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Growth and Survival of International Joint Ventures: An External-Internal Legitimacy Perspective[†]

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The authors examine the growth and survival of international joint ventures (IJVs) from a legitimacy perspective. In a sample of 291 Sino-Japanese joint ventures in China, they found that Chinese parent age, Chinese parent size, and IJV industry relatedness to either parent had a positive effect on IJV growth and/or survival. However, IJV industry relatedness to both parents led to lower rates of IJV growth and survival. The findings highlight the importance for IJVs to obtain both external and internal legitimacy, as well as the difficulties IJVs face in acquiring internal legitimacy from both parents simultaneously.

Keywords: *legitimacy; growth; survival; international joint ventures*

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Research in international strategic management has paid growing attention to the legitimacy issues faced by multinational firms and their foreign subsidiaries (Hillman & Wan, 2005; Kostova & Roth, 2002; Kostova & Zaheer, 1999; Rosenzweig & Singh, 1991; Xu & Shenkar, 2002). Legitimacy is relevant to multinational firms because it is an important resource for gaining other resources (Zimmerman & Zeitz, 2002), and a multinational firm, like any organizational form, requires resources and social support from the environment in order to grow and survive (D'Aunno, Sutton, & Price, 1991; Meyer & Rowan, 1977). Because of the structural complexity of a multinational firm system, a foreign subsidiary is situated in both an external and an internal environment and requires resources and support from both environments. Thus, both external and internal legitimacy issues have been raised (Hillman & Wan, 2005; Rosenzweig & Singh, 1991; Westney, 1993). The external legitimacy of a foreign subsidiary is its acceptance and approval by host-country institutions, whereas internal legitimacy refers to its acceptance and approval by the parent firm and other subunits (Kostova & Zaheer, 1999). The literature has recognized the difficulty faced by a subsidiary in obtaining both external and internal legitimacy, as this would require isomorphic conformity to conflicting institutional rules and norms (Kostova & Zaheer, 1999; Xu & Shenkar, 2002).

What remains unknown, however, is whether and how this legitimacy perspective can be applied to a specific type of foreign subsidiary—an international joint venture (IJV). The uniqueness of an IJV lies in the fact that it involves, in the simplest and most typical case, a foreign parent and a local parent. The local parent constitutes a part of the IJV's local institutions, as well as a part of its internal environment. The overlap between an IJV's local and internal environments makes fulfilling the dual-legitimacy requirement an even more complicated task, as legitimacy with the local parent may evoke rejection, disapproval, and distrust by the foreign parent. With few exceptions (e.g., Xu & Shenkar, 2002), however, legitimacy-based international management research has not explored this situation. The existence of this gap is surprising, as one can easily conjecture that an IJV, because of its linkage to the local parent, enjoys more external legitimacy than a wholly foreign-owned subsidiary. Identifying the contributing and moderating factors of such legitimacy may help identify and establish the competitive advantage of an IJV.

In the following sections, we first provide theoretical background on the legitimacy perspective and its application in studies of multinational firms. We then develop hypotheses by extending the legitimacy perspective to IJVs. Next, we report our data sources and present the results of statistical analyses. Finally, we conclude by discussing implications and directions for future research.

Theory

Research in international strategic management has posited that a major cost of operating in an overseas market is the lack of external legitimacy of foreign firms (Rosenzweig & Nohria, 1994; Zaheer, 1995). This lack of legitimacy can be caused by, among other things, political and economic nationalism in the host country (Moran, 1985; Murtha & Lenway, 1994), as well as cultural and institutional distances between the host and home countries (Kogut & Singh, 1988; Kostova & Zaheer, 1999). Consequently, foreign subsidiaries of a multinational firm might display lower performance than local firms in the host country (Zaheer,

1995). To overcome this disadvantage, a foreign subsidiary can try to gain external legitimacy by conforming to the rules and norms of the local institutions (Westney, 1993). Research in this area suggests that conformity to local institutions can take a variety of forms, including isomorphism in organizational structure and practices (Rosenzweig & Nohria, 1994; Rosenzweig & Singh, 1991).

Another way to overcome this disadvantage is to form joint ventures with local firms. Being a partially owned subsidiary of a local firm, an IJV may enjoy a higher level of external legitimacy simply because it is perceived as consistent—at least partly—with its local parent, in terms of structures and practices, and therefore isomorphic with local institutions in general. This is what Suchman (1995) termed “structural legitimacy”: The organization is legitimized because the public believes that it is the “right organization for the job.” Because all local firms have some kind of local legitimacy vis-à-vis foreign firms, an IJV subsidiary of a local firm may enjoy similar legitimacy because it falls in the same category of a legitimate organization (Zucker, 1986), in this case its local parent. The more local legitimacy this parent has in the local community, the more external legitimacy the IJV enjoys.

External legitimacy, however, is not the only type of legitimacy that a foreign subsidiary needs to grow and survive. An important issue faced by a foreign subsidiary is whether it can ensure internal legitimacy within the multinational firm system. Internal legitimacy is necessary because a subsidiary typically relies on internal resources and support from its parent firm—at least initially—as a major source of its competitive advantage (Westney, 1993). As in the case of external legitimacy, internal legitimacy can be achieved by a subsidiary conforming to the rules, norms, and routine practices of the parent firm (Kostova & Zaheer, 1999; Zaheer, 1995). The nature of the relationship between a subsidiary and its parent can also influence its attainment of internal legitimacy (Kostova, 1999; Kostova & Roth, 2002).

An important issue facing any foreign subsidiary is the dual demands for obtaining both external legitimacy and internal legitimacy, and the dual pressures for conforming to both host-country and parent-firm institutional pressures (Rosenzweig & Singh, 1991; Westney, 1993). Because of the institutional distance between a firm’s host and home countries, the external rules and norms in the local environment may be substantially different from, or even in conflict with, the internal rules and norms of the firm (Kostova & Zaheer, 1999; Xu & Shenkar, 2002). Thus, it is difficult for a subsidiary to achieve external and internal legitimacy simultaneously.

Because of its structural duality, an IJV not only has difficulty in balancing external and internal legitimacy but also faces a unique challenge in determining what exactly constitutes its internal legitimacy. There are two internal structures in which an IJV is situated, corresponding to the foreign and local parents, respectively. The local parent is a part of the local institutions, whereas the foreign parent is a part of the home-country institutions. The rules and norms they represent, respectively, can potentially conflict with each other in an IJV as it tries to secure internal legitimacy by conforming to isomorphic pressures of both parents.

The Local Parent and External Legitimacy

Like other overseas ventures, an IJV has to interact with its external environment and obtain necessary resources from the environment in order to grow and survive. In comparison

to a wholly owned subsidiary, an IJV enjoys a reduced level of foreignness and a higher level of local legitimacy because of its status as partly a child organization of a local firm. Local institutional constituents may perceive the IJV to be in a morally favored taxonomic category (i.e., being local) and thus worth their support (Suchman, 1995; Zucker, 1986). An IJV may enjoy such structural legitimacy (Suchman, 1995) based on the legitimacy of a “similar” organization, namely, its local parent. In other words, the legitimacy and reputation of the local parent will spill over to the IJV (Kostova & Zaheer, 1999; Yiu & Makino, 2002). A local parent with higher legitimacy can enhance the external legitimacy of its IJVs as a result of this legitimation process.

In the literature, firm age is an important contributing factor to external legitimacy. Research has shown that increased organizational age leads to higher survival rate, whereas young organizations generally suffer from a liability of newness (Singh, Tucker, & House, 1986). Underlying this liability of newness is a young firm’s lack of social approval, constituent endorsement, and external legitimacy that come only after years of experience in providing certain products or services (Baum & Oliver, 1991; Stinchcombe, 1965). Over time, the firm may become increasingly accepted by, and isomorphic with, the local institutions through economic exchanges and social interactions with other organizations in the environment, thus obtaining cognitive or taken-for-granted external legitimacy (Carroll & Delacroix, 1982; Shane & Foo, 1999; Suchman, 1995). Regardless of its sources, the legitimacy associated with a local firm will spill over to its subsidiary in the same environment, which in turn should enhance the latter’s growth and survival chances. Thus, we posit the following:

Hypothesis 1: The age of the local parent has a positive effect on IJV growth and survival.

Firm size is another important contributing factor to external legitimacy. As with studies on organizational age, research has shown that increased organizational size leads to higher survival rate, whereas small firms confront a liability of smallness that leads to higher organizational mortality rates (Freeman, Carroll, & Hannan, 1983; Singh et al., 1986). Large size tends to legitimate organizations, to the extent that it is interpreted by external stakeholders as an outcome of an organization’s prior success and accumulated reputation, trustworthiness, and prestige (Baum & Oliver, 1991; Staw & Epstein, 2000). Thus, larger firms also enjoy cognitive, taken-for-granted external legitimacy (Aldrich & Auster, 1986; Carroll & Delacroix, 1982; Shane & Foo, 1999).

Business connections with large firms—in the form of either one-time business transactions or long-term partnerships—are likely to enhance the legitimacy of transacting parties (Barringer & Harrison, 2000). In a similar vein, having a large local firm as a partner in the joint venture arrangement helps the IJV shorten the time it takes to establish legitimacy in the local environment. The attainment of local legitimacy will, in turn, make it easier for the IJV to obtain financial and human resources in local markets and develop networks with local suppliers and buyers (Stuart, Hoang, & Hybels, 1999). All of these benefits related to the acquisition of local legitimacy through partnering with a large local firm should enhance the growth and survival of an IJV. Thus,

Hypothesis 2: The size of the local parent has a positive effect on IJV growth and survival.

Industry Relatedness and Internal Legitimacy

The requirement of internal legitimacy reflects the need of a subsidiary for resources from, and coordination by, the parent firm and other subunits in the multinational firm system. Needless to say, a subsidiary receives invested resources from its parent firm to start with. It also requires, more or less, continued support from its parent for sustained growth and long-term survival. This is where its competitive advantage lies—at least partly (Zaheer, 1995). Although all subsidiaries may be seen as “legitimate” in the eyes of the parent firm, one can reasonably argue that resource scarcity and strategic priority considerations will prompt the parent firm to provide more resources and support for the more “legitimate” subunits.

Internal legitimacy can be a result of replication of organizational structure (Rosenzweig & Singh, 1991). When firms establish their overseas subunits, there is a tendency for them to replicate their existing organizational features and practices in order to deal with uncertainty in the host market (Lu, 2002). Subsidiaries may also replicate parent structures to facilitate exchanges of inputs and outputs with the parent firm (Rosenzweig & Nohria, 1994). Compared to subsidiaries that are more locally oriented and thus more reliant on external legitimacy for their survival, these more internally oriented subsidiaries are usually under more direct control and integration by the parent firm (Hillman & Wan, 2005). As a result, parent firm practices are more easily institutionalized in the subunits that are more closely connected to the parent firm (Kostova, 1999).

An important factor that increases the connectedness between a subsidiary and its parent firm is their industry relatedness. Industry relatedness is an important channel for transferring competencies, technologies, and routines from the parent firm to an IJV (Luo, 1997, 2002). Subsidiaries that operate in the same industry segments of the parent firm enjoy an advantage over industry-unrelated subsidiaries in terms of resource match and industry-specific knowledge (Chang, 1996; Li, 1995). This suggests that industry-related IJVs are more isomorphic with parent firm practices and procedures as a result of their dependence on the parent (Kostova, 1999; Kostova & Roth, 2002). It also implies that industry-related IJVs are more similar to the parent firm in structure because, conceivably, resource and knowledge transfers will be more efficient when the recipient unit replicates the structure of the originating unit. Thus, industry-related IJVs are likely to enjoy both “procedural” (i.e., resulting from accepted procedures and techniques) and structural legitimacy internally (Suchman, 1995).

Hypothesis 3: Industry relatedness of an IJV to its foreign parent has a positive effect on IJV growth and survival.

Hypothesis 4: Industry relatedness of an IJV to its local parent has a positive effect on IJV growth and survival.

Industry Relatedness and External Legitimacy

The literature has long recognized the industry—broadly or narrowly defined—as a channel for transporting legitimacy. An industry can be a source of legitimacy from which its members will benefit or suffer (Aldrich & Fiol, 1994; Zimmerman & Zeitz, 2002; Zucker, 1988). An individual firm can also confer legitimacy on similar firms within or entering the same

industry (Haveman, 1993). Whatever credentials and reputation a local firm has, such legitimacy has the highest value when it is within the same context. Thus, a subsidiary that is not only created by a legitimate firm but also operates in the same industry segment as its creator is more likely to have legitimacy than its sister subsidiaries outside the parent's industry and than firms in the same industry that are not linked to a legitimate organization in any way.

Following this logic, we expect a positive interaction between an IJV's industry relatedness to its local parent and its external legitimacy springing from the same parent. Because industry relatedness has been associated with internal legitimacy, external legitimacy of the local parent will more easily spill over to an IJV when the IJV has internal legitimacy with the local parent.

Hypothesis 5: Industry relatedness of an IJV to the local parent strengthens the positive effect of local parent age on IJV growth and survival.

Hypothesis 6: Industry relatedness of an IJV to the local parent strengthens the positive effect of local parent size on IJV growth and survival.

Dual Industry Relatedness and Internal Legitimacy

Research on the legitimacy of multinational firms suggests that obtaining external legitimacy and maintaining internal legitimacy within the multinational firm system simultaneously are not easy tasks (Kostova & Zaheer, 1999). Subsidiaries of a multinational firm are situated in dual institutional environments (host- and home-country institutions) and under dual isomorphic pressures from these environments for conformity (Rosenzweig & Singh, 1991; Westney, 1993). Local institutions and home-country institutions represent two different sets of legitimacy rules and norms. They may place conflicting legitimacy requirements on the subsidiary, especially when there is a large institutional distance between the host and home countries (Kostova & Zaheer, 1999; Xu & Shenkar, 2002). Even if two nations' institutions are similar to each other, there are always aspects of the institutional environment that make them different to some extent—including, for example, political and economic systems (regulative institutions) and cultures (normative institutions), which constitute some basis for the prevailing rules and norms (Hofstede, 1980; North, 1990). Thus, conformity to, and legitimacy from, one of these two institutions may imply inconsistency and lack of legitimacy with the other. What extant research has not discussed, however, is the added complexity of a foreign subsidiary being an IJV, in which case the local parent is a part of the local institutions.

Although industry relatedness to a parent firm is a source of internal legitimacy with that parent, dual relatedness to both parents does not necessarily bring dual legitimacy benefits. On the contrary, given that industry relatedness is associated with the replication of structures and processes, as discussed earlier, dual industry relatedness may involve the difficult task of integrating incompatible structures and processes of the two parents, and the underlying conflicting institutional rules and legitimacy norms of the host and home institutions. An IJV that is industry related to both parents could face the risk of losing legitimacy with both sides: Both parents may be unsatisfied with the IJV because it has adopted some structures and processes that are in conflict with their own rules and norms. As this happens, the growth and survival of an IJV will be adversely affected. Thus, we posit the following:

Hypothesis 7: Industry relatedness of an IJV to one of its parents reduces the positive relationship between industry relatedness of the IJV to the other parent, on one hand, and IJV growth and survival on the other hand.

Method

Sample and Data Sources

For the implementation of our investigation, we used a sample of Japanese IJVs in China. The sample represents a history of Japanese IJVs in China formed during the period 1981-1999. This empirical setting is appropriate for the test of our theoretical framework because of the prominent role of Japanese IJVs in China and because of the significant differences between the institutional environments of Japan and those of China. With the increasing importance of the Chinese market in the world economy, China has become one of the most popular host sites for foreign direct investments (FDIs) worldwide, including those from Japan. The country has been home to 40% of Japan's annual outflows of foreign investment since 1996, and 70% of Japanese FDIs in China are established as joint ventures with Chinese firms (Beamish, Delios, & Lecraw, 1997; Lu, 2000). In addition, there are significant differences in the institutional environments in which Japanese and Chinese firms are embedded, one being a developed country, the other an emerging market, respectively. The differences between foreign and local institutions—and the difficulty in meeting legitimacy requirements for Japanese subsidiaries in China—present an ideal setting for a study on the role of legitimacy in IJVs.

We collected data on Japanese IJVs in China, and on their Japanese and Chinese parents. The source of information for the FDI of Japanese firms in China is *Kaigai Shinshutsu Kigyō Souran, Kuni-Betsu* (Japanese Overseas Investments, by Country). This information is published annually by Toyo Keizai Inc., a large Japanese compiler and publisher of business-level statistical and economic information. The data reported in *Kaigai Shinshutsu Kigyō Souran* were based on responses to questionnaires sent to all firms listed on Japanese stock exchanges, as well as to major unlisted firms. The coverage of *Kaigai Shinshutsu Kigyō Souran* is close to the population of foreign subsidiaries for Japanese firms that responded to the survey (Beamish et al., 1997). For this study, we used editions from 1986 to 2001 to develop a longitudinal database of Japanese IJVs in China.

The main source of listed Japanese parent-company information is the Nikkei NEEDS tapes, an electronic database compiled by Nihon Keizai Shinbun-sha, one of the largest compilers and publishers of statistical and corporate information in Japan. This database provides annual financial information on all Japanese firms listed on the Tokyo Stock Exchange since 1964. The information on unlisted Japanese parent companies is from the Japanese Accounts and Data on Enterprises (JADE) database, compiled by Teikoku Databank and published by Bureau van Dijk. The coverage of firm-level information of the JADE database is similar to that reported in the Nikkei NEEDS tapes.

We collected information on the Chinese parent firms from Wanfang Data Company (www.wanfangdata.com.cn), a Beijing-based business- and academic-information provider

under China's Ministry of Science and Technology. Wanfang's *Chinese Enterprises and Companies Database* was started in 1988. Its data are included in the DIALOG online systems. These data were collected through multiple means, including mailed questionnaires, telephone surveys, and printed materials, and are updated annually. Research using this data source has appeared in academic journals (Li & Wong, 2003).

Variables

Dependent variables. The first dependent variable is IJV sales growth. We operationalized this variable as the compound annual sales growth rate of an IJV. We obtained IJV sales information from *Kaigai Shinshutsu Kigyō Souran* and computed sales growth for each IJV using the following formula:

$$\text{IJV sales growth} = \left(\frac{\text{last year sales}}{\text{first year sales}} \right)^{\left(\frac{1}{\text{no. of years}} \right)} - 1.$$

IJV survival is the second dependent variable for this study. We identified exiting subsidiaries by comparing preceding editions of *Kaigai Shinshutsu Kigyō Souran* with later editions. The earliest edition we used was 1986, and the latest edition was 2001. Exits were coded as 1, and surviving IJVs were coded as 0. The duration of the IJV was computed as the number of years from foundation to its time of exit, or to 2001. We backtracked the exact exit year by consulting consecutive editions of *Kaigai Shinshutsu Kigyō Souran* from 1986 to 2001. The exit year was the year that the joint venture was delisted in the database. Although one could not equate exit completely with failure, one could expect that an IJV would remain in operation as long as it represented the most efficient organization mode (Inkpen & Beamish, 1997). For instance, a sell-off of the IJV to a third party implies a competitive setback (Park & Russo, 1996; Porter, 1987). The acquisition of the IJV by one of the partners, according to Kogut (1991), is related to unexpectedly high growth and industry concentration, which suggests that the original governance form has failed to meet changing conditions. Empirical evidence from prior studies also indicates that survival correlates positively with financial and satisfaction measures of performance (Geringer & Hébert, 1989).

We found that there were few exits in IJVs founded in the year 1999 or later. To minimize the sample bias toward survivors arising from the "honeymoon effect" (Li, 1995; Park & Russo, 1996), the sample was restricted to IJVs that were at least 2 years old.

Independent variables. We operationalized the Chinese parent's age as the difference between its founding year and that of its IJV. We measured the size of the Chinese parent by the number of employees at the time of IJV formation. We used logarithm transformation of both variables in our regressions.

Following Li (1995), we used an indicator variable to indicate whether the three-digit Standard Industrial Codes (SICs) of an IJV's primary industry matched those of its Japanese parent's primary industry at the time of the IJV foundation. If there was an overlap in an IJV and

its Japanese parent's three-digit SICs, we assigned a value of 1 to the indicator variable, industry relatedness between the Japanese parent and its IJV (Japanese parent–IJV relatedness).

We also used an indicator variable to indicate whether the three-digit SICs of an IJV's primary industry matched those of its Chinese parent's primary industry at the time of the IJV's foundation. We gave the indicator variable—industry relatedness between the Chinese parent and IJV (Chinese parent–IJV relatedness)—a value of 1 if there was an overlap in their three-digit SICs. We focused on primary industries on our coding of industry relatedness because one could reasonably expect that a firm has its maximum legitimacy in its primary industry rather than secondary industries.

Control variables. Consistent with prior research (e.g., Li, 1995; Luo, 2002), we included four measures to account for major factors at the IJV level that could affect IJV survival. They are IJV age (measured as the logarithm of years of age), IJV location (a dummy variable that we gave a value of 1 if the IJV was located in either a special economic zone or an open coastal city), IJV size (measured as the logarithm of total number of employees), and the industry in which the IJV operates (a set of industry dummies based on two-digit industry codes). We expected IJV age, location, and size to have positive effects on IJV growth and survival. Control in IJVs is an important factor affecting the survival of foreign subsidiaries (Li, 1995), although there are conflicting findings on the effect of control on IJV performance. We controlled for the Japanese parent's equity ownership in the IJV, which was measured as equity owned by the Japanese parent as a percentage of total equity in the IJV. We also controlled for Japanese expatriates in the IJV, which we defined as the percentage of Japanese expatriates among IJV employees.

We next calculated two measures to control for factors at the Japanese parent level. We computed the size of the Japanese parent as the logarithm of number of employees. We then controlled for the technological capability of the Japanese parent measured by R&D intensity (R&D expenditure as a percentage of total sales). We expected both to have a positive effect on IJV growth and survival. We further controlled for the type of company at the Chinese parent level. We used an indicator variable to identify whether a Chinese parent is a state-owned enterprise (SOE). The SOE status has brought about both advantages and disadvantages for Chinese firms (Nee, 1992; Peng & Luo, 2000). We coded the result 1 if a Chinese parent is state owned.

After matching the parent information with FDI information and deleting cases with missing values, we obtained a sample comprising 291 Sino-Japanese IJVs established in China, 83% of which were in the manufacturing industries.

We estimated two types of models to test our hypotheses. First, we ran an OLS regression analysis on the compound annual growth rate of IJVs. Second, we employed event history analysis to examine the hazard rate of IJV exit. We used exponential model specification because it provided the best fit and had the largest log-likelihood compared with other specifications such as Weibull and log-normal.

Results

Table 1 presents the descriptive statistics and a correlation matrix for this study's variables. The descriptive statistics show that the exit rate was 12%. About 47 percent of the IJVs in our samples were located in either the special economic zones or open coastal cities. On average, the number of employees was 251 for the IJVs, 10,446 for their Japanese parents, and 13,589 for their Chinese parents. Furthermore, the average equity ownership of Japanese parents was about 55%, and the average of Japanese expatriate employment was 2%. Forty-nine percent of the IJVs were in the same (three-digit SIC) industry as their Japanese parents. In contrast, only 37% of the IJVs were related to their Chinese parents. Finally, 68% of the Chinese parents were state-owned enterprises (SOEs).

We tested our hypotheses in two sets of 10 regressions. Because we tested a series of interaction effects, we mean-centered related variables to avoid the problem of multicollinearity. We report the results on IJV growth in Table 2 and display the results on IJV survival in Table 3. All models were significant. For the interpretation of the results, a positive sign indicates an improvement in IJV sales growth in Table 2, whereas a hazard ratio *lower* than 1 suggests an increase in the survival chances of an IJV in Table 3.

Model 1 in both tables is the baseline model, which only included control variables and the set of industry dummies (not reported in the tables). In Table 2, Japanese parents' equity ownership in the IJV is the only significant variable. Its positive coefficient estimate indicates that a higher level of equity owned by Japanese parents was associated with a higher rate of IJV sales growth. In Table 3, three control variables are significant. As expected, IJV sales growth had a positive impact on IJV survival, providing further evidence that IJV exit is often associated with negative economic outcomes such as low sales growth. Meanwhile, IJV age enhanced IJV survival, as did IJV size measured by the number of employees.

Hypotheses 1 and 2 make predictions about the effects of external legitimacy related to local parents. Models 2 and 3 tested these hypotheses by entering the age and size of Chinese parent firms while including all the control variables. The Chinese parent's age had a significant and positive impact on IJV sales growth ($p < .05$), but it did not have a significant impact on IJV survival. Hypothesis 1 was partially supported. In contrast, the Chinese parent's size only had a positive and significant impact on IJV survival ($p < .05$). Hypothesis 2 was also partially supported.

Model 4 in Tables 2 and 3 tested the main effect of industry relatedness between an IJV and its Japanese parent, as predicted in Hypothesis 3. As shown in Table 2, Japanese parent-IJV relatedness had a positive and significant impact on IJV sales growth ($p < .05$). Furthermore, this variable had a value smaller than 1 in Table 3 ($p < .10$), indicating a positive impact on the survival rates of IJVs. Our Hypothesis 3 received support in both the growth and survival models. Model 5 examined, in turn, the main effect of industry relatedness between an IJV and its Chinese parent, as specified in Hypothesis 4. Chinese parent-IJV relatedness was signed as predicted in both tables, but the effect was only statistically significant in Table 2 ($p < .01$). Hypothesis 4 was partially supported.

Model 6 entered all four independent variables (Chinese parent age, Chinese parent size, Japanese parent-IJV relatedness, and Chinese parent-IJV relatedness) as the baseline model

for Hypotheses 5, 6, and 7. In this full main-effect model, the signs and significance of all four independent variables remained stable, compared with those in Models 2, 3, 4, and 5—confirming the robustness of the results reported in these models.

Model 7 included the interaction term of Chinese parent age and Chinese parent–IJV relatedness to test Hypothesis 5. In a similar manner, Model 8 introduced the interaction term of Chinese parent size and Chinese parent–IJV relatedness to test Hypothesis 6, whereas Model 9 added the interaction term of Japanese parent–IJV relatedness and Chinese parent–IJV relatedness to test Hypothesis 7. To guard against spurious significance of the interaction results, we first checked whether the overall change in the fit of each model was significant, compared to Model 6, after the inclusion of each interaction term. A significant change in R^2 or chi-square suggests that the inclusion of an interaction term was a significant improvement over Model 6, the baseline model.

In Table 2, the three interactions terms introduced, respectively, in Models 7, 8, and 9 were signed as predicted, and each corresponding change in R^2 was significant. Specifically, the significant and positive sign of the interaction term of Chinese parent age and Chinese parent–IJV relatedness in Model 7 ($p < .10$) suggests that the sales growth rate of an IJV improves when its local parent is relatively old—and when the IJV operates in the same industry as this local parent—as predicted in Hypothesis 5. The positive sign of the interaction term of Chinese parent size and Chinese parent–IJV relatedness in Model 8 ($p < .05$) confirms the prediction of Hypothesis 6 that the size of the local parent further enhances IJV growth when the IJV is industry related to the local parent. Last, the negative sign of the interaction term of Japanese parent–IJV relatedness and Chinese parent–IJV relatedness in Model 9 ($p < .05$) confirms that dual-industry relatedness to both parents depresses sales growth, supporting Hypothesis 7.

In Table 3, however, only Model 9 had a significant incremental chi-square. The value of the coefficient estimate of the interaction term of Japanese parent–IJV relatedness and Chinese parent–IJV relatedness in Model 9 was larger than 1 and significant ($p < .05$), indicating that the survival rate of an IJV falls when the IJV is related to both the Japanese and Chinese parents. Taken together, Hypotheses 5 and 6 received partial support, whereas Hypothesis 7 received full support.

In the final step, we entered all the independent variables and their interaction terms in Model 10. In Tables 2 and 3, the signs and significance levels of the interaction terms remained largely unchanged from Models 7, 8, and 9, proving the consistency and stability of previously reported results.

To gain further insights into the significant interaction terms, we plotted Figures 1 through 4 for projected sales growth and expected probabilities of IJV exit in Models 7, 8, and 9 based on the significant coefficients of the four independent variables. Specifically, the plots were made for varying values of the independent variables in the interaction terms while holding all the other variables at their mean values.

We also conducted robustness checks on both dependent variables. On IJV sales growth, we ran regressions on an alternative operationalization of sales growth, average sales growth (sales differentials divided by the number of years). The regression results on average sales growth were very consistent with those reported in Table 2 on compound annual sales growth rate. For IJV survival, we estimated additional model specifications such as logistic regression and Cox proportional hazard models. The results were very similar for the different model

(text continues on p. 442)

Table 1
Descriptive Statistics and Correlations^a

Variable	M	SD	1	2	3	4	5	6	7	8	9	10	11	12	13
IJV exit	0.12	0.32	1.00												
IJV sales growth	0.11	0.34	-.16	1.00											
IJV age ^b	1.97	0.37	.01	-.15	1.00										
IJV location	0.47	0.50	.07	.05	.12	1.00									
IJV size ^b	4.85	1.15	-.16	-.05	.00	-.02	1.00								
Japanese parent's equity ownership in IJV	0.55	0.18	.02	.20	-.18	.03	-.11	1.00							
Japanese expatriates in IJV	0.02	0.04	.07	.06	-.04	.01	-.46	.22	1.00						
Japanese parent size ^b	8.17	1.33	.05	-.02	-.11	-.10	.15	-.04	.08	1.00					
Japanese parent's technological capability	0.01	0.02	-.11	-.03	-.09	-.11	.08	.02	.07	.25	1.00				
Chinese parent type (SOE)	0.68	0.47	.04	.06	.01	.07	-.05	.12	-.05	-.01	-.01	1.00			
Chinese parent age ^b	2.63	1.30	-.01	.16	-.19	-.07	-.06	.06	-.01	.06	.09	.25	1.00		
Chinese parent size ^b	7.32	1.98	-.17	.10	.04	.00	.17	.01	-.14	.19	.03	.01	.07	1.00	
Japanese parent-IJV relatedness	0.49	0.50	-.16	.15	-.16	.01	-.01	.04	.02	-.07	-.03	.03	.05	-.14	1.00
Chinese parent-IJV relatedness	0.37	0.48	-.15	.18	-.11	-.01	.08	.01	-.02	.02	.20	-.09	.12	.27	-.07

Note: IJV = international joint venture; SOE = state-owned enterprise.

a. Significant at the .05 level (two-tailed test) when Pearson correlations are > .11 or < -.11.

b. Logarithmic transformation.

Table 2
Regression on Sales Growth of 291 Sino-Japanese International Joint Ventures (IJVs) in China^{a, b}

Variable	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Constant	0.16 (0.27)	0.15 (0.27)	0.19 (0.27)	0.17 (0.27)	0.10 (0.27)	0.14 (0.27)	0.09 (0.27)	0.10 (0.27)	0.09 (0.27)	0.01 (0.26)
IJV age ^c	-0.07 (0.05)	-0.06 (0.05)	-0.07 (0.05)	-0.06 (0.05)	-0.06 (0.05)	-0.04 (0.05)	-0.04 (0.05)	-0.04 (0.05)	-0.03 (0.05)	-0.03 (0.05)
IJV location	0.04 (0.04)	0.04 (0.04)	0.04 (0.04)	0.03 (0.04)	0.03 (0.04)	0.03 (0.04)	0.03 (0.04)	0.04 (0.04)	0.03 (0.04)	0.03 (0.04)
IJV size ^c	-0.01 (0.02)	-0.01 (0.02)	-0.02 (0.02)	-0.01 (0.02)	-0.02 (0.02)	-0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)
Japanese parent's equity ownership in IJV	0.33** (0.12)	0.33** (0.11)	0.32** (0.11)	0.34** (0.11)	0.33** (0.11)	0.32** (0.11)	0.32** (0.11)	0.28** (0.11)	0.31** (0.11)	0.28* (0.11)
Japanese expatriates in IJV	0.01 (0.61)	0.07 (0.61)	0.12 (0.61)	-0.06 (0.61)	0.06 (0.60)	0.10 (0.60)	0.18 (0.60)	0.02 (0.60)	0.12 (0.59)	0.13 (0.59)
Japanese parent size ^c	0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)	0.01 (0.02)	0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)	-0.01 (0.02)	0.01 (0.02)	-0.01 (0.02)
Japanese parent's technological capability	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)	-0.01 (0.01)
Chinese parent type (SOE)	0.02 (0.04)	0.01 (0.04)	0.02 (0.04)	0.02 (0.04)	0.03 (0.04)	0.01 (0.04)	0.01 (0.04)	0.01 (0.04)	0.01 (0.04)	-0.01 (0.04)
Chinese parent age ^c (Hypothesis 1)	0.03* (0.02)	0.03* (0.02)	0.04 (0.04)	0.04 (0.04)	0.04 (0.04)	0.03 [†] (0.02)	0.03 [†] (0.02)	0.03 [†] (0.02)	0.03 [†] (0.02)	0.03 [†] (0.02)
Chinese parent size ^c (Hypothesis 2)		0.02 (0.01)				0.01 (0.01)	0.01 (0.01)	0.01 (0.01)	0.01 (0.01)	0.01 (0.01)
Japanese parent-IJV relatedness (Hypothesis 3)				0.08* (0.04)		0.09* (0.04)	0.10* (0.04)	0.10* (0.04)	0.10* (0.04)	0.10** (0.04)
Chinese parent-IJV relatedness (Hypothesis 4)					0.11** (0.04)	0.09** (0.04)	0.09** (0.04)	0.07 [†] (0.04)	0.09** (0.04)	0.07 [†] (0.04)
Chinese Parent Age ^c × Chinese Parent-IJV Relatedness (Hypothesis 5)						0.06 [†] (0.03)				0.06* (0.03)
Chinese Parent Size ^c × Chinese Parent-IJV Relatedness (Hypothesis 6)								0.05* (0.02)		0.04* (0.02)
Japanese Parent-IJV Relatedness × Chinese Parent-IJV Relatedness (Hypothesis 7)									-0.18* (0.08)	-0.17* (0.08)

R^2	.16	.17	.16	.17	.18	.21	.22	.22	.22	.22	.25
Adjusted R^2	.11	.13	.12	.12	.13	.15	.16	.17	.17	.17	.19
F-statistics	3.65***	3.77***	3.61***	3.74***	3.94***	3.95***	3.99***	4.12***	4.08***	4.22***	4.22***
Change in R^2							.01 [†]	.02*	.02*	.02*	.04*

Note: SOE = state-owned enterprise.

a. Fixed effects for two-digit Standard Industrial Codes were included in the models but are not reported in the table.

b. Cell entries are unstandardized coefficient estimates. Numbers in parentheses are standard errors.

c. Logarithmic transformation.

[†] $p < .10$ (two-tailed)

* $p < .05$ (two-tailed)

** $p < .01$ (two-tailed)

*** $p < .001$ (two-tailed)

Table 3
Survival Analysis on 291 Sino-Japanese International Joint Ventures (IJVs) in China^{a, b}

Variable	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
IJV sales growth	0.08** (0.07)	0.08** (0.07)	0.12* (0.10)	0.10** (0.09)	0.10** (0.09)	0.17** (0.15)	0.13* (0.12)	0.18 [†] (0.17)	0.22 (0.20)	0.20 [†] (0.19)
IJV age ^c	0.29** (0.12)	0.29** (0.12)	0.31** (0.13)	0.25*** (0.10)	0.29** (0.12)	0.27** (0.11)	0.27** (0.11)	0.27** (0.11)	0.24*** (0.10)	0.25*** (0.10)
IJV location	1.56 (0.59)	1.57 (0.60)	1.52 (0.57)	1.65 (0.63)	1.55 (0.59)	1.64 (0.63)	1.62 (0.63)	1.64 (0.63)	1.59 (0.62)	1.53 (0.61)
IJV size ^c	0.69* (0.12)	0.69* (0.12)	0.70 [†] (0.13)	0.68* (0.12)	0.70* (0.12)	0.71 [†] (0.13)	0.74 [†] (0.13)	0.71 [†] (0.13)	0.67* (0.13)	0.68* (0.13)
Japanese parent's equity ownership in IJV	1.07 (1.16)	1.07 (1.16)	1.34 (1.45)	0.92 (0.95)	1.09 (1.16)	1.06 (1.07)	1.12 (1.14)	1.05 (1.07)	1.01 (0.99)	1.01 (1.00)
Japanese expatriates in IJV	0.01 (0.07)	0.02 (0.08)	0.01 (0.01)	0.03 (0.13)	0.01 (0.05)	0.01 (0.01)	0.01 (0.01)	0.01 (0.01)	0.01 (0.01)	0.01 (0.01)
Japanese parent size ^c	1.18 (0.19)	1.17 (0.19)	1.25 (0.20)	1.14 (0.18)	1.17 (0.18)	1.20 (0.20)	1.20 (0.20)	1.20 (0.19)	1.15 (0.18)	1.15 (0.19)
Japanese parent's technological capability	0.86 (0.11)	0.86 (0.11)	0.87 (0.11)	0.85 (0.11)	0.88 (0.12)	0.87 (0.12)	0.87 (0.12)	0.87 (0.12)	0.85 (0.11)	0.84 (0.12)
Chinese parent type (SOE)	1.30 (0.54)	1.29 (0.54)	1.29 (0.53)	1.46 (0.61)	1.25 (0.52)	1.35 (0.59)	1.36 (0.59)	1.33 (0.58)	1.46 (0.65)	1.43 (0.64)
Chinese parent age ^c (Hypothesis 1)	1.01 (0.14)	1.01 (0.14)			1.07 (0.16)	1.07 (0.16)	1.31 (0.30)	1.08 (0.17)	1.04 (0.16)	1.32 (0.34)
Chinese parent size ^c (Hypothesis 2)			0.81* (0.08)		0.81* (0.09)	0.80* (0.09)	0.80* (0.09)	0.80* (0.09)	0.83 [†] (0.09)	0.78 [†] (0.11)
Japanese parent-IJV relatedness (Hypothesis 3)				0.45 [†] (0.19)		0.43* (0.19)	0.41* (0.18)	0.43* (0.19)	0.57 (0.27)	0.53 (0.26)
Chinese parent-IJV relatedness (Hypothesis 4)					0.60 (0.29)	0.68 (0.34)	0.42 (0.31)	0.66 (0.33)	0.80 (0.43)	0.43 (0.37)
Chinese Parent Age ^c × Chinese Parent-IJV Relatedness (Hypothesis 5)						2.38 (1.35)				2.46 (1.61)
Chinese Parent Size ^c × Chinese Parent-IJV Relatedness (Hypothesis 6)								0.87 (0.21)		0.81 (0.27)
Japanese Parent-IJV Relatedness × Chinese Parent-IJV Relatedness (Hypothesis 7)									11.30* (11.70)	8.78* (9.42)

Log-likelihood	-92.77	-92.77	-90.47	-90.95	-92.15	-88.10	-86.46	-87.94	-85.14	-83.63
Model chi-square	34.31**	34.32**	38.92***	37.95***	35.55**	43.66***	46.94***	43.98**	49.58***	52.59***
Incremental chi-square							3.28	0.32	5.92*	8.93 [†]

a. Fixed effects for two-digit Standard Industrial Codes were included in the models but are not reported in the table.

b. Cell entries are unstandardized coefficient estimates. Numbers in parentheses are standard errors.

c. Logarithmic transformation.

[†] $p < .10$ (two-tailed)

* $p < .05$ (two-tailed)

** $p < .01$ (two-tailed)

*** $p < .001$ (two-tailed)

specifications. For our key independent variables—Japanese parent–IJV relatedness and Chinese parent–IJV relatedness—we constructed alternative measures using two-digit SICs to define relatedness between parents and IJVs. The results with these alternative measures remained the same, although somewhat less significant when compared with three-digit SIC relatedness measures.

Discussion and Conclusions

Our study adds to research on legitimacy and IJVs in several ways. First, we showed that a legitimacy perspective is useful in explaining the outcome of an IJV. Although not significant in all models, our two sources of external legitimacy—local parent age and local parent size—had a positive effect on IJV growth and IJV survival, respectively. The differential results of Chinese parent age and Chinese parent size may illustrate that different sources of legitimacy have differential effects on different dimensions of IJV performance. Age-based external legitimacy makes a difference to venture growth, whereas size-based external legitimacy seems to be crucial for IJV survival. Despite the differences, our results point to the general spillover effect of external legitimacy coming from the local parent.

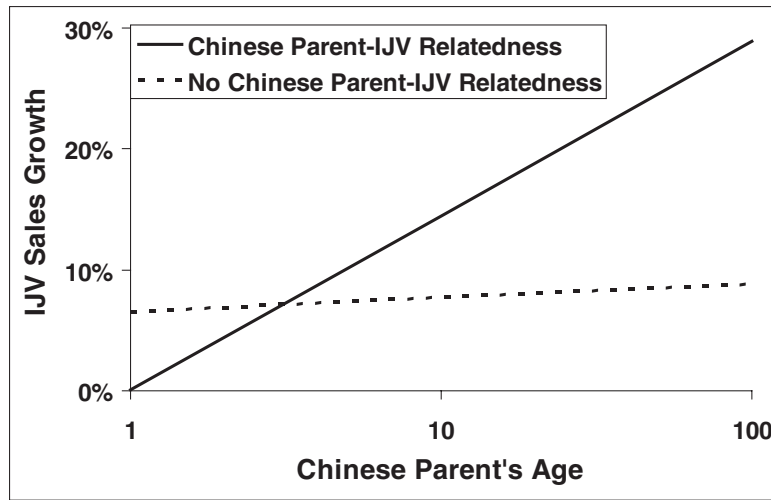
Likewise, our two sources of internal legitimacy—foreign parent–IJV relatedness and local parent–IJV relatedness—enhanced the chances of IJV growth and survival, although the positive effect of industry relatedness to the Chinese parent on IJV survival was not statistically significant. Taken together, these findings suggest that it is important to consider legitimacy consequences when firms choose partnering and product-diversification strategies in overseas markets. We urge researchers to consider additional factors in the IJV legitimation process to further the application of a legitimacy perspective to the IJV context.

Second, the findings regarding the interaction effects suggest that external legitimacy and internal legitimacy are interdependent, rather than independent, factors in IJVs. Our results indicate that industry relatedness of an IJV to its local parent will strengthen the positive effect of the local parent's age and size. This highlights the importance of the simultaneous attainment of both external and internal legitimacy.

Third, our analysis on the interaction effects also points to the negative impact of industry relatedness of an IJV to both foreign and local parents, which may arise from the conflicting legitimacy requirements of these parents. Whereas literature in international management has discussed some implications of internal legitimacy for a subsidiary and its strategies (Hillman & Wan, 2005; Kostova, 1999; Kostova & Zaheer, 1999), we go further by investigating the potential downside of trying to achieve “unified” legitimacy in a complex internal environment such as that of an IJV.

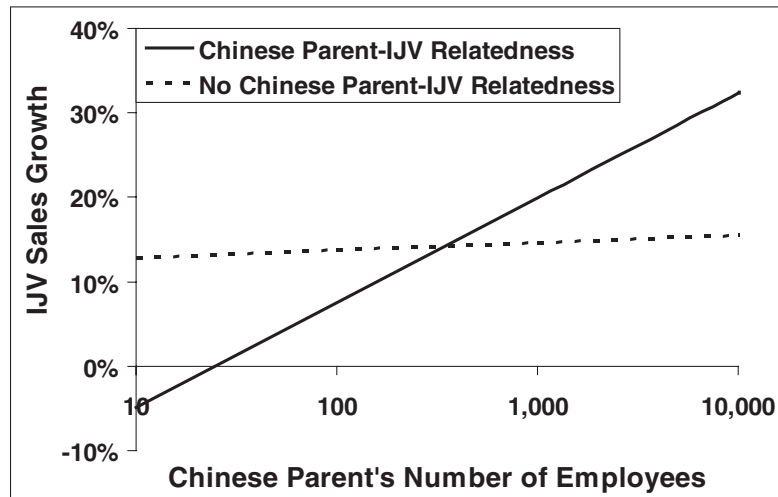
The negative interaction effect on growth and survival depicted here seems to contradict the findings of Luo (2002). This could be due to the fact that our sample consisted of parent firms from two countries with a relatively large institutional distance, whereas Luo's sample covered parent firms from a mixture of home regions, including Hong Kong and Singapore. The differences in the samples, coupled with the contrasting results between our study and Luo (2002), seem to suggest that the level of internal conflict when an IJV is related to both parents may be associated with the institutional distance between the host and home countries. Even

Figure 1
Interaction Effect of Chinese Parent Age and
Chinese Parent-IJV Relatedness on IJV Growth^a



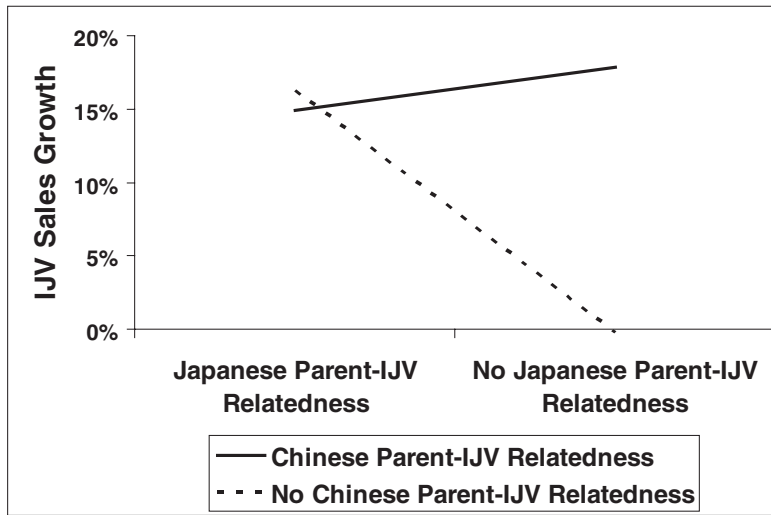
Note: IJV = international joint venture.
 a. X-axis uses logarithmic scale.

Figure 2
Interaction Effect of Chinese Parent Size and
Chinese Parent-IJV Relatedness on IJV Growth^a



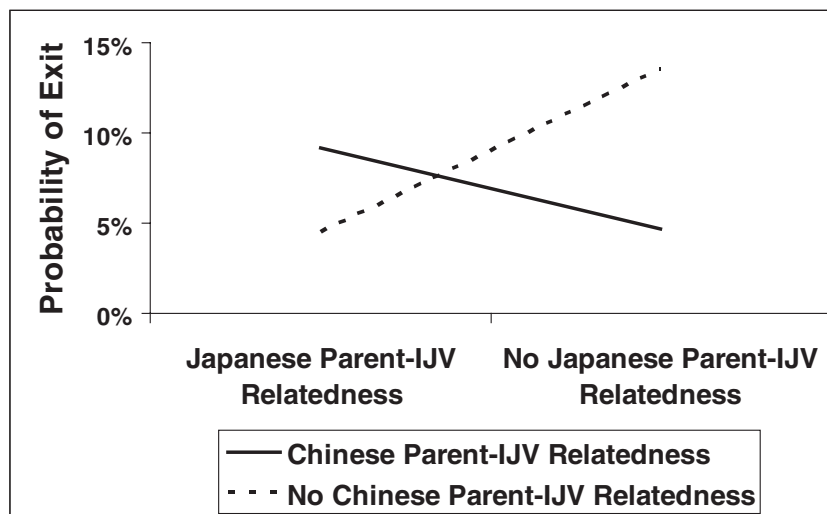
Note: IJV = international joint venture.
 a. X-axis uses logarithmic scale.

Figure 3
Interaction Effect of Japanese Parent-IJV Relatedness and Chinese Parent-IJV Relatedness on IJV Growth



Note: IJV = international joint venture.

Figure 4
Interaction Effect of Japanese Parent-IJV Relatedness and Chinese Parent-IJV Relatedness on IJV Survival



Note: IJV = international joint venture.

so, managers need to carefully consider the internal organizational implications of product-diversification strategy in international expansion.

Fourth, the present study is one of the few empirical studies to examine factors leading to IJV survival and growth mainly from a local parent's perspective. Although research in IJVs has emphasized the various advantages of having a local partner (Beamish & Banks, 1987; Buckley & Casson, 1996), many empirical studies simply equated a local partner to local knowledge or local advantage, which in turn should contribute to IJV success (e.g., Makino & Delios, 1996). In contrast, this study begins to "decompartmentalize" the broad concept of local advantage and explore the aspects of the local parent that are most relevant to the performance of an IJV from a legitimacy perspective. The significant effects of local parent age and local parent size we found in this study suggest that without such investigation, our understanding of the true contribution of local partners is rather limited. In this sense, the present study may be a good starting point to shift the attention of current research on IJVs from a preoccupation with foreign parent-based competitive advantages or learning benefits (Delios & Beamish, 2001; Lyles & Salk, 1996; Yiu & Makino, 2002) to more locally oriented considerations.

Finally, one of the strengths of this study is its use of both growth and survival as measures of IJV success. Empirical research in strategic management has long been criticized for having a sampling bias toward surviving firms; on the other hand, researchers focusing on joint-venture survival/exit have been unable to establish an unequivocal relationship between IJV exit and failure (Yan & Zeng, 1999). The inclusion of both survival and growth performance in this article, and the consistent results for both of them, may alleviate a major criticism against research in this field.

It is also important to note the limitations of the present study. The most notable of these is the fact that our empirical results were derived from a sample of Japanese IJVs in China; hence the concern that the findings might be country-specific. We believe that our findings are applicable to other countries because all foreign subsidiaries are subject to external and internal legitimation processes (Hillman & Wan, 2005). However, the level of conflict in the dual internal legitimation processes (argument for Hypothesis 7) is likely to differ as the institutional distance between the host and home countries changes. We expect that as institutional distance decreases, the level of legitimacy conflict will decrease, and relatedness to both parents might have a less negative—or even positive—effect on IJV performance. Therefore, it is important for future studies to use samples from other countries in order to test and extend the generalizability of our findings.

In addition, we examined industry-based relatedness, although there could be other types of relatedness, such as asset-based relatedness, as recommended by Markides and Williamson (1994). An exploration of other types of relatedness between an IJV and its parents in future studies will enrich our understanding of the relatedness issue. For industry relatedness, we focused on primary industries in our coding of the relatedness measure. Similar measures could be developed for secondary industries. Although we did not have information on secondary industries, it would be useful for future studies to compare the effects of industry relatedness based on primary industries and secondary industries to assess the reliability of our measure.

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