVIEW**

Gori Olusina Daniel, Kun Fu, Wilfred Dolfsma, Rick Aalbers,
and Valentina Materia

ABSTRACT

MNEs operating across emerging and developing economies (EMDEs) need to develop distinct capabilities that enable them to navigate and respond to both formal and informal institutions, which co-exist to constitute the institutional landscape in host countries. Combining country-level data on institutional quality with enterprise survey data on 96,320 firms from 128 countries over 11 years, we investigate how formal and informal institutions interact to shape the institutional landscape foreign and domestic firms encounter in host countries, and how this impacts firm performance. We challenge empirically the notion of institutional voids, and find that informal institutions can serve to complement or substitute for high as well as low-quality formal institutions. We propose and operationalise measures for three proxies for informal institutions and find that they generally enhance the positive effect of high-quality formal institutions, but with some intriguing regional variations. And that foreign firms benefit less from the institutional complementarity between informal and formal institutions.

KEYWORDS

Institutional voids, informal institutions, institutional environments, business-government relations, emerging markets

04. DISENTANGLING INSTITUTIONAL VOIDS:
HOW INFORMAL INSTITUTIONS INTERACT WITH FORMAL INSTITUTIONS TO IMPACT FIRM PERFORMANCE IN EMERGING MARKETS

4.1. Introduction

The International Business (IB) literature has increasingly emphasized the importance of considering the institutional environment as a critical lens with which to understand firm strategy and performance in host-country environments (Mbalyohere & Lawton, 2022; Donnelly & Manolova, 2020; Halaszovic & Lundan, 2016; Dunning & Lundan, 2008; Peng, M. W., 2002; Peng, et al., 2008).

Institutions define and regulate how economic actors derive the social and legal legitimacy with which to pursue their activities and business interests (North, 1990, 1991); and are distinct from the organisations that develop and enforce them (Peng, 2002).

IB Scholars have recognised that informal and formal institutions co-exist to form the institutional configuration of host-country environments (Barbalet, 2022; Doh et al., 2017; Holmes, et al., 2013; North, 1990; Rodrik, 2016; Rodrıguez-Pose, 2013; Scott, 1995); and collectively establish the incentive structure of a society. However, comparably more attention has been paid to formal institutions (Doh et al., 2017; Dau et al., 2022).

Informal institutions also play an important role and have been defined as the unwritten but socially accepted rules, values, norms and traditions that shape how people within a society inter-relate between themselves and organisations (Sartor & Beamish, 2014; Sauerwald & Peng, 2013; Pejovich, 1999; North, 1990). Often associated with culture (Scott, 1995; Hofstede, 1980), we adopt a definition more consistent with an institutional perspective that sees informal institutions as distinct from informal behaviour and weak institutions (Helmke & Levitsky, 2004).

There is growing interest in better understanding informal institutions, and in particular how they inter-relate with formal institutions; and combine to impact firm strategy and performance (Dau et al., 2022). Yet the relationship between formal and informal institutions and how they impact firm performance remains under-analyzed due to difficulties in establishing measures for informal institutions (Helmke & Levitsky, 2004; Xu & Yao, 2015; Qiu et al 2021), and its conflation with culture, which in IB while linked, as informal institutions are considered embedded in culture and ideology (Peng, 2002, Scott, 1995) is not considered one and the same (Helmke & Levitsky, 2004).

This paper seeks to address this research gap by applying the framework provided by Helmke and Levitsky's (2004) seminal work to identify three widely observed and established norms as captured in the World Bank Enterprise Survey (WBES) data, which we operationalise as proxies for informal institutions (i.e. senior management time spent on formal institutions (TMT), informal payments and local sourcing). We then empirically test how these informal institutions, interplay with formal institutions as captured by the Economic Freedom Index – a comprehensive measure of the institutional quality of the host country's formal institutions, to constitute the institutional configuration of host-country environments, and how these combine to impact the performance of multinational enterprises.

Our theoretical framework integrates IB research on institutional theory with insights from institutional economics (North, 1990; Trebing, 1987) in an attempt to examine how informal and formal institutions interrelate, and how this impacts firm performance.

The remainder of this paper is organised as follows: Section 2 sets out the theoretical framework for how informal and formal institutions interact and outlines six hypothesis which we test empirically in Section 3, which sets out the data and the statistical model used. Section 4 sets out the results, which are discussed in Section 5, with our conclusions in Section 6.

4.2. Theory And Hypotheses

Institutional economics and institutional theory

Institutional economics provides a framework for understanding how formal institutions in particular, shape economic activity and the behaviour of economic actors (North, 1991; Williamson, 2000). Rooted in the transactions cost perspective (Coase, 1937), formal institutions play a critical role in determining the efficiency and effectiveness of economic markets. For example, market supporting institutions such as effective public service delivery organisations (e.g. courts, trade and licensing agencies) and the constitutional provisions and regulations that underpin them, provide a stable and predictable legal framework that can encourage investment and innovation. Anti-trust legislation, intellectual property, product standards and consumer protection laws can promote competition that can lead to lower prices and higher quality goods and services.

Institutional theory on the other hand takes a broader view and provides a framework for understanding how organizations adapt to the institutional configurations of their host countries (Scott, 1995). And in so doing, establishes the bi-directional relationship that has paved the way for research on the co-evolution of institutions and organisations (Dau et al., 2022; Chidlow et al., 2021).

Defined as socially constructed rules that regulate acceptable behaviour, institutions can include formal institutions, such as laws and regulations, and informal institutions, such as norms and values (North, 1991; Scott, 1995). As such, organizations are embedded in a complex web of institutions, including economic, political, social, and cultural institutions. These institutions shape the organization's structure, strategy, and behaviour, which reflect the mechanisms that capture how organizations adapt to their environment in order to survive and thrive.

Institutional theory therefore establishes how institutions play a critical role in shaping social outcomes. For example, institutions that promote local content can enhance the local embeddedness of MNEs, who from a transaction cost perspective may derive greater utility and cost efficiencies from minimising their exposure to the cost and uncertainties associated with sourcing inputs and processes they can deploy more cheaply elsewhere, locally. The incorporation of local firms into the supply chain of MNEs and jobs for local people can also result in economic externalities such as knowledge transfer, inclusive economic growth and improve the acceptability and receptiveness of local consumers and stakeholders.

Understanding the contribution, overlaps and distinctions between institutional economics which empathises how western-style market supporting formal institutions improves the efficiency and effectiveness of economic markets, and institutional theory, which takes a broader view on the complex interplay of formal and informal institutions and how they impact the structure, strategy and behaviour of organisations can be particularly useful for understanding how MNEs navigate different institutional environments in emerging markets (Peng et al., 2008). Particularly so as emerging markets are characterized by a variety of institutional configurations and challenges, including weak legal frameworks, corruption, and unstable political systems (Dau et al., 2022). MNEs that operate in these markets must be able to adapt their strategies to these unique institutional environments. For example, MNEs operating in emerging markets with weak legal systems may need to rely on trust-based informal institutions such as guanxi, to protect their interests (Kafouros, 2022), and those operating in emerging markets with high levels of corruption may need to develop strategies to mitigate the risks of corruption.

Formal and informal institutions

In clear departure from the neoclassical view, it is generally accepted that formal institutions matter (Burki & Perry, 1998) and play a key role in the proper functioning of markets (Dolfsma, 2013) to the benefit of not only society as a whole, but notably, private enterprise (Khanna & Palepu, 2000; Lee & Kim, 2009; Mair & Marti, 2009). These arguments have been extended to suggest EMDEs that establish western-style formal institutions will experience similar results and that without proper formal institutions, an "institutional void" might exist that negatively impacts the performance of multinational firms (Mair et al., 2012). Olthaar et al., (2017) however, challenge the idea of an institutional "vacuum" implied by the term "voids", and have suggested that even where formal institutions that regulate the proper functioning of markets and economic activity are absent or do not function as expected, institutions still affect firms; and these can either be informal institutions or formal institutions from a different or adjacent practice or domain.

In reality, formal and informal institutions co-exist to establish the institutional mix of host countries (Barbalet, 2022; Kafouros 2022), particularly in emerging markets (Kafouros, 2023). And depending on the context, can have a variety of configurations or interrelations (Mbalyohere, 2016), including, complementing and increasing their joint effectiveness, substituting informal institutions for non-functioning formal institutions, or informal institutions competing against ineffective formal institutions (Helmke & Levitsky, 2004).

Institutions have been defined as the "rules of the game" and "humanly devised constraints" (North, 1990), that serve to shape the social and economic interactions between members of society. They promote order and stability by providing authoritative guidelines that enable the formation of acceptable forms of behaviour and associated consequences for non-compliance (Scott,1995; North, 1990). In a sense, they serve as the incentive structure of society in a way that reduces uncertainty and enhances efficiency by reducing the costs associated with exchanges and transactions in an economy (North, 1990).

Both North (1991) and Scott (1995) recognise the existence of formal and informal institutions; and scholars have attempted to distinguish between the two observed types of institutions, primarily by how they are developed and enforced (see Table 4.1).

Table 4.1: Distinctions between formal institutions and informal institutions

Scholars	**Formal institutions**	**Informal institutions**
Boussard (2000); Manor (2001); Tsai (2002)	State-enforced rules	Self-enforced social norms
North (1990); Helmke & Levitsky (2004); Doh et al., (2017)	Written	Normally, unwritten; yet widely accepted
Dia (1996); Pejovich (1999)	Best practice rules, often similar across countries	Informal norms rooted in cultural traditions
Helmke & Levitsky (2004)	Official	Unofficial

We find Helmke & Levitsky's (2004) definition of informal institutions comprehensive, and helpful in framing our study:

> *"Informal institutions are socially shared rules, usually unwritten, that are created, communicated and enforced outside officially sanctioned channels."*

By contrast, formal institutions as rules and procedures created, communicated and enforced by official channels such as courts, legislatures, bureaucracies, constitutions, laws and regulations. This therefore establishes the view that public sector departments, agencies, parastatals and other similarly empowered public bodies play a functional role in the regulation of society and industry.

Guided by these formal, state-enforced rules, public sector organisations also deliver a range of key services to firms that are vital to their legal legitimacy, operational efficiency, sense of safety and security, as well as those critical to the sustainability and continuity of their operations such as licenses, permits, access to electricity, water, efficient transport system and other public services such as health and education, tax administration, legal underpinning of contracts between parties, and certainty of intellectual property rights. The quality of institutions can therefore be reflected in the experience and expectation of firms and other actors as they interact with the officials and organisations charged with implementing and enforcing these rules (Kafourous et al.., 2023; Olusina Daniel et al., 2018; Li & Zhang, 2007).

Institutional quality and firm performance

Good or high-quality institutions provide clear rules, which are widely known, coherent, predictable, applicable to all, and properly and evenly enforced (Burki & Perry, 1998). This is often taken for granted in developed countries and supports the view that as institutions develop, they reduce uncertainty, transaction costs and market imperfections (Kafouros et al. 2023) and that in high-quality institutional environments (Olusina Daniel at al., 2018), firms can focus their efforts on value-creating activities that impact directly on their performance. By contrast, firms operating in low-quality institutional environments tend to adopt what Peng (2003) describe as relationship-based strategies. This approach, typical in emerging markets for instance, require firms, as a matter of necessity, to actively invest time and resources they could otherwise devote to activities that directly impact on their performance, to engage with public officials to access, understand and influence the development and implementation of key regulations and the provision of vital public services the need for the organisations to thrive. Across many sub-Saharan African countries for instance, even the most successful firms have been known to take up responsibility for the provision of vital infrastructure and utilities typically provided by government agencies, such as access roads, electricity and water which are critical to the development and delivery of their products and services (Aderibigbe, 2014).

It therefore follows that generally, firms operating in high-quality environments benefit from advantages arising from not having to account for the costs or uncertainty associated with addressing the absence of one or more of the vital public services or principles they rely on, and which govern predictable and efficient exchange between transacting parties (Cuervo-Cazurra & Dau, 2009). Our baseline hypothesis, is therefore that;

> ***Hypothesis 1:*** *The quality of formal institutions is positively associated with firm performance.*

Institutional voids and institutional mix

EMDEs institutional environments are often reported to be characterised by so called institutional voids, defined as the absence or underdevelopment of (formal) institutions that regulate, facilitate and support the efficient functioning of markets and economic activity (Doh et al.,2017; Khanna & Palepu, 1997).

In reality, host country environments consist and evolve over time from a complex interplay of formal and informal institutions (Doh et al., 2017; Holmes et al.,, 2013; Olthaar et al., 2017; Mbalyohere, 2016). As such, in practice the concept of institutional voids should not be understood to imply that firms operate within an institutional vacuum nor require the complete absence of institutions as we understand the literal definition of voids to mean.

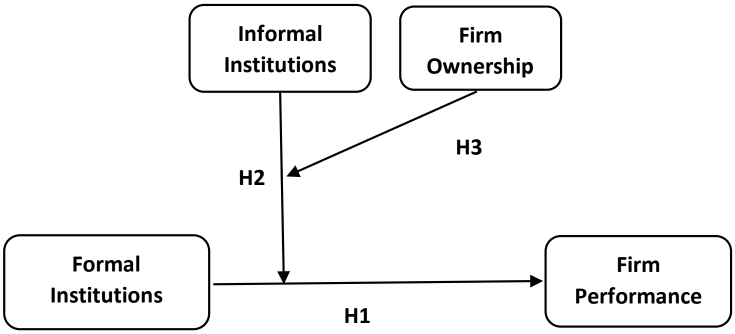
Khanna & Palepu (1997) attempt to address this point and suggest that the institutional voids thesis does not in practice represent a void or vacuum of institutions. Indeed, Doh et al., (2017) posit that the institutional voids perspective facilitates consideration of a wide range of institutions that impact on firm performance. And reflect conditions that steer the interaction of market actors – buyers, sellers, public officials and NGOs towards inefficient outcomes; which manifests in higher costs for procuring material inputs, capital, information, skills and new ideas. Firms respond to these deficiencies in a variety of ways (Boddewyn & Doh, 2011), including – relying more on informal institutions (Mair et al., 2012; Olthaar et al., 2017).

This study seeks to disentangle this phenomenon by identifying three widely expected and practiced firm responses or norms, we adopt as proxies for informal institutions and empirically testing how they interact with informal institutions to impact the performance of firms in emerging markets.

The interplay between formal and informal institutions

We adopt Helmke & Levitsky's (2004) typology of informal institutions in conceptualising how formal and informal institutions interact to either complement, substitute or compete with formal institutions (see Fig 1, which shows our conceptual framework). As suggested by Helmke & Levitsky (2004), we also consider informal institutions as distinct from weak or low-quality institutions, informal behaviour and informal organisations.

Figure 4.1. Conceptual Framework



Formal and informal institutions do not only coexist in the social and economic context, they also interact with each other constantly in varying forms and natures (Barbalet, 2022; Helmke & Levitsky, 2004; Pejovich, 1999). To gain a comprehensive understanding of the institutional impact on firms' performance, we need to look into the relationship between formal rules and informal norms together and investigate how the interactions affect firms' performance in host country environments.

Formal institutions – for example, business-related regulations of a country such as trade and operating licensing requirements, consumer protection laws, tax legislation and labour regulations are specified by host-country government authorities. Top level Managers are expected to familiarise themselves with and ensure their firms comply with the established rules. As a result, we posit that, irrespective of the actual time this takes up, it is an established norm and practice that top level managers spend some proportion of their time liaising with public officials, and familiarising and ensuring their firms comply with relevant regulations.

Some countries have developed munificent business environment by, for example, simplifying firm registration and financial reporting process, offering tax credits for some types of business where certain conditions are met. Firms operating in such countries are likely to benefit from the high-quality institutions if managers spend the time required to understand the rules and run their business accordingly. This however, may not always be the case. For instance, in many emerging and developing countries, western-style formal institutions tend to be poorly developed and enforced. Navigating through formal rules and regulations, where they exist, therefore tend to be relatively tedious – particularly for multinationals, who may be less familiar with local norms or bound by home-country institutional constraints such as anti-bribery regulations which often provide disclosure requirements and limits on corporate gifts.

Crucially, the opportunity cost of time spent by top level managers this way, is time that could have been devoted to more value adding activities and constitutes a cost to the business. In this case, firms may be better off if their top management limited the amount of their time and energy dealing with bureaucracies, and work on other more effective ways to enhance firm's efficiency and performance.

We therefore hypothesise a complementary relationship between the quality formal institutions and TMT effort in driving firms' performance and propose that:

> ***Hypothesis 2a:*** *the positive effect of the quality formal institutions on firms' performance is enhanced by the degree of sector-level senior management effort spent in dealing with regulations.*

Informal payments or gift-giving is another example of an important informal norm prevalent in many economies (Dolfsma, 2009). Where it exists, it is often expected, and paid to cultivate relationships, facilitate service delivery, secure access to key officials and opportunities, or to some extent, influence the development or implementation of government policy (Krammer, 2019). Such practices, while not exclusive to EMDEs are more commonly observed and expected in less developed economies where formal institutions are poorly defined and enforcement is largely discretionary or non-existent (Krammer, 2019; Dolfsma et al, 2009). Informal payments thus satisfy the boundary conditions captured in Helmke and Levitsky (2004) definition of informal institutions and provide firms with alternative channels to compensate for the less efficient formal rules and laws.

The giving and receiving of informal payments is generally regarded as a social vice in many developed economies with high-quality institutions. Where corporate hospitality or gifts are permitted – for instance, as expense items in the tax code – they are restricted by the government in its scope and scale. This as noted by Dolfsma et al., (2009) has nonetheless been able to limit and discourage the practice of informal payments in more advanced economies.

Bribes have been shown to have positive impacts on firms' performance especially for large firms operating in the extractive industries for example (Zhou & Peng, 2012).

In societies with high quality formal institutions, gift-giving can help firms create and sustain relationships with influential individuals such as government officials, which will give the firms relatively easy and timely access to resources and information (Krammer, 2019). It can enhance the positive impact of formal institutions on firms' performance. The opposite is true for countries with poor quality formal institution which often exist with very high levels of uncertainty, making it much more difficult to build a stable and trustworthy relationship with government officials (Olusina et al., 2018).

Bribes can also translate to significant additional costs for firms (Wei, 2000). And firms may be exploited by public officials who control the allocation of resources that are strategically important for the firms, which in turn can harm firms' performance. We therefore hypothesise a complementary relationship between informal payments and formal institutions in driving firms' performance, such that:

> ***Hypothesis 2b:*** *the positive effect of the quality of formal institutions on firms' performance is enhanced by the degree of sector-level informal payments.*

While, as argued, generally, high-quality formal institutions are conducive to business and generally serve to stimulate firm performance by creating a stable and predictable environment, a third informal practice or institution – i.e. local sourcing, can enhance this effect. Halaszovich and Lundan (2016) have drawn attention to the benefits of using local suppliers to establish local embeddedness.

Local sourcing, defined as the process in which foreign firms procure inputs from local suppliers (Jung and Lee, 2018), has been argued to play a crucial role in meeting the needs of local stakeholders by providing access to jobs, contracts and economic activity that promotes capital formulation and knowledge spillovers to local suppliers and in return affording local subsidiaries of MNEs with a degree of social legitimacy in institutionally distant host markets (Oki & Kawai, 2022). The increased local embeddedness associated with local sourcing also provides access to information that leads to product innovation or serves as an early warning signal to enable foreign firms cope and adapt to shifts in institutional policy and pressures; and may be considered as an alternative to greater degrees of local ownership.

Some scholars have emphasised the need for MNEs to proactively implement a high level of input localisation as an isormorphic adaptation strategy to reduce the risks of being viewed by local stakeholders as outsiders (Rickley and Karim, 2018: Forstenlechner and Mellahi, 2011; Luo, 2007). A firm's environment, however stable and predictable in terms of the rules of the game, will still be affected by unforeseen developments. These developments can constitute opportunities that a firm could seize upon and profit from, or the developments can be threats that a firm may want to be prepared to address. If a firm is well embedded locally, thereby endowing it with social legitimacy as a critical and important part of the local economy as well as access to local networks and information flows, it will be better positioned to learn early and respond effectively to unforeseen developments.

Conversely, the benefits of being well prepared for unforeseen developments may be in less demand in a society and economy that is formally well instituted, as the behaviours of third parties are more predictable.

We therefore hypothesise that:

> ***Hypothesis 2c:*** *the positive effect of the quality of formal institutions on firms' performance is enhanced by the degree of sector-level local sourcing.*

Foreignness and firm performance

Previous studies have confirmed the superiority of foreign firms to domestic firms in areas such as innovation, productivity and capabilities that enable them to adapt and outcompete their domestic counterparts (Wernerfelt, 1984).

These firm specific or ownership advantages – so called "O" advantages, are based on the possession of intangible assets, such as patents, trademarks, management skills (Caves, 1996), brand names, skilled labour, knowledge of technology, and efficient production processes (Lavie & Fiegenbaum, 2000); which allow firms to achieve high levels of technical and price efficiency (Caves, 1996). They may also be better able to manage rapid change than their local counterparts (Holburn & Zelner, 2010; Hennart, 2009; Cuervo-Cazurra & Genc, 2008).

Others have theorised that the possession of superior O advantages does not always translate to better performance in less developed countries (Halaszovich & Lundan, 2016). This is consistent with Dunning's eclectic or OLI theory, which supposes that an MNEs ability to outcompete its competitors in the domestic market depends not only on its unique capabilities, but also on its ability to 'internalise' – i.e. adapt and successfully carry out its operations in the host environment ('I'- advantages) given the host countries stock of resources, institutions and regulations (so called 'L'- advantages), which may be different to its home market, and its ability to structure its internal operations to internalise or translate its capabilities across national boundaries within its own organisation in such a way as to be able to successfully exploit the opportunities and market failures of its host market ('I'-advantages). Notwithstanding this, the evidence remains overwhelmingly in support of the superiority of foreign firms in emerging markets, perhaps most notably because studies tend to exclude failed or failing firms who have chosen or have had to exit the field.

Our study explicitly examines how the interplay between informal and formal institutions impacts the comparative performance of multinational enterprises. We therefore test empirically the impact, of the interplay of the three widely practiced norms – top management time (TMT), informal payments and local sourcing, which we identify in this paper as proxies for informal institutions, and the formal institutions for our sample of firms on the comparative performance of foreign firms.

Foreign firms – multinational enterprises have been shown to be more capable at managing operations, change, and attracting the resources and capabilities required to deliver superior results. In particular the senior management team usually have or can leverage head office's knowledge of different institutional environments or can buy in the necessary expertise to understand, navigate and effectively comply with established business regulations. In high quality environments, with clear predictable and evenly enforced rules, we expect any investment of senior management effort spent on regulations to enhance firm performance, as the institutions are by definition effective. In low quality environments, senior managers are better off exploring other ways to enhance firm performance as we do not expect the same complementarity. We therefore propose:

> ***Hypothesis 3a:*** *The moderation effect of sector-level senior management time spent in dealing with regulations on quality of formal institutions is stronger for foreign firms than for domestic ones.*

Foreign firms typically have access to more capital and resources from which to make informal payments. And are generally expected to pay more than their domestic counterparts for the same level of access. In high quality environments, informal payments – where expected, and made – are more likely to have a positive effect on performance as public officials can be relied on to fulfil the obligations set by the giving and receiving of informal payments, even if this is not immediate. By contrast, low quality institutional environments are impacted by issues such as the capacity and reliability of such officials to deliver on such implied or explicit obligations; and the organisations they operate from are more prone to changes arising from political or organisational instability. For example, in situations where officials change frequently and with little notice, new incumbents may feel less inclined to live up to previous arrangements, and as such a new cycle of 'relationship building' begins. We therefore propose that:

> ***Hypothesis 3b:*** *The moderation effect of the average sector-level informal payments on quality of formal institution is stronger for foreign firms perform than domestic ones*

Foreign firms need to optimise their sourcing strategy to reflect their need for reliable, and cost-effective quality inputs and supplies that can be efficiently and sustainably deployed where and when required (Wu & Zhang, 2014; Niu et al., 2020). In many instances – particularly in developing and emerging markets, local suppliers are at a cost disadvantage when compared with established suppliers in other regions who can often deliver at lower-marginal costs (Wu & Zhang, 2014; London & Hart, 2004), while meeting the same exacting standards multinationals expect and demand in other markets. The incorporation of local suppliers into a firm's supply chain however, provides intangible benefits, not least environmental and geo-political risk management, which is growing in significance, that can compensate for the initial comparative cost disadvantage of localising supply (Niu et al., 2020; London & Hart, 2004). Generally, local firms, being fully embedded in the host country, are more familiar with cultural norms, tastes and expectations of the market (Adomako & Tran, 2022; London & Hart, 2004). They have more ready access to information on upcoming developments that can prove useful in times of societal change and upheaval. They can also act as brand ambassadors for the foreign firm and a source of social legitimacy the firm can leverage in its positioning with the market and host government officials (Adomako & Tran, 2022; Ernst et al., 2014). We therefore hypothesise the complementarity of the effectiveness of formal institutions and the sector level local sourcing as follows:

> ***Hypothesis 3c:*** *The moderation effect of the sector-level local sourcing on the quality of formal institution is stronger for foreign firms than domestic*

Table 4.2: Summary of hypothesis

Hypothesis	Expected impact on performance
Hypothesis 1:	*The quality of formal institutions is positively associated with firm performance.*
Hypothesis 2a:	*The positive effect of quality formal institutions on firms' performance is enhanced by the degree of sector-level senior management effort spent in dealing with regulations*
Hypothesis 2b	*The positive effect of quality formal institutions on firms' performance is enhanced by the degree of sector-level informal payments.*
Hypothesis 2c:	*The positive effect of quality formal institutions on firms' performance is enhanced by the degree of sector-level local sourcing*
Hypothesis 3a:.	*The moderation effect of sector-level senior management time spent in dealing with regulations on quality of formal institutions is stronger for foreign firms than for domestic ones*
Hypothesis 3b:.	*The moderation effect of the average sector-level informal payments on quality of formal institution is stronger for foreign firms perform than domestic ones*
Hypothesis 3c:.	*The moderation effect of the sector-level local sourcing on the quality of formal institution is stronger for foreign firms than domestic*

4.3. Methods

Data and Sample

We draw on firm-level data using the World Bank Enterprise Surveys (WBES), which contains information about private firms from key manufacturing and service sectors for 139 countries across the world. Applying a uniform sampling frame and standardized survey, the WBES produces a representative sample and harmonized data that are comparable across a wide range of economies across the globe. It enables researchers to understand how and which factors and institutions in the business environment affect firm performance over time and across countries. We combine this with country-level variables from the Economic Freedom Index of the Fraser Institute, and we use statistics regarding countries' overall socioeconomic conditions from the World Bank and the IMF. We draw our sample from a population of firms surveyed in 128 countries over 11 years between 2006 and 2016. A total of 96,320 observations are included in our sample.

Variables and Measures

The key variables used in the study are defined and operationalised as follows:

Firm performance is the dependent variable and is measured by total sales of a firm in a fiscal year. We convert the local currency into the U.S. dollar and factor in the purchasing power parity to ensure the comparability across countries over time. Given that our sample has domestic and foreign owned firms of different sizes, the variable is log-transformed in the regression models to normalise its distribution.

4

There are four key explanatory variables in the current study:

Institutional quality, we are particularly concerned with the quality of formal institutions as defined by their propensity towards market-orientation as proposed by the so-called Washington consensus – i.e. degree to which they are widely known or information about is readily accessible, coherent, predictable, applicable to all, and properly and evenly enforced (Burki & Perry, 1998). This pro-market orientation also has a bearing on how well existing institutions relate with each other and are fit for purpose from the perspective of the wider society (McGahan & Victer, 2010). We adopt the quality of institutions, given their theoretic role (North, 1990) and the availability of applicable metrics from a range of institutions, as a proxy for formal institutions. We measure this by their score on the overall degree of Economic Freedom Index provided by the Fraser Institute (Dao & Cuervo-Cazurra, 2014; Haan, Lundstrom & Sturm, 2006), which draws on a composite measure of 42 distinct variables across five major areas a) Size of Government; b) Legal system and security of property rights c) Sound money d) Freedom to trade internationally; and e) Regulation at the country level.

Informal institutions, we identify and examine three widely shared business norms that satisfy the framework proposed by Helmke & Levitsky (2004) for distinguishing informal institutions from weak institutions and informal behavioural practices, and thus propose them as suitable proxies for informal institutions, as follows: a) Top management team effort (TMT effort), which is measured by the country-sector level average value of the percent of firms' senior management's time spent in dealing with regulations in the country in which the firms are located. b) Informal payment (Inf_pmt), identified as the gifts or unofficial payments made to public officials to “get things done” with regard to customs, taxes, licenses, regulations, services etc. This is measured by the country-sector level average value of the percent of firms’ total annual sales paid as informal payment in the country in which the firms are located. c) Local sourcing (Loc_sourc) captures the extent to which firms source locally in the host countries. It is measured by the country-sector level average value of the percentage of firms’ material inputs and supplies of domestic origin in last fiscal year.

Ownership, which distinguishes between firms owned by private foreign individuals, companies or organizations (Stinchcombe, 1965) and domestic firms; and is measured by a dummy variable, which takes the value “1” for foreign firms with more than 10% foreign ownership, and “0” for domestic firms.

Control Variables

We control for a set of variables at both firm and country-sector levels, which are associated with firms’ performance. Studies have shown that older firms experience superior performance than the younger ones due to learning effects (Bain, 1956). We control for the *Age* of a firm and measure it by the difference between the year of observation and the year in which the firm was formally registered.

Larger firms tend to perform better than smaller firms due to economies of scale and scope as a result of formalisation and standardisation (Penrose, 1959). We, therefore, control for the *Size* of a firm and measure it by the number of employees of the firm, which we code as a categorical variable taking the value ‘1’ for small size firms with less than 20 employees, ‘2’ for medium size firms with less than 100 employees, and ‘3’ for large size firms with no less than 100 employees. The small size firm is the reference group in the regressions.

Industry specific factors such as *growth*, *concentration*, *competition* and *advertising intensity* define firms’ level of performance (Ayyagari, Demirgüç-Kunt, & Maksimovic, 2011). In the current study, the industrial sector in which a firm’s primary business lies is measured by a categorical variable taking the value ’1’ for manufacturing industry, ’2’ for service industry. *Manager’s experience* affects firms’ performance positively (Hofmann, Griffin, & Gavin, 2000). And is measured by the number of years a firm’s top manager has been working in the sector.

We also control for the country’s *GDP per capita (USD)* adjusted for purchasing power parity (PPP) and GDP growth as a country’s wealth and growth rate has been shown to influence firms' performance. We control for *population size* of country as it captures the size of the market within the country (Campbell & Hopenhayn, 2005) which could potentially affect firms' performance. The time effect is controlled for in the analyses using year dummy variables.

Statistical Analysis

The dataset was a cross-sectional panel with a hierarchical structure, with individual firms nested within their host countries. As such, we employ multilevel linear regression techniques to test the hypothesis. This method is adopted because we investigate the cross-level direct impacts and integration effects of institutional variables at national level on MNEs' performance at firm level. Firm-level data are likely to be correlated within countries in this case. OLS regressions with a pooled data could result in biased estimations due to ignoring the nested data structure, thus violating the assumption of data independence (Halaszovich & Lundan, 2016).

We first verified that there existed a sufficient amount of variance in firms' performance between country-sectors by calculating the intraclass correlation coefficient (ICC). It shows that about 53.6 % (chi2 (1) = 69864.56, p<0.01) of the variance in firms' performance reside in country-sector levels, which justifies our choice of the multilevel analysis. We specify a two-level model with random intercept to evaluate firms' performance by factoring in both the impacts at the firm level (level-1) and country-sector level (level-2). The models are specified below.

Level-1 equation:

$$Y_{ij} = \beta_{0j+}\beta_{1j}X_{ij} + e_{ij} \tag{1}$$

Level-2 equations:

$$\beta_{0j} = \gamma_{00} + \gamma_{01}W_j + u_{0j} \tag{2}$$

$$\beta_{1j} = \gamma_{10} + u_{1j} \tag{3}$$

Multilevel equation:

$$Y_{ij} = \gamma_{00+}\gamma_{01}Formal\ Institution_j\ + \gamma_{02}Informal\ Institutions_j + \gamma_{03}GDPperCap_j + \gamma_{04}GDP\ growth_j + \gamma_{05}Population_j + \gamma_{10}Ownership_{ij} + \gamma_{20}Size_{ij} + \gamma_{30}Age_{ij} + \gamma_{50}ManagerExperience_{ij} + \gamma_{60}Sector_{ij} + \gamma_{70}Year_{ij} + u_{0j} + e_{ij} +\ u_{1j} \tag{4}$$

The level-1 equation (i.e., (1)) predicts the direct effects (i.e., β) of level-1 predictors on level-1 outcomes, where Y_{ij} is the dependent variable for an individual observation at level 1 (subscript i refers to a firm, subscript j refers to the country that the firm belongs to). X_{ij} is the firm-level

4

(level-1) predictor. β_{0j} is the intercept of the dependent variable in country-sector j (level-2). β_{1j} is the slope for the relationship in country j between the firm-level predictor and the dependent variable. e_{ij} is the firm-level residual. The level-2 equations (i.e., (2) and (3)) predict the effects (i.e., γ) of level-2 predictors on level-1 betas as well as on the level-1 intercept, where γ_{00} is the overall intercept, which is the mean of the intercepts across country-sectors in the current study. W_j is the country-sector level predictor. γ_{01} is the slope or main effect of country-sector level predictor. γ_{10} is the slope or main effect of individual-level predictor. u_{0j} and u_{1j} are level-2 residuals.

The overall multilevel regression model (i.e., (4)) allows for testing the impacts of factors at both the firm and country-sector levels on firms' performance at the same time, while accounting for variation in firms' performance across country-sectors. We adopt maximum likelihood algorithms for fitting the models.

4.4. Results

The descriptive statistics of the variables are presented in Table 4.3. The correlations of all variables for the analysis are shown in Table 4.4. Variance inflation factors (VIFs) of all variables in the analyses are between 1.19 and 2.92. The average value of VIFs is 1.74. It indicates the analyses in the current study are unlikely to be influenced by multicollinearity between variables.

Table 4.3. Descriptive Statistics

Variable	**Observations**	**Mean**	**Std. Dev.**	**Min**	**Max**
Sales (billions USD adjusted for PPP)	96,320	15.00	1589.08	0	345203.5
Formal institutions	96,320	57.50	7.54	22.1	78
TMT efforts	96,320	10.72	6.79	0.51	47.39
Informal payment	96,320	1.59	2.02	0	25.56
Local sourcing	96,320	68.87	20.40	0.5	100
Firm ownership	96,320	0.11	0.31	0	1
Firm age	96,320	19.17	15.50	1	341
Firm size	96,320	1.75	0.77	1	3
Sector	96,320	1.38	0.49	1	2
TMT experience	96,320	17.62	11.64	0	60
GDP per capita (thousands USD adjusted for PPP)	96,320	9.51	7.05	0.61	31.43

GDP growth	96,320	4.85	4.16	-14.81	20.74
Population (millions)	96,320	205.38	409.72	0.07	1350.70
Year	96,320	2010.75	3.07	2006	2016

Table 4.4. Correlation Matrix

	1	2	3	4	5	6	7	8	9	10	11	12	13
1 Sales (billions USD adjusted for PPP)	1												
2 Formal institutions	-0.01	1											
3 TMT efforts	-0.10	0.11	1										
4 Informal payment	0.01[a]	-0.06	0.12	1									
5 Local sourcing	0.08	-0.20	-0.26	-0.05	1								
6 Firm ownership	0.17	0.01	0.07	0.06	-0.09	1							
7 Firm age	0.13	0.05	0.05	-0.05	0.02	0.02	1						
8 Firm size	0.44	0.02	-0.02	-0.07	0.08	0.18	0.24	1					
9 Sector	-0.07	-0.02	0.11	0.01[b]	-0.27	-0.002[c]	-0.13	-0.17	1				
10 TMT experience	0.03	0.08	0.19	-0.05	-0.04	0.04	0.34	0.11	-0.07	1			
11 GDP per capita (thousands USD adjusted for PPP)	-0.05	0.43	0.34	-0.18	0.01	-0.03	0.07	0.09	-0.002[c]	0.14	1		
12 GDP growth	0.04	-0.28	-0.19	-0.02	0.20	-0.01[a]	0.01[b]	-0.02	-0.1	-0.02	-0.29	1	
13 Population (millions)	0.10	-0.31	-0.28	-0.09	0.64	-0.13	-0.003[c]	0.12	-0.2	-0.08	-0.05	0.28	1
14 Year	0.05	-0.11	-0.28	-0.10	0.24	-0.06	0.01[b]	0.04	0.03	-0.03	-0.02	0.05	0.30

Number of observations: 96,320
a: indicates statistical significances at $p < 0.01$; b: indicates statistical significances at $p < 0.1$; c: indicates statistical significances at $p > 0.1$; all the rest: statistical significances at $p<0.001$.

Table 4.5 shows the multilevel linear regressions results, in which Model 1 is the baseline model including only control variables; Model 2 is the main effect model containing the key explanatory variables; Model 3 is the model testing interaction effects of formal and informal institutions on firms' performance by adding three 2-way interaction terms to the model; Model 4 is the model testing the moderating effect of firm's ownership on the interaction effects between formal and informal institutions on firms' performance by adding three 3-way interaction terms to the model.

Main Effects

Results shown in Model 2 indicate that Foreign firms, on average, outperform domestic firms (0.75, $p < 0.001$).

The direct impact of both formal and informal institutions on firms' performance is however, not straightforward. As we can see from the Model 2, the effect of formal institution is not significant (0.02, $p>0.1$). Two out of three informal institutions do not show significant influence on firms' performance (-0.11, $p>0.1$ for the country-sector level top management effort in dealing with regulations; -0.13, $p>0.1$ for the local sourcing at the country-sector level).

Table 4.5. Multilevel Regression Results

	Model 1	Model 2	Model 3	Model 4
Fixed part estimates				
Firm ownership: foreign		0.75***	0.75***	0.75***
		(0.019)	(0.019)	(0.020)
Formal Institution: Overall economic freedom		0.02	-0.04	-0.07*
		(0.027)	(0.028)	(0.028)
Informal Institution: TMT efforts		-0.11	-0.08	-0.10
		(0.161)	(0.172)	(0.169)
Informal Institution: Informal payment		0.35**	0.45***	0.44***
		(0.122)	(0.131)	(0.129)
Informal Institution: Local sourcing		-0.13	-0.14	-0.15
		(0.174)	(0.185)	(0.182)
Formal institutions * Informal institution: TMT efforts			0.38***	0.33***
			(0.026)	(0.026)
Formal institutions * Informal institution: Informal payment			0.14***	0.16***
			(0.037)	(0.037)
Formal institutions * Informal institution: Local sourcing			0.16***	0.13***
			(0.025)	(0.025)
Foreign * Formal institutions			-0.11***	-0.13***
			(0.017)	(0.018)
Foreign * Informal institution: TMT efforts			0.13***	0.08***
			(0.019)	(0.020)
Foreign * Informal institution: Informal payment			-0.01	0.03*
			(0.015)	(0.015)
Foreign * Informal institution: Local sourcing			0.06**	0.10***
			(0.020)	(0.020)
Foreign * Formal institutions * Informal institution: TMT efforts				-0.15***
				(0.019)
Foreign * Formal institutions * Informal institution: Informal payment				-0.09***
				(0.011)
Foreign * Formal institutions * Informal institution: Local sourcing				-0.10***

				(0.021)
Firm Age	0.15***	0.16***	0.16***	0.16***
	(0.006)	(0.006)	(0.006)	(0.006)
Firm Size: Medium (20-99) (Small as reference group)	1.68***	1.63***	1.63***	1.63***
	(0.013)	(0.013)	(0.013)	(0.013)
Firm Size: Large (100 And Over) (Small as reference group)	3.70***	3.56***	3.57***	3.57***
	(0.016)	(0.016)	(0.016)	(0.016)
Sector: Services (Manufacturing as reference group)	0.30	0.29	0.34	0.34
	(0.327)	(0.322)	(0.343)	(0.337)
TMT experience	-0.05***	-0.05***	-0.06***	-0.06***
	(0.006)	(0.006)	(0.006)	(0.006)
GDP per capita (PPP) (Log transformed)	0.30***	0.32***	0.54***	0.49***
	(0.091)	(0.093)	(0.098)	(0.097)
GDP growth	-0.02	-0.03**	-0.12***	-0.12***
	(0.012)	(0.012)	(0.013)	(0.013)
Population (Log transformed)	0.11	0.15	-0.04	-0.03
	(0.165)	(0.176)	(0.186)	(0.184)
year = 2007	-0.06	-0.00	-0.06	-0.05
	(0.051)	(0.052)	(0.052)	(0.052)
year = 2008	-0.49***	-0.48***	-0.61***	-0.59***
	(0.067)	(0.066)	(0.067)	(0.067)
year = 2009	-0.04	-0.04	-0.19***	-0.19***
	(0.055)	(0.056)	(0.056)	(0.056)
year = 2010	0.44***	0.45***	0.48***	0.50***
	(0.028)	(0.028)	(0.028)	(0.028)
year = 2011	0.76***	0.83***	0.52***	0.55***
	(0.079)	(0.080)	(0.084)	(0.084)
year = 2012	0.51***	0.53***	0.56***	0.57***
	(0.080)	(0.080)	(0.080)	(0.080)
year = 2013	-0.37***	-0.35***	-0.38***	-0.36***
	(0.049)	(0.049)	(0.050)	(0.050)
year = 2014	-0.51***	-0.50***	-0.62***	-0.60***
	(0.067)	(0.069)	(0.070)	(0.070)
year = 2015	0.64***	0.65***	0.58***	0.59***
	(0.072)	(0.072)	(0.073)	(0.073)
year = 2016	1.27***	1.28***	1.25***	1.25***

	(0.060)	(0.060)	(0.060)	(0.060)
Constant	14.61***	14.45***	14.41***	14.40***
	(0.262)	(0.257)	(0.273)	(0.269)
Random part estimates				
Level-2 variance: σ_u^2	5.87	5.59	6.34	6.13
Level-1 variance: σ_e^2	2.81	2.76	2.75	2.74
Model fit statistics				
Observations	96,320	96,320	96,320	96,320
Number of country-sectors	225	225	225	225
Likelihood-ratio test of σ_u^2 [a]: Prob > chi^2 (1)	92116.6***	91933.1***	89578.0***	89466.1***
Likelihood-ratio test of model fit: Prob > chi^2	50956.2***	1632.9***	442.8***	190.0***
Degree of freedom	18	5	7	3

Notes:

Continuous variables in the models are standardized.

Standard errors are in parentheses.

*** $p < 0.001$, ** $p < 0.01$, * $p < 0.05$

a: The null hypothesis is that $\sigma_u^2 = 0$. If the null hypothesis is rejected, we conclude that the multi-level model provides a better fit than the single-level model.

Informal institutions, as captured by the country-sector level informal payment shows significant positive influence on firms' performance (0.35, p<0.01); and implies that the higher the level of informal payment in a sector of a country where a firm is located, the better the firm's performance.

Interaction Effects

Model 3 in Table 3 shows the two-way interaction effects of formal and informal institutions on firms' performance. Overall, formal and informal institutions complement each other in driving firms' performance. Firms tend to perform better when the overall quality or effectiveness of a country's formal institution and TMT efforts in dealing with formal regulations at the sector level are both at their high values (0.05, p<0.001), when the quality of a country's formal institution and sector-level informal payments are both high (0.14, p< 0.001), and when the quality of a country's formal institution and sector-level average scale of firms' local sourcing are both high (0.16, p<0.001). Therefore, the hypotheses 2a, 2b, and 2c are supported.

Model 4 in Table 3 shows the moderating role of firms' ownership on the interaction effects of the formal and informal institutions on firms' performance. Overall, the results show that foreign firms benefit less from the institutional complementarity between the formal and informal institutions. The three 3-way interaction terms are all negative and statistically significant at 0.1% level. Therefore, the hypotheses 3a, 3b, and 3c are not supported.

We graphically illustrate the interaction effects between formal and informal institutions (Figures 2, 3, and 4), and the moderating role of firms' ownership on the interaction effects of the formal and informal institutions on firms' performance (Figures 5, 6, and 7). We will have an in-depth discussion about the unexpected findings in the discussion section.

Figure 4.2. Interaction Effects between Formal Institutions and TMT Efforts (Informal institution)

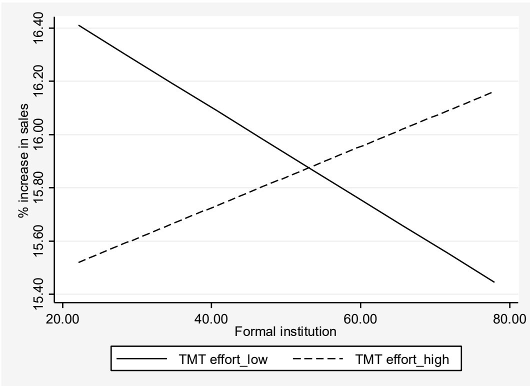


Figure 4.3. Interaction Effects between Formal Institutions and Informal Payment (Informal institution)

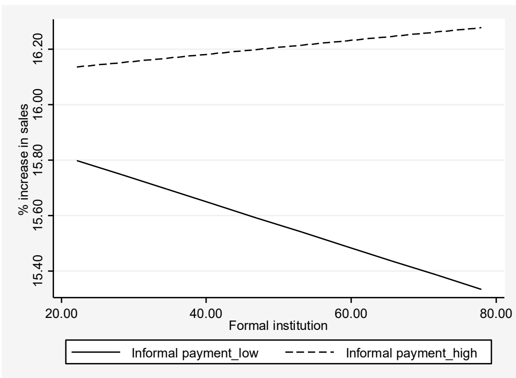


Figure 4.4. Interaction Effects between Formal Institutions and Local Sourcing (Informal institution)

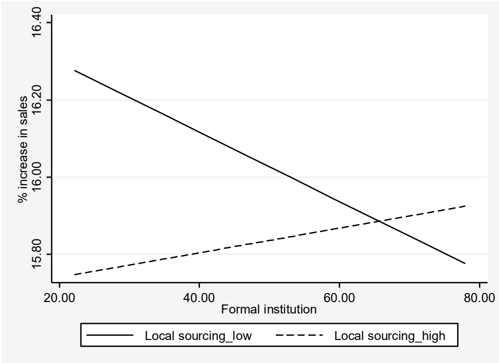


Figure 4.5. 3-way Interaction Effects between Formal Institution, Informal institution: TMT Efforts, and Firm Ownership

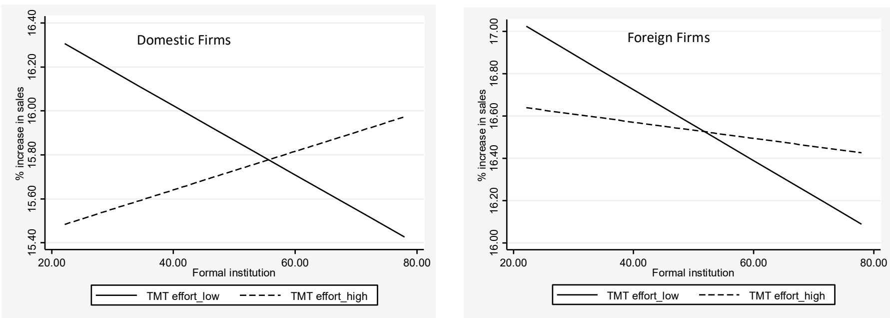


Figure 4.6. 3-way Interaction Effects between Formal Institution, Informal institution: Informal Payment, and Firm Ownership

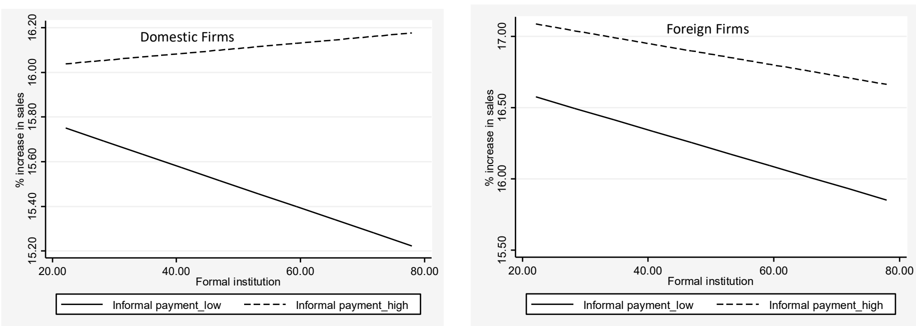
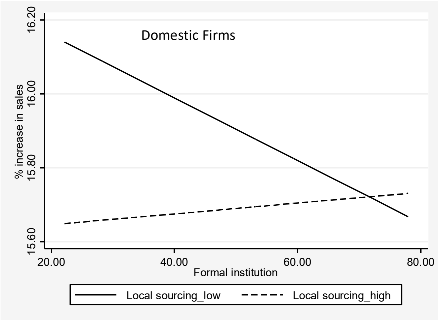
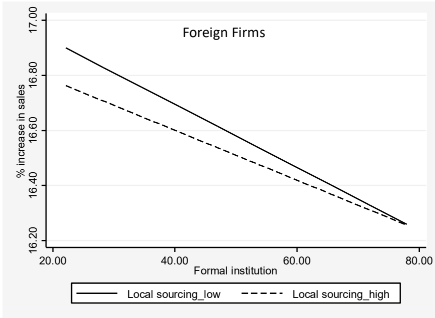


Figure 4.7. 3-way Interaction Effects between Formal Institution, Informal institution: Local Sourcing, and Firm Ownership





Robustness Checks

We, furthermore, carry out additional analyses by splitting the full sample into emerging market (EM) and Sub-Saharan Africa (SSA) subsamples to see if the results would hold across different regional groupings and socioeconomic settings.

The regression results based on EM and SSA subsamples are presented in the Appendix A3 and A4. We compare and discuss the results across three different samples in detail in the following section.

Table 4.6 Descriptive Statistics (Emerging Markets Sample)

Variable	Observation	Mean	Std. Dev.	Min	Max
Sales (billions USD adjusted for PPP)	60,047	16.28	1427.18	0	292633.6
Formal institutions	60,047	58.46	6.98	37.1	78
Informal institution: TMT efforts	60,047	11.19	7.43	1.30	47.39
Informal institution: Informal payment	60,047	1.28	1.77	0	14.85
Informal institution: Local sourcing	60,047	73.68	20.76	0.5	100
Firm ownership (Foreign)	60,047	0.09	0.29	0	1
Firm age	60,047	19.71	15.74	1	341
Firm size	60,047	1.82	0.78	1	3
Sector	60,047	1.34	0.47	1	2
TMT experience	60,047	18.02	11.56	0	60
GDP per capita (thousands USD adjusted for PPP)	60,047	12.37	6.92	4.26	31.43
GDP growth	60,047	4.55	4.43	-14.81	20.74
Population (millions)	60,047	312.79	487.45	1.32	1350.70
Year	60,047	2010.95	2.95	2006	2016

Table 4.7 Descriptive Statistics (Sub-Saharan Africa Sample)

Variable	Observation	Mean	Std. Dev.	Min	Max
Sales (billions USD adjusted for PPP)	19,514	21.72	2480.34	0	345203.5
Formal institutions	19,174	55.17	8.49	22.10	74.30
Informal institution: TMT efforts	19,514	8.85	3.74	2.14	24.47
Informal institution: Informal payment	19,514	2.67	2.60	0.10	25.56
Informal institution: Local sourcing	19,514	65.23	16.73	3.33	86.46
Firm ownership (Foreign)	19,514	0.16	0.36	0	1
Firm age	19,514	15.94	13.71	1	191
Firm size	19,514	1.51	0.69	1	3
Sector	19,514	1.44	0.50	1	2
TMT experience	19,514	13.78	9.69	0	60
GDP per capita (thousands USD adjusted for PPP)	19,514	3.84	3.50	0.56	15.31
GDP growth	19,514	6.56	3.85	-4.01	20.74
Population (millions)	19,514	54.62	57.56	1.25	176.46
Year	19,514	2009.83	3.07	2006	2015

Table 4.8 Multilevel Regression Results (Emerging Markets Sample)

	Model 1	Model 2	Model 3	Model 4
Fixed part estimates				
Firm ownership: foreign		0.78***	0.79***	0.78***
		-0.024	-0.026	-0.026
Formal Institution: Overall economic freedom		0.38***	-0.12*	-0.08
		-0.04	-0.058	-0.058
Informal Institution: TMT efforts		-0.23	-0.3	-0.37+
		-0.22	-0.239	-0.226
Informal Institution: Informal payment		-0.36+	0.02	-0.03
		-0.215	-0.241	-0.228
Informal Institution: Local sourcing		0.17	0.09	0.07
		-0.275	-0.299	-0.283
Formal institutions * Informal institution: TMT efforts			0.74***	0.56***
			-0.05	-0.052
Formal institutions * Informal institution: Informal payment			-0.40***	-0.35***
			-0.069	-0.068
Formal institutions * Informal institution: Local sourcing			0.29***	0.26***
			-0.028	-0.028
Foreign * Formal institutions			-0.04	0.02
			-0.022	-0.027
Foreign * TMT efforts			0.14***	0.05+
			-0.024	-0.027

Foreign * Informal payment			-0.14***	-0.09**
			-0.019	-0.03
Foreign * Local sourcing			0.14***	0.18***
			-0.024	-0.025
Foreign * Formal institutions * TMT efforts				-0.22***
				-0.026
Foreign * Formal institutions * Informal payment				-0.05**
				-0.018
Foreign * Formal institutions * Local sourcing				-0.06*
				-0.027
Firm Age	0.10***	0.11***	0.11***	0.11***
	-0.007	-0.007	-0.007	-0.007
Firm Size: Medium (20-99) (Small as reference group)	1.58***	1.55***	1.55***	1.55***
	-0.015	-0.015	-0.015	-0.015
Firm Size: Large (100 And Over) (Small as reference group)	3.62***	3.50***	3.51***	3.51***
	-0.018	-0.018	-0.018	-0.018
Sector: Services (Manufacturing as reference group)	0.15	0.24	0.15	0.16
	-0.472	-0.466	-0.505	-0.477
TMT experience	0.04***	0.04***	0.03***	0.02**
	-0.008	-0.008	-0.008	-0.008
GDP per capita (PPP) (Log transformed)	0.18	-0.15	0.40**	0.31*
	-0.12	-0.124	-0.137	-0.135
GDP growth	-0.07***	-0.08***	-0.22***	-0.22***
	-0.016	-0.016	-0.018	-0.018
Population (Log transformed)	0.77**	0.83**	0.47	0.52+
	-0.259	-0.297	-0.328	-0.312
year = 2007	-1.54**	-1.58**	-1.71**	-1.61**
	-0.555	-0.552	-0.598	-0.565
year = 2008	-0.93+	-1.13*	-0.92	-0.87
	-0.556	-0.553	-0.599	-0.566
year = 2009	-1.24*	-1.37*	-1.79**	-1.67**
	-0.555	-0.552	-0.599	-0.566
year = 2010	0.36***	0.33***	0.41***	0.45***
	-0.039	-0.039	-0.042	-0.042
year = 2012	-0.65	-0.68	-0.84	-0.71
	-0.559	-0.557	-0.602	-0.57
year = 2013	-1.30*	-1.43**	-1.67**	-1.53**
	-0.555	-0.552	-0.599	-0.566
year = 2014	-2.31***	-2.23***	-2.71***	-2.57***
	-0.568	-0.567	-0.614	-0.581
year = 2015	-0.65	-0.81	-0.83	-0.78
	-0.565	-0.563	-0.609	-0.576

year = 2016	-1.52	-2.39	-2.19	-2.2
	-1.648	-1.68	-1.822	-1.719
Constant	15.62***	15.77***	15.81***	15.72***
Random part estimates				
Level-2 variance:	4.86	4.57	5.37	4.78
Level-1 variance:	2.46	2.41	2.39	2.38
Model fit statistics				
Observations	60,047	60,047	60,047	60,047
Number of groups	88	88	88	88
Likelihood-ratio test of Level-2 variance: Prob > chi2 (1)	53741.2***	49057.86***	46860.43***	46671.07***
Likelihood-ratio test of model fit: Prob > chi2	34603.39***	1193.11***	523.74***	124.28***
Degree of freedom	17	5	7	3

Table 4.9 Multilevel Regression Results (Sub-Saharan Africa Sample)

	Model 5	**Model 6**	**Model 7**	**Model 8**
Fixed part estimates				
Firm ownership: Foreign		0.72***	0.72***	0.68***
		-0.039	-0.039	-0.04
Formal Institution: Overall economic freedom		0.91***	0.84***	0.86***
		-0.146	-0.155	-0.154
Informal Institution: TMT efforts		-4.80**	-4.11***	-4.12***
		-1.507	-1.168	-1.17
Informal Institution: Informal payment		3.10*	3.73***	3.73***
		-1.249	-0.978	-0.98
Informal Institution: Local sourcing		-5.68**	-3.29*	-3.31*
		-1.871	-1.465	-1.467
Formal institutions * Informal institution: TMT efforts			-1.65***	-1.60***
			-0.151	-0.151
Formal institutions * Informal institution: Informal payment			0.87***	0.87***
			-0.155	-0.155
Formal institutions * Informal institution: Local sourcing			-0.68***	-0.66***
			-0.116	-0.116
Foreign * Formal institutions			-0.05	-0.11**
			-0.036	-0.04
Foreign * TMT efforts			-0.07+	-0.15***
			-0.036	-0.04
Foreign * Informal payment			0.06+	0.12**
			-0.033	-0.039
Foreign * Local sourcing			-0.06+	0.04
			-0.039	-0.043
Foreign * Formal institutions * Informal institution: TMT efforts				-0.33***

				-0.051
Foreign * Formal institutions * Informal institution: Informal payment				0.04
				-0.03
Foreign10 * Formal institutions * Informal institution: Local sourcing				-0.17***
				-0.041
Firm Age	0.22***	0.22***	0.22***	0.22***
	-0.016	-0.016	-0.016	-0.016
Firm Size: Medium (20-99) (Small as reference group)	1.73***	1.66***	1.65***	1.64***
	-0.031	-0.031	-0.031	-0.031
Firm Size: Large (100 and over) (Small as reference group)	3.72***	3.52***	3.53***	3.53***
	-0.046	-0.047	-0.047	-0.047
Sector: Services (Manufacturing as reference group)	0.48	-1.57	-0.56	-0.56
	-5.002	-3.748	-2.882	-2.888
TMT experience	0.04*	0.04*	0.04*	0.04*
	-0.015	-0.015	-0.015	-0.015
GDP per capita (PPP) (Log transformed)	-11.37***	-10.45***	-9.30***	-9.33***
	-0.419	-0.435	-0.482	-0.482
GDP growth	-0.53***	-0.49***	-0.50***	-0.49***
	-0.032	-0.032	-0.032	-0.032
Population (Log transformed)	11.55***	9.36***	5.07***	5.04***
	-1.55	-1.451	-1.301	-1.302
year = 2007	0.87***	0.72***	0.37***	0.38***
	-0.083	-0.093	-0.104	-0.104
year = 2009	2.10***	1.91***	0.70*	0.72*
	-0.196	-0.195	-0.292	-0.292
year = 2010	1.50***	1.30***	1.48***	1.50***
	-0.168	-0.17	-0.163	-0.163
year = 2011	3.34***	2.12***	1.96***	1.96***
	-0.286	-0.353	-0.391	-0.391
year = 2013	0.83**	0.77**	0.85**	0.88**
	-0.296	-0.286	-0.279	-0.279
year = 2014	1.28***	1.12***	1.06***	1.09***
	-0.294	-0.288	-0.298	-0.298
year = 2015	7.03***	5.08***	4.98***	4.99***
	-0.471	-0.574	-0.671	-0.67
Constant	19.37***	16.62***	14.92***	14.89***
	-3.486	-2.604	-2.055	-2.058
Random part estimates				
Level-2 variance:	368.60	192.82	113.75	114.22
Level-1 variance:	3.35	3.29	3.26	3.26
Model fit statistics				

Observations	19,514	19,514	19,514	19,514
Number of groups	60	60	60	60
Likelihood-ratio test of Level-2 variance: Prob > chi2 (1)	8186.03***	7666.15***	6921.66***	6931.67***
Likelihood-ratio test of model fit: Prob > chi2	9135.13***	392.88***	172.45***	42.41***
Degree of freedom	15	5	7	3

4.5. Discussion

To a large extent, our theoretical model is supported by our empirical analysis. There are, nonetheless, some intriguing findings in our main analysis that warrant additional consideration. The contrast between the main findings, and the analysis of emerging markets and Sub-Saharan Africa sub-samples, while consistent for the majority of variables examined, present some variation in some of the key variables, which are worthy of note.

We find that the direct effects of formal and informal institutions on firms' performance is not entirely as expected. In the full sample, for instance, it appears that formal institutions do not stimulate firm performance. In addition, the direct effects of Informal Payments ('bribes') seem to positively contribute to firm performance. There is also some variance across samples and the interaction effects are unexpected at times as well.

Three out of four direct effects of formal and informal institutions are *not* significant in the full sample. We start to see more significant effects emerge when the full sample is divided into subsamples according to regional and economic criteria. The effect of formal institutions on firm performance , affecting firms' performance by reducing transaction cost and improving operational efficiency (Dollar, Hallward-Driemeier, & Mengistae, 2005; Olusina Daniel, Fu, & Dolfsma, 2018) is mixed: negative for the full sample, insignificant for emerging economies and positive for Sub-Saharan Africa. Many emerging markets might have been experiencing growth-enhancing reforms in their formal institutional landscape in the last decade, which has had the effect of turning appropriate formal institutions into a 'hygiene factor' that a country must have, but that does not make a difference for firm performance between countries. An alternative interpretation is that the effect of formal institutions on firm performance in formal countries is overrated in the literature.

The sector-level Top Management Team (TMT) effort in dealing with regulations imposed by the government seems mostly to show a negative impact on firms' performance. Such efforts aggregated at the sector level seem to reflect how onerous a country's business-related regulation is. The more cumbersome the rules and regulations associated with operating a business in a country, the more time and effort will be needed from the top management team to understand and comply with the regulatory requirements at the sector level, which is much in line with conventional thinking (Djankov, La Porta, Lopez-de-Silanes, & Shleifer 2002). Local sourcing, against intuitive argumentation, does not seem to directly impact firm performance positively.

Counter-intuitively, the degree of sector-level informal payment is *positively* associated with firms' performance in the full (0.35, $p<0.001$) and SSA samples (3.1, $p<0.05$). The effect is only marginally negative for the EM sample (-0.36, $p<0.1$). Meaning Informal payments, or bribes, on the whole, positively impact firm performance.

Regarding the two-way interaction effects between sector-level formal and three informal institutions, the current research finds that the effects particularly seem to vary across different regional and socioeconomic contexts, which resonates with existing research positing formal-informal institutional relationships can appear in a variety of ways (Helmke & Levitsky, 2004).

Formal and informal institutions reinforce each other's influence on firms' performance in the full sample and EM sample as predicted, except for the moderating role of the sector-level informal payment in the relationship between formal institutions and firms' performance in the EM sample, which is marginally negative (-0.36, $p<0.1$). What is most remarkable is that sector-level informal payments enhance the positive impact of effective formal institution on firms' performance in the emerging markets.

This is a remarkable and counter-intuitive finding that is hard to explain. The finding is probably because informal payments are expected and made, despite formally seen as an activity to be frowned upon. So much so that governments in emerging economies seek to impose anti-bribery and anti-corruption measures to enhance the (perceived) quality and effectiveness of the institutional environment they take responsibility for during what might be a period of social and economic transition. For example, the G20 countries, which includes ten leading emerging economies across the world, have committed to fighting corruption by establishing the Anti-Corruption Working Group (ACWG) with the support of IMF and other international organisations and taking a series of anti-corruption initiatives systematically since

2010.[5] A high level of informal payment at the sector level can therefore be perceived by firms as a major source of (regulatory) uncertainty and flexibility due to the prevalence of corruption in a sector, which reduces firms' operational efficiency and profitability.

It is worth noting that in Sub-Saharan African countries, formal and some informal institutions substitute each other's impact on firms' performance. Local sourcing and TMT efforts in particular substitute for possibly lower quality formal institutions – but not Informal payments. This finding is in line with research showing that less developed countries tend to have weaker and more underdeveloped formal institutions, the enforcement of which is also likely to be unreliable (M. W. Peng, Sun, Pinkham, & Chen, 2009). In the presence of such (formal) "institutional voids", firms will resort to informal institutions or formal institutions developed in different and yet related fields (Olthaar, et al. 2017). Again, the only exception is the sector-level informal payment, which complement the enabling role of formal institutions role in driving firms' performance in SSA countries instead of substituting its effect. Gift-giving and bribery may be regarded as acceptable practices in some of these countries.

While Cintra et al. (2018) find that the effects of corruption differ across times, places and in its degree of harmfulness, we suggest that perhaps countries on the ascendance who need to adhere to a view of the proper place of Informal payment may be most keen to clamp down on this practice, potentially to their economic detriment.

Arising from greater endowments of capital, experience and technology – so-called 'ownership advantages' foreign firms tend to possess capabilities that enable them to perform better than domestic firms (Almodóvar & Nguyen 2022), particularly in emerging and in the developing economies of Sub-Saharan Africa where local firms face difficulties access capital, quality infrastructure and key skills (McCarthy & Aalbers, 2016). Our results bear this out, pointing to an enigma for the IB literature: what makes foreign firms, who generally face a liability of foreignness – particularly as regards familiarity with local formal institutions and norms perform better than domestic firms? Our analysis of how informal and formal institutions impact firm performance in industries helps shed further light on this issue.

[5] G20 Anti-Corruption Action Plan: G20 Agenda for Action on Combating Corruption, Promoting Market Integrity, and Supporting a Clean Business Environment (2010). Seoul. https://www.bmjv.de/DE/Themen/G20/G20_node.html

Foreign firms do not seem to benefit from strong formal institutions. Foreign firms also seem to benefit from making informal payments, across the board. Since Local sourcing and TMT efforts benefit them in Emerging markets and Sub-Saharan Africa but not in the full sample, the effect in developed economies must be particularly strong.

In developed economies formal institutions might be a mere hygiene factor, while perhaps in Sub-Saharan Africa a somewhat better formal institutional 'furniture' does not make enough of a difference. These suggestions are speculations and need further research. Furthermore, foreign firms do not seem to be able to use informally institutionalized ways of accessing information and influencing government officials. Our analysis is unable to differentiate for origin of the foreign firm, however, and we should not assume that foreign firms investing in another country are western firms. Increasingly, they are not. Nevertheless, as we largely rule out the suggestion that foreign firms do better because they have experience navigating intricate institutional settings in which formal and informal institutions combine in complex ways, we may need to conclude that perhaps they perform better because they are better organized and managed (Bloom & Van Reenen, 2007).

Further research into what constitutes such different capabilities beyond size and capitalization is needed, however. Being able to differentiate between the origins of the foreign firms might help as well.

4.6. Conclusions

This paper explores how the institutional mix of different countries affect the performance of foreign and domestic firms. We test empirically the notion of institutional voids, and find that informal institutions can serve to complement or substitute for weak or low-quality formal institutions. We propose and operationalise measures for three proxies for informal institutions as exemplified by time spent by senior managers on regulations, informal payments, and local sourcing – and find that they often enhance the positive effect of formal institutions; but with some intriguing regional variations.

We find that institutions matter, but that the picture of how different institutions matter is mixed. In particular the finding that the often-practiced norm of Informal payments helps firm performance is unexpected – what is more, we show that this informal institution enhances the positive effect of formal institutions, except in emerging markets.

While our findings support the mainstream view that foreign firms generally outperform their domestic counterparts, we establish that this is not down to any clear advantage in navigating the institutional environment such firms have accumulated. For the full sample as well as for Sub-Saharan Africa, any expertise that senior managers and business leaders might have will not help foreign firms to informally deal with officials. Here, Local sourcing is of limited help, yet informal payments do help. Foreign firms might be better at persuading officials, or might have more resources to engage in such behaviours. In Emerging markets, Informal payment does not enhance firm performance for foreign firms – TMT efforts and Local sourcing work here, perhaps as an imperfect substitute for informal payments.

REFERENCES

Adomako, S. and Tran, M. D. (2021). Local embeddedness, and corporate social performance: the mediating role of social innovation orientation. Corporate Social Responsibility and Environmental Management, 29(2), 329-338

Almodóvar, P., & Nguyen, Q. T. (2022). Product innovation of domestic firms versus foreign MNE subsidiaries: The role of external knowledge sources. Technological Forecasting and Social Change, 184, 122000.

Ayyagari, M., Demirgüç-Kunt, A., & Maksimovic, V. (2011). Firm innovation in emerging markets: The role of finance, governance, and competition. *Journal of Financial and Quantitative Analysis*.

Bain, J. S. (1956). *Barriers to new competition: their character and consequences in manufacturing industries*. *Harvard University series on competition in American industry 3*. Burki, S. J., & Perry, G. (1998). *Beyond the Washington consensus: institutions matter*. World Bank Publications.

Banalieva, E. R., Cuervo-Cazurra, A., & Sarathy, R. (2018). Dynamics of pro-market institutions and firm performance. Journal of International Business Studies, 49(7), 858–880. https://www.jstor.org/stable/48725190

Burki, S. J., & Perry, G. (1998). Beyond the Washington consensus: institutions matter. World Bank Publications.

Bloom, N., & Van Reenen, J. (2007). Measuring and explaining management practices across firms and countries. *Quarterly Journal of Economics*.

Boddewyn, J., & Doh, J. (2011). Global strategy and the collaboration of MNEs, NGOs, and governments for the provisioning of collective goods in emerging markets. *Global Strategy Journal*, *1*(3–4), 345–361.

Barbalet J., 2022 Conceptualising informal institutions: Drawing on the case of guanxi. British Journal of Sociology, 74 (1):70-82.

Campbell, J. R., & Hopenhayn, H. A. (2005). Market size matters. *The Journal of Industrial Economics*, *LIII*(1), 1–25.

Cantwell, J., Dunning, J. H., & Lundan, S. M. (2015). An evolutionary approach to understanding international business activity: The co-evolution of MNEs and the institutional environment. In *The Eclectic Paradigm*.

Caves, R. E., & Caves, R. E. (1996). *Multinational enterprise and economic analysis*. Cambridge university press.

Chidlow, A., Wang, J., Liu, X., Wei, Y. (2021), A co-evolution perspective of EMNE internationalization and institutions: An integrative framework of 5Cs, International Business Review, Volume 30, Issue 4, 2021, 101843, ISSN 0969-5931,

Cintra, R. F., Cassol, A., Ribeiro, I., & de Carvalho, A. O. (2018). Corruption and emerging markets: Systematic review of the most cited. *Research in International Business and Finance*. https://doi.org/10.1016/j.ribaf.2017.07.177

Cuervo-Cazurra, A., & Dau, L. A. (2009). Promarket reforms and firm profitability in developing countries. Academy of Management Journal, 52(6), 1348–1368.

Cuervo-Cazurra, A., & Genc, M. (2008). Transforming disadvantages into advantages: developing-country MNEs in the least developed countries. *Journal of International Business Studies*, *39*(6), 957–979.

Dau, L.A., Li, J., Lyles, M.A. et al. (2022) Informal institutions and the international strategy of MNEs: Effects of institutional effectiveness, convergence, and distance. J Int Bus Stud 53, 1257–1281 (2022).

Djankov, S., La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. (2002). The regulation of entry. The quarterly Journal of economics, 117(1), 1-37.

Doh, J., Rodrigues, S., Saka-Helmhout, A., & Makhija, M. (2017). International business responses to institutional voids. *Journal of International Business Studies*.

Dolfsma, W., van der Eijk, R., & Jolink, A. (2009). On a source of social capital: Gift exchange. *Journal of Business Ethics, 89*(3), 315–329.

Dollar, D., Hallward-Driemeier, M., & Mengistae, T. (2005). Investment climate and firm performance in developing economies. *Economic Development and Cultural Change*, *54*(1), 1–31.

Donnelly, R., & Manolova, T. S. (2020). Foreign location decisions through an institutional lens: A systematic review and future research agenda. In *International Business Review* (Vol. 29, Issue 4). Elsevier Ltd.

Dunning, J. H., & Lundan, S. M. (2008). Institutions and the OLI paradigm of the multinational enterprise. *Asia Pacific Journal of Management*, *25*(4), 573–593.

Ernst, H., Kahle, H. N., Dubiel, A., Prabhu, J., & Subramaniam, M. (2014). The antecedents and consequences of affordable value innovations for emerging markets. Journal of Product Innovation Management, 32(1), 65-79. https://doi.org/10.1111/jpim.12171

Forstenlechner, I., & Mellahi, K. (2011). Gaining legitimacy through hiring local workforce at a premium: The case of MNEs in the United Arab Emirates. *Journal of World Business*, *46*(4), 455-461.

Halaszovich, T. F., & Lundan, S. M. (2016). The moderating role of local embeddedness on the performance of foreign and domestic firms in emerging markets. *International Business Review*, *25*(5).

Helmke, G., & Levitsky, S. (2004). Informal Institutions and Comparative Politics: A Research Agenda. *Perspectives on Politics*, *2*(4), 725–740.

Hennart, J. F. (2009). Theories of the Multinational Enterprise. In *The Oxford Handbook of International Business (2 ed.)*.

Hofmann, D. A., Griffin, M. A., & Gavin, M. B. (2000). The application of hierarchical linear modeling to organizational research. In *Multilevel theory, research, and methods in organizations: Foundations, extensions, and new directions*.

Hofstede, G. H. (1980). *Culture's consequences: international differences in work-related values*. *Cross-Cultural Research and Methodology series* (Vol. 41).

Holburn, G. L. F., & Zelner, B. A. (2010). Political capabilities, policy risk, and international investment strategy: Evidence from the global electric power generation industry. *Strategic Management Journal*, *31*(12), 1290–1315.

Holmes, R. M., Miller, T., Hitt, M. A., & Salmador, M. P. (2013). The Interrelationships Among Informal Institutions, Formal Institutions, and Inward Foreign Direct Investment. *Journal of Management*, *39*(2), 531–566.

Kafouros, M., Aliyev, M., Piperopoulos, P., Au, A., Ho, J., & Wong, S. Y. N. (2023). The role of institutional quality and industry dynamism in explaining firm performance in emerging economies. Global Strategy Journal.

Kafouros, M., Chandrashekar, S. P., Aliyev, M., & Ming Au, A. K. (2022). How do formal and informal institutions influence firm profitability in emerging countries? Journal of International Management.

Khanna, T., & Palepu, K. (1997). Why focused strategies may be wrong for emerging markets. Harvard Business Review, 75(4), 41–51.

Khanna, T., & Palepu, K. (2000). The Future of Business Groups in Emerging Markets: Long - Run Evidence From Chile. *Academy of Management Journal*, *43*(3), 268–285.

Krammer, S. (2019). Greasing the wheels of change: bribery, institutions, and new product introductions in emerging markets. Journal of Management, 45(5), 1889-1926.

Lavie, D., & Fiegenbaum, A. (2000). The strategic reaction of domestic firms to foreign MNC dominance: The Israeli experience. *Long Range Planning*, *33*(5), 651–672.

Lee, K., & Kim, B. Y. (2009). Both Institutions and Policies Matter but Differently for Different Income Groups of Countries: Determinants of Long-Run Economic Growth Revisited. *World Development*, *37*(3), 533–549.

London, T. and Hart, S. L. (2004). Reinventing strategies for emerging markets: beyond the transnational model. Journal of International Business Studies, 35(5), 350-370.

Luo, Y. (2007). From foreign investors to strategic insiders: Shifting parameters, prescriptions and paradigms for MNCs in China. *Journal of world Business*, *42*(1), 14-34.

Mair, J., & Marti, I. (2009). Entrepreneurship in and around institutional voids: A case study from Bangladesh. *Journal of Business Venturing*, *24*(5), 419–435.

Mair, J., Martí, I., & Ventresca, M. J. (2012). Building inclusive markets in rural Bangladesh: How intermediaries work institutional voids. *Academy of Management Journal*, *55*(4), 819–850.

Mbalyohere, C., & Lawton, T. C. (2022). Engaging informal institutions through corporate political activity: Capabilities for subnational embeddedness in emerging economies. *International Business Review*, *31*(2).

McCarthy, K. J., & Aalbers, H. L. (2016). Technological acquisitions: The impact of geography on post-acquisition innovative performance. Research Policy, 45(9), 1818-1832.

McGahan, A. M., & Victer, R. (2010). How much does home country matter to corporate profitability. *Journal of International Business Studies*.

Niu, B., Xie, F., Mu, Z., & Ji, P. (2020). Multinational firms' local sourcing strategies considering unreliable supply and environmental sustainability. Resources, Conservation and Recycling, 155, 104648.

North, D. C. (1990). Institutions, Institutional Change, and Economic Performance. *Cambridge University Press*, *5*(1), 1–153.

Oki, K. and Kawai, N. (2022), "Local sourcing and MNC subsidiary performance: a legitimacy perspective", Cross Cultural & Strategic Management, Vol. 29 No. 4, pp. 729-760.

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. (2017). Markets and institutional swamps: Tensions confronting entrepreneurs in developing countries. *Journal of Institutional Economics*, *13*(2), 243–269.

Pejovich, S. (1999). The Effects of the Interaction of Formal and Informal Institutions on Social Stability and Economic Development. *Journal of Markets & Morality*, *2*(2), 164–181.

Peng, M. W., Wang, D. Y., & Jiang, Y. (2008). An institution based view of international business strategy A focus on emerging economics.pdf. *Journal of International Business Studies*, *39*(5), 920–936.

Peng, M. W. (2002). Towards an institution-based view of business strategy. *Asia Pacific Journal Management*, *19*, 251–267.

Peng, M. W. (2003a). Institutional transitions and strategic choices. *Academy of Management Review*.

Peng, M. W. (2003b). Institutional transitions and strategic choices. *Academy of*

Management Review.

Peng, M. W., Sun, S. L., Pinkham, B., & Chen, H. (2009). The Institution-Based View as a Third Leg for a Strategy Tripod. *Academy of Management Perspectives*, *23*(3), 63–81.

Peng, M. W., Wang, D. Y. L., Jiang, Y., Peng1, M. W., Wang2, D. Y., Jiang3, Y., & Peng, M. (2008). An Institution-Based View of International Business Strategy: A Focus on Emerging An institution-based view of international business strategy: a focus on emerging economies. *Journal of International Business Studies*, *39*(39), 920–936.

Penrose, E. T. (1959). *The Theory of the Growth of the Firm*. Oxford: Basil Blackwell

Qiu, T., Zhang, D., Choy, S. T. B., & Luo, B. (2021). The interaction between informal and formal institutions: A case study of private land property rights in rural China. *Economic Analysis and Policy*, *72*, 578–591.

Rickley, M., & Karim, S. (2018). Managing institutional distance: Examining how firm-specific advantages impact foreign subsidiary CEO staffing. *Journal of World Business*, *53*(5), 740-751.

Rodrik, D. (2016). An African Growth Miracle? *Journal of African Economies*.

Rodrıguez-Pose, A. (2013). Do Institutions Matter for Regional Development? *Regional Studies*.

Sartor, M. A., & Beamish, P. W. (2014). Offshoring innovation to emerging markets: Organizational control and informal institutional distance. *Journal of International Business Studies*, *45*(9), 1072–1095.

Sauerwald, S., & Peng, M. W. (2013). Informal institutions, shareholder coalitions, and principal–principal conflicts. *Asia Pacific Journal of Management*, *30*(3), 853–870.

Scott, W. . (1995). *Institutions and organizations*. *Thousand Oaks* (Vol. 2).

Stinchcombe, A. L. (1965). Organizations and social structure. In *Handbook of Organizations*.

Tanzi, V. (1998). Corruption around the world: Causes, consequences, scope, and cures. Staff Papers, 45(4), 559-594.

Trebing, H. M. (1987). Regulation of Industry: An Institutionalist Approach. *Journal of Economic Issues*, *11*(4), 1707–1737.

Wei, S.-J. (2000). How Taxing is Corruption on International Investors? *Review of Economics and Statistics*, *82*(1), 1–11.

Wernerfelt, B. (1984). A resource-based view of the firm. *Strategic Management Journal*, *5*(2), 171–180.

Williamson, O. E. (1981). The Economics of Organization: The Transaction Cost Approach. *American Journal of Sociology*, *87*(3), 548–577.

Williamson, O. E. (2000). The New Institutional Economics: Taking Stock, Looking Ahead. Journal of Economic Literature, 38(3), 595–613. http://www.jstor.org/stable/2565421

Wu, X. and Zhang, F. (2014). Home or overseas? an analysis of sourcing strategies under competition. Management Science, 60(5), 1223-1240.

Xu, Y., & Yao, Y. (2015). Informal Institutions, Collective Action, and Public Investment in Rural China. *American Political Science Review, 109*(2), 371-391.

Zhou, J. Q., & Peng, M. W. (2012). Does bribery help or hurt firm growth around the world? *Asia Pacific Journal of Management*, *29*(4), 907–921.

4

Chapter 5

POLICY IMPERATIVES FOR ATTRACTING FDI FOR AGRO-INDUSTRIAL PROCESSING IN AFRICA

ABSTRACT

This paper examines the policy imperatives for attracting FDI and private capital for agro-industrial processing in sub-Saharan Africa. Drawing on institutional theory, we develop a seven-point policy framework that offers policy guard rails for policymakers, investors, and development practitioners. We adopt Dunning's OLI framework as the conceptual framework to understand the determinants for mobilising FDI and domestic private sector capital for agro-industrial processing in Africa. And posit that the absence or under-development of market-supporting institutions can explain why countries in Africa have not been able to replicate the experience of comparator countries in Asia. Given the global competition for FDI, by adopting a collaborative approach to developing and implementing agro-industrial processing zones, government policy can encourage foreign and domestic private firms to invest and integrate value chain activities within their host countries in recognition of the potential these special economic zones present to drive value through economies of scale and efficiencies. By reviewing successful implementations in other EMDEs, this paper provides valuable insights to promote agro-industrial processing as a catalyst for inclusive economic development in sub-Saharan Africa.

KEYWORDS

Industrialising Africa; FDI; Industrial Policy; Institutional Voids; Institutions; Special Economic Zones; Global Value Chains.

05. POLICY IMPERATIVES FOR ATTRACTING FDI FOR AGRO-INDUSTRIAL PROCESSING IN AFRICA

5

5.1. Introduction

This paper seeks to establish the policy imperatives for attracting FDI and domestic private capital to deepen agro-processing capabilities across the African region. It builds on the renewed interest in enhancing agri-food systems as a strategy to accelerate the goal of food security, creation of sustainable jobs, and harness the potential benefits of what the World Bank projects could become a $1 trillion market by 2030 (World Bank, 2020; AfDB 2023).

Policy imperatives refer to policy choices considered critical to establishing a specific programme. The 2nd Dakar Feed Africa Summit held in January 2023 established the transition from a primary focus on commodity exports to a more integrated value chain approach as a continued policy imperative for Africa.[6] If successful, this would translate to greater value addition across all aspects of the agro-value chain through a renewed focus on processing primary crops and livestock for food products and chemicals.

Yet, despite its apparent potential, outside of a few regional exemplars, Africa's agro-industrial sector has so far not made the significant contribution to economic transformation and sustainable development thought to be possible given the experience of comparator countries in Asia (FAO, 2017; AGRA, 2019). This is an indication of market failure brought about by market limiting constraints and inefficient allocation of scarce resources (Rodrik, 2004). This therefore presents the need for a policy response from governments across the region to address the constraints and facilitate the reallocation of resources to factors that attract the much-needed private sector capital, technology and agro-processing capabilities required to transform the sector and replicate the success of comparator countries in Asia (Newman et al.,

[6] See "Time for Africa to feed itself" African Business https://african.business/2023/02/resources/time-for-africa-to-feed-itself-dakar-2-summit-takes-africas-food-agenda-forward

2016; AGRA, 2022). This is of particular interest to policymakers across the region and the result of missing or ineffective market-making institutions, often referred to as institutional voids (Khanna & Palepu, 1997) in International Business literature.

These so-called institutional voids have undermined attempts by countries in Africa to mirror the success of comparator countries like Malaysia, Indonesia and Vietnam, who have successfully transitioned towards agro-sector industrialisation over the last 40 years (AGRA, 2019; Newman et al., 2016). By drawing on institutional theory, policymakers and researchers can analyse the institutional factors that hinder or facilitate investment in the agro-processing sector (Amin, Bell & Wang, 2020).

Institutional theory provides a theoretical framework for understanding how formal and informal rules, norms, and practices shape the behaviour and decision-making of organisations within a given institutional context (North, 1990; Scott, 1995). In the context of the agro-processing sector, this involves complex value chains and interactions between various stakeholders and institutional factors – particularly investment climate reforms, which play a crucial role in shaping investment dynamics (Newman et al., 2016).

Our approach to evidence-based policy formulation hence involves examining the role formal and informal institutions can play in providing the enabling industrial, logistical, and supporting infrastructure, access to financing, and facilitating knowledge transfer and technology adoption required to transform the sector.

The rest of the paper is organised as follows: Section 2 briefly sets out the theoretical rationale for industrial policy as a mechanism for reallocating productive resources to address market imperfections. It draws on the literature on institutional theory, FDI and Dunning's OLI framework. Drawing on a review of case study evidence from successful implementations, we examine the critical success factors and how these can be adopted successfully across the region. Section 3 introduces the concept of Agro-industrial Processing Zones – a type of special economic zone made popular in China that has served as a laboratory for structural reforms which have played a significant role in economic liberalisation and sustainable development more broadly (Zeng, 2016). In section 4, we set out a seven-point policy framework for improving the delivery and benefits realisation of agro-industrial processing zones across the continent. Finally, section 5 concludes with policy implications and recommendations for future research.

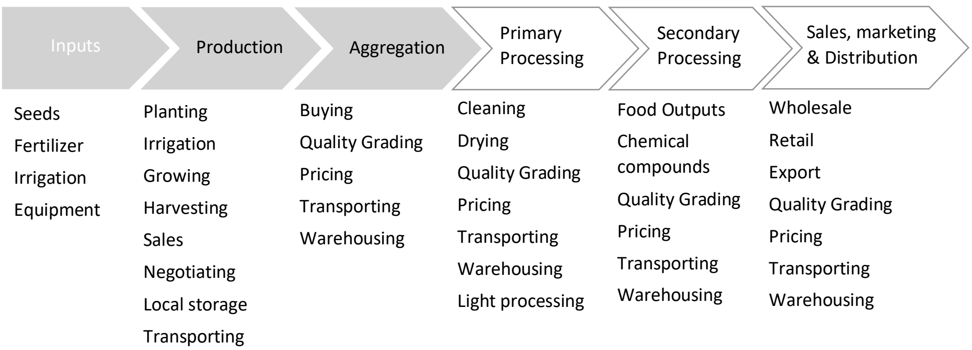
5.2. Industrial Policy as a mechanism for structural change and addressing market failures.

The challenge and opportunity for structural change in Africa's agro sector

Most countries in Africa have not been able to match the success of their contemporaries in East Asia in attracting the investment and know-how required to develop the agro-industrial processing and marketing capabilities that contribute to food security, participation in global value chains, and sustainable incomes for their people (OECD-FAO, 2016; FAO, 2017; AGRA, 2019).

The World Bank estimates that African agriculture could become a $1 trillion market by 2030 (World Bank, 2020). Despite this potential, from a value-chain perspective, African participation in agriculture is still mainly dominated by smallholder farmers specialising in a commodity mix of staple crops and primary exports, accounting for around 90 per cent of total output (Osabuohien, 2020).

Fig 5.1. Agricultural Value Chain



Source: Authors summary for illustration purposes only

As illustrated above (Fig 5.1), agricultural activities in most African countries primarily focus on producing and aggregating primary products. They are characterised by restricted production and market limiting conditions that result in high concentration in the production and aggregation components of the value chain, as well as high transaction and input costs and low incomes for predominantly smallholder farmers (Barett et al., 2012: Osabuohien, 2020).

The implication of this concentration in the input, production, and aggregation components of the agro-value chain is an over-reliance on imports for food and chemical compounds that could be produced domestically. This presents the clear commercial justification for investment in improved practices, storage, electricity access, transport and trade logistics facilities that could improve yields, reduce post-harvest losses and resilience against the impact of climate change, reduce transaction costs, and enhance the quality and grade of finished goods and commodities. It also raises the theoretical question of how the fragmentation of agricultural markets in Africa impacts the sectors' ability to address these market imperfections and whether this can be adequately achieved without targeted government intervention.

For example, it is estimated that 40% of food production across the region is impacted by post-harvest losses (FAO & AfDB, 2019) due to a range of factors, including poor transport, logistics and storage infrastructure, as well as weak market linkages for primarily smallholder farmers (Tadesse and Bahiigwa, 2015). Much of this could be addressed by investment in industrial (i.e., electricity, transport, storage, and logistics) infrastructure and the adoption and adaptation of best practice approaches from elsewhere – such as special economic zones, which serve as geographic enclaves where all the critical components that can support, facilitate, and attract private sector investment in industrial processing capabilities can be located (Zeng, 2015).

The fragmentation of agricultural markets in Africa affects farmers' ability to access price information, credit and inputs, and negotiate with buyers (Barett et al. 2012). Without access to the required capital, knowledge and expertise, smallholder farmers lack the resources to build the resilient infrastructure and know-how to respond to environmental factors such as drought, pests, and diseases, which significantly impact yields and profitability (Murendo et al. 2012). This market failure, characterised by the inefficient allocation of the resources required to address supply-side constraints that exist, combined with the fast-growing demand for food that is projected to double by 2050 due to rising population, urbanisation (AGRA, 2022; FAO, 2020; FAO and AfDB, 2019), and the devastating impact of climate change on yields and conflict, makes the transformation of Africa's agriculture a key policy imperative in the face of unprecedented existential threats to food security and sustainable development in the region (AGRA, 2022).

Institutional theory and Government's role in fostering structural change.

Institutional theory examines how institutions shape and influence the behaviour of economic actors through the 'rules of the game' (North, 1990) that are either established and enforced by government-backed institutions such as laws, regulations, government policy, etc. (i.e., formal institutions) or social conventions such as customs, traditions, and norms (North, 1990; Scott, 1995). Compliance with these formal and informal institutions which form the institutional configuration of host countries (Doh et al., 2017) tends to be critical to the legal legitimacy of actors operating within the country (Scott, 1995). This gives governments a unique opportunity to use policies, regulations, and laws to encourage or channel resources from one sector to another to foster structural change (Rodrik, 2008; Stiglitz, 2013; Mbate 2016).

5

The justification for industrial policy, therefore, rests on the premise that governments can drive economic development and facilitate transformative processes (Rodrik, 2004). This is relevant for EMDEs in Africa, where the potential for structural change to lead to economic growth and poverty reduction is considered significant (McMillan & Headey, 2014).

Structural change is the process of transforming the economic structure of a country or region, such as the sectoral composition of output and employment (Lewis, 1954; Kuznets, 1966), the level and distribution of income etc. (Rodrik, 2008; Acemoglu & Autor, 2011). It is often driven by technological change, market forces, globalisation, and environmental challenges (Rodrik, 2008), all of which have led to the transformation of the agro-sector in comparator countries in Asia and could be replicated in Africa (FAO, 2019).

Market failure and imperfect market mechanisms underlie the difficulties economies face in achieving goals such as efficient resource allocation and structural transformation without some degree of government intervention (Stiglitz, 2013; Chen & Xie, 2019). The market operation mechanism is not perfect as externalities, information incompleteness and asymmetry in the operation system of the market economy – particularly in low- and middle-income countries of Africa and Southern Asia consistently result in inefficient resource allocation and excess or insufficient production capacity (Hausmann and Rodrik 2003; Rodrik 1996; Stiglitz, 2013). By designing and implementing reasonable and practical industrial policies, market economy efficiency can be improved, and industrial structure can be upgraded and optimised, thus contributing to economic growth (Aghion et al. 2015).

By accelerating the transfer of resources (capital, labour, and knowledge) from low to high-productive sectors, industrial policy has the potential to promote and sustain inclusive economic growth. In doing so, governments can facilitate structural change and address constraints related to socioeconomic challenges (Mbate, 2016), such as poverty, unemployment, and lack of access to capital, markets, and opportunities.

Evidence from East Asia underscores the importance of commodity-based industrialisation as a viable channel for addressing poverty and unemployment (Mbate, 2016) and that new entrants can succeed in global manufacturing. Countries that add value to their natural resources and promote labour movement to productive sectors are associated with increased per capita income and technology accumulation (UNIDO & UNCTAD, 2011).

While this is yet to be replicated in the region, rising wages and input costs in Asia could offer Africa – the poorest region per capita – a renewed opportunity to industrialise, particularly in the labour-intensive, light-manufacturing sectors such as agro-processing (Newman et al., 2016).

Industrial policy can, therefore, effect structural change by creating or modifying institutions that help overcome market failures and coordination problems that hinder structural transformations by shaping the incentives and capabilities of firms and workers in different sectors (Rodrik, 2004). For example, governments can offer policy instruments such as subsidies, tax incentives, streamlined export and import processes where bureaucratic bottlenecks exist, credit guarantees, infrastructure development, research and development support, skills training, etc., to foster the emergence or growth of strategic sectors and hence provide incentives to foreign and private investors alike to invest locally in higher value agro-processing capabilities necessary to exploit the comparative advantages unique to the host community such as the availability of high priority crops, transport and industrial infrastructure.

The OLI Framework and the determinants for attracting FDI.

Recognised as a comprehensive framework for analysing the determinants of foreign direct investment (FDI) and the strategic decisions of multinational enterprises (MNEs), we adopt

Dunning's (1988) OLI framework as the conceptual framework to understand government policy responses for mobilising FDI and private sector capital more generally, for agro-industrial processing in Africa.

The framework identifies three main factors that attract FDI: ownership, location, and internalisation advantages.

- **Ownership advantages (O)** are the assets or specific capabilities or 'advantages' that MNEs seeking to invest in a foreign country possess that give them an edge over their competitors. These assets can include access to advanced technology, managerial expertise, brand reputation, capital or access to marketing and distribution channels. Such firms may exploit these capabilities and extend their reach by entering foreign markets to source necessary input resources such as land, labour, and commodities (i.e., resource seeking) or access new consumers for their products and services (i.e., market seeking). In order to achieve such outcomes, MNEs also need to be able to overcome the difficulties - so-called liabilities of foreignness, foreign firms typically face when trying to position their companies in new markets to gain acceptance and social legitimacy for their products and services. These same ownership advantages also make them attractive to governments seeking to attract investment capital and expertise and have been the key driver for adopting investment climate reforms and policies targeted at attracting FDI across the region.
- **Location advantages (L)** are the factors or specific attributes of the host country that make it attractive for FDI. These factors can include abundant and low-cost agricultural raw materials, proximity to target markets (both regional and international), supportive government policies, access to transport, industrial and logistical infrastructure, and a skilled workforce. For example, countries with comparative advantages in the production and availability of specific primary crops, and preferential access to large and growing consumer markets for agro-industrial products through trade agreements, may be attractive to foreign investors. Given the global competition for FDI, governments can use policy levers to develop or enhance the L advantages in their countries by prioritising the development of transport, industrial and logistic infrastructure, as well as streamlined export, import, company set-up and tax administration processes around specific areas where priority crops and inputs are abundantly available. To be successful, this requires

the institutional capacity to coordinate the implementation of government policy across multiple national and subnational agencies responsible for customs, transport, land, trade, fiscal and monetary policy.

- **Internalization advantages (I)** are the benefits MNEs gain from directly owning or controlling their operations in the host country rather than engaging in arm's length transactions. These benefits can include avoiding tariffs, protecting intellectual property, maintaining quality control standards, reducing transaction costs, gaining access to local knowledge and networks and tailoring products to local preferences by integrating various stages of the value chain within the country. Unlike O advantages which are endogenous to MNEs, I advantages are impacted by government policies that incentivise MNEs to set up local processing facilities, incorporate local companies in the supply chain, and promote knowledge sharing to leverage I advantages. This can be done by negotiating favourable trade agreements, providing protection for intellectual property, and ensuring that the legal system is fair and transparent.

Thus, by combining the OLI framework and institutional theory, policy makers can develop policy responses to attract FDI in the agro-industrial processing sector. For instance, by prioritising investments in critical industrial, transport and logistical infrastructure that enhance the L advantages associated with proximity to resource and labour inputs, and promoting or incentivising the development of the I advantages foreign need to access these incentives, African governments can create the conditions to attract foreign investors with relevant O advantages that enable them to compete favourably within the host country, while capturing some of the benefits associated with encouraging local participation and inclusive economic growth.

The global competition for FDI

EMDEs compete with OECD countries and countries in transition for FDI. Therefore, the competitive landscape for FDI should be an essential consideration for policymakers. FDI is seen to varying degrees as an important catalyst for economic development, income growth and unemployment. This is because there is evidence that in its efficiency (or resource-seeking) and market-seeking forms, FDI can serve as an important mechanism for the importation of much-needed capital, innovation, and has the potential for significant spillovers such as knowledge transfer and domestic capital accumulation – through the participation of local (or indigenous) companies in global value chains.

EMDEs often offer lower production costs, including cheaper labour and input resources. They may also have untapped consumer markets with significant growth potential. Where these assumptions hold, these cost and market access advantages can translate to L advantages that make them attractive to foreign investors seeking such opportunities.

Over the last twenty years, the importance of EMDEs as a destination for FDI has gradually increased, accounting for over 50% of global inward FDI in 2020 (UNCTAD, 2021). While this represented a slight increase in the previous year despite the overall decline of FDI flows due to the COVID-19 pandemic, FDI inflows to SSA declined by 27% to $28 billion (2020) to reach their lowest level in a decade.

The decline in FDI inflows to SSA was driven by several factors, including a sharp drop in global demand, lower commodity prices, travel restrictions, and supply chain disruptions. In addition, many investors adopted a wait-and-see approach, delaying investment decisions until the economic outlook became clearer. Despite the overall decline, some countries in SSA were able to maintain or even increase their FDI inflows during the pandemic. For example, Ethiopia and Kenya saw an increase in FDI inflows in 2020 thanks to investments in infrastructure, manufacturing, and services. In addition, some sectors, such as healthcare and technology, experienced a surge in investment, driven by the need to address the challenges posed by the pandemic.

FDI inflows to Africa have since shown signs of uneven recovery across the region, with FDI inflows on aggregate increasing by 15% in the first half of 2021 compared to the same period in 2020 (UNCTAD, 2022). For example, FDI inflows increased by 46%, while those to Central Africa declined by 57%. The recovery of FDI inflows to SSA, given the global competitive landscape for FDI, is likely to depend on a range of factors, including the pace of global economic recovery, the implementation of policy measures to support investment, and the ability of countries in the region to address structural challenges such as weak infrastructure and institutional capacity.

Market and efficiency-seeking MNEs can expand their global footprint by using their capital, knowledge, market access and superior global sourcing capabilities to either acquire large farms for commercial production of input crops or provide smallholder farmers with the know-how and support required to improve their yields and optimise the quality of their produce.

There is evidence that this happens regularly across the region, particularly in the global sourcing of tropical commodities such as cocoa and coffee for processing (Feyearts et al., 2020). The challenge to policymakers in sub-Saharan Africa, however, lies in the lack of progress in sustaining, at scale, the integration of higher-order value chain activities within host countries across the region, given the structural challenges, weak institutional frameworks, and inadequate infrastructure that have undermined the industrialisation agenda in Africa (Dinh & Clark, 2012; Newman et al., 2016).

Countries in sub-Saharan Africa, therefore, miss out as the competition for FDI is global. By their very construct, MNEs have the capabilities to source input crops from one country for processing in another (as well as sales to end customers in multiple others), with market conditions that enable them to produce cheaper, more reliably and to the quality standards that match their production standards as expected by their end customers and (Lee et al., 2023). This is increasingly prevalent as digital technologies present virtual entry modes such as firm-specific websites or trade platforms such as Ali Baba or Amazon that enhance import or export opportunities, as well as enable instant communication and the collection and analysis of large volumes of data, thereby enabling remote management of operations across multiple geographic locations (Meyer et al., 2023).

Due to limited resources and implementation capacity, EMDE governments often cannot create the business environment or build enabling infrastructure nationwide all at once (Feng & Wang, 2016). In addition, EMDEs often have limited political capital to defend policies and reforms against vested interest groups and political opposition (Zeng, 2015b). This makes targeted interventions or a pilot approach necessary.

Lessons from Successful Government interventions in transforming agro value chains.

Many economists believe Special Economic Zones (SEZs) can be adopted to achieve industrial development efficiently and effectively (Lin & Monga, 2011). In particular, investing in SEZs can provide a bundling of public services in a geographically concentrated area; improve the efficiency of limited government budget allocations for infrastructure, facilitate cluster development or agglomeration of specific industries; and enhance urban development by providing facilities conducive to improved living conditions for both basic wage workers and highly skilled technical workers (Feng, 2016), taking advantage of economies of scale in the provision of industrial infrastructure and environmental services, such as electricity, transport networks, water treatment plants and solid waste treatment plants.

In the following section, we draw on case study evidence from a selection of successful SEZs in the agricultural sector, which we summarise in Table 1 below. Our analysis identifies 5 key factors - a) implementation of effective policy frameworks, b) provision of critical infrastructure, skills development, technology adoption and innovation, c) Trade and Market linkages, and d) public-private partnerships – encapsulating factors which also align with theoretical and conceptual frameworks related to agro-industrial development, FDI, and Investment facilitation (Smith et al., 2020; UNCTAD, 2020).

Drawing on Dunning's OLI framework, we can analyse and assess the policies and measures policy makers can adopt to support the development and implementation of agro-industrial processing zones as a mechanism to attract FDI in the agro-industrial processing sector, given their potential to focus limited government resources in creating environments conducive for investment.

This involves examining how MNEs can leverage their O advantages to capitalise on L advantages in host countries. And how government policies can be used to develop and enhance their L advantages and incentivise MNEs to develop I advantages by setting up their operations in the host countries to maximise efficiency, adaptability, and spillover opportunities to local communities from increased foreign and private capital investment.

Case selection

Several case studies were identified from a literature review search using keywords such as "successful SEZ implementations in developing economies" and successful SEZ implementations in emerging economies" with the results analysed. Cases used were selected based on comparability and availability of sufficient information to draw inferences that could be useful for drawing out key lessons from the successful implementation of agro-industrial zones, as evidenced by successfully attracting FDI and the transformation of the agro-industrial sector.

We conduct a comparative analysis of different policy approaches and their outcomes by reviewing cases from comparator countries. This allows for a broader understanding of the factors that contribute to success in attracting FDI and private capital in the agro-industrial processing sector. Our case selection provides real-world examples that allow us to evaluate practical insights and render policy recommendations rooted in actual policy experiences, as summarised in Table 5.1 below.

We discuss the limitations of this approach in the conclusion but retain their use in drawing out from practice critical success factors for developing special agro-industrial processing zones. By understanding these success factors from successful SEZ implementations, policymakers in African countries can gain valuable insights into developing their agro-industrial processing zones.

Table 5.1 Key Success Factors for Delivering Successful Agro-industrial Zones.

Key Success Factors	Authors	OLI Framework	Key insights
Effective Policy Frameworks	Smith et al., 2020	L & I advantages	Thailand, Vietnam, and Malaysia have implemented proactive policies and regulatory frameworks that support the establishment and operation of agro-industrial processing zones. These policies include investment incentives, streamlined administrative procedures, as well as the provision of infrastructure tailored to the needs of agro-industrial enterprises.
Provision of Critical Infrastructure	Hanh, 2019	L advantages	Developing specialised industrial infrastructure, including logistics networks, transportation systems, reliable electricity supply, and research and development facilities, has been crucial in attracting FDI and promoting agro-industrial activities.
Skills development, Technology Adoption, and Innovation	Rajalahti, 2021	O, L & I advantages	Southeast Asian countries have emphasised technology adoption and innovation in their agro-industrial processing zones. By integrating advanced technologies, including automation, precision agriculture, and biotechnology, these zones have increased productivity, improved product quality, and enhanced value addition.
Trade and Market Linkages	Ketudat, 2021, Akimova et al., 2016	L & I advantages	Governments have partnered with international organisations to provide market access support to agro-industrial enterprises.

Public-Private Partnerships	Ketudat, 2021, Akimova et al., 2016	O, L & I advantages	Collaboration between public, private, and other stakeholders has played a significant role in the success of agro-industrial processing zones. Governments have partnered with industry associations, research institutions, and international organisations to provide technical assistance, market access, and capacity-building support to agro-industrial enterprises.

Malaysia: Northern Corridor Economic Region (NCER)

The Northern Corridor Economic Region (NCER) was launched in 2008. It is one of the five economic regions established by the Malaysian government to drive economic development and growth in specific areas of the country; and forms part of Malaysia's larger national development agenda. It is in the northern part of Peninsular Malaysia and covers the states of Perlis, Kedah, Penang, and Northern Perak.

5

As part of the government's efforts to promote balanced regional development and boost economic activities in less developed areas, the NCER attracted investments worth about RM113billion and created 103,6000 jobs in the region in the first phase (Athukorrala & Narayanan, 2018). Its success has contributed to the country's overall economic growth and regional development, contributing to an annual growth rate of 5.8% of the combined GDP of the four states between 2010 and 2014, compared to 3% between 2005 and 2009 (Malaysian Digest 2017).

The NCER builds upon Malaysia's strong agricultural base by providing comprehensive infrastructure, supportive policies, and access to global markets to develop agro-commodity clusters, including palm oil, rubber, and fisheries, through the establishment of integrated agro-industrial complexes (UNCTAD, 2020). For example, the NCER was conceptualised to address the critical challenges of poor industry-supporting infrastructure, including transportation networks, utilities and energy supply that can hinder the movement of goods and services, those attempting to this market-limiting constraint into a clear L advantage.

Addressing the skills gap by working with various education and research institutions to align education and training programmes with industry needs was also a vital issue to be tackled, as was the creation of the Northern Corridor Implementation Authority to collaborate with various government agencies, private sector stakeholders and local communities to ensure the coordinated and effective planning and implementation of projects and initiatives within the region. These policies were implemented to increase the availability of workers with the skills relevant to the sector and encourage foreign and local investors to establish processing capabilities in the region.

These factors have combined to attract significant investments from foreign agri-business investors such as Wilmar International Limited, a Singapore-based company that is one of the world's largest palm oil producers and traders, which has invested in various plantations, refineries, and downstream industries in the NCER; Cargill, a US-based company that is one of the world's largest agri-food corporations, which has invested in poultry farming, animal feed production, and palm oil processing; Charoen Pokphand Group, a Thailand-based conglomerate that is one of the world's largest agri-businesses, that has invested in aquaculture, animal feed production, and food processing.

Other foreign investors who have invested in the region include the Louis Dreyfus Company. This Netherlands-based company is one of the world's largest commodity traders. It has invested in rice milling, sugar refining, and biofuel production in the NCER and Singapore-based Olam International Limited, which has invested in cocoa processing, coffee trading, and spices sourcing.

By investing in infrastructure, human capital, economic diversification, tourism promotion, agro-industrial processing and industrial and services development, the NCER's focus on attracting both domestic and foreign investments was supported by a range of tax incentives, investment allowances, customs and duties exemptions, and one-stop centres to assist companies in obtaining necessary licenses, permits and facilitate business setup and operations. These have encouraged investors to develop the 'I' advantages required to secure access to the enhanced 'L' advantages unique to the region. Additionally, collaboration between public and private stakeholders has played a significant role in providing technical assistance, market access, and capacity-building support to agro-industrial enterprises.

5.3. Agro-industrial processing zones as a vehicle for attracting market-seeking FDI in agro-value chains.

About $150bn is required annually to sustain food production in Africa, less than half of which can be supported by the public sector (AGRA, 2022). This shortfall in investment requires

African governments, the private sector and development partners to work together to accelerate the transformation of agrifood systems. It also acknowledges the need for a collaborative and participatory approach to policymaking to achieve the shifts in orientation and resource mobilisation necessary to influence sustainable change. This requires the removal of barriers to trade and agricultural development across the continent aided by new investments committed to developing critical value chains in food production, value addition and distribution (AfDB, 2023).[7]

Compared to half and three-fifths in developing Asia and the Pacific, agro-industrial processing currently accounts for less than a sixth of African agricultural production (AfDB, 2023). Consequently, the value-added agri-business to primary production ratio in SSA has remained the lowest in the world at 0.6 compared to 5 in Latin America. This is evidence by the steady decline over the past four decades from about 25 per cent of GDP in 1980 to about 17.5 per cent in 2018 (AfDB, 2021).

The African Union's Comprehensive Africa Agriculture Development Programme (CAADP) calls for a pan-African planning and policy framework for agricultural transformation and increased public investment in the sector, with food security, rural job creation and poverty reduction identified as key objectives.

A growing number of studies have identified concrete opportunities for Africa to attract agro-industrial and light manufacturing industries (Dinh et al. 2012; Fine et al. 2012; Newman et al. 2016; Oqubay 2015). These studies also provide answers to the question of where in Africa new policies to attract and promote manufacturing industries have started to get hold – in Ethiopia, Mauritius, Rwanda, and on a much smaller population base: Botswana and Namibia, to mention a few (FAO, 2019).

For example, Ghana has implemented policies to address post-harvest losses, including establishing a National Food and Agriculture Extension Programme, developing post-harvest handling technologies, and promoting public-private partnerships to improve infrastructure. Rwanda has also made significant progress in reducing post-harvest losses through a

[7] Lenin Ndebele, Feed Africa Summit: Continent plans to achieve zero hunger by 2030. See https://www.news24.com/news24/africa/news/feed-africa-summit-continent-plans-to-achieve-zero-hunger-by-2030-20230124

combination of policies and investments. The country has implemented a national strategy to reduce post-harvest losses, which includes the development of storage facilities, transport infrastructure, and processing facilities, as well as the promotion of value-added products to increase the value of agricultural produce.

Ambitious industrial plans remain futile in countries where economic fundamentals are not in order. Yet, structural change and employment creation have remained limited even in African countries that have made considerable headway in the World Bank’s Doing Business and the World Economic Forum’s Competitiveness rankings (DCED, 2013). Therefore, structural industrial policy beyond these horizontal approaches is freshly required, particularly in Africa, where the opportunities and the needs are as significant as they are urgent.

Lessons can also be drawn from how other EMDEs have addressed these challenges. For example, investments in transport connectivity, such as roads, railways, and ports, to support efficient transport and trade. Technologies and techniques have also been developed to improve post-harvest handling and storage, such as refrigeration and controlled atmosphere storage (FAO, 2019).

Upgrading the base infrastructure required to achieve similar outcomes requires significant investment and know-how. While governments have a key role to play, the potential exists to facilitate FDI, technology and techniques from other regions. Central to this is improving the investment climate (FAO, 2019) and a key policy lever for policymakers to embrace and implement as an ever-more conducive business and investment climate. The challenge remains how to achieve this in a way that is sustainable and extends beyond multiple political cycles and parties. Successful interventions must also be capable of scaling the challenge of policies and regulations that actually get implemented, enforced, and evaluated to establish effectiveness and impact.

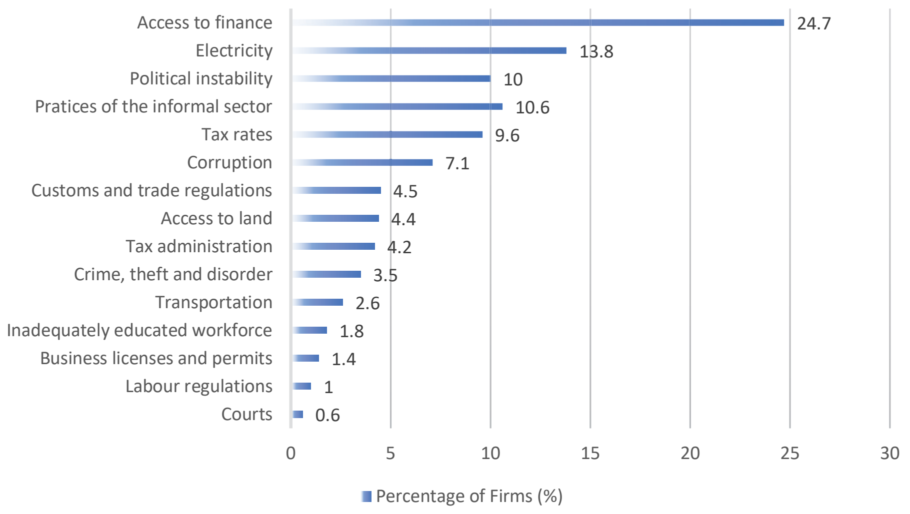
This has implications not just for the design and availability of investor-friendly policies such as tax credits, custom duty waivers, and access to concessional lending for priority sectors that balance the need to provide an incentive with the need to ensure that the government ability to generate revenues from taxes are not unduly depleted. It also affects the quality of institutions and institutional arrangements that govern the sector as required to decrease market failures caused by externalities and imperfect market mechanisms to improve resource allocation efficiency and promote industrial development (Wei & Zuo, 2018).

Next, we consider the concept of Agro-industrial Processing Zones, a type of SEZ focussed on developing domestic processing capacities for agro-clusters of priority crops that draw on the comparative advantages of host communities and how they can serve as a mechanism for testing out investment climate reforms that if successful could be applied more broadly to inform sector-wide reforms.

SEZs as a laboratory for investment facilitation and economic reform

Since the 1990s, in recognition of the binding constraints firms operating particularly in the manufacturing sector, face in doing business in Africa (Newman et al., 2016), policies aimed at promoting industrialisation across the region have focused on reform of the investment climate as well as the physical, institutional and policy environments in which firms operate (Mbate, 2016; Newman et al., 2016). Their success, however, has not matched the experience of their East Asian peers (FAO, 2019).

Figure 5.2: Top obstacles faced by businesses in sub-Saharan Africa (2023)



Source: World Bank Enterprise Survey (2023)

Newman et al. (2016) examine several reasons why African countries can reasonably aspire to break into the market for industrial goods by capitalising on economic and policy shifts in Asia, by focussing on areas – such as agro-industry suited to their natural endowment of factors, skills, and capabilities. This said, whether countries in the region can capitalise on the opportunities presented by rising costs and growing demand in China and Asia more generally, to capitalise on their comparative advantages in the agro-processing sector, will depend on whether governments can act decisively to address the key constraints (i.e. inadequate access to critical infrastructure, weak institutions as reflected in political instability, corruption, etc.) firms continue to face across the region (see figure 5.2).

The limited resources and delivery capacity of governments to address the observed binding constraints that undermine the productivity and competitiveness of African industry discussed earlier, present the rationale for targeted interventions like SEZs.

SEZs typically provide a mechanism for the bundling of quality public services and infrastructure in a geographically concentrated area, delivering input cost efficiencies, relatively higher economic impact and returns from government investments in infrastructure. This has the impact of facilitating cluster development or agglomeration of specific industries, and key economic linkages arising from job creation and participation of local firms in the supply chain (Feng, 2016). In essence, SEZs could prove effective where market failures or binding constraints (Rodrik, 2004) cannot be addressed through countrywide reforms, sector-wide incentives or universal approaches due to funding constraints or limited political capital to sustain and enforce reforms.

Various studies (Madani, 1999; Cling and Letilly, 2001; FIAS, 2008; Zeng, 2010; Farole & Akinci, 2011; Fuller & Romer, 2012) have shown that SEZs are typically established to achieve one or more of four policy objectives: a) attract foreign direct investment and promote export-oriented industrialisation; b) alleviate large-scale unemployment; c) support a more comprehensive economic reform strategy; and d) act as designated test environments for the application of new economic, environmental and investment policies that if successful could be more widely applied.

Thus, as conceptualised, SEZs can contribute to job creation and income generation, environmental protection, and promote green growth and eco-friendly cities (Lin and Wang, 2014). At their best, SEZs create a better business environment in a geographically defined area through a more effective legal and regulatory framework, efficient public services, and better infrastructure within the zone, including better roads, power, water, and wastewater treatment (Aggarwal, 2019). This concept of pursuing limited locational upgrading within an SEZ relies on attracting foreign firms with specific capabilities that can leverage the comparative locational advantages of the host communities where the SEZ is located (Narula & Zhan, 2019).

In practice, however, the results of SEZ programmes in different countries are mixed. Narula & Zhan (2019), in their review of research and background papers that fed into UNCTAD's World Investment Report 2019, observe that the immediate net benefits of SEZs, such as employment, capital flows and technology flows, are often modest, and when considering the costs of infrastructure upgrading, foregone customs revenues, subsidies and incentives, etc., the net benefits could be negative (Jayanthakumaran, 2003; Cirera & Lakshman, 2017; Alkon, 2018). They conclude that SEZs can act as important catalysts to kickstart larger and more pervasive benefits to the broader economy. Through these mechanisms, they accrue longer-term benefits of SEZs.

Some scholars, however, view SEZs as a suboptimal strategy or second or third-best option for development. Engman et al., 2007 contend that SEZs benefit a few and distort resource allocation. Others believe the zones' success is confined to specific conditions over a limited time horizon (Hamada, 1974; Madani, 1999). Some studies have found SEZs to be welfare-reducing (Chen, 1995; Hamada, 1974; Hamilton & Svensson, 1982; Wong, 1986), with a tendency towards becoming "enclaves" (Kaplinsky, 1993), with limited beneficial impact outside the zones.

This is contrasted by research that shows that overall social welfare may be improved under certain conditions, such as by attracting foreign direct investment and enhancing export diversification (Alder et al., 2013; Jenkins et al., 1998; Miyagiwa, 1986; Wang, 2013).

Empirical research shows that many SEZs have attracted foreign direct investment, generated jobs and exports, and demonstrated a marginally positive cost-benefit effect (Chen, 1994; Jayanthakumaran, 2003; Monge-Gonzalez & Monge-Arino, 2005; Warr, 1989; Zeng, 2010; Fuller and Romer, 2012).

Given the mixed results observed by researchers, it is, therefore, worth exploring further the conditions that support the successful implementation and benefits realisation from SEZs, which remains the focus of this paper in what follows.

Expected benefits from the successful implementation of SEZs

Building on 50 years of observation and analysis of mixed results, Aggarwal (2019) concludes that successful zones adopt a "holistic" or "systematic" approach. To succeed, special economic zones must be adapted to the host country's specific situation and build on its comparative advantages and endowments.

The basic economic model for establishing SEZs highlights the potential for spillovers to the local economy. Hamada (1974) notes that there may be externalities or learning effects for domestic, non-zone-based firms, which may become more efficient after introducing foreign investment. SEZs may also affect the welfare and labour markets of the local economy. Case studies have highlighted the spillover effects of establishing SEZs (Creskoff & Walkenhorst, 2009). Positive spillover effects can come in the form of enhanced economic productivity, newly available technology, and local social welfare effects on the domestic population (FIAS, 2008; Wang, 2013; Ge, 1999).

If implemented successfully, SEZs confer two main types of benefits: Firstly, the "static" or "direct" economic benefits such as employment generation, export growth, government revenues, and foreign exchange earnings. As well as the more "dynamic" or "indirect" economic benefits such as skills upgrading, technology transfer and innovation, economic diversification, and productivity enhancement of local firms (Zeng, 2010), which are harder to achieve unless the zones are very successful.

Having a long-term vision that transcends multiple political cycles is particularly important because economic transformation can take decades. In this regard, policymakers need to promote synergies and coordination among the different players – including private sector players, financial institutions, donors, and government agencies. As exemplified by Malaysia's Northern Corridor Implementation Authority, to be successful, this needs to be superintendent by a government agency empowered to operate and coordinate across government departments and agencies as required to deliver all associated government services and approvals necessary for the efficient and smooth running of the zone (e.g. one, stop shop proving company and tax registrations, import, export, operating licences, permits, approvals, etc.)

Lessons from successful case studies

Visitors to China in the mid-1970s and early 1980s were shocked by the same constraints Sub-Saharan Africa faces today (Chen & Xie, 2019). Other low and middle-income economies, such as Malaysia and Vietnam, have also managed to expand production and exports of light manufactured goods while grappling with the same constraints currently observed in sub-Saharan Africa.

5

Central to this success has been the implementation of effective policy frameworks that facilitate and attract private sector investment, infrastructure development that improves connectivity and reduces input costs, and a public-private partnership approach to the development, management and operation of Agro-industrial Processing Zones (Smith et al., 2020).

While there is limited specific research on such Agro-industrial processing zones, the concepts and experiences from SEZs we examine in this section, and the lessons we draw from successful case study evidence in section 2 can be applied to understand their potential impact, as follows:

(a) **Reducing input costs through economies of scale:** As outlined above, agro-industrial processing zones can serve as concentrated hubs for agro-processing activities, co-locating or linking agricultural production with primary and post-processing facilities. This has the added advantage of significantly reducing the transport and logistics costs that constitute a significant proportion of the cost of production. It can also improve supply chain efficiency and create the potential for collaboration and knowledge-sharing amongst businesses in the same agro-cluster. Facilitating the location of these processing capabilities near where the priority feed crops are produced must be entrenched in national development strategies and implementation plans developed by national planning institutions and agencies consulting across multiple stakeholders. This requires the capacitation of these institutions to perform these functions as well as the allocation of funding and resource support for the development and delivery of physical, digital and logistical infrastructure and critical public services (e.g., supply of fertilizers, irrigation, access to trade finance and agricultural extension services for smallholder farmers) necessary to ensure uninterrupted access to quality inputs and consumer markets.

(b) **Priority access to critical infrastructure:** Access to critical transport, logistical and industrial infrastructure, such as reliable electricity, transportation networks, cold and ambient storage facilities, and water and waste management systems, continues to pose a massive challenge in many African countries. This also increases the operating costs of firms who have to fill this void by providing or augmenting services that in other countries would have been delivered by competent third parties (Doh et al., 2017). Agro-industrial zones are designed to provide these as shared services and facilities, and as such constitute a targeted intervention by governments to address constraints in the wider economy and enhance the locational advantage of these zones. By providing access to modern processing facilities and technologies, agro-industrial zones can transform raw agricultural products into higher-value processed products cost-effectively, improving market competitiveness. At scale, shared infrastructure such as reliable power supply, water and waste management systems, provided at such industrial zones, could be delivered relatively quickly at a relatively low per unit cost, reducing the need for individual businesses to deploy considerable capital to provide these themselves (outside of the special economic zone) in countries where access to electricity and critical industrial infrastructure continue to be a challenge. Careful thought needs to be given to the institutional arrangements that need to be in place to oversee the development and implementation of integrated infrastructure masterplans critical to the successful operation of proposed zones – including the coordination of roles and obligations of a wide array of public, private and multilateral stakeholders (see Table 5.2).

(c) **Priority market access and trade:** Systemic constraints such as poor product quality and production standards, lack of quality systems and controls, price competitiveness of substitutes arising from cheaper imports and higher input costs for domestic production, as well as international restrictions and trade barriers remain some of the critical factors that limit access to market for finished products. Tackling this is central to the success of agro-industrial processing zones. Addressing these barriers requires multiple actors, government, private sector, multilateral institutions, donors, and regional institutions working together. Specifically, government-backed institutions can play a central coordination role through a mix of policy, advocacy and facilitation to a) negotiate and establish trade agreements with other countries or regional blocs to secure preferential market access from products originating from agro-industrial processing zones b) develop and build capacity around enforcing technical and quality standards that align with international standards for product quality, safety and ESG compliance c) provide market intelligence on consumer market trends, export market opportunities and linkages that enables businesses to make informed decisions to identify potential markets for their products d) establish commodity exchanges that provide smallholder farmers with technical support and guarantee off taker agreements for their produce e) streamline customs procedures and reduce bureaucratic processes for relevant licenses, permits and applications (e.g. through pre-packaged SPVs with relevant permits or one-stop shops) f) access concessionary loans and other trade and export finance instruments to support working capital, promote technology adoption and innovative approaches.

5

(d) **Additional spillover effects from knowledge and skills transfer:** The most significant critique of SEZs is their inability to deliver the expected benefits of job creation and distribution of value created outside the 'enclave' of the geographic zone (Kaplinsky, 1993). Government-backed institutions can use a mix of targeted policies, capacity building and incentives to a) encourage operators and tenants of the agro-industrial zone to establish linkages with local businesses b) facilitate collaboration with park operators, research and educational institutions and industry associations to design and implement training programmes tailored to the needs of the agro-industrial sector. c) promote collaboration and research partnerships between operators, research institutions that can facilitate the exchange of knowledge, innovation and technology adoption, adaptation, and advancement. d) prescribe and enforce contractual obligations for local sourcing, supply chain development, and employment to promote technology transfer, skills development, local embeddedness, and community stakeholder buy-in and support. e) actively promote the development of agro-industrial clusters around areas with comparative advantage in priority crops; and, by so doing, create a thriving, sustainable ecosystem centred around shared industrial infrastructure, knowledge exchange, commitment to high standards, market access and access to high-quality, cost-effective inputs. F) establishing robust monitoring and evaluation mechanisms to assess the impact of agro-industrial processing zones on additional spillover effects from knowledge and skills transfers. Regular assessments can help to identify gaps and challenges, enabling governments to refine policies and interventions accordingly.

The level of political will, institutional delivery capacity, policy congruency, stability and institutional alignment required to deliver these observed benefits from the successful implementation of SEZs cannot be overemphasised. For countries where the institutional furniture is considered weak or underdeveloped, governments can introduce and empower coordinating agencies such as Malaysia's Northern Corridor Implementation Authority, which is dedicated and empowered to collaborate with various stakeholders to ensure the coordination and effective planning and implementation of projects and initiatives necessary to create a conducive business environment that will attract and sustain investment in the zone.

5.4. Towards a new policy framework for promoting and improving the delivery of special agro-processing zones in Africa

Theoretical foundation for a new approach to policy formulation

In his review of the global experience of special economic zones, Feng (2016) concludes that investing in SEZs can: a) provide a bundling of public services in a geographically concentrated area; b) improve the efficiency of limited government funds/budgets for infrastructure; c) facilitate cluster development or agglomeration of specific industries; and d) enhance urban development by providing facilities conducive to improved living conditions for both basic wage workers and highly skilled technical workers, taking advantage of economies of scale in provision of environmental services, such as water treatment plants and solid waste treatment plants.

The challenges faced by governments in achieving these outcomes in sub-Saharan Africa, compared to their East Asian peers lies at least in part to their differences in the institutional environments (McGaughey et al., 2016) that make investments in manufacturing capabilities less favourable due to relatively higher input and transaction costs caused by the absence or under-development of formal market-supporting institutions (Doh et al., 2017).

Farole (2011) find that apart from Mauritius and partial success in a few regional exemplars, most African special export zones have failed to attract significant investment, promote exports, or create sustainable employment. The causal factors they ascribe to the failure of these schemes provide evidence of poor or weak formal institutions considered synonymous with African countries – notably, lack of physical or social infrastructure, regulatory uncertainty, policy instability, weak implementation capacity, or lack of institutional alignment or coordination (Farole & Moberg, 2017).

Governments of African countries often lack the know-how, resources, funding, or implementation capacity to execute projects at a scale that matches their needs or ambitions, particularly in the face of fiscal constraints and competing priorities. This manifests as poor, underdeveloped or weak formal institutions, which can be reflected in multiple points of failure in different aspects of their mission: regulatory, monitory, enforcement, protection and incentivisation (Do et al., 2017). Such failures impact firms adversely and are often referred to as evidence of institutional voids.

The characterisation of this phenomenon as suggesting an institutional vacuum exists where formal market-supporting institutions are absent or under-developed having played a dominant role in the IB literature over the last two decades, has increasingly been challenged by scholars who recommend a more nuanced investigation of the rich interplay between informal and formal institutions in emerging markets (Olthaar et al., 2017, Doh et al., 2017; Bothello et al., 2019; Olusina Daniel et al., 2019).

This is a characterisation that I have also sought to examine empirically in Chapter four of this thesis, which, for instance, finds that in the sample of African countries, local sourcing and senior management effort/time spent on regulations (used as proxies/measures for informal institutions) serve as substitutes for low-quality formal institutions, while bribes or informal payments, which are perhaps more acceptable in certain countries (Krammer, 2019) are seen as complementary to high-quality institutions. This provides empirical support for Doh et al.'s (2017) recognition that the absence, weakness, or failure of market-supporting institutions does not always suggest a vacuum. In their review of the extant literature, they find that much of the literature on how firms respond to so-called 'institutional voids' has focussed on a) how firms adapt their business model to local conditions by internalising functions that external intermediaries would have otherwise delivered b) shaping or altering their business environment or c) avoiding or exiting the environment altogether.

However, it is achieved, addressing the impact of so-called 'voids' comes at a cost. For example, foreign (as well as domestic) investments in Africa can include the need to incorporate the cost of providing infrastructure and education programmes for employees that would otherwise be provided by government or other third parties in different regions (Van Dijk, 2009; Boddewyn & Doh, 2011). One notable alternative strategic approach for mitigating the impact of absent or weak formal institutions seen in literature includes geographic clustering, where favourable institutional conditions can be created at the microcosmic level (Lundan, 2012).

This rationale informs a key feature of successful SEZs, regarded as demarcated geographical areas, where the institutional regimes are different from those that prevail in the national territory and offer advantages to investors in terms of infrastructure, special customs regimes such as duty-free import and export, special regulatory regimes, and a range of fiscal incentives (Farole & Moberg, 2017).

We contribute to this discussion by extending and applying the concept of the co-evolution of institutions to how policymakers can work with investors (Doh et al., 2008; Cantwell et al., 2010; Ge et al., 2019) and other actors to address the impact of poor, weak or under-performing institutions in the agro-industrial processing sector. And in doing so, establish a seven-point framework for improving the delivery of agro-industrial parks in Africa.

We take the view that the chronic under-resourcing and fiscal pressure faced by African governments, made worse by the COVID-19 pandemic, calls for a collaborative approach to policy formulation and implementation. This is particularly relevant for specific economically viable sectors that can be managed and operated by the private sector, that through initial pilot pro-market reforms, can see the government transition from active owner, promoter, developer, and operator role to playing a facilitator role (Frye & Shleifer, 1997; World Bank, 1995) such as in the development of agro-industrial processing zones.

This partnership model can be used to test a new approach to industrial policy formulation that would a) be a direct attempt to mitigate against evident underdevelopment or weakness of existing formal institutions while reducing or eliminating the effectiveness or need for informal norms such as bribes to grease the wheel for the timely delivery of government services such as access to electricity, permits and licenses (Krammer et al., 2019) b) invite willing collaborators across the foreign and domestic private sectors, DFIs and donor communities to pilot a new approach to cross-sector collaboration, and c) establish the evidence base for broader homegrown institutional reforms that could potentially address or eliminate the impact of weak or underdeveloped formal institutions while reducing or eliminating the efficacy of bribes or other corrupt practices that serve to substitute for weak or underperforming formal institutions.

These arrangements should be perceived and executed as a deliberate attempt by governments to address the impact of so-called institutional voids evident in the wider population within these zones in a way that reduces uncertainty, promotes policy stability, and reduces the costs of arms-length transactions through the proper functioning on market-supporting institutions within the zone.

Adopting a multi-pronged strategic programme of interventions.

Aggarwal (2005) finds that establishing a successful SEZ programme is a complex undertaking that requires more than removing a few obstacles. To succeed, all obstacles (across the value chain) to facilitating trade and investment in the country must be removed simultaneously. This has implications for the number, scale and scope of projects that can be supported, given the need to size projects at a level that matches not only the market demand for such facilities but the capacity of the government to deliver on its obligations as a facilitator through the instrumentation of policy, advocacy, trade diplomacy and incentives that if successful in these locations, could provide a template for scaling such approaches and interventions more broadly.

While not attempting to be exhaustive, in what follows, we draw on case study evidence from section 5.2 to identify four critical success factors for industrial zones in EMDEs, notably – access to industrial land and critical infrastructure not readily available outside the zone, cost reduction through economies of scale derived from a shared services model for industrial, storage and logistics infrastructure, priority market access, and the achievement of additional spillovers through knowledge and skills transfer.

In the context of African economies where a key motivation for establishing SEZs is to pilot legal, regulatory and investment promotion reforms not widely applicable in the host country, maximising the benefits of SEZs depends on the degree to which they are integrated with their host economies and the national trade and investment reform agenda. Establishing these linkages in the design and operationalisation of the schemes, as we have discussed in section 5.2, is critical to the success of such schemes.

Dinh et al. (2012) identify six binding constraints that work against the competitiveness of light manufacturing in Africa; i) input costs and quality (i.e. transport, electricity, and input materials or feedstock) ii.) access to industrial land; iii) access to finance; iv) lack of entrepreneurial skills, both technical and managerial; v) worker skills; and vi) trade logistics. The most significant constraints for small firms are entrepreneurial skills, land, inputs, and finance, while the most significant constraints for large firms are trade logistics, land, and inputs.

The success of industrial zone initiatives is primarily determined by choices made in the selection and promotion of sites, design and delivery options adopted (i.e., public, private, or public-private), establishment, implementation and regulation of policy frameworks, incentive packages and various other provisions and bureaucratic procedures that support the smooth and efficient running of SEZs (FIAS, 2008).

Table 5.2: Key Stakeholders and responsibility matrix for establishing SEZs.

	Public institutions	Private companies	Financial institutions	Regional & multilateral inst.	Civil society or comm. groups
Enabling Policy Framework	x	x	x	x	x
Finance (CAPEX, Working capital, Trade Finance)	x	x	x	x	
Other financial instruments (e.g., Insurance)			x	x	
Extension services and support for smallholder farmers	x	x		x	
Off-taker agreements	x	x			
Hard infrastructure	x	x	x	x	
Soft infrastructure	x	x	x	x	x
Training & skills development	x	x	x	x	x
R&D	x	x	x	x	
Trade Agreements (i.e., bilateral, regional & international)	x			x	
Product, labour & production standards	x			x	x

Environmental standards	x		x	x	x
Community and social safeguards	x				x

Source: Authors' analysis

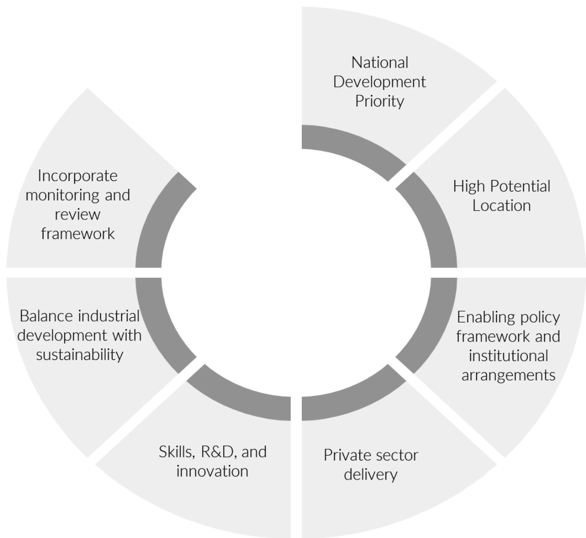
As summarised in Table 5.2 above, public institutions across a wide range of policy (e.g., ministries and government departments), research (universities and publicly funded research institutes), regulatory (licensing, standards agencies, dispute resolution and enforcement mechanisms) and service delivery (e.g., customs, public utilities, extension support services) agencies have a critical and central role to play in supporting the successful implementation of SEZs. This suggests the need for a multi-pronged strategic framework of interventions that makes the delivery and execution capacity of government institutions important in determining the scale and scope of initiatives that can be supported.

In other words, in developing market linkages, for instance, critical to establishing market access for operators, the scope and scale of trade agreements the relevant host countries can negotiate either bilaterally, regionally (e.g., AfCFTA, EU) or multilaterally through the WTO have a clear and distinct impact on the potential scope and size of the industrial zone. As does the size of the domestic market demand amidst competing product alternatives (i.e., imports), access to working capital and trade finance for investors, domestic labour laws that impact on the availability of skilled labour and restrictions on foreign labour, as well as the comparative cost impact of production and environmental standards, firms and zone operators must comply with.

This illustrates the need for policy congruency and alignment across multiple public institutions (i.e., customs, various ministries (Finance, Trade, Labour, Environment), municipal and central government etc.), as well as coordination and collaboration with private companies (investors, contractors, and zone operators), financial institutions, regional and multilateral institutions and community groups that may not be possible or currently obtainable outside of the zone.

This undertaking requires multiple actors (host communities, private companies, government agencies, financial, regional, and multi-lateral institutions, and donors) working in concert (see Table 5.2) and calls for high levels of senior-level political capital and commitment to be invested in the project, as well as a deliberate shift in institutional delivery capacity and policy alignment, often endemically sub-par in low-quality institutional environments (Doh et al., 2017).

Figure 5.3: 7 Point framework for successful agro-industrial parks



Having established the need for a multi-pronged programme of interventions, in what follows. we draw on our review of the literature and case study evidence from successful implementation in EMDEs to propose a seven-point framework for delivering successful agro-industrial parks, as illustrated in Figure 5.3 (above).

1) National Development Priority

As the conceptualisation, design, development, and operationalisation of agro-industrial zones extend across multiple decades and political cycles, it is critical that they are established as a national development priority and that proposed schemes are fully integrated into national or regional industrial policy and economic development strategies. This requires a high level of coordination, collaboration, and policy congruency across multiple national, sub-national and municipal government agencies and levels, often absent in low-quality institutional environments. It is nonetheless necessary to establish the high-level political commitment, policy stability and year-in-year resource allocation required to address investor concerns, support the smooth running of the zones, and ensure the sustainability and success of proposed schemes over the programme life cycle.

The experiences of Malaysia, China, Korea, Dubai, and Singapore all highlight this point. These countries treat SEZ programmes as an important instrument in their national or regional economic and industrial development agenda and ensure political support or endorsement from the very top level of the government.

In China, SEZs are mainly used to implement national and regional development strategies and build growth poles of economic development and export-oriented industrialisation (Narula & Zhan, 2019). Such a strategic vision signals the government's long-term commitment and is vital to the zones' success. To be effective, the inclusion of agro-industrial zones as a national development priority should be reflected in national and regional plans for research, skills development and innovation, trade policy and sectoral reform (e.g., customs, company formation, access to concessionary working capital and trade finance, etc.) as required to support the smooth running the zone. This, as in Malaysia's Northern Corridor Implementation Authority, might require the creation of a single agency to play a facilitator role working across the whole range of public, private, financial and civil society actors to strengthen and enhance the service delivery capacity of multiple government agencies and ensure the elimination of bureaucratic bottlenecks and binding constraints that serve as locational disadvantages that repel rather than attract private investment (Dinh et al., 2012).

2) High Potential Locations

In many countries, such as India and some SSA countries, zones are often criticised as "enclaves" without much linkage to the local economy (Aggarwal, 2019). Despite the past successes of some "enclave" model zones, the success of contemporary SEZs is increasingly interconnected with the local economy. Connectivity is increasingly understood to be critical in achieving competitiveness and sustainable, inclusive economic growth. It has digital, physical and policy dimensions, as trade, migration, information, transport and transit, energy, and financial flows interact in complex ways (Narula & Zhan, 2019).

Industrial zones need to build on local comparative advantages and have local suppliers as part of their value chains. Evidence from East Asia shows that, in the long run, zones with strong linkages to the local economy tend to be very successful ones (Aggarwal, 2019; Narula and Zhan, 2019). To fully benefit from the zone programmes, governments and zone operators need to consider the local comparative advantages as they target priority value addition for priority crops as determined by detailed value chain assessments to establish the crops with the highest gross value-added potential. Governments and zone facility managers should also help local firms to link with zone investors through supply chains or sub-contracting relations (Zeng, 2015a).

These backward and forward linkages hold the potential to maximise spillover effects on the economic benefits that accrue beyond the zone itself. This requires the government to play a crucial coordination role in engaging with relevant private sector, national and sub-national agencies, donors, and financial institutions to contribute to and support market-enhancing activities and services across the entire value chain from inputs to marketing and distribution of finished goods for export or domestic consumption.

From the review of the extant literature on SEZs, this paper has established that in order to be a catalyst for structural transformation, agro-industrial zones need to a) have or be linked to critical enabling infrastructure such as reliable electricity supply, water and waste management systems, highways, access roads, sea and airports and railways, with good trade logistics and streamlined customs services; b) be well-matched to local resources that leverage the national, regional or local comparative advantages (e.g. priority crops, domestic market size, trade agreements, labour, etc.); c) capable of achieving the standards to be part of global value chains; d) be focused not only on exports but also on the domestic market to ensure the delivery of the much-need spillover effects from successful implementations. Government back institutions through the instrumentation of industrial policy (e.g. identification and support for SEZs), strategic infrastructure investments, trade policy and international trade agreements, as well as trade, labour and environmental standards have a critical role to play.

Given policymakers' resource constraints, scheme promoters must select and prioritise locations with critical enabling infrastructure, strong transport connectivity and market linkages, and the potential to leverage national, regional, and local comparative advantages to create products that can competitively address domestic and international market demand. Where these do not exist, resources need to be prioritised and allocated through public-sector budgets, but also increasingly through Public Private Partnerships (PPPs) to provide them.

It therefore follows that resource constraints may impact the number of such zones that can be built. As such, the choice and prioritisation of locations for agro-industrial parks should be based on a thorough analysis of the market potential, comparative advantage (e.g., priority crops determined by detailed value chain assessments), resource availability (inputs, commodities, land, and labour), environmental impact, and social inclusion of each option. The analysis should consider both domestic and regional markets, as well as the potential for export diversification and gross value added.

Given the importance of social legitimacy and community support for such schemes, the selection should also involve consultations with relevant stakeholders, such as farmers' organisations, private sector associations, local governments, and development partners, to ensure the benefits from the scheme extend well beyond the boundaries of the zone and its investors.

Individual schemes or zones should therefore be designed and prioritised to complement and support comparative local and regional advantages (so-called L advantages), which themselves should be validated through detailed value chain assessments and strategic improvement plans, market outreach and market demand assessments, technical and commercial feasibility studies, which take into consideration the design and comparatively cost-efficient delivery of critical infrastructure and associated inputs that can reduce and enhance transaction and operational costs, and quality of feedstock and input (including skilled and non-skilled labour) commercial sustainability, target markets and businesses, growth trajectory, infrastructure availability, technology innovation capability, and environment sustainability. (Zeng, 2015a; Farole, 2011).

As mentioned, previous successful industrial zones require quality infrastructure to facilitate the movement of goods and services within and outside the zones. This includes roads, railways, ports, airports, electricity, water, sanitation, telecommunications, and waste management. The infrastructure development should be coordinated with the national and regional plans and policies and leverage public-private partnerships where possible. The infrastructure should also be climate-resilient and environmentally friendly, as this not only contributes to the global commitments towards net zero but is also increasingly an important consideration for achieving bankability which is critical to securing project finance.

3) Enabling policy framework and institutional arrangements

One of the key objectives of SEZ programmes is to overcome the constraints of doing business in an economy. In this respect, they serve as a credible mechanism for facilitating foreign direct investment as well as greater private sector participation more generally.

A predictable and effective legal and regulatory framework, consistent with strong institutional environments (Narula & Zhan, 2019), is needed to facilitate trade, reduce transaction costs, and provide protection and certainty to private sector developers and investors. This involves ensuring legal security, property rights protection, contract enforcement, access to industrial land and critical infrastructure services that enable industrial production and competitiveness (i.e., electricity, water and waste management systems, logistics and trans-shipment services, streamlined customs processes for import and export etc), as well as intellectual property rights protection.

Such a framework also helps to ensure that the zones attract the right investments and are established with high business, social and environmental standards. A solid legal framework will also buffer zones from unpredictable risks, such as political setbacks or interference and land speculation, among other factors. In addition, agro-industrial zones should have clear institutional arrangements for their governance and management. This includes defining the roles and responsibilities of different actors at the national, regional, and local levels; establishing coordination mechanisms among them; creating dedicated agencies or units for overseeing the implementation of AIPs; setting up monitoring and evaluation systems; and ensuring accountability and transparency. The institutional arrangements should also foster public-private dialogue and collaboration for addressing common challenges and opportunities.

Strong and long-term government commitment, beyond party affiliations and political lifecycles, supports a zone's success by ensuring policy continuity and adequate provision of various public goods and services.

In Singapore, the Republic of Korea, Malaysia, China, Mauritius, Jordan and other countries with successful SEZ programs, relevant laws and regulations were already in place or established when they first launched their programs; the various levels of government implemented these laws and regulations with concerted, long-term support (Aggarwal, 2019;

Zeng, 2016). This requires close coordination between the central and municipal governments and political parties.

Given the critical goal of attracting FDI and domestic private sector participation, SEZs are expected to offer investors a conducive and attractive business environment (Narula & Zhan, 2019). This often includes providing fiscal incentives, such as tax exemptions or reductions, duty-free imports of raw materials and equipment, and accelerated depreciation. This also provides for the elimination of non-tariff barriers by simplifying administrative procedures, such as licensing, registration, customs clearance, and dispute resolution. Zones can also be used to "pilot" policy and regulatory reforms to support economic development beyond the zones' immediate vicinity, as evidenced in many East Asian countries. In this way, the benefits (e.g., the simplification of customs procedures) can then be made available economy-wide (Fruman & Zeng 2015).

Sound legal and institutional frameworks with strong and long-term, well-coordinated government commitment to enhancing the ease of doing business are therefore critical to the success and sustainability of agro-industrial parks. In order, however, to ensure the long-term sustainability of these schemes and the realisation of the spillover benefits that are critical to sustained host-community support, instead of focusing only on fiscal incentives such as tax holidays which can severely deplete the expected benefits from SEZ's, a balanced approach that safeguards the sustainable delivery of the anticipated benefits from the zones should be adopted.

4) Private sector delivery

At c. $150m – $400m, the typical cost of developing a zone is a costly undertaking and requires meticulous planning, design, and operational management to be successful; and should be preceded and informed by a rigorous assessment of the market demand situation, local market conditions, connectivity, the industrial base, the supply chain, the business environment, and land and labour supplies.

In the early days, when the government developed most SEZs. Increasingly more zones are being developed through public-private partnerships (PPPs), with increasing private sector participation (Feng, 2016). In such cases, the public sector's functions typically include implementing a transparent and clear regulatory framework, providing land and efficient public services, financing basic infrastructure, and oversight of private developers or operators.

On the other hand, private-sector partner(s) take responsibility for zone development and operation, provision of specific on-site infrastructure, and services like asset management, global outreach, and investor relations. Evidence from Ethiopia has shown that ensuring that the siting and development of the zone is driven by market demand is of paramount importance to avoid creating poorly performing “white elephant” zones (Oqubuay, 2019).

To ensure smooth and efficient zone operations, private-sector development and management of the zones should be encouraged by leveraging private-sector expertise and access to capital. In such cases, experienced private-sector partners can take on demand risk and help plan, manage, and even provide specific infrastructures and services within the zone. This is particularly important as in almost all the successful zones in the world, basic infrastructure is of high quality, and one-stop-shop services and aftercare are efficient and effective. These features – characteristic of model zones in Singapore, China, Malaysia, Korea, and Dubai – make the zones very attractive to investors (Narula & Zhan, 2019).

5) Skills, R&D & innovation

The availability of skilled and unskilled labour required to operate and service the plant, equipment and the managerial and operational requirements of their businesses is a key consideration by investors in assessing the locational advantages and viability of any investment opportunity. Ongoing skills training and commitment to innovation must be a shared commitment of all key stakeholders.

In collaboration with other key stakeholders (private sector, donors, academic institutions and civil society), governments should invest in human capital development to enhance the skills and capacities of the workforce involved in agro-processing clusters. This includes providing vocational training, technical assistance, extension services, and mentoring programs for farmers, processors, and other workers; promoting entrepreneurship and innovation among youth and women; supporting research and development institutions; facilitating knowledge transfer and technology adoption; and encouraging linkages with universities and other educational institutions.

Policy incentives can also be provided to encourage firms to offer skills training and retraining to upgrade their employees. When specific talents are unavailable locally, policies can be implemented to attract these skills from other parts of the country or overseas.

To enhance productivity and sustain long-term competitiveness, AIP zone operators must be able to keep pace with technological and industrial innovation. It is therefore important to catalyse and facilitate industrial upgrading by promoting technology innovation/transfer and high-valued sectors targeted toward different development stages. These efforts include expanding well-focused, applicable R&D expenditures; strengthening university-industry linkages; supporting targeted business incubators; and attracting talent (Zhang, 2008).

One of the highest priorities of any zone is to provide the customised and specialised education and training that generate, upgrade, and deepen knowledge and skills required to support the zone's operations. This issue has become an indispensable part of the overall business environment, and investors increasingly recognise its importance. The content and training modalities will vary based on the different needs of different zones and sectors, and can be provided by a range of actors including private companies, universities or technical and vocational colleges. Without exception, training must be constantly updated to keep pace with changing business and industrial development needs; government ministries and agencies responsible for education, skills, trade and science & and technology have a critical role in facilitating this.

Fostering both “hardware” (such as science and technology bases and platforms, innovation labs, incubators, and pioneering parks) and “software” (such as sound regulatory regimes, targeted incentives and, most importantly, talent-recruiting strategies that attract businesses that employ workers with high-end skills) policy interventions should therefore be part of the framework for successful interventions.

6) Balance industrial development and sustainability.

It is important to note that community acceptance plays a critical role in the social legitimacy of economic actors and that the impacts of special economic zones on host societies go well beyond access to increased economic activity. This underlines the importance of striking a balance between industrial development, social development of rural and peri-urban areas, and addressing environmental and sustainability issues.

According to Zeng (2016), special economic zone programs are more likely to succeed if they offer opportunities for quality employment and upward mobility for trained staff, promote environmental sustainability, and avoid the temptation of deriving their competitive advantage from exploiting low-wage workers. Zone programmes that leverage CSR and non-political activity to encourage and support schemes that support and improve the quality and cost of housing, health services, schooling, community security, the cleanliness of the environment, and the state of the physical infrastructure serve to signal their commitment to their community and are rewarded with continued loyalty and support of their host communities.

Therefore, good corporate social responsibility should be encouraged through a mix of recognition (e.g., regional or national awards, membership of national or regional development boards, etc.) and policy incentives.

Beyond these softer approaches, zone operators should be required to ensure that their operations are socially and environmentally sustainable. This includes complying with national and international standards and regulations on labour rights, health and safety, environmental protection, and social responsibility; implementing social safeguards and mitigation measures to prevent or minimize adverse impacts on local communities and natural resources; promoting inclusive growth and poverty reduction by creating decent jobs, increasing incomes, and improving livelihoods; and supporting climate change adaptation and mitigation by reducing greenhouse gas emissions, enhancing energy efficiency, and expanding the use of renewable energy sources.

7) Incorporate monitoring and review mechanisms.

Zone programmes are an expensive undertaking that, irrespective of their primary funding sources, requires significant government commitment and support through fiscal and policy incentives that make them attractive for private sector investment. The primary rationale is that this is critical to creating incentives for investors (Zeng, 2016) who otherwise would not be attracted to invest in the country due to the existence of so-called binding constraints to economic growth (Rodrik, 2014).

Despite support from some economists, the views on SEZs in the economic literature remain mixed. This is due in part to the heterogeneity in outcomes of zone programmes in different countries (Zeng, 2016). Therefore, to justify the level of investment made by various stakeholders in establishing SEZs, governments are well advised to build review and monitoring mechanisms to ensure the realisation of intended benefits.

In addition, based on the experience of South Korea, where, following the initial success, many zones were created without proper business demand, ran into trouble, and were then cancelled, it might be necessary to have sunset rules for non-performing a zone programmes. Legislation must therefore be put in place and implemented effectively to stipulate the performance criteria of zone programmes and to set conditions for handling the transitions necessary when zones reach the end of their productive lifecycles and for dealing with underachieving programs.

This requires a rigorous monitoring and evaluation system to monitor and evaluate their performances regularly. Without such a system, SEZs may diverge from their initial purposes, and achieve sub-optimal outcomes that provide tenants a free-rider effect of access to government-supported access to enhance infrastructure and government services, without the corresponding benefits. To ensure policy efficacy, it is important to assess the economic feasibility of zones before they are set up and monitor the outcomes once set up, with incentives designed to match their performances.

5.5. Conclusion and Policy Implications

Despite the significant potential of Africa's agricultural sector, the development of the agro-processing industry in the region continues to be plagued by structural impediments and market-limiting constraints that result in high input and transaction costs, low competitiveness, low productivity, and low-quality outputs that limit the value countries across the region can derive from their vast endowment of natural and human resources.

In this paper, we examine the contribution of industrial policy aimed at tackling market failure and fostering the structural change, can make in transforming Africa's agro sector. We consider the potential for agro-industrial processing zones – a form of SEZ credited for China's transition into an economic powerhouse, focused on developing agro-clusters of priority crops that build on the comparative advantages of host communities in promoting value addition. And in so doing, support the creation of sustainable jobs, food security, agro-industrialisation, and inclusive economic growth in Africa.

Drawing on case study evidence from multiple countries and a review of the mixed outcomes captured in the literature on SEZs, we established that, where successful, a multi-pronged approach is required to facilitate investment and ensure that the intended benefits from SEZ's are realized.

Policy implications

Our findings have important policy implications: To be successful, African governments need to establish an integrated, comprehensive policy framework that addresses the structural impediments, market failures and limiting constraints that translate to high transaction costs, poor quality, low yields, and productivity that undermine the competitiveness of African agriculture.

This requires a more collaborative participatory approach, where government actors play a central facilitator role in coordinating the contributions of various actors, including the private sector, donors, academic, financial, and multilateral institutions, and civil society organisations.

While not attempting to be exhaustive, this paper draws from the extant literature on SEZs and case study evidence of successful agro-industrial processing zones to establish the important role successful SEZs can play in piloting key reforms capable of addressing the binding constraints and under-developed institutions that undermine industrial development in Africa. We then identify seven policy imperatives for the establishment of an integrated policy framework to support the implementation of successful agro-industrial processing zones in the region.

Future Research Directions and Limitations

While this policy paper provides valuable insights and recommendations, there are certain limitations and areas for future research. Firstly, the analysis primarily focused on the successful experiences of a selection of Asian countries identified in the review of the literature. Further comparative studies with other regions and unsuccessful implementations of similar policy frameworks could provide additional perspectives. Additionally, more empirical research is needed to assess the impact of specific policy interventions and their effectiveness in attracting FDI and promoting sustainable development in agro-industrial processing zones across Africa, which considers the heterogeneity in the institutional strength and quality of different African countries.

Furthermore, it would be beneficial to explore the social and environmental implications of agro-industrial processing zones, including the potential displacement of local communities, land tenure issues, and the sustainability of resource use. Future research could also delve into the role of technology and digital innovations in enhancing agro-industrial activities' efficiency, productivity, and sustainability. And policies aimed at strengthening the capacity and capability of domestic private sector actors either as a strategic intervention to enhance a country's L advantages or as an attempt to mitigate against the global competition for FDI.

In conclusion, this policy paper has established the central role of governments in coordinating the wide range of stakeholders and market interventions required to attract and sustain the benefits from increased FDI and private sector participation in agro-industrial parks. By adapting and contextualising the successful implementations of AIPZs in several comparator countries, we provide a seven-point framework that African governments can use to implement tailored policy frameworks to address challenges, leverage opportunities, and promote sustainable agro-industrial development. The significance of this work lies in the potential of successful AIPZs to contribute to economic growth, job creation, poverty reduction, and food security, leading to inclusive and resilient development in Africa.

REFERENCES

Acemoglu, D., & Autor, D. (2011). Skills, tasks, and technologies: Implications for employment and earnings. Handbook of labor economics, 4, 1043-1171.

AfDB (2021). *African Economic Outlook 2020.* Abidjan: African Development Bank Group (AFDB)

AfDB (2023). *Feed Africa: Strategy for agricultural transformation in Africa 2016–2025.* Abidjan: African Development Bank Group (AFDB).

Aggarwal, A. (2005). *Export processing zones in India: Analysis of the export performance* (No. 148). Working paper.

Aggarwal A (2019) SEZs and economic transformation: towards a developmental approach, Transnational Corporations, Volume 26, Issue 2, Sep 2019, p. 27 – 48

Aghion, P., Cai, J., Dewatripont, M., Du, L., Harrison, A., & Legros, P. (2015). Industrial policy and competition. *American economic journal: macroeconomics*, *7*(4), 1-32.

AGRA (2019). Africa Agriculture Status Report 2019. The hidden middle: A quiet revolution in the private sector driving agricultural transformation. Nairobi: AGRA

AGRA (2022). *Africa Agriculture Status Report. Accelerating African Food Systems Transformation* (Issue 10). Nairobi, Kenya: AGRA

Akimova, Y. A., Kochetkova, S. A., Kovalenko, E. G., & Zinina, L. I. (2016). Public-private partnership in agribusiness. *International review of management and marketing*, *6*(4), 814-822.

Alder, S., Shao, L., & Zilibotti, F. (2013). The effect of economic reform and industrial policy in a panel of Chinese cities. *Center for Institutions, Policy and Culture in the Development Process, Working Paper*, *207*.

Alkon, M. (2018). Do special economic zones induce developmental spillovers? Evidence from India's states. *World Development*, *107*, 396-409.

Alemayehu, D. B., et al. (2020). Agriculture and food security in Ethiopia. In F. Belay & D. Guèye (Eds.), Ethiopia: Agricultural transformation and agro-industrialization (pp. 1-32). Elsevier.

Al-kasasbeh, O., Alzghoul, A. & Alghraibeh, K. Global FDI inflows and outflows in emerging economies post-COVID-19 era. *Futur Bus J* **8**, 53 (2022).

Altenburg T (2011) Industrial policy in developing countries, overview and lessons from seven country cases. Discussion Paper 4/2011. German Development Institute, Bonn

Amin, M., Bell, M., & Wang, C. (2020). Institutions and Entrepreneurship in Developing Countries. Journal of International Business Studies, 51(4), 497-517.

Asiedu, E. (2014). Foreign Direct Investment in Africa: The Role of Natural Resources, Market Size, Government Policy, Institutions and Political Instability. World Economy, 37(1), 003-018.

Athukorala, P. and Narayanan, S. (2018) Economic Corridors and Regional Development: The Malaysian Experience. ADB Economics Working Paper Series No. 520. Asian Development Bank.

Ayuk, E. T., & Obi, A. I. (2019). Access to Finance and Agro-Industrialization in Africa: A Conceptual Framework. African Journal of Science, Technology, Innovation and Development, 11(1), 77-87.

Badiane, O., & Ulimwengu, J. (2019). Agro-Industrialization and Structural Transformation: Potential of African Economies. World Bank Policy Research Working Paper 8786.

Barrett, C. B., Bachke, M. E., Bellemare, M. F., Michelson, H. C., Narayanan, S., & Walker, T. F. (2012). Smallholder participation in contract farming: comparative evidence from five countries. *World development*, *40*(4), 715-730.

Boddewyn, J., & Doh, J. (2011). Global strategy and the collaboration of MNEs, NGOs, and governments for the provisioning of collective goods in emerging markets. *Global Strategy Journal*, *1*(3-4), 345-361.

Bothello, J., Nason, R. S., & Schnyder, G. (2019). Institutional Voids and Organization Studies: Towards an epistemological rupture. Organization Studies, 40(10), 1499–1512.

Brouthers, L. E., & Hennart, J. F. (2007). Boundaries of the firm: Insights from international entry mode research. Journal of Management, 33(3), 395-425.

Cantwell, J., Dunning, J. & Lundan, S. (2010) An evolutionary approach to understanding international business activity: The co-evolution of MNEs and the institutional environment. J Int Bus Stud 41, 567–586

Chen, X. (1994). The changing roles of free economic zones in development: A comparative analysis of capitalist and socialist cases in East Asia. *Studies in Comparative International Development*, *29*, 3-25.

Chen, X. (1995). The evolution of free economic zones and the recent development of cross-national growth zones. *International Journal of Urban and Regional Research*, *19*(4), 593-621.

Chen, J., Xie, L. (2019) Industrial policy, structural transformation and economic growth: evidence from China. *Front. Bus. Res. China* **13**, 18

Cirera, X., & Lakshman, R. W. (2017). The impact of export processing zones on employment, wages and labour conditions in developing countries: systematic review. *Journal of development effectiveness*, *9*(3), 344-360.

Cling, J. P., & Letilly, G. (2001). Export Processing Zones: A threatened instrument for global economy insertion.

Creskoff, S., & Walkenhorst, P. (2009). Implications of WTO disciplines for special economic zones in developing countries. *World Bank Policy Research Working Paper*, (4892).

Dang, T. T., Doan, T. T., & Nguyen, T. T. (2019). Investment Promotion Policies and Attractiveness of Vietnam's Industrial Zones. Journal of International Studies, 12(1), 36-52.

DiMaggio, P. J., & Powell, W. W. (1983). The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields. American Sociological Review, 48(2), 147-160.

Dinh, H. T., and Clarke, G. (2012). Performance of Manufacturing Firms in Africa: An Empirical Analysis. Directions in Development: Private Sector Development. Washington, DC: World Bank.

Dinh, H. T., Palmade, V., Chandra, V., & Cossar, F. (Eds.). (2012). *Light manufacturing in Africa: Targeted policies to enhance private investment and create jobs*. World Bank Publications.

Doh, J. P., Hahn, E. D., & Bunyaratavej, K. (2008). Multinational investment and host country development: Location efficiencies for services offshoring. *Journal of World Business*, *43*(2), 227-242.

Doh, J. P., Lawton, T. C., & Rajwani, T. (2012). Advancing nonmarket strategy research: Institutional perspectives in a changing world. *Academy of Management Perspectives, 26(3),* 22-39

Doh, J., Rodrigues, S., Saka-Helmhout, A. (2017) International business responses to institutional voids. J Int Bus Stud 48, 293–307 (2017).

ECA and AUC (2013) Economic report on Africa 2013 – making the most of Africa's

5

commodities: industrializing for growth, jobs and economic transformation. Economic Commission for Africa, Addis Ababa

FAO (2017). Territorial tools for agro-industry development: A sourcebook. Edited by Nogales, E. and M. Webber. Rome: FAO (2019). Africa Regional Overview of Food Security and Nutrition 2018. Rome: FAO

FAO (2020). *The state of food security and nutrition in the world 2020: transforming food systems for affordable healthy diets*. Rome: FAO

FAO and AfDB (2019). Agricultural transformation centres in Africa: Practical guidance to promote inclusive agro-industrial development. Rome: FAO

Farole, T. (2011). *Special economic zones in Africa: comparing performance and learning from global experiences*. World Bank Publications.

Farole, T., & Akinci, G. (Eds.). (2011). *Special economic zones: progress, emerging challenges, and future directions*. World Bank Publications.

Farole, T., and Lotta, M., (2017) 'Special Economic Zones in Africa: Political Economy Challenges and Solutions', in John Page, and Finn Tarp (eds), The Practice of Industrial Policy: Government—Business Coordination in Africa and East Asia (Oxford, 2017; online edn, Oxford Academic, 20 Apr. 2017),

Feyaerts, H., Van den Broeck, G., & Maertens, M. (2020). Global and local food value chains in Africa: A review. Agricultural Economics, 51(1), 143-157.

FIAS (2008). 2008 Annual Report: The Investment Climate Advisory Service

Fine, D., van Wamelen, A., Lund, S., Cabral, A., Taoufiki, M., Dörr, N., Leke, A., Roxburgh, C., Schubert, J. and Cook, P., (2012.) Africa at work: Job creation and inclusive growth. *McKinsey Global Institute, Boston*.

Fruman, C., & Zeng, D. Z. (2015). How to make zones work better. *World Bank Private Sector Development Blog*.

Frye, T., & Shleifer, A. (1997). The invisible hand and the grabbing hand. Vol. 87, No. 2, Papers and Proceedings of the Hundred and Fourth Annual Meeting of the American Economic Association (May, 1997), pp. 354-358

Fuller, B., & Romer, P. (2012). Success and the City. *How charter cities could transform the developing Word. A Macdonald-Laurier Institute Publication, publikacja na portalu*

Ge, J., Carney, M., & Kellermanns, F. (2019). Who Fills Institutional Voids? Entrepreneurs' Utilization of Political and Family Ties in Emerging Markets. Entrepreneurship Theory and Practice, 43(6), 1124–1147.

Ge, W. (1999). *Special economic zones and the economic transition in China* (Vol. 5). World Scientific.

Gereffi, G., Humphrey, J., & Sturgeon, T. (2005). The governance of global value chains. Review of International Political Economy, 12(1), 78-104.

Haeri, A., & Arabmazar, A. (2018). *Designing an industrial policy for developing countries: A new approach (no. 89048)*. Munich Personal RePEc Archive.

Hamada, K. (1974). An economic analysis of the duty-free zone. *Journal of international Economics*, *4*(3), 225-241.

Hamilton, C., & Svensson, L. E. (1982). On the welfare effects of a 'duty-free zone'. *Journal of International Economics*, *13*(1-2), 45-64.

Hanh, V. T. K. (2021). A Brief Study Discussing Competitiveness of Vietnam Logistics Industry. *Modern Perspectives in Economics, Business and Management Vol. 4*, 55-74.

Hausmann, R., & Rodrik, D. (2003). Economic development as self-discovery. *Journal of Development Economics*, *72*(2), 603-633.

Hoefer, R. Institutionalism as a Theory for Understanding Policy Creation: An

Underused Resource. J of Pol Practice & Research 3, 71–76 (2022).

Jayanthakumaran, K. (2003). Benefit–cost appraisals of export processing zones: A survey of the literature. *Development Policy Review*, *21*(1), 51-65.

Jenkins, M., Larrain, F., & Esquivel, G. (1998). Export processing zones in Central America. *Harvard Institute for International Development Working Paper*, (646).

Kaplinsky, R. (1993). Export processing zones in the Dominican Republic: Transforming manufactures into commodities. *World Development*, *21*(11), 1851-1865.

Khanna T. & Palepu K. G. (1997). Why Focussed Strategies May Be wrong for Emerging Markets. Harvard Business Review (July – August 1997). 28(1), 100890.

Krammer, S. M. S. (2019). Greasing the Wheels of Change: Bribery, Institutions, and New Product Introductions in Emerging Markets. Journal of Management, 45(5), 1889–1926.

Kuznets, S. (1966). Modern economic growth: Rate, structure, and spread. Yale University Press.

Lee, J.Y., Kim, D., Choi, B. et al. (2023) Early evidence on how Industry 4.0 reshapes MNEs' global value chains: The role of value creation versus value capturing by headquarters and foreign subsidiaries. J Int Bus Stud 54, 599–630 (2023).

Lewis, A. (1954). Economic development with unlimited supplies of labor. The Manchester School, 22(2), 139-191.

Lin, J. Y., & Monga, C. (2011). Growth identification and facilitation: the role of the state in the dynamics of structural change. *World Bank policy research working paper*, (5313).

Lin, J. Y., & Wang, Y. (2014). China–Africa cooperation in structural transformation: Ideas, opportunities, and finances.

Lundan, S. M. (2012). The new eclectic paradigm and international business strategy. *Handbook of research on international strategic management*, 64-76.

Madani, D. (1999). A review of the role and impact of export processing zones. *Available at SSRN 629169*.

Malaysian Digest. 2017. "NCIA to Achieve Accumulated Investment of RM87.3 Billion by End-2017." January 25.

Mbate, M. (2016). Industrial Policy and Structural Change: Some Policy Perspectives. In: Seck, D. (eds) Accelerated Economic Growth in West Africa. Advances in African Economic, Social and Political Development. Springer, Cham.

McCulloch, N., et al. (2016). Agro-Processing in Africa: Political Economy, Agribusiness, and Value Chains. World Bank Publications.

McGaughey, S. L., Kumaraswamy, A., & Liesch, P. W. (2016). Institutions, entrepreneurship and co-evolution in international business. *Journal of World Business*, *51*(6), 871-881.

McMillan, M., & Headey, D. (2014). Introduction–understanding structural transformation in Africa. *World Development*, *63*, 1-10.

McCulloch, N., et al. (2016). Agro-Processing in Africa: Political Economy, Agribusiness, and Value Chains. World Bank Publications.

Meyer, K.E., Li, J., Brouthers, K.D. et al. International business in the digital age: Global strategies in a world of national institutions. J Int Bus Stud 54, 577–598 (2023).

Meyer, K. E., Mudambi, R., & Narula, R. (2011). Multinational enterprises and local contexts: The opportunities and challenges of multiple embeddedness. Journal of Management Studies, 48(2), 235-252.

Mghenyi, E., Omiti, J., Nyanamba, T., & McCullough, E. (2017). Determinants of smallholder farmers' access to agricultural credit: The case of Kenya. Journal of Agricultural Economics, 68(1), 201-216.

Monge-González, R., & Monge-Ariño, F. (2005). Anti-dumping policies and safeguard measures in the context of Costa Rica's economic liberalization. *Available at SSRN 744665*.

Murendo, C., Wollni, M., & de Brauw, A. (2012). Understanding the adoption of a new agricultural technology: Case of conservation agriculture in Tanzania. Agricultural Economics, 43(1), 27- 41.

Mwega, F. M. (2021). Investment Climate and Attractiveness for Investment in Africa. In F. M. Mwega & M. Ndung'u (Eds.), Africa's Path to Prosperity: Lessons from its Successful Economies (pp. 93-116). Oxford University Press.

Narula, R. and Zhan J. X. (2019) Using special economic zones to facilitate development: Policy implications, Transnational Corporations, Volume 26, Issue 2, Sep 2019, p. 1 – 26. DOI: https://doi.org/10.18356/72e19b3c-en

Nathan, M., & Overman, H. (2013). Agglomeration, clusters, and industrial policy. *Oxford Review of Economic Policy, 29*(2), 383–404.

Newman, C., Page, J., Ran, J., Shimeles, A., Soderbom, M., & Tarp, F. (2016), 'Can Africa Industrialize?', in Newman et al., (eds), Manufacturing Transformation: Comparative Studies of Industrial Development in Africa and Emerging Asia (Oxford, 2016), https://doi.org/10.1093/acprof:oso/9780198776987.003.0013

North, D. C. (1990). Institutions, institutional change and economic performance. Cambridge University Press.

OECD-FAO (2016). OECD-FAO Agricultural Outlook 2016-2025. *Outlook, 2025.*

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. (2017). Markets and institutional swamps: tensions confronting entrepreneurs in developing countries. *Journal of Institutional Economics*, *13*(2), 243-269.

Olusina Daniel, G., Fu, K., & Dolfsma, W. (2019). Institutional quality and economic development in sub-Saharan Africa: Can management effort and bribes compensate for low-quality institutions? *Journal of Economic Issues*, *52*(2), 473-482.

Oqubay, A. (2015). *Made in Africa: Industrial Policy in Ethiopia* (p. 374). Oxford University Press.

Osabuohien, E.S. (2020), "Guest editorial", African Journal of Economic and Management Studies, Vol. 11 No. 2, pp. 185-191. https://doi-org.ezproxy.library.wur.nl/10.1108/AJEMS-06-2020-406

Pack, H., & Saggi, K. (2006). The case for industrial policy: A critical survey. *Policy Research Working Paper, 3022*(2), 368–379.

Peng, M. W., Ahlstrom, D., Carraher, S. M., & Shi, W. S. (2009). History and the Institutional Basis of Economic Change. Journal of Management, 35(3), 643-671.

Piemonte C, Cattaneo O, Morris R, Pincet A, Poensgen K (2019) Transition finance: introducing a new concept. OECD Development Cooperation Working Papers, No 54

Rajalahti, R. (2021). *Agricultural Innovation in Developing East Asia: Productivity, Safety, and Sustainability*. World Bank Publications.

Rasiah, R., Gammeltoft, P., & Nielsen, C. (2018). FDI and Industrial Policy in Southeast Asia. Journal of Southeast Asian Economies, 35(1), 1-10.

Rodrik, D. (1996). Understanding economic policy reform. Journal of Economic Literature, 34(1), 9–41.

Rodrik, D. (2004). Industrial policy for the twenty-first century. *Available at SSRN 666808*.

Rodrik, D. (2008). The real exchange rate and economic growth. Brookings Papers on Economic Activity, 2, 365-439.

Rodrik, D. (2014). Green industrial policy. *Oxford review of economic policy*, *30*(3), 469-491.

Sanjaya, L. (2004). *Reinventing industrial strategy: The role of government policy in building industrial competitiveness (no. 28)*. United Nations conference on trade and development.

Scott, W. R. (1995), *Institutions and Organizations. Ideas, Interests and Identities.* Sage Publications ISBN: 978-142242224

Smith, K. J., Mishra, A. K., & Herath, H. M. (2020). Agro-industrial processing zones: Creating opportunities for value addition and diversification in agriculture. World Development Perspectives, 19, 100225.

Stiglitz, J. E. (1993). The role of the state in financial markets. The World Bank Economic Review, 7(suppl_1), 19–52.

Stiglitz, J. E. (2013). Promoting Sustainable Industrial Policies in Industrialize Africa: Strategies, Policies, Institutions and Finance. AfDB Economic Research, 12–14.

Tadesse, G., & Bahiigwa, G. (2015). Agricultural productivity and rural infrastructure in sub-Saharan Africa. Journal of African Economies, 24(suppl_1), i24-i62.

UNCTAD (2019) World Investment Report: Special Economic Zones, United Nations Publications

UNCTAD (2020). World Investment Report: International production beyond the pandemic. Geneva: United Nations Publications.

UNCTAD (2021). World Investment Report: Investing in Sustainable Recovery. Geneva: United Nations Publications

UNCTAD (2022). World Investment Report: International tax reforms and sustainable investment. Geneva: United Nations Publications.

UNIDO & UNCTAD (2011) "Economic Development in Africa Report: Fostering industrial development in Africa in the new global environment". Special Issue UNCTAD/ALDC/Africa/2011.

Van Dijk, M. P. (2009). *The new presence of China in Africa* (p. 224). Amsterdam University Press.

Wang, J. (2013). The economic impact of special economic zones: Evidence from Chinese municipalities. *Journal of development economics*, *101*, 133-147.

Wang, T., & Qi, J. (1996). *Industrial policy and economic growth*. Beijing: Social Sciences Academic Press.

Warr, P. G. (1989). Export processing zones: The economics of enclave manufacturing. *The World Bank Research Observer*, *4*(1), 65-88.

Wei, J., & Zuo, Y. (2018). The certification effect of R&D subsidies from the central and local governments: evidence from China. *R&D Management*, *48*(5), 615-626.

Wong, K. Y. (1987). China's special economic zone experiment: an appraisal. *Geografiska Annaler. Series B. Human Geography*, 27-40.

World Bank, 1995. World Development Report: Workers in an Integrating World. Washington, DC: The World Bank

World Bank, 2020. Scaling up Action for Transformative Change: Food Systems 2030. Washington, DC, the World Bank.

Zeng, D. Z. (Ed.). (2010). *Building engines for growth and competitiveness in China: Experience with special economic zones and industrial clusters*. World Bank Publications.

Zeng, D. Z. (2015). Global experiences with special economic zones: Focus on China and Africa. *World Bank Policy Research Working Paper*, (7240)

Chapter 6

GENERAL DISCUSSION & CONCLUSION

social legitimacy necessary to overcome so-called liabilities of foreignness, adapt their product mix appropriately to changing local tastes, developments and requirements, and deal with social norms – such as informal payments or bribes, that may conflict with home-country institutional compliance requirements (Saka-Helmhout et al., 2020).

This thesis takes a mixed-methods approach to identify and empirically test three social norms that are adopted as proxies for informal institutions (chapter 2 and 4), and draw on case study evidence of MNEs operating across Africa from advanced and emerging economies, to argue that the wide-scale reality of institutions that significantly differ from what some MNEs are familiar with, should not necessarily imply an absence of institutions (chapter 3).

Chapter 5 examines how government responses through industrial policy can be used to pilot specific business environment reforms targeted at facilitating FDI and private sector investment that would otherwise be difficult given the weakness or absence of market-supporting institutions that render such countries less attractive, given the global competition for FDI.

In this section, we provide a summary of the contribution and relevance of each chapter to the thesis. This is followed by a summary of the implications for policymakers and multilateral institutions like the African Development Bank, focussed on promoting private sector-led economic development of emerging markets and developing economies. We then discuss some limitations and directions for future research.

6.1. Summary, contribution and relevance of each chapter

Chapter 2 Institutional Quality and Industrial Development in Sub-Saharan Africa: Can Management Effort and Bribes Compensate for Low-Quality Institutions?

This chapter explores how firms operating in countries with weak or under-developed institutions, as observed in sub-Saharan Africa, compensate for or seek alternative strategies to obtain what they need for their firms to operate.

Without high-quality institutions – reflected in the existence of transparent, predictable and enforced rules (World Bank, 1998), top management teams are faced with one of two options – either spending a lot of effort and time (TMT efforts) monitoring and responding to inefficient bureaucratic procedures and authorities to access utility services, relevant licences, permits and other government services. Alternatively, they may choose to make informal payments to create an obligation (Darr, 2003; Dolfsma et al., 2009) for public sector officials working in public authorities to deliver public services that match the needs and expectations of their companies in a timely manner. Under these conditions, informal payments and TMT efforts would be considered substitutes for high-quality institutions and be able to compensate for the strength or quality of a country's institutional furniture.

Drawing on a sample of firms surveyed from 35 African countries over a ten-year period (2006 – 2015), the expectation that TMT and informal payments can be used as substitutes for high-quality institutions is tested empirically and found to only be true for the former.

Indeed, comparatively less top management effort is required to navigate regulations in high-quality institutional environments. Predictably, TMT efforts dealing with authorities and regulations also have a significant direct and negative impact on firm performance.

What is surprising, however, is that informal payments are not a substitute for low-quality institutional environments. This is perhaps reflective of the idea that while gift-giving is thought to create and sustain relationships between individuals, much uncertainty exists in societies characterised by low institutional quality, which implies that the circumstances for relations to be stable and afford sufficient time to encapsulate the three essential aspects of gift-giving; i.e., giving, receiving and reciprocating (Mauss, 1954), may be absent.

The positive effect of high-quality institutions on firm performance, however, is enhanced by informal payments, even though informal payments do not directly affect firm performance.

In other words, SSA countries that have relatively high-quality institutions may still not have high enough quality institutions that treat all equally and equally efficiently. Their relative stability, however, allows recipients of informal payments the latitude to respond or reciprocate by ensuring the giver of the gifts receives the services they would otherwise have been unable to access when they needed it, or spend extensive periods of time waiting. It is a complex interplay, that is common place in EMDEs, but not exclusive to this category of countries (Olthaar et al., 2017, Krammer, 2017)

While these findings may raise ethical questions given the implications for corruption in EMDEs, they provide, at least in part, empirical support for the view that an inappropriate or unsatisfactory institutional 'furniture' (Veblen, 1961, p.236) forces managers of firms to seek alternative routes to obtain what they need for their firm to function. It also provides the opportunity to reflect on whether the perception of gift-giving, considered more culturally acceptable in some EMDEs, can or should be examined in the context of a cultural norm.

These conclusions provide validation that the concept of institutional voids, which for the last 25 years has been the prevailing theory to explain the concept of weak or underdeveloped institutions in EMDEs, could be challenged or further explored empirically by testing if informal institutions – characterised as informal norms and unwritten expectations can act as substitutes for weak or under-developed institutions (Helmke & Levitsky, 2004).

Chapter 3 Navigating Institutional Difference in Africa: Moving Beyond the Institutional Voids Perspectives

This chapter examines the institutional voids perspective from the lens of MNEs operating across Africa. It draws on case study evidence from AMNES and EMNEs operating across Africa to contribute to the observation that relying on the 'institutional voids' thesis, most studies examining the institutional environment in Africa and its implications for firm performance and strategy do so, primarily from a western lens (Mair et al., 2012; Olthaar et al., 2017).

Moreover, the concept of voids ignores the reality that African institutions have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that may be different from other regions and worthy of closer examination (Mbalyohere et al., 2017). Olthaar et al. (2017) for instance, have suggested that informal norms, practices, or formal institutions from a different or adjacent practice or domain still affect firms, even where formal institutions that regulate the proper functioning of markets and economic activity are absent or do not function as expected.

In essence, while the wide-scale reality is that institutions in Africa differ significantly from what some MNEs are familiar with, this does not necessarily imply the absence of institutions (Olthaar et al., 2017). In reality, informal and formal institutions co-exist to establish the institutional mix of host countries (North, 1990; Scott, 1995; Barbalet, 2022), particularly in emerging markets. Though their enforcement is not regulated in the strict Western-style, the influence of informal institutions in EMDEs in Africa cannot be ignored (Bagire & Namada, 2015; George et al., 2016; Zoogah et al., 2015), as they form a significant part of the rules of the game that guide economic activity in these countries.

Evidence from the sample of regional AMNE and EMNEs operating in Africa, used in the study, result in the following observations:

- EMNEs are most competitive at the early stages of pro-market reforms, when formal institutions are least developed and informal institutions are most prevalent, exhibiting capabilities that are better suited to informal institutions.
- Conversely, AMNEs adapt more effectively at later stages, reflecting capabilities to effectively respond to more formal institutions.
- When they enter strategic partnerships, however, EMNEs and AMNEs appear to create synergies and complementarity in the capabilities to respond to both informal and formal institutions.

These findings establish that what the MNEs in the study respond to, are not voids, but rather an array of institutions with generally different rules than those AMNEs from highly formally institutionalized contexts are familiar with (Mbalyohere, 2016). And that the lack of effective formal institutions, something that characterizes the early stages of pro-market reforms in sub-Saharan African and other emerging and emerging markets (Hoskisson et al., 2012) does not necessarily translate into a universal competitive disadvantage for MNEs.

In reality MNEs operating in Africa respond to a mix of informal and formal institutions that have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that is distinctively different from other regions. Given this difference, MNEs need to critically consider what strategies can be transferred from institutionally different contexts; and what new capabilities are required to successfully operate across the region.

Chapter 4 Disentangling Institutional Voids: How Informal Institutions interact with formal institutions to impact firm performance in Emerging Markets.

EMDE institutional environments are often thought to be characterised by institutional voids defined as the absence or underdevelopment of Western-style formal institutions that regulate, facilitate and support the efficient functioning of markets and economic activity (Doh et al., 2017; Khanna & Palepu, 1997). In reality, host country environments consist and evolve over time from a complex constellation of formal and informal institutions (Doh et al., 2017; Holmes et al., 2013; Olthaar et al., 2017).

The central proposition of this thesis is that the institutional voids perspective, should not be understood literally as implying that firms operate within an institutional vacuum. Informal and formal institutions co-exist to form the institutional configuration of host-country environments (Holmes, Miller, Hitt, & Salmador, 2013; North, 1990; Rodrik, 2016; Rodrıguez-Pose, 2013; Scott, 1995; Barbalet, 2022); and collectively establish the incentive structure of a society.

While comparably more attention has however been paid to formal institutions (Doh et al., 2017, there is growing interest in better understanding informal institutions, and in particular how they inter-relate with formal institutions; and combine to impact firm strategy and performance (Doh et al., 2017). Yet the relationship between formal and informal institutions and how they impact firm performance remains under-analyzed. This is considered to be due to difficulties in establishing measures for informal institutions (Helmke & Levitsky, 2004; Xu & Yao, 2015; Qiu et al 2021), and its conflation with culture, which in IB while linked, as informal institutions are considered embedded in culture and ideology (Peng, 2002, Scott, 1995), is not considered one and the same (Helmke & Levitsky, 2004). This paper seeks to make a contribution in addressing this research gap.

By proposing and operationalising measures for three widely practiced norms, identified in this paper as proxies for informal institutions as exemplified by time spent by senior managers on regulations (TMT), informal payments or bribes, and local sourcing – and testing to see if they complement or substitute formal institutions across our sample, this paper addresses a key constraint to research on the interplay between formal and informal institutions.

It explores how the institutional mix of different countries affects the performance of foreign and domestic firms. Drawing on firm-level data using the World Bank Enterprise Survey (WBES) of firms operating across 128 countries over 11 years, and empirically tests the notion of institutional voids, by examining how informal and formal institutions impacts the comparative performance of MNEs.

Generally, the study establishes that informal institutions often enhance or complement the positive effect of formal institutions; but with some intriguing regional variations. There are, nonetheless, some intriguing findings, which may underline the heterogeneity and distinct differences in the full sample, and emerging markets and sub-Saharan African sub-samples.

Notably, local sourcing and TMT efforts substitute for possibly lower quality institutions in the SSA sub-sample but not for informal payments; nor in the full sample or wider EM sample. This finding is in line with research showing that less developed countries tend to have weaker and more underdeveloped formal institutions, the enforcement of which is also likely to be unreliable (Peng et al., 2009). In the presence of such formal "institutional voids", firms will resort to informal institutions or formal institutions developed in different and yet related fields (Olthaar, et al. 2017). Again, the only exception is the sector-level informal payment, which complement the enabling role of formal institutions role in driving firms' performance in SSA countries instead of substituting its effect.

Meanwhile, broadly speaking informal payments or bribes across the full, EMDEs and SSA sub-samples positively impact firm performance, and suggest a complementary role. This is a remarkable and counter-intuitive finding that is hard to explain, yet probably exists because informal payments are expected and made, despite being officially seen as an activity to be frowned upon (Saka-Helmhout, 2020; Krammer, 2019, Dolfsma et al., 2009).

Chapter 5 Policy imperatives for attracting FDI for Agro-industrial Processing in Africa

In the preceding three chapters, which form the body of this thesis, we have sought to establish and contribute to addressing the research gaps in understanding how informal institutions can and do substitute for or complement formal institutions in emerging markets and developing economies.

Drawing on Dunning's OLI paradigm, which is adopted as the conceptual framework for this paper, attention is shifted to how government's particularly in Africa, in light of the under-development of their market-supporting institutions more generally, can adopt policies that facilitate FDI and private capital for specific sectors where they identify the potential for developing a competitive or comparative advantage.

Institutional theory provides a theoretical framework for understanding how formal and informal rules, norms, and practices shape the behaviour and decision-making of organisations within a given institutional context. In the context of the agro-processing sector, this involves complex value chains and interactions between various stakeholders; institutional factors – particularly investment climate reforms also play a crucial role in shaping investment dynamics (Newman et al., 2016).

The justification for industrial policy rests on the premise that governments can drive economic development and facilitate transformative processes (Rodrik, 2004). This is relevant for emerging economies in Africa, where the potential for structural change to lead to growth and poverty is considered significant (McMillan & Headey, 2014).

Countries that add value to their natural resources and promote labour movement to productive sectors are associated with increased per capita income and technology accumulation (UNCTAD and UNIDO 2011). Indeed, Newman (2016) posit that rising wages and input costs in Asia could offer Africa – the poorest region per capita – a renewed opportunity to industrialise, particularly in the labour-intensive, light-manufacturing sectors such as agro-processing. Evidence from East Asia underscores the importance of commodity-based industrialisation as a viable channel for addressing poverty and unemployment (Mbate, 2016) and that new entrants can succeed in global manufacturing.

This paper contributes to this discussion by extending and applying the concept of the co-evolution of institutions and the influential theoretical framework provided by Dunning's Eclectic Paradigm, to explore how policymakers can work with investors (Doh et al., 2008; Cantwell et al., 2010; Ge et al., 2019) and other actors to address the impact of poor, weak or under-performing institutions in the agro-industrial processing sector. For instance, by developing Location advantages and promoting or incentivising the development of Internalisation advantages, public sector policymakers can create the conditions to attract foreign investors with relevant Ownership advantages that enable them to compete favourably within the host country.

We take the view that the chronic under-resourcing and fiscal constraints faced by African governments, made worse by the COVID-19 pandemic, call for a collaborative approach to policy formulation and implementation. This is particularly relevant for specific economically viable sectors that can be managed and operated by the private sector, that through initial pilot pro-market reforms, can see the government transition from active owner, promoter, developer, and operator role to playing a facilitator role (Frye and Shleifer, 1997; World Bank, 1995) such as in the development of agro-industrial processing zones.

While not attempting to be exhaustive, this paper draws from the extant literature on SEZs and case study evidence of successful agro-industrial processing zones to identify seven policy imperatives for the establishment of an integrated policy framework to support the implementation of successful agro-industrial processing zones in the region.

In conclusion, this chapter policy establishes the central role governments can and must play in coordinating the wide range of stakeholders and market interventions required to attract and sustain the benefits from increased FDI and private sector participation in agro-industrial zones. By adapting and contextualizing the successful implementations of AIPZs in several comparator countries, a seven-point framework is developed that African governments can use to implement tailored policy frameworks to address challenges, leverage opportunities, and promote sustainable agro-industrial development. The significance of this work lies in the potential for successful AIPZs to contribute to economic growth, job creation, poverty reduction, and food security, leading to inclusive and resilient development in Africa.

Conclusions

The findings presented in this doctoral thesis highlight the need for MNEs to recognise that EMDEs institutions – particularly those at the earlier stages of institutional reform are distinctively different from developed country institutional environments (Rottig, 2016). And are characterised by a number of unique institutional features that make them distinct from the home-country institutions advanced-country MNEs (AMNEs) are used to. MNEs who choose to take advantage of the opportunities in these markets must develop distinct capabilities for addressing the prevalence of missing and underdeveloped formal institutions. They require some degree of autonomy from HQ and will need to develop country-specific strategies that include leveraging the capabilities of local firms embedded in the supply chain to provide social legitimacy necessary to overcome so-called liabilities of foreignness, adapt appropriately to changing local tastes, developments and requirements, and deal with social norms – such as informal payments or bribes, that may conflict with home-country institutional compliance requirements (Krammer, 2019).

6.2. Implications

EMDEs offer a number of potential benefits, such as large and growing consumer markets, low-cost labour, and access to commodities, rare earth minerals that form vital factor components for new and emerging technologies, and arable land for agriculture, for example. However, MNEs that choose to operate in these markets must also be prepared to face a number of challenges, including:

- **Missing or underdeveloped western-style formal institutions:** EMDEs often have poor, weak or non-existent legal systems, regulatory frameworks, infrastructure, public services, and enforcement mechanisms typical of advanced country institutional environments. This can make it difficult to secure basic services, permits, enforce contracts, protect intellectual property, and resolve disputes using capabilities developed in and relevant to advanced country institutional environments. They may be exposed to increased risk of corruption, fraud, and other forms of malfeasance. As a result, MNEs often need to develop distinct capabilities for addressing these challenges – or buy in this expertise from local firms who are better positioned to anticipate and deal with the challenges through informal social networks and trust-based relationships.
- **Liability of foreignness:** One important capability is the ability to overcome the liability of foreignness. This comes with being a foreign entrant into a market with different institutional arrangements, culture and social norms from the home country, and can be addressed by building relationships with a broad range of local stakeholders, including government officials, business leaders, and community members. By building strong relationships – for example, including local firms within their supply chains, MNEs can gain access to information, resources, and support. They can also build trust and legitimacy, which can help them increase their local embeddedness, and overcome the "liability of foreignness."
- **Adapting to Local Tastes:** Another important capability is the ability to adapt to local tastes and conditions. This includes understanding local cultures, regulations, and business practices. MNEs need to be willing to modify their products, services, and business models to meet the needs of local customers. They also need to be prepared to deal with unexpected challenges, such as political instability or economic volatility.
- **Dealing with cultural differences and social norms:** Finally, MNEs need to be aware of the cultural expectations and social norms in the countries where they operate. In some EMDEs, it is common for businesses to make informal payments, such as bribes, to government officials or other individuals in order to get things done (Krammer, 2019).

While MNEs may be tempted to engage in these practices, this may conflict with home-country institutional compliance requirement, which could raise ethical implications or legal repercussions in their home country. This presents a dilemma as MNEs need to balance their ethical obligations with the need to operate effectively in the local environment.

Implications for HQ and subsidiary relations

- **Country-specific strategies:** There is no one-size-fits-all approach to operating in EMDEs. Each market economy is unique, and MNEs need to develop country-specific strategies that take into account the specific challenges and opportunities that exist in each location, in order to be successful.
- **Autonomy from HQ:** MNE subsidiaries operating in EMDEs often need to be well resourced and have a high degree of autonomy from their parent companies in order to be successful. This is because the challenges and opportunities in each market are unique, they need to be able to adapt quickly to changing local conditions and requirements, and to make decisions that are tailored to their specific circumstances. This has implications for the ownership structure and corporate governance controls of local subsidiaries that needs to reflect a balance between corporate risk management and operational realities.
- **Local embeddedness**: Local firms are often better equipped to anticipate and deal with the challenges associated with missing or underdeveloped formal institutions, which can make it difficult for MNEs to do business in EMDEs. Incorporating local firms into the supply chain, may require specific supply chain development programmes that may initially be seen to increase the cost of operations, when compared to other alternatives, but could in time be seen as a strategic investment in social legitimacy, and innovation possible from incorporating capabilities and social networks unique to local firms.

Implications for policymakers

FDI can play a significant role in promoting economic development in EMDEs (Li & Liu, 2005; Borensztein et al., 1998). Given the global competition for FDI, government policy needs to be focussed on building and enhancing host country comparative advantages in commodities and other factors of production through investments in industrial infrastructure, availability of skilled workforce, local companies and third-party agencies capable of supporting local sourcing and delivery of services to support the efficient operations, and supportive business environment.

The full benefits of FDI can however, only be realised if there is strong collaboration between foreign and domestic firms and skilled workforce (Borensztein et al., 1998). Collaboration between foreign and domestic firms can facilitate the spillover benefits of FDI in a number of ways: First, it can help to transfer knowledge and technology from foreign firms to domestic firms. This can help domestic firms to upgrade their skills and capabilities, which can lead to increased productivity and innovation.

Second, collaboration can help domestic firms to participate in global value chains. This can provide domestic firms with access to new markets and customers, as well as opportunities to learn from foreign firms about best practices in production, marketing, and management.

Third, collaboration can help to build domestic capital. When foreign firms see that there are domestic firms capable of collaborating with them and, supporting their business operations and strategic objectives, they are more likely to invest. This can help to build a more dynamic and competitive domestic economy.

Fourth, collaboration can help to create sustainable jobs. When foreign and domestic firms work together, they can create more productive and better paying jobs. This can help to reduce poverty and inequality in EMDEs.

There are a number of things policy makers can do to promote, encourage, and facilitate collaboration between foreign and domestic firms. These include:

- **Creating a supportive business environment:** This includes developing (either directly or through strategic innovative partnerships with private sector players or multilateral institutions) industrial infrastructure, providing access to concessional finance, reducing red tape, protecting intellectual property rights, tax breaks for innovation, R&D, and incentives for job creation and local content. Where economy-wide reforms are not considered achievable, targeted interventions in geographically segmented areas (e.g., SEZs) provide governments with the opportunity to pilot market-supporting reforms that could eventually be scaled more broadly.

- **Creating a favourable regulatory and operating environment for collaboration:** Policy makers can create a regulatory environment that promotes local content and facilitates collaboration between foreign and domestic firms. This includes local content requirements for strategic sectors, ensuring adequate protection for intellectual property rights, financial incentives to foreign and domestic firms that collaborate on joint ventures, research and development projects, provision of training, technical assistance and access to capital to domestic firms to help them build the skills and capabilities they need to collaborate effectively with foreign firms.
- **Securing international trade agreements:** Opening up new markets and expanding the global market for exports through trade agreements will enhance the locational advantages of host countries, with established comparative advantages in selected commodities and factors of production. This would enhance their global competitiveness and make it easier for foreign investors to enter these markets.
- **Support the availability of skilled workforce:** Policy makers can work with a range of public and private institutions to assess the skills required to support industrial development and develop tailored education and skills development programmes that will help to create a more skilled workforce that is attractive to investors. This can include financial incentives and tax breaks for employer delivered professional apprenticeships.
- **Encouraging networking, exhibitions and matchmaking events:** Policymakers can play an active role in promoting international trade missions and other initiatives and events to encourage networking and matchmaking events. This can help foreign and domestic firms connect with each other and identify potential areas of collaboration. They can also support the establishment of professional associations to promote professionalisation and the adoption of best practice standards and practices across strategic sectors.

6.3. Limitations and directions for future research

While this thesis provides valuable insights and contributions to how formal and informal institutions interact to establish the institutional configuration of EMDEs, and how firms and governments can and do respond to achieve their objectives, there are certain limitations and areas for future research.

Firstly, informal institutions are often implicit, unwritten and difficult to observe directly. In this study we propose the use of proxies of three broadly accepted norms, which have worked reasonably well. More however, needs to be done to bridge the gap that exists in acceptable measures for informal institutions that have undermined further research in this topic.

Furthermore, the relationship between formal and informal institutions is often complex and dynamic, with feedback loops and mutual reinforcement. This complexity makes it difficult to isolate the effects of each type of informal institution, boundary distinctions of when prevailing responses to institutions become informal institutions in their own right.

EMDEs exhibit significant variation in their historical, cultural and political backgrounds that inform their unique institutional configurations. This heterogeneity makes it challenging to generalize findings across countries and develop universal theories about the interaction of formal and informal institutions.

Directions for future research

Looking ahead, there are several areas that deserve further attention. Researchers need to explore and establish more effective methods for identifying and measuring informal institutions, which could include establishing and codifying the boundary criteria for when responses to weak or absent formal institutions become informal institutions, and how these can be captured and measured reliably. This is central to investigating and developing a better understanding of the interplay and interactions between formal and informal institutions in EMDEs.

Research is also needed to isolate and better understand the factors that shape the interaction between formal and informal institutions across different countries. This is needed to address the complexities associated with the significant heterogeneity across EMDEs, and could involve multi-country indepth case studies that examine the historical, cultural and political factors that influence the prevalence and impact of informal institutions.

Finally, future studies that seek to bridge the research and policy divide is crucial to ensuring that research output from academic institutions can be repurposed to support evidence-based policy making that can support and enable sustainable economic development and social progress in EMDEs.

REFERENCES

Bagire, V., & Namada, J. 2015. Management theory, research and practice for sustainable development in Africa : A commentary from a practitioner's perspective. Africa Journal of Management, 1(1): 99–108.

Barasa. L., Knoben J., Vermeulen P., Kimuyu P., Kinyanjui B. (2017). Institutions, resources and innovation in East Africa: A firm level approach. Research Policy, 46, 280–291.

Barbalet J., 2022 Conceptualising informal institutions: Drawing on the case of guanxi. British Journal of Sociology, 74 (1):70-82.

Borensztein, E., Gregorio, J. D., & Lee, J. (1998). How does foreign direct investment affect economic growth?. Journal of International Economics, 45(1), 115-135.

Bothello, J., Nason, R. S., & Schnyder, G. (2019). Institutional Voids and Organization Studies: Towards an epistemological rupture. Organization Studies, 40(10), 1499–1512.

Cantwell, J., Dunning, J. & Lundan, S. (2010). An evolutionary approach to understanding international business activity: The co-evolution of MNEs and the institutional environment. J Int Bus Stud 41, 567–586.

Darr, A. (2003) Gifting Practices and Inter-Organisational Relations: Constructing Obligations Networks in Electronics Sector. *Sociological Forum* 18(1), p31-51.

Dau, L. A., Li, J., Lyles, M. A., & Chacar, A. S. (2022). Informal institutions and the international strategy of mnes: effects of institutional effectiveness, convergence, and distance. Journal of International Business Studies, 53(6), 1257-1281.

Doh, S. Rodrigues, Saka-Helmhout, M. Makhija (2017) International business responses to institutional voids. J. Int. Bus. Stud., 48 (2017), pp. 293-307

Dolfsma, W., van der Eijk, R., & Jolink, A. (2009). On a source of social capital: Gift exchange. *Journal of Business Ethics, 89*(3), 315–329.

Frye, T., & Shleifer, A. (1997). The invisible hand and the grabbing hand. The American Economic Review. Vol. 87, No. 2, Papers and Proceedings of the Hundred and Fourth Annual Meeting of the American Economic Association (May, 1997), pp. 354-358

Ge, J., Carney, M., & Kellermanns, F. (2019). Who Fills Institutional Voids? Entrepreneurs' Utilization of Political and Family Ties in Emerging Markets. Entrepreneurship Theory and Practice, 43(6), 1124–1147.

George, G., Corbishley, C., Khayesi, J. N. O., Haas, M. R., & Tihanyi, L. 2016. Bringing Africa in: Promising directions for management research. Academy of Management Journal, 59(2): 377–393.

Helmke, G. and Levitsky, S. (2004). Informal institutions and comparative politics: a research agenda. Perspectives on Politics, 2(04), 725-740.

Holmes, R. M., Miller, T., Hitt, M. A., & Salmador, M. P. (2013). The Interrelationships Among Informal Institutions, Formal Institutions, and Inward Foreign Direct Investment. Journal of Management, 39(2), 531–566.

Hoskisson, R. E., Wright, M., Filatotchev, I., & Peng, M. W. (2012). Emerging multinationals from mid-range economies: the influence of institutions and factor markets. Journal of Management Studies, 50(7), 1295-1321.

Kafouros, M., Chandrashekar, S. P., Aliyev, M., & Ming Au, A. K. (2022). How do formal and informal institutions influence firm profitability in emerging countries? Journal of International Management.

Khanna T. & Palepu K. G. (1997). Why Focussed Strategies May Be wrong for Emerging Markets. Harvard Business Review (July – August 1997). 28(1), 100890.

Khanna, T., Palepu, K. G., and Bullock, R. (2010) Winning in Emerging Markets: A Road Map for Strategy and Execution. Boston: Harvard Business Press.

Krammer, S. (2017). Greasing the wheels of change: bribery, institutions, and new product introductions in emerging markets. Journal of Management, 45(5), 1889-1926.

Li, X. and Liu, X. (2005). Foreign direct investment and economic growth: an increasingly endogenous relationship. World Development, 33(3), 393-407.

Mair, J., Marti, I. and Ventresca, M.J. (2012) Building Inclusive Markets in Rural Bangladesh: How Intermediaries Work Institutional Voids. Academy of Management Journal, 55, 819-850.

Mauss, M. (1954). The gift. Forms and Functions of Exchange in Archaic Societies. Cohen and West, London.

Mbalyohere, C. G. (2016). Corporate political activity in sub-Saharan Africa: the influence of multinational enterprises in the institutionalisation of Uganda's electricity industry. PhD thesis The Open University.

Mbalyohere, C., Lawton, T., Boojihawon, R., & Viney, H. (2017). Corporate political activity and location-based advantage: MNE responses to institutional transformation in Uganda's electricity industry. J. World Bus., 52 (6) (2017), pp. 743-759

Mbate, M. (2016). Industrial Policy and Structural Change: Some Policy Perspectives. In: Seck, D. (eds) Accelerated Economic Growth in West Africa. Advances in African Economic, Social and Political Development. Springer, Cham.

McMillan, M., & Headey, D. (2014). Introduction–understanding structural transformation in Africa. World Development, 63, 1-10.

Newman, C., Page, J., Ran, J., Shimeles, A., Soderbom, M., & Tarp, F. (2016), 'Can Africa Industrialize?', in Newman et al., (eds), Manufacturing Transformation: Comparative Studies of Industrial Development in Africa and Emerging Asia (Oxford, 2016),

North, D. C. (1990). Institutions, institutional change and economic performance.

North, D. C. (1991). Institutions. Journal of Economic Perspectives, 5(1), 97-112.

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. (2016). Markets and institutional swamps: tensions confronting entrepreneurs in developing countries. Journal of Institutional Economics, 13(2), 243-269.

Palepu, K. G., & Khanna, T. (1998). Institutional Voids and Policy Challenges in Emerging Markets. The Brown Journal of World Affairs, 5(1), 71–78.

Peng, M.W., Sun, S.L., Pinkham, B. and Chen, H. (2009) The Institution-Based View as a Third Leg for a Strategy Tripod. Academy of Management Perspective, 23, 63-81.

Qiu, T., Zhang, D., Choy, S. T. B., & Luo, B. (2021). The interaction between informal and formal institutions: A case study of private land property rights in rural China. *Economic Analysis and Policy*, *72*, 578–591.

Rodrıguez-Pose, A. (2013). Do Institutions Matter for Regional Development? *Regional Studies*.

Rodrik, D. (2008). The real exchange rate and economic growth. Brookings Papers on Economic Activity, 2, 365-439.

Rodrik, D. (2016). An African Growth Miracle? *Journal of African Economies*.

Rottig, D. (2016). Institutions and emerging markets: effects and implications for multinational corporations. International Journal of Emerging Markets, 11(1), 2-17.

Saka-Helmhout, A., Chappin, M., & Vermeulen, P. (2020). Multiple Paths to Firm Innovation in Sub-Saharan Africa: How informal institutions matter. Organization Studies, 41(11), 1551-1575.

Scott, W. R. (1995), Institutions and Organizations. Ideas, Interests and Identities. Sage (1995) Language: English ISBN: 978-142242224

UNIDO and UNCTAD (2011) "Economic Development in Africa Report: Fostering industrial development in Africa in the new global environment". Special Issue

UNCTAD/ALDC/Africa/2011

Veblen, Thorstein B. "The Limitations of Marginal Utility." In: *The Place of Science in Modern Civilization*, Thorstein Veblen , pp. 231-51. New York: Russell and Russell, 1961.

World Bank, (1995). World Development Report: Workers in an Integrating World. Washington, DC: The World Bank

World Bank, (1998). World development report 1998/1999: Knowledge for development. The World Bank.

Xu, Y., & Yao, Y. (2015). Informal Institutions, Collective Action, and Public Investment in Rural China. American Political Science Review, 109(2), 371-391.

Zoogah, D. B., & Peng, M. W. 2015. Effectiveness in Africa. Academy of Management Perspectives, 29(1): 7–31.

SUMMARY

Overall, the findings presented in this doctoral thesis highlight the need for MNEs to recognise that EMDE institutions – particularly those at the earlier stages of institutional reform are distinctively different from developed country institutional environments (Rottig, 2016) and as such, require distinct capabilities not required in western style institutional environments.

EMDEs are characterised by a number of unique institutional features that make them distinct from the home-country institutions advanced-country MNEs (AMNEs) are used to; and in the case of sub-Saharan Africa, which we examine to some degree, have evolved from their unique histories and social norms (Mbalyohere et al., 2017).

MNEs operating in these markets must develop distinct capabilities for addressing the prevalence of what is typically referred to as institutional voids, but in reality, reflect a different institutional mix than AMNE firms operating in EMDEs are used to.

The purpose of this thesis is to contribute to this debate through a series of empirical and qualitative studies that explore how MNEs navigate different institutional environments in EMDEs.

The thesis takes a mixed-methods approach to identify and empirically test three social norms that are adopted as proxies for informal institutions. It also draws on case study evidence of MNEs operating across Africa from advanced and emerging economies, to argue that the wide-scale reality of institutions that significantly differ from what some MNEs are familiar with, should not necessarily imply an absence of institutions.

In an attempt to bridge the divide between academic research and practice, a chapter is dedicated to developing policy imperatives for implementing some of the insights generated from this thesis to attract FDI for developing agro-processing capabilities through special economic zones in Africa.

More specifically, it addresses the research questions summarised below:

Research Questions and Findings

Chapter 2 | *Can Management Effort and Bribes Compensate for low-quality institutions in Africa?*

Faced with weak or under-developed institutions, as observed in sub-Saharan Africa, foreign and domestic firms alike need to compensate for or seek alternative strategies to obtain what they need for their firms to operate (Veblen, 1961).

Drawing on a sample of firms surveyed from 35 African countries over a ten-year period (2006 – 2015), this paper empirically tests the expectation that without high-quality institutions – reflected in the existence of transparent, predictable and enforced rules (World Bank, 1998), top management teams are faced with one of two options – either spending a lot of effort and time (TMT efforts) monitoring and responding to inefficient bureaucratic procedures and authorities to access utility services, relevant licences, permits and other government services. Alternatively, they may choose to make informal payments to create an obligation (Darr, 2003; Dolfsma et al., 2009) for public sector officials working in public authorities to deliver public services that match the needs and expectations of their companies in a timely manner.

Under these conditions, informal payments and TMT efforts would be considered substitutes for high-quality institutions (Helmke, 2004) and be able to compensate for the strength or quality of a country's institutional furniture.

This is found to be true only for the former. Comparatively less top management effort is required to navigate regulations in high-quality institutional environments. Predictably, TMT efforts dealing with authorities and regulations also have a significant direct and negative impact on firm performance.

However, surprisingly, informal payments are not a substitute for low-quality institutional environments. This is perhaps reflective of the idea that while gift-giving is thought to create and sustain relationships between individuals, much uncertainty exists in societies characterised by low institutional quality, which implies that the circumstances for relations to be stable and afford sufficient time to encapsulate the three essential aspects of gift-giving; i.e., giving, receiving and reciprocating (Mauss, 1954), may be absent.

The positive effect of high-quality institutions on firm performance, however, is enhanced by informal payments, even though informal payments do not directly affect firm performance.

In other words, SSA countries that have relatively high-quality institutions may still not have high enough quality institutions that treat all equally and equally efficiently. Their relative stability, however, allows recipients of informal payments the latitude to respond or reciprocate by ensuring the giver of the gifts receives the services they would otherwise have been unable to access when they needed it, or spend extensive periods of time waiting. It is a complex interplay, that is commonplace in EMDEs, but not exclusive to this category of countries (Olthaar et al., 2017, Krammer, 2019)

While these findings raise ethical questions given the implications for corruption in EMDEs, they provide, at least in part, empirical support for the view that an inappropriate or unsatisfactory institutional 'furniture' (Veblen, 1961, p.236) forces managers of firms to seek alternative routes to obtain what they need for their firm to function. It also provides the opportunity to reflect on whether the perception of gift-giving, considered more culturally acceptable in some EMDEs, can or should be examined in the context of a cultural norm.

Chapter 3 | *To what extent does the experience of MNEs operating in Africa equate the existence of different institutional environments across Africa, with the notion of 'institutional voids'?*

The concept of 'institutional voids' ignores the reality that African institutions have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that may be different from other regions and worthy of closer examination (Mbalyohere et al., 2017). Olthaar et al. (2017) for instance, have suggested that informal norms, practices, or formal institutions from a different or adjacent practice or domain still affect firms, even where formal institutions that regulate the proper functioning of markets and economic activity are absent or do not function as expected.

In essence, while the wide-scale reality is that institutions in Africa differ significantly from what some MNEs are familiar with, this does not necessarily imply the absence of institutions (Olthaar et al., 2017). Informal and formal institutions co-exist to establish the institutional mix of host countries (North, 1990; Scott, 1995; Barbalet, 2022), particularly in emerging markets. Though their enforcement is not regulated in the strict Western-style, the influence of informal institutions in EMDEs in Africa cannot be ignored (Bagire & Namada, 2015; George et al., 2016; Zoogah et al., 2015), as they form a significant part of the rules of the game that guide economic activity in these countries.

Evidence from the sample of regional AMNE and EMNEs operating in Africa (Mbalyohere, 2016) used in the case study, result in the following observations:

- EMNEs are most competitive at the early stages of pro-market reforms, when formal institutions are least developed and informal institutions are most prevalent, exhibiting capabilities that are better suited to informal institutions.
- Conversely, AMNEs adapt more effectively at later stages, reflecting capabilities to effectively respond to more formal institutions.
- When they enter strategic partnerships, however, EMNEs and AMNEs appear to create synergies and complementarity in the capabilities to respond to both informal and formal institutions.

These findings establish that what the MNEs in the study respond to, are not voids, but rather an array of institutions with generally different rules than those AMNEs from highly formally institutionalized contexts are familiar with (Mbalyohere, 2016). And that the lack of effective formal institutions, something that characterizes the early stages of pro-market reforms in sub-Saharan African and other emerging and emerging markets (Hoskisson et al., 2012) does not necessarily translate into a universal competitive disadvantage for MNEs.

In essence MNEs operating in Africa respond to a mix of informal and formal institutions that have evolved from a distinct history that accentuates the relevance of informal institutions in a manner that is distinctively different from other regions. Given this difference, MNEs need to critically consider what strategies can be transferred from institutionally different contexts; and what new capabilities are required to successfully operate across the region.

Chapter 4 | *How do formal and informal institutions interact to impact the performance of foreign and domestic firms in emerging markets and developing economies?*

EMDE institutional environments are often thought to be characterised by institutional voids defined as the absence or underdevelopment of Western-style formal institutions that regulate, facilitate and support the efficient functioning of markets and economic activity (Doh et al., 2017; Khanna & Palepu, 1997). In reality, host country environments consist and evolve over time from a complex constellation of formal and informal institutions (Doh et al., 2017; Holmes et al., 2013; Olthaar et al., 2017), which co-exist to form the institutional configuration of host-country environments (Holmes, Miller, Hitt, & Salmador, 2013; North, 1990; Rodrik, 2016; Rodrıguez-Pose, 2013; Scott, 1995; Barbalet, 2022); and collectively establish the incentive structure of a society.

While comparably more attention has however been paid to formal institutions (Doh et al., 2017, there is growing interest in better understanding informal institutions, and in particular how they inter-relate with formal institutions; and combine to impact firm strategy and performance (Doh et al., 2017).

Yet the relationship between formal and informal institutions and how they impact firm performance remains under-analysed. This is considered to be due to difficulties in establishing measures for informal institutions (Helmke & Levitsky, 2004; Xu & Yao, 2015; Qiu et al 2021), and its conflation with culture, which in IB while linked is not considered one and the same (Helmke & Levitsky, 2004). This paper seeks to make a contribution in addressing this research gap.

By proposing and operationalising measures for three widely practiced norms, identified in this paper as proxies for informal institutions as exemplified by time spent by senior managers on regulations (TMT), informal payments or bribes, and local sourcing – and testing to see if they complement or substitute formal institutions across our sample, this paper addresses a key constraint to research on the interplay between formal and informal institutions.

It explores how the institutional mix of different countries affects the performance of foreign and domestic firms. Drawing on firm-level data using the World Bank Enterprise Survey (WBES) of firms operating across 128 countries over 11 years, and empirically tests the notion of institutional voids, by examining how informal and formal institutions impacts the comparative performance of MNEs.

Generally, the study establishes that informal institutions often enhance or complement the positive effect of formal institutions; but with some intriguing regional variations. There are, nonetheless, some intriguing findings, which may underline the heterogeneity and distinct differences in the full sample, and emerging markets and sub-Saharan African sub-samples.

Notably, local sourcing and TMT efforts substitute for possibly lower quality institutions in the SSA sub-sample but not for informal payments; nor in the full sample or wider EM sample.

This finding is in line with research showing that less developed countries tend to have weaker and more underdeveloped formal institutions, the enforcement of which is also likely to be unreliable (Peng et al., 2009). In the presence of such formal "institutional voids", firms will resort to informal institutions or formal institutions developed in different and yet related fields (Olthaar, et al. 2017). The only exception is the sector-level informal payment, which complement the enabling role of formal institutions role in driving firms' performance in SSA countries instead of substituting its effect.

Meanwhile, broadly speaking informal payments or bribes across the full, EMDEs and SSA sub-samples positively impact firm performance, and suggest a complementary role. This is a remarkable and counter-intuitive finding that is hard to explain, yet probably exists because informal payments are expected and made, despite being officially seen as an activity to be frowned upon (Saka-Helmhout, 2020; Krammer, 2019, Dolfsma et al., 2009).

Chapter 5

What are the policy imperatives for attracting FDI for agro-industrial processing in Africa?

The justification for industrial policy rests on the premise that governments can drive economic development and facilitate transformative processes (Rodrik, 2004). This is relevant for emerging economies in Africa, where the potential for structural change to lead to growth and poverty is considered significant (McMillan & Headey, 2014).

Drawing on Dunning's OLI paradigm, which is adopted as the conceptual framework for this paper, this paper in light of the under-development of market-supporting institutions more generally, considers how governments in Africa can adopt policies that facilitate FDI and private capital for develop agro-processing capabilities through special economic zones for food and chemical products where the potential exists for developing a competitive or comparative advantage.

Countries that add value to their natural resources and promote labour movement to productive sectors are associated with increased per capita income and technology accumulation (UNCTAD and UNIDO 2011). Indeed, Newman, (2016) posit that rising wages and input costs in Asia could offer Africa – the poorest region per capita – a renewed opportunity to industrialise, particularly in the labour-intensive, light-manufacturing sectors such as agro-processing. Evidence from East Asia underscores the importance of commodity-based industrialisation as a viable channel for addressing poverty and unemployment (Mbate, 2016) and that new entrants can succeed in global manufacturing.

This paper contributes to this discussion by extending and applying the concept of the co-evolution of institutions and the useful framework provided by Dunning's OLI paradigm, to explore how policymakers can work with investors (Doh et al., 2008; Cantwell et al., 2010; Ge et al., 2019) and other actors to address the impact of poor, weak or under-performing institutions in the agro-industrial processing sector. For instance, by developing L advantages and promoting or incentivising the development of I advantages, African governments can create the conditions to attract foreign investors with relevant O advantages that enable them to compete favourably within the host country.

We take the view that the chronic under-resourcing and fiscal constraints faced by African governments, made worse by the covid pandemic, calls for a collaborative approach to policy formulation and implementation. This is particularly relevant for specific economically viable sectors that can be managed and operated by the private sector, that through initial pilot pro-market reforms, can see the government transition from active owner, promoter, developer, and operator role to playing a facilitator role (Frye and Shleifer, 1997; World Bank, 1995) such as in the development of agro-industrial processing zones.

While not attempting to be exhaustive, this paper draws from the extant literature on SEZs, and case study evidence of successful agro-industrial processing zones, to identify seven policy imperatives for the establishment of an integrated policy framework to support the implementation of successful agro-industrial processing zones in the region.

In conclusion, this policy paper has established the central role governments can and must play in coordinating the wide range of stakeholders and market interventions required to attract and sustain the benefits from increased FDI and private sector participation in agro-industrial zones. By adapting and contextualizing the successful implementations of AIPZs in several comparator countries, a seven-point framework is developed that African governments can use to implement tailored policy frameworks to address challenges, leverage opportunities, and promote sustainable agro-industrial development.

Main Conclusions and Future Directions

While this dissertation provides valuable insights and contributions to how formal and informal institutions interact to establish the institutional configuration of EMDEs, and how firms and governments can and do respond to achieve their objectives, there are certain limitations and areas for future research.

Firstly, informal institutions are often implicit, unwritten and difficult to observe directly. In this study we propose the use of proxies of three broadly accepted norms, which have worked reasonably well. More however, needs to be done to bridge the gap that exists in acceptable measures for informal institutions that have undermined further research in this topic.

Furthermore, the relationship between formal and informal institutions is often complex and dynamic, with feedback loops and mutual reinforcement. This complexity makes it difficult to isolate the effects of each type of informal institution, boundary distinctions of when prevailing responses to institutions become informal institutions in their own right.

EMDEs exhibit significant variation in their historical, cultural and political backgrounds that inform their unique institutional configurations. This heterogeneity makes it challenging to generalize findings across countries and develop universal theories about the interaction of formal and informal institutions.

Directions for future research

Looking ahead, there are several areas that deserve further attention. Researchers need to explore and establish more effective methods for identifying and measuring informal institutions, which could include establishing and codifying the boundary criteria for when responses to weak or absent formal institutions become informal institutions, and how these can be captured and measured reliably. This is central to investigating and developing a better understanding of the interplay and interactions between formal and informal institutions in EMDEs.

Research is also needed to isolate and better understand the factors that shape the interaction between formal and informal institutions across different countries. This is needed to address the complexities associated with the significant heterogeneity across EMDEs, and could involve multi-country indepth case studies that examine the historical, cultural and political factors that influence the prevalence and impact of informal institutions.

Finally, future studies that seek to bridge the research and policy divide is crucial to ensuring that research output from academic institutions can be repurposed to support evidence-based policy making that can support and enable sustainable economic development and social progress in EMDEs.

REFERENCES

Barasa. L., Knoben J., Vermeulen P., Kimuyu P., Kinyanjui B. (2017). Institutions, resources and innovation in East Africa: A firm level approach. Research Policy, 46, 280–291.

Barbalet J., 2022 Conceptualising informal institutions: Drawing on the case of guanxi. British Journal of Sociology, 74 (1):70-82.

Borensztein, E., Gregorio, J. D., & Lee, J. (1998). How does foreign direct investment affect economic growth? Journal of International Economics, 45(1), 115-135.

Bothello, J., Nason, R. S., & Schnyder, G. (2019). Institutional Voids and Organization Studies: Towards an epistemological rupture. Organization Studies, 40(10), 1499–1512.

Cantwell, J., Dunning, J. & Lundan, S. (2010). An evolutionary approach to understanding international business activity: The co-evolution of MNEs and the institutional environment. J Int Bus Stud 41, 567–586.

Darr, A. (2003) Gifting Practices and Inter-Organisational Relations: Constructing Obligations Networks in Electronics Sector. *Sociological Forum* 18(1), p31-51.

Doh, S. Rodrigues, Saka-Helmhout, M. Makhija (2017) International business responses to institutional voids. J. Int. Bus. Stud., 48 (2017), pp. 293-307

Dolfsma, W., van der Eijk, R., & Jolink, A. (2009). On a source of social capital: Gift exchange. *Journal of Business Ethics, 89*(3), 315–329.

Frye, T., & Shleifer, A. (1997). The invisible hand and the grabbing hand. The American Economic Review. Vol. 87, No. 2, Papers and Proceedings of the Hundred and Fourth Annual Meeting of the American Economic Association (May, 1997), pp. 354-358

Ge, J., Carney, M., & Kellermanns, F. (2019). Who Fills Institutional Voids? Entrepreneurs' Utilization of Political and Family Ties in Emerging Markets. Entrepreneurship Theory and Practice, 43(6), 1124–1147.

George, G., Corbishley, C., Khayesi, J. N. O., Haas, M. R., & Tihanyi, L. 2016. Bringing Africa in: Promising directions for management research. Academy of Management Journal, 59(2): 377–393.

Helmke, G. and Levitsky, S. (2004). Informal institutions and comparative politics: a research agenda. Perspectives on Politics, 2(04), 725-740.

Holmes, R. M., Miller, T., Hitt, M. A., & Salmador, M. P. (2013). The Interrelationships Among Informal Institutions, Formal Institutions, and Inward Foreign Direct Investment. Journal of Management, 39(2), 531–566.

Hoskisson, R. E., Wright, M., Filatotchev, I., & Peng, M. W. (2012). Emerging multinationals from mid-range economies: the influence of institutions and factor markets. Journal of Management Studies, 50(7), 1295-1321.

Kafouros, M., Chandrashekar, S. P., Aliyev, M., & Ming Au, A. K. (2022). How do formal and informal institutions influence firm profitability in emerging countries? Journal of International Management.

Khanna T. & Palepu K. G. (1997). Why Focussed Strategies May Be wrong for Emerging Markets. Harvard Business Review (July – August 1997). 28(1), 100890.

Krammer, S. (2019). Greasing the wheels of change: bribery, institutions, and new product introductions in emerging markets. Journal of Management, 45(5), 1889-1926.

Mauss, M. (1954). The gift. Forms and Functions of Exchange in Archaic Societies. Cohen and West, London.

Mbalyohere, C. G. (2016). Corporate political activity in sub-Saharan Africa: the influence of multinational enterprises in the institutionalisation of Uganda's electricity industry. PhD thesis The Open University.

Mbalyohere, C., Lawton, T., Boojihawon, R., & Viney, H. (2017). Corporate political activity and location-based advantage: MNE responses to institutional transformation in Uganda's electricity industry. J. World Bus., 52 (6) (2017), pp. 743-759

McMillan, M., & Headey, D. (2014). Introduction–understanding structural transformation in Africa. World Development, 63, 1-10.

Newman, C., Page, J., Ran, J., Shimeles, A., Soderbom, M., & Tarp, F. (2016), 'Can Africa Industrialize?', in Newman et al., (eds), Manufacturing Transformation: Comparative Studies of Industrial Development in Africa and Emerging Asia (Oxford, 2016),

North, D. C. (1990). Institutions, institutional change and economic performance.

Olthaar, M., Dolfsma, W., Lutz, C., & Noseleit, F. (2016). Markets and institutional swamps: tensions confronting entrepreneurs in developing countries. Journal of Institutional Economics, 13(2), 243-269.

Palepu, K. G., & Khanna, T. (1998). Institutional Voids and Policy Challenges in Emerging Markets. The Brown Journal of World Affairs, 5(1), 71–78.

Peng, M.W., Sun, S.L., Pinkham, B. and Chen, H. (2009) The Institution-Based View as a Third Leg for a Strategy Tripod. Academy of Management Perspective, 23, 63-81.

Qiu, T., Zhang, D., Choy, S. T. B., & Luo, B. (2021). The interaction between informal and formal institutions: A case study of private land property rights in rural China. *Economic Analysis and Policy*, *72*, 578–591.

Rodrıguez-Pose, A. (2013). Do Institutions Matter for Regional Development? *Regional Studies*.

Rodrik, D. (2016). An African Growth Miracle? *Journal of African Economies*.

Rottig, D. (2016). Institutions and emerging markets: effects and implications for multinational corporations. International Journal of Emerging Markets, 11(1), 2-17.

Saka-Helmhout, A., Chappin, M., & Vermeulen, P. (2020). Multiple Paths to Firm Innovation in Sub-Saharan Africa: How informal institutions matter. Organization Studies, 41(11), 1551-1575.

Scott, W. R. (1995), Institutions and Organizations. Ideas, Interests and Identities. Sage (1995) Language: English ISBN: 978-142242224

UNIDO and UNCTAD (2011) "Economic Development in Africa Report: Fostering industrial development in Africa in the new global environment". Special Issue UNCTAD/ALDC/Africa/2011

Veblen, Thorstein B. "The Limitations of Marginal Utility." In: *The Place of Science in Modern Civilization*, Thorstein Veblen , pp. 231-51. New York: Russell and Russell, 1961.

World Bank, (1995). World Development Report: Workers in an Integrating World. Washington, DC: The World Bank

World Bank, (1998). World development report 1998/1999: Knowledge for development. The World Bank.

Xu, Y., & Yao, Y. (2015). Informal Institutions, Collective Action, and Public Investment in Rural China. American Political Science Review, 109(2), 371-391.

Zoogah, D. B., & Peng, M. W. 2015. Effectiveness in Africa. Academy of Management Perspectives, 29(1): 7–31.

ACKNOWLEGDEMENTS

This thesis would not have been possible without the relentless support of my academic advisors, academic and non-academic colleagues at Loughborough and WUR, friends, family and external reviewers. Their invaluable investment of time and support in the development of these articles and the final thesis helped me overcome the many challenges I faced.

While I may be the one to defend this thesis, this PhD journey has been every bit a team sport. There are so many people to thank, including colleagues past and present and my friends and family who have supported me throughout this process – especially my wife and mother, who have carried the emotional and financial weight of going through this process with me, and my children – Demi and Joelah, who fill my heart with joy and love every time I see them, and inspire me every day by their commitment to become all they can dream to be, to be the best version of myself.

I must however single out for mention my academic advisors, without whom this achievement would not have been possible.

First and foremost, I would like to thank Wilfred for preparing me for the challenging process of completing a PhD, right from the process you undertook in signing me up. The process took months. It is now clear to me that you were determined to assess my commitment to pursuing and completing this process. Neither of us would have anticipated how that resolve you wanted to see me demonstrate would be tested. I thank you for your consistent support throughout this journey. How you have led my academic supervision has shaped me into a better person. It has made me more self-aware about my own leadership and how grace and strength can be balanced while being uncompromising about delivering quality outcomes. From encouraging me to translate a germ of an idea you, Kun and I discussed in a supervision meeting into a paper that was published in JEI within the first year of my PhD. This boosted my confidence in what was possible and set me on the path towards the development of a policy paper that positions my academic research as a bridge between academic and practice,

having produced a framework that can be adopted by policymakers to mobilise private capital for agro-processing zones in Africa. Our journey has been most memorable and impactful. You may not be aware that I came to see this process as an academic apprenticeship and myself as your apprentice. This is why when I had the opportunity to complete my PhD at our former university, perhaps sooner, I chose to move to WUR with you. I look forward to all that our future holds together, as I see this as merely the end of the beginning. Thanks Prof! I would not be here today without your help, encouragement and support.

Kun, I have benefitted immensely from your expert guidance and support throughout this journey. We spent many a time together reviewing and testing ideas – some of which became papers that are now in publication or under review. We have had some false starts and some setbacks; but I have thoroughly grown from our work together and your steadfast support when it counted. Your patience in helping me develop a better understanding of quantitative modelling and analysis, and interpretation of results from large complex datasets, has proven crucial in preparing for and responding to questions raised by external reviewers and conference participants throughout this journey. Thank you so much. I look forward to our future collaborations on translating academic research to evidence-based policy.

Rick, you came into the picture when I moved over to Wageningen. You have pushed me to focus on getting this PhD across the finish line. I was able to easily connect with you and your style given we both have a background in the consulting industry. Your detailed and constructive feedback has significantly improved the quality of my papers and relevance of my citations. You are a doctoral researchers dream supervisor, as you take the role of co-pilot without ever seeking to take the wheel. You have balanced clear and uncompromising constructive feedback with committed support. I have always been mindful even during the most challenging times I have faced, not to let you down, because of your level of encouragement, commitment and support in reviewing every version of the many manuscripts I have submitted for discussion and review. Thanks Prof. I look forward to what we might do next.

Valentina, I have benefitted immensely from your expertise and insights on both the content, structure and process elements of my research. Your candid, constructive and detailed feedback on all the chapters in this thesis has been instrumental in improving the presentation, logical flow and readability of each chapter. You have a kind way of passing across crucial yet critical feedback, that mirrors what I would expect to receive from external reviewers with detailed ideas of how these can be remedied to address concerns that would otherwise have become an issue. Thank you so much.

Throughout this process, I have experienced grace and favour from my academic advisors, university colleagues, friends, co-workers and family. For this, I am grateful to Almighty God from whom all blessings flow, for everyone that has been part of this journey.

I am grateful for all my work and PhD colleagues, staff and friends from Loughborough and Wageningen, and my mentors who have encouraged, supported and willed me to succeed all through this journey, and inspired me by their own success – particularly Jasmina, who showed me tremendous kindness by not only offering me free room and board in her home on my trips to Wageningen, but demonstrated such resilience and determination in her own PhD journey that it made me realise the efficacy of the words of the 21st century rapper and poet – Eminem, "*success is the only [radio edit] option, failure is not.*"

This is our achievement. Thank you to everyone who has been part of this journey.

E ṣeun gàn ní. A dúpẹ́. (Translated from Yoruba – an indigenous language spoken across West Africa, Brazil and beyond, as: Thank you. I am deeply grateful).

COMPLETED TRAINING AND SUPERVISION PLAN

Goriola G. Olusina Daniel
Wageningen School of Social Sciences
Completed Training & Supervision Plan

Wageningen School of Social Sciences

Name of the learning activity	Department/Institute	Year	ECTS*
A) Project related competences			
Research Proposal Writing	IIE/Loughborough University	2017/18	6.0
PGR Induction Course	Doctoral College/Loughborough University	2017	0.3
International Business Masterclass	Reading University	2017	2.0
Overview of Qualitative & Quantitative Research Methods	IIE/Loughborough University	2017	2.0
Qualitative Research Methods	LSE Summer School	2017	2.0
East Midlands Doctoral Conference	Nottingham Trent University	2017	1.0
SBE Doctoral Conference	Doctoral College/Loughborough University	2017	1.0
Exploring Research Article Abstracts	Doctoral College/Loughborough University	2018	0.2
Fundamentals of NVivo	Doctoral College/Loughborough University	2017/18	0.5
Making an impact with posters	Doctoral College/Loughborough University	2018	0.2
Writing your Doctoral thesis	Doctoral College/Loughborough University	2018	0.2
Getting the most out of your supervision	Doctoral College/Loughborough University	2018	0.2
Being an effective researcher	Doctoral College/Loughborough University	2018	0.2
Data Management with STATA	University College London	2018	1.0
B) General research related competencies			
"Institutional Quality and Industrial Development in Sub-Saharan Africa"	44th AIB UKI Conference, Reading University Doctoral Consortium	2017	1.0
	EIBA Conference, Politecnico, Milano Doctoral Consortium	2017	
LUL Doctoral Seminars	IIE/Loughborough University	2017-19	4.0
"Institutional Quality and Industrial Development in Sub-Saharan Africa"	SBE Doctoral Conference, School of Business & Economics, Loughborough University	2017	1.0
"How Informal institutions interact with formal institutions to impact firm performance in emerging markets"	EIBA Conference, Poznan Poland	2018	1.0
	46th AIB UKI Conference, University of Sussex	2019	

C) Career related competencies/personal development			
MEP Training Day	Careers Service/Loughborough University	2017	0.5
23rd Nigeria Economic Summit	Nigeria Economic Summit Group	2017	1.0
Chaired and moderated a Special Panel on Institutions, output of which was published in the AIB Insights Special Issue on Africa	2018 AIB Africa Chapter, Kigali Rwanda	2018	3.0
Co-chair Young Scholars Panel	2018 EIBA Conference, Poznan Poland	2018	2.0
Teaching Skills 1 - III	Doctoral College, Loughborough University	2017 - 2019	4.0
Teaching and supervision of MSc & MBA Students	Loughborough University London & Imperial College London	2017 - 2019	4.0
Total			**39.3**


WAGENINGEN
UNIVERSITY & RESEARCH