The Effects of Ownership Concentration and Institutional Distance on the Foreign Equity Ownership Strategy of Turkish MNEs

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ABSTRACT

We investigate how ownership concentration and institutional distance both directly influence the equity-based ownership strategies of a sample of Turkish MNEs, and also how institutional differences moderate the link between ownership concentration and the equity-based ownership strategies of these firms. The findings suggest that neither ownership concentration nor institutional distance significantly affects the level of equity ownership. Although institutional distance variables have no direct effects on equity ownership, they tend to moderate the relationships between the ownership concentration and foreign equity ownership strategy of Turkish MNEs. In particular, we provide evidence that the regulative and normative dimensions of institutional distance affect the strength of the relationships between equity ownership strategy of MNEs and ownership concentration more so than the cognitive dimension of institutional distance.

1. Introduction

Over the last two decades, international equity ownership strategies of multinational enterprises (MNEs) have attracted a good deal of attention (Brouthers & Hennart, 2007; Pla-Barber, Sanchez-Peinado, & Madhok, 2010). Despite increasing interest in the strategies of emerging country (EC) MNEs (Brouthers, Brouthers, & Werner, 2000; Filatotchev, Strange, Piessel, & Lien, 2007; Peng, Wang, & Jiang, 2008; Demirbag, Tatoglu, & Glaister, 2009), there is a paucity of empirical research that explores the effect of their corporate governance (CG) mechanisms by considering the institutional context of emerging markets (Bhaumik, Driffield, & Pal, 2010). Some studies examine the association between ownership concentration and international entry mode selection (e.g. Rhoades & Rechner, 2001; Musteen, Datta, & Herrmann, 2009; Meyer, Ding, Jing, & Zhang, 2014) or export behavior (e.g. Lu, Xu, & Liu, 2009; Hobdari, Gregoric, & Sinani, 2011). Only one study (Bhaumik et al., 2010), has examined the effect of ownership concentration on equity ownership of MNEs from EC MNEs.

This study provides several contributions to the literature. Presenting an integrative model, we investigate how the conflicts between large and small shareholders from the viewpoint of the principal-principal perspective affect the equity ownership of EC MNEs in their internationalization process. This contributes to the literature on MNEs' entry strategies in emerging countries, which has mainly concentrated on investigating the impact of ownership concentration from the principal-agent perspective (Lu et al., 2009). Furthermore, we test the interaction effects of institutional factors and ownership concentration on foreign equity ownership strategies of EC MNEs, as this perspective has been largely neglected in previous research. We intend to fill this lacuna by analyzing both the direct and interaction effects of the ownership and institutional differences on equity ownership strategies of EC MNEs.

Developed and emerging countries vary greatly with regard to the investment environment and institutional factors that may influence MNEs' strategy choices of equity ownership in their subsidiaries (Makino, Isobe, & Chan, 2004). A general feature of emerging countries is that market-supporting institutions are less developed, and hence restrict MNEs' strategic decisions (Khanna & Palepu, 2000; Yaprak & Demirbag, 2015). Emerging countries are assumed to have weaker institutional environments than developed countries. The uncertainty caused by a weak institutional environment complicates the legitimacy process for EC MNEs, while certain

institutions in developed countries are expected to facilitate isomorphism. This gives rise to an interesting research topic concerning the impact of institutional dissimilarities between home and host country on EC MNEs' equity ownership strategies. Concentrating on this research gap, this study improves an institutional based view of international business strategy by examining ownership strategies of EC MNEs that invest in both developed and emerging country markets.

Turkey is chosen as the site of this research because its characteristics make it a good representative example. In Turkey, structural diversity is weak, ownership is concentrated, and external monitoring is ineffective (Ararat, Aksu, & Tansel, 2015, p. 84). Furthermore, the structure of industrial organizations in Turkey resembles that of other emerging countries, such as, Brazil, Mexico, India and South Korea (Demirbag, Mirza, & Weir, 1995). MNEs from these countries need to cope with some challenges, such as, weak knowledge infrastructure, the liability of emergingness[1], and capability gap between themselves and their rivals in developed countries (Wilkinson, Wood, & Demirbag, 2014). Turkey is a country in the French civil law tradition that is least protective of minority shareholders (La Porta, Lopez-de-Silanes, Shleifer, & Vishny et al., 1997). Selekler-Goksen and Karatas (2008) note that external CG mechanisms are quite poor in Turkey. Families own more than two-thirds of all listed businesses and maintain majority control (Yurtoglu, 2003). Hence, it is not likely to rely on the market for corporate control as an external mechanism for CG (Selekler-Goksen & Karatas, 2008). In corporate environments, where there is no active market for corporate control, the emerging CG form is concentrated ownership (Gunduz & Tatoglu, 2003). Gursoy and Aydogan (2002) point out that ownership concentration is a significant determinant of CG mechanism in Turkey, and conclude that identifying controlling owners may significantly affect risk-taking behavior of the firms, where higher concentration leads to less risk-taking.

Recently, Turkey has experienced significant economic success and institutional change, but as an emerging country, it is still characterized by its fluid and weak institutions (Demirbag et al., 2014). Despite a fluid institutional structure, Turkey has generated a significant amount of both inward FDI and outward FDI (Vale Columbia Center, 2014). Therefore, the Turkish context

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[1]Emerging market MNEs face additional weaknesses due to their country of origin in addition to the *liability of foreignness* that they generally have to deal with while operating in foreign markets, (Nair, Demirbag and Mellahi, 2015). These are often acknowledged as the "*liability of emergingness*" (Madhok & Keyhani 2012, p. 28).

provides a relevant research setting for examining EC MNEs' equity ownership strategies since its proximity to, and level of integration with, the European Union (EU) creates both marketization and infusion of several social characteristics of the EU model (Agartan, 2010). Despite this, relatively few studies investigate the entry mode selection of Turkish MNEs' foreign affiliates (Demirbag et al., 2009; Anil, Tatoglu, & Ozkasap, 2014), with most prior studies in the Turkish context focusing on entry mode strategy of Western MNEs in Turkey (Tatoglu, Glaister, & Erdal, 2003; Demirbag, Tatoglu, & Glaister, 2008, 2010). Importantly, no prior studies investigate the direct or interaction effects of ownership concentration and institutional distance on Turkish MNEs' foreign equity ownership strategy. This study provides a crucial attempt to fill this lacuna by investigating the moderating impact of home country institutional factors on the link between ownership concentration and Turkish MNEs' equity ownership strategies.

2. Theoretical background and hypotheses

To investigate the foreign equity ownership decisions of MNEs, we integrate two key theoretical streams – agency theory and institutional theory – but also take into account an emerging country setting. Agency theory posits that ownership structure is a substantial element in the strategic decision-making process in MNEs by influencing perception of, and attitude towards, risk in internationalization activities (Filatotchev & Wright, 2011). Ownership structure may be a key antecedent of managerial ability to implement internationalization strategies (Carpenter & Fredrickson, 2001; Filatotchev, Stephan, & Jindra, 2008). However, the impact of ownership structure on the internationalization strategy of EC MNEs is likely to be different from that of developed country MNEs (DC MNEs), viz., there may be significant differences between equity ownership choices of DC MNEs and EC MNEs in terms of different CG mechanisms (Filatotchev et al., 2007; Cuervo-Cazurra, 2012).

CG research conducted in western settings is mostly based on principal-agent conflict (Jensen & Meckling, 1976), emanating from the separation of ownership and control (Berle & Means, 1932). In contrast, in emerging countries, the principal-agent conflict turns into a principal-principal conflict between controlling shareholders and minority shareholders (Young, Peng, Ahlstrom, Bruton, & Jiang, 2008). As noted, a key feature of many emerging countries is that market-supporting institutions are too weak to regulate governance matters and thus confine the firm's

strategic choices (Ramamurti, 2004). In this context, based on agency theory the board and ownership structures, responsibilities, actions, and risk aversion of EC MNEs are significantly dissimilar from those in developed countries. Consequently, the effect on entry strategy of the ownership structure is context-dependent, with EC MNEs following different internalization paths (Demirbag et al., 2009) and entry strategies (Filatotchev et al., 2007) from their counterparts in developed countries.

A second theoretical perspective we adopt is institutional theory (DiMaggio & Powell, 1983; Scott, 1995), which presents a conceptual tool to examine the key antecedents of strategies of EC MNEs (Peng, 2003; Wright, Filatotchev, Hoskisson, & Peng, 2005). Institutions are usually defined as the "rules of the game in a society" (North, 1990, p. 3). These involve formal rules and informal constraints, which form the strategy of MNEs (Meyer & Peng, 2005). In this context, the main thesis of institutional theory is that the survival and success of an MNE depends on its conformity to the belief systems and rules prevalent in the market environment (Deephouse, 1996; Xu & Shenkar, 2002; Dacin, Oliver, & Roy, 2007). Drawing on existing conceptual work by Scott (1995) and Kostova (1996), we expand the notion of distance by including regulative, normative and cognitive pillars (Kostova & Roth, 2002; Xu & Shenkar, 2002).

Institutional sources of inefficiency at home may force EC MNEs to enter developed markets where they may have access to new capabilities, which enable them to close knowledge and capability gaps between themselves and their developed country rivals. Therefore, institutional voids provide significant motives for EC MNEs to create a portfolio of international operations in emerging and developed markets (Khanna & Palepu, 2006). Often, these are in the form of mergers and acquisitions through which EC MNEs aim to manage the liability of emergingness (Hennart, 2012), and increase reverse knowledge flow from acquired subsidiaries (Nair, Demirbag, & Mellahi, 2015). In this study, we improve the extant research on EC MNEs' internationalization by examining the impact of the parent level ownership concentration based on an institutional theory perspective.

2.1. The impact of ownership concentration on EC MNE ownership strategies

Internal CG characteristics, such as share ownership structure, influence the strategies of EC MNEs, and consequently their internationalization efforts (Filatotchev et al., 2007; Hodbari,

Gregoric, & Sinani, 2011), because different types and levels of owners have various degrees of risk aversion and decision-making views (Thomsen & Pedersen, 2000; Hoskisson, Hitt, Johnson, & Grossman, 2002; Filatotchev, Lien, & Piesse, 2005). The interests of shareholders vary with respect to their extent of equity stake in the parent company (Musteen, Datta, & Herrmann, 2009). The more concentrated the ownership of the EC MNE, the lower the likelihood of its equity ownership in foreign subsidiaries (Laamanen, Simula, & Torstila, 2012).

Agency theory views minority shareholders, who can distribute their overall risk in diversified portfolios, as risk neutral (Rhoades & Rechner, 2001; Wright, Kroll, Lado, & Van Ness, 2002). Minority shareholders' interests of maximizing return on investment lead to higher risk and higher return equity ownership, for instance, a wholly owned subsidiary (WOS) instead of a joint venture (JV). According to agency theory, based on principal-agent conflict, ownership concentration and the presence of dominant shareholders play a central role in protecting minority shareholders' interests against management (Aguilera & Jackson, 2003; Filatotchev & Wright, 2011). However, in an emerging country, this relationship can be different, as the principal-agent conflict turns into a principal-principal conflict between controlling shareholders and minority shareholders (Peng et al., 2008; Young et al., 2008). As external CG mechanisms are poor in many emerging countries, it is not possible to hinge on the market for corporate control as an external CG mechanism (Selekler-Goksen & Karatas, 2008). In the absence of active market for corporate control, concentrated ownership is an optimal response to CG (Heugens, Essen, & van Oosterhout, 2009). Filatotchev and Wright (2011) argue that if there is not a strong institutional environment that provides protection to minority shareholders, large shareholders may have a greater influence on EC MNEs' strategy.

While concentrated ownership confers specific competitive advantage, such as flexibility, long-term orientation, low agency costs, and swift decision-making, it has some disadvantages, such as lack of international experience and limitations of gaining access to the relevant resources and capabilities required for the internationalization process (Fernandez & Nieto, 2006). Large shareholders perceive the high risk and cost of outward FDI and prefer not to enter the foreign market. Decisions regarding international growth present a high degree of uncertainty, because EC MNEs enter geographically or institutionally distant foreign markets. The large shareholders tend to avoid high-risk international modes of entry characterized by high equity ownership.

Such risk aversion intensifies as the equity ownership of large shareholders increases (Liu, Li, & Xue, 2011; Garcia-Marco & Robles-Fernandez, 2008). When the extent of ownership concentration is relatively low, large shareholders may be encouraged to increase shareholder value by engaging in value-adding strategic initiatives (Lu et al., 2009). In contrast, when the level of ownership concentration is relatively high, they can use their high equity ownership to follow their own interests to the detriment of minority shareholders because of goal incongruence (Lu et al., 2009; Connelly, Hoskisson, Tihanyi, & Certo, 2010). Differences between the interests of minority shareholders and large shareholders will be more pronounced when large shareholders' equity stake constitutes a significant proportion of their personal wealth. Internationalization involves considerable risk-taking, especially for EC MNEs with limited knowledge of foreign markets. Generally, large shareholders will be unwilling to lose control of the company or to design growth strategies (Fernandez & Nieto, 2006). International growth entails the execution of complex strategies, organizational structures, and formal control mechanisms, while decentralization is seen as a loss of control. The desire of large shareholders to maintain independence and control thus hinders internationalization.

Large shareholders who cannot diversify their portfolios sufficiently may prefer less risk to more risk (Wright, Ferris, Sarin, & Awasthi, 1996, 1996). They may pursue to maximize turnover from a few foreign markets rather than relentlessly follow internationalization on a broad scope (Zahra, 2003; Kontinen & Ojala, 2010). They may be more reluctant to undertake operations in markets where the firm lacks familiarity (Claver, Rienda, & Quer, 2008). Therefore, with highly concentrated ownership, especially with a founding family or family members, EC MNEs are likely to adopt low control and low risk equity ownership in order to diversify portfolio risk.

H1. The greater the ownership concentration the lower the level of equity ownership of Turkish MNE subsidiaries.

2.2. The impact of institutional distance on EC MNE ownership strategies

Formal and informal rules of the game determined by host country regulatory, normative and cognitive dimensions of institutions (North, 1990) significantly shape the MNEs' equity ownership strategies in the host country (Scott, 1995; Meyer, Estrin, Bhaumik, & Peng, 2009; Guler &

Guillen, 2010). The regulative dimension reflects prevailing laws and rules in a host country that endorses particular forms of behaviors and restricts others. The cognitive pillar on the other hand refers to "cognitive categories that are widely shared by the people in a particular society" (Kostova, 1999, p. 314). The normative dimension consists of values, norms, and beliefs that describe expected behavior in a society and may have direct relevance with the strategy of the MNE (Xu & Shenkar, 2002).

Relying on Scott (1995), Kostova (1996) developed the construct of institutional distance, denoting the degree of the difference or similarity between the regulatory, cognitive, and normative institutional environments of the home and host countries of an MNE. The greater the institutional distance, the harder it becomes for the MNE to understand the host environment and its legitimacy requirements (Kostova, 1996; Kostova & Zaheer, 1999). If there are great institutional distinctions between home and host countries, the MNE will have to make a choice between internal or external legitimacy oriented strategy alternatives (Xu, Pan, & Beamish, 2004). Many studies claim that gaining external legitimacy is more vital than internal legitimacy for EC MNEs, especially in countries with very dissimilar institutional settings (Xu & Shenkar, 2002). The larger the institutional distance the harder it becomes to establish external legitimacy in host countries (Kostova & Zaheer, 1999). Lack of external legitimacy causes lower levels of performance for the overall EC MNE (Chao & Kumar, 2010). In this context, EC MNEs' strategic decisions are motivated initially by their search for external legitimacy and they will prefer a low level of equity shareholding in their subsidiaries (Gaur & Lu, 2007). A huge institutional distance between the home and host countries entails the MNE to assess, learn and adapt more broadly to local institutional norms and agents (Ferreira, Li, & Jang, 2007). EC MNEs, more than DC MNEs, are likely to display more risk aversion behavior, adopting a low proportion of equity ownership when institutional dissimilarities between home and host countries are huge. They shy away from investing in institutionally distant host country markets because their corporate activities in those markets necessitate compliance with institutional contexts that contradict with those of the home country (Xu & Shenkar, 2002).

In order to cope with institutional distance and reduce risk, EC MNEs select a more flexible entry mode, such as a JV or lower equity ownership mode. The local partner reduces the EC MNE's liability of foreignness (Zaheer, 1995) and increases the gaining of external institutional legitimacy

in the host country (Baum & Oliver, 1991). In summary, large institutional distance in terms of regulative, normative and cognitive pillars leads EC MNEs to choose a lower equity stake in their foreign subsidiaries.

H2a. The greater the regulative distance between home and host countries the lower the level of equity ownership of Turkish MNE subsidiaries.

H2b. The greater the normative distance between home and host countries the lower the level of equity ownership of Turkish MNE subsidiaries.

H2c. The greater the cognitive distance between home and host countries the lower the level of equity ownership of Turkish MNE subsidiaries.

2.3. Moderating effect of institutional distance

The regulative, normative and cognitive pillars of institutional distance may directly affect EC MNEs' internationalization strategies, and also indirectly through other determinants of entry strategies such as CG mechanisms (Young et al., 2008). Institutional distance as a moderator variable influences the direction and strength of the relationship between ownership concentration of EC MNEs and equity ownership strategies in their subsidiaries (Lu et al., 2009).

The moderating effect of institutional distance may differ for each of the three pillars (Eden & Miller, 2004; Arslan, 2012). When there is a huge regulative distance, DC MNEs may tend to prefer a higher level of equity stake to provide more efficient monitoring, coordination and control of foreign subsidiaries (Gaur & Lu, 2007, p. 89). As institutional distance increases, it becomes much tougher to find reliable indigenous partners. Moreover, the regulative pillar is more formal and more clearly stated than the cognitive and normative pillars (Scott, 1995). The regulative institutions are defined and coded in laws, rules and regulations, so DC MNEs can observe, understand and interpret the host country regulative environment more easily than the country's normative and cognitive settings (Eden & Miller, 2004), which reduces the unfamiliarity hazard for DC MNEs. Even where the regulative distance is large, DC MNEs can manage this easily through a high level of equity stake (Gaur & Lu, 2007). This means DC MNEs do not have to count on indigenous partners for overcoming liability of foreignness in international markets characterized by high levels of regulative distance.

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However, this situation is somewhat different for EC MNEs. When the institutional distance is high, decisions regarding international growth present a high degree of uncertainty. The large shareholders tend to avoid high-risk international modes of entry characterized by high equity ownership when the institutional distance between home and host countries is huge. Therefore, they prefer low equity ownership in their subsidiaries to mitigate risk. On the other hand, in comparison with DC MNEs, a larger regulative distance presents difficulties for EC MNEs to understand host country regulative institutions and to establish legitimacy in this foreign environment. EC MNEs cannot observe, understand and interpret the host country regulative environment easily. Therefore, in terms of gaining legitimacy, it is preferable for the EC MNEs to involve indigenous partners that are knowledgeable about the host country regulative environment, thereby being more likely to prefer an equity stake with a lower degree of control (Xu et al., 2004). Although the selection of a partner in an unfamiliar environment is a challenge because of opportunistic behavior of partners and relational hazards in unfamiliar settings, in practice, the indigenous partner may assist the EC MNE to increase legitimacy and reduce the internationalization risks emanating mostly from liability of foreignness when the regulative distance is high.

H3a. The regulative institutional distance moderates the link between ownership concentration and the level of equity ownership of Turkish MNEs' subsidiaries: When the regulative distance is high, the link between ownership concentration and the level of equity ownership of Turkish MNEs in their subsidiaries is negative.

There are some distinctions between the regulative, normative and cognitive dimensions of institutional distance for equity shareholding. Compared to normative and cognitive distances, the regulative distance is more appropriate for comparing the success of WOS and high equity ownership modes to lower equity ownership modes (Xu et al., 2004). Like regulative distance, both normative and cognitive distances also cause great unfamiliarity hazard for EC MNEs. The normative features of institutions are typically informal and deep-rooted in the social environment (Scott, 1995). Large normative distance makes it challenging for an EC MNE to acquire information about these features, and indigenous partners are supportive in dealing with unfamiliarity arising from high normative and cognitive distances (Cui & Jiang, 2012). Large

normative and cognitive distances increase the effects of ownership concentration on equity stake of EC MNEs in their subsidiaries towards low equity ownership modes. That is, in the presence of high normative and cognitive distances between home and host countries, EC MNEs characterized by a high degree of ownership concentration will be more willing to choose a lower equity stake in their foreign subsidiaries.

H3b. The normative institutional distance moderates the link between ownership concentration and the level of equity ownership of Turkish MNEs' subsidiaries: When the normative distance is high, the link between ownership concentration and the level of equity ownership of Turkish MNEs in their subsidiaries is negative.

H3c. The cognitive institutional distance moderates the link between ownership concentration and the level of equity ownership of Turkish MNEs' subsidiaries: When the cognitive distance is high, the link between ownership concentration and the level of equity ownership of Turkish MNEs in their subsidiaries is negative.

Fig. 1 shows the direct impacts of ownership concentration and institutional distance on Turkish MNEs' equity ownership strategies in their foreign subsidiaries along with the moderating effects of each of the dimensions of institutional distance. A set of control variables are also considered.

Fig. 1
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3. Research methodology

3.1. Sample

The sample for this study was picked from the overall population of 364 firms listed on the Istanbul Stock Exchange (BIST) (http://www.kap.gov.tr) based the following selection criteria: (1) parent firms with at least one FDI at the minority JV level; (2) parent firms with at least 10% ownership of subsidiaries; (3) parent firms where necessary data relating to institutional distances and the other variables at parent, subsidiary and host country levels could not be obtained were

excluded from the sample; (4) parent companies operating in the finance and banking sectors were excluded because, in general, they do not use FDI strategies. These selection criteria resulted in a database of 355 foreign subsidiaries of 68 listed Turkish MNEs as parent companies as of 2014.

The sample consists of WOSs (47.6%) and JVs (52.4%) with various levels of ownership. The sample subsidiaries operate in 52 different host countries, almost half of which are developed countries, with the other half emerging countries. The sectoral breakdown of the subsidiaries is as follows; manufacturing industries including agriculture, forestry, fishing, mining, and others (29.9%); wholesale and retail trade (33.0%); services including construction, communication, gas and sanitary services, electric, insurance, real estate, transportation, and other services (37.2%).

3.2. Operationalization of variables

Dependent variable. The equity ownership level (EQOWN) of Turkish MNEs in their subsidiaries constitutes the dependent variable, measured by the percentage of equity shareholding of the Turkish MNE in its subsidiary operating in the host country on a range from 10% to 100% (Demirbag et al., 2009). This variable was acquired from the *Public Disclosure Platform* (http://www.kap.gov.tr) and the annual reports of the companies.

Predictor variable. The ownership concentration of Turkish MNEs was measured from firm annual reports and audited financial tables (Demirag & Serter, 2003; Perrini, Rossi, & Rovetta, 2008; Sahin, Basfirinci, & Ozsalih, 2011; Caprio, Croci, & Giudice, 2011). The largest shareholder (CONCEN) was calculated by the percentage of the greatest number of shares directly owned by the controlling shareholders (Mitton, 2002; Chrinko, Van Ees, Garretsen, & Sterken, 2004).

Control variables. We included control variables at the parent (international diversification and unrelated product diversification), host country (country risk, corruption distance and emerging country) and subsidiary (subsidiary size and industry) levels.

International diversification (INTDIVER) denotes the degree to which Turkish MNEs are active in different foreign geographic regions or markets (Hitt & Ireland, 1994; Hitt, Hoskisson, & Kim, 1997). International diversification is likely to raise MNEs' risks due to increased organizational complexities and uncertainties related to operating in new markets (Tihanyi, Griffith,

& Craig, 2005). Therefore, we expect Turkish MNEs to choose lower equity ownership in their subsidiaries in order to avoid the potential risks stemming from institutional and cultural differences between home and host country operations. Consistent with relevant literature (Delios & Beamish, 1999; Lu & Beamish, 2004; David, O'Brien, Yoshikawa, & Delios, 2010), this variable was computed as:

$$INTDIVER = \left[\frac{\text{Subidiary (i)}}{\text{Subsidiary(Max)}} + \frac{\text{Country (i)}}{\text{Contry (Max)}} \right] / 2$$

Where subsidiary (i) is the Turkish MNE's total number of foreign subsidiaries; subsidiary (max) is maximum number of foreign subsidiaries in the sample; country (i) is the number of host countries in which the MNE invests; and country (max) is the maximum number of FDI host countries in the sample. Data were acquire from the *Public Disclosure Platform* in Turkey and firms' annual reports.

Unrelated product diversification (UNREDIV) is the degree to which firms expand their operations by developing new products (Hitt et al., 1997). In line with prior research (Cuervo-Cazurra, Maloney, & Manrakhan, 2007; Demirbag et al., 2009), we envisage that Turkish MNEs that diversify will be more willing to prefer lower equity ownership in their subsidiaries. UNREDIV was operationalized by an entropy measure of diversification proposed by Palepu (1985), which has been adopted in prior studies (Hitt et al., 1997; Delios & Beamish, 1999; Sanders, 2001; Carpenter & Fredrickson, 2001; Hillman, Shropshire, & Cannella, 2007; Bouquet, Morrison, & Birkinshaw, 2009; David et al., 2010). Data for product diversification were obtained again from the *Public Disclosure Platform*, firms' financial reports, and SIC codes from the US Department of Labor. UNREDIV was measured as follows:

$$DU = \sum_{j=1}^{M} P^J \ln(1/P^J)$$

Where *DU* is unrelated diversification, and P^J is the share of the *j*th group sales in the total sales of the firm.

The subsidiary size (SUBSIZE) was measured by the contributed capital of the subsidiary.

The industry sectors of the subsidiaries (SECTOR) were classified as mining, agriculture, forestry and fishing, manufacturing, electric, transportation, construction, insurance, wholesale and retail trade, communication, real estate, gas and sanitary services. To create industry dummies, these sectors were then categorized into three industry groups of manufacturing, service, and wholesale and retail trade.

A dummy variable (EMRGCON) was created, assigned 0 where the host country is an emerging country, or 1 otherwise, using the International Monetary Fund's country classification based on the host country's level of economic development.

Country risk (COUNTRISK) refers to the uncertainty derived from the host country's social, legal, economic and political contexts (Quer, Claver, & Rienda, 2007). Host country risk scores were obtained from the *International Country Risk Guide* (ICRG, 2012) published by the Political Risk Services (PRS) Group (http://www.prsgroup.com). The country risk scores are based on a composite risk rating which include political (50%), financial (25%) and economic (25%) risk ratings. The composite risk index allows evaluation of country risk between 0 and 100. Higher overall risk scores indicate a lower country risk, while lower scores denote a higher country risk.

The corruption distance (CORDIST) was computed via Kogut and Singh's (1988) procedure based on the scores obtained from the *Corruption Perception Index* (CPI) published by Transparency International (TI, 2012). Corruption is defined as "use or abuse of public power for private benefits" (Judge, McNatt, & Xu, 2011, p. 93) and "generally includes practices such as bribery, fraud, extortion and favoritism" (Luo, 2004, p. 122). However, the most noticeable aspect of the concept can be considered as unmerited contacts and rights provided to firms in exchange for bribes (Rodriguez & Rodriguez, 2005). Consistent with previous research (e.g., Demirbag, Glaister, & Tatoglu, 2007), we expect that as the corruption distance increases, Turkish MNEs will prefer a lower equity stake in their subsidiaries.

Moderator variables. Data for regulative and normative institutional dimensions were collected from data in *Global Competitiveness Report* (World Economic Forum, 2012). Several studies (Kaynak, Demirbag, & Tatoglu, 2007; Chao & Kumar, 2010) have relied on information provided by these reports to measure regulative and normative dimensions. Following Ilhan-Nas (2012), data

for measuring cognitive distance (COGDIST) were obtained from the *Knowledge Economy Index* of the World Bank (KEI, 2012).

Regulative distance (REGDIST) was evaluated by the average of the following six items: efficiency of legal framework, judicial independence, property rights, burden of government regulation, intellectual property rights protection, and transparency of government policy-making.

Normative distance (NRMDIST) was measured through five items: efficacy of corporate boards, strength of auditing and reporting standards, ethical behavior of firms, quality of management schools, and local availability of specialized research and training services.

Cognitive distance (COGDIST) was evaluated by the average of the normalized performance scores of a country or region based on three aspects associated with the knowledge economy: education and human resources (adult literacy rate, secondary enrollment and tertiary enrollment); information and communication technology (telephone, computer and internet penetrations); and innovation (scientific and technical journal articles, patent applications granted by the US patent and trademark office, and total royalty payments and receipts).

Following Kogut and Singh's (1988) approach, these distances were separately calculated as:

$$D = \sqrt{\sum_i \frac{(I_{i,host} - I_{i,origin})^2}{V_i}}$$

Where I_i, host (I_i, origin) is the *i*th dimension of the index for the host country (country of origin- Turkey) and V_i is the variance of ith dimension. Standardized values for each sub-index were used since scales are not the same across dimensions.

3.3. Data analysis

The study's hypotheses were tested by means of multiple linear regression analyses. Following Aiken and West (1991), the interactive terms were created by multiplying together the centered values of CONCEN and institutional distance variables. Consistent with other studies (Thwaites & Dagnan, 2004; Harber, 2005; Hoffman, Bynum, Piccolo, & Sutton, 2011), a moderator analysis technique was selected as the model in this study. A moderator (M) is a qualitative or quantitative variable that influences the direction and strength of the relationship between a

dependent (Y) and an independent (X) variable (Baron & Kenny, 1986). Moderation was tested through the following regression equation (Preacher, Rucker, & Hayes, 2007).

$$Y = b_0 + b_1 X + b_2 M + b_3 XM$$

In line with Baron and Kenny (1986), our research framework (Fig. 1), consists of three causal effects on EC MNE ownership strategies: (1) "ownership concentration" as an estimator, (2) "institutional distance" as both another estimator and a moderator variable, and (3) "the interaction" produced by these two variables. There is no direct conceptual relationship between the estimator and moderator variables to test the moderator hypothesis. The relationship is based on the significance of the effect of interaction. A significant effect of interaction on ownership strategies means that the effects of ownership concentration on foreign equity ownership strategies are shaped to some extent by the institutional distance (Zeitner, 1998). However, the results of the moderator analysis do not clearly demonstrate how high or low levels of the moderator variable (institutional distance) have an impact on high or low levels of the independent variable (ownership concentration). To overcome this limitation, we use the graphs of regression coefficients for significant moderator models as recommended by Aiken and West (1991) and Cohen, Patricia, West, and Aiken (2003).

4. Results

Table 1 presents the descriptive statistics and the correlation matrix. None of the correlations between explanatory variables have correlation coefficients above 0.70, and the variance inflation factors (VIF) for our variables are much lower than the acceptable threshold value of 10 (Freund, Wilson, & Sa, 2006). Hence, the issue of multicollinearity in models does not pose a risk in this study (Gujarati, 1995; Kennedy, 1999). However, there are strong correlations between control variables, viz., country risk, corruption distance, emerging country and institutional distances, which can lead to multicollinearity problems. Therefore, we do not use these control variables in the models containing institutional distance variables. Similarly, correlation coefficients between institutional distance variables are out of tolerance limits. Consequently, these variables are tested in separate models. The analyses are also checked for heteroscedasticity by the Breusch-Pagan/Cook-Weisberg test and no serious problem is detected.

Table 1

4.1. The main effects of ownership concentration on equity ownership strategies of Turkish MNEs

Table 2 presents regression models predicting the direct and interaction effects of the ownership concentration and institutional distance on the Turkish MNEs' equity ownership choice. There are six models for main effects (Model 1 through Model 6) and three models for examining interactions (Model 7 through Model 9). Model 3 shows the full model containing whole set of independent and control variables. This arrangement is to accommodate the variables that we used to measure ownership structure and institutional distance for H1, H2a, H2b, H2c (Model 1 through Model 6) and H3a, H3b and H3c (Model 7 through Model 9).

Overall, no support is found for H1, as the coefficient of CONCEN (the largest shareholder) is negative, but insignificant in Models 1 to 9.

Considering the control variables, Table 2 indicates that the most influential variables are found to be parent-level control variables of INTDIVER and UNREDIV, whose coefficients are negative and significant (p-value < 0.01). Neither subsidiary-level nor country-level control variables are significant.

Table 2

We predicted that the greater the regulative (H2a), normative (H2b) and cognitive (H2c) distances, the more likely that Turkish MNEs will choose lower equity positions in their subsidiaries. However, the coefficients of the regulative and normative distances are negative though the coefficient of cognitive distance is positive but not significant in all three models (Models 4 to 6), providing no support for H2a to H2c. It appears that differences in all three dimensions of institutional distance between the home and host countries do not have a direct impact on the foreign equity ownership strategies of Turkish MNEs.

4.2. Moderating effects of institutional distance

To determine the moderating impact of institutional distance on the link between ownership concentration and equity ownership strategies of Turkish MNEs, we executed a series of moderated regression analyses with equity ownership as the dependent variable (Models 7 to 9 of Table 2). A significant interaction term means that the effects of the ownership concentration on the equity ownership of Turkish MNEs in their subsidiaries is determined to some extent by the institutional

distance between home and host countries (Zeitner, 1998). In such cases, institutional distance strengthens the link between the ownership concentration and equity ownership strategies. However, the interaction term does not identify the conditions that dictate how the estimator is explicitly related to the outcome, which constitutes the subject of this study. Hence, to test the effect of ownership concentration on foreign equity ownership strategies of Turkish MNEs with high versus low institutional distance levels, simple slope tests are performed whereby we check whether the interaction is significant when the institutional distance is high vs. low. Interaction effects are then plotted at low and high levels of each of the institutional distance dimensions, as shown in Figs 2a to 2c, and are interpreted in line with Aiken and West (1991).

Model 7 of Table 2 indicates that the interactions between REGDIST (regulative distance) and ownership concentration at CONCEN level is significantly associated with the equity ownership of Turkish MNEs in their subsidiaries (p-value < 0.01). To enhance our understanding of the effects of REGDIST, a simple slope analysis is conducted by plotting interaction results at high and low levels of REGDIST for CONCEN, as shown in Fig. 2a.

Fig. 2a shows that the ownership concentration (CONCEN) negatively influences equity ownership when REGDIST is high (β = -0.259; p-value < 0.01). That is, when the REGDIST between Turkey and the host country is high, the larger CONCEN, the lower the extent of Turkish MNEs' equity shareholding in their subsidiaries. This finding supports H3a stating that the association between ownership concentration and the Turkish MNEs' equity ownership level in their subsidiaries is negative when the REGDIST is high.

Figs 2a, 2b, 2c

Model 8 of Table 2 indicates that the interaction effects between NRMDIST (normative distance) and ownership concentration (CONCEN) is significantly associated with equity ownership of Turkish MNEs in their subsidiaries (p-value < 0.01). Therefore, a simple slope analysis is conducted by plotting interaction results at high and low levels of NRMDIST for CONCEN level, as shown in Fig. 2b.

Fig. 2b shows the plot of the interaction between CONCEN and NRMDIST on the equity shareholding levels of Turkish MNEs in their subsidiaries. This plot indicates a negative relationship between CONCEN and equity ownership levels when NRMDIST is high (β = -0.243;

p-value < 0.05). This finding supports H3b stating that the link between ownership concentration and the equity ownership of Turkish MNEs in their subsidiaries is negative when the normative distance is high.

The moderating effect of COGDIST (cognitive distance) on the link between ownership concentration and the equity ownership level of Turkish MNEs in their subsidiaries is displayed in Model 9 of Table 2. We support the moderating impact of COGDIST on the link between CONCEN (Fig. 2c) and equity ownership of Turkish MNEs, as the interaction term between CONCEN and COGDIST is significant (*p*-value < 0.05). The plot of the significant interaction between CONCEN and COGDIST in Fig. 2c shows a negative relationship for high level of COGDIST (β = -0.171; *p*-value < 0.05). This finding is consistent with our expectation in H2c stating that the link between ownership concentration and the equity ownership level of Turkish MNEs is negative when the COGDIST is high. We find support for H3c.

5. Discussion and conclusions

Drawing upon agency theory and institutional theory from the viewpoint of emerging countries, we estimate how institutional differences and ownership concentration both directly affect the equity-based ownership strategies of Turkish MNEs and also how institutional differences moderate the link between ownership concentration and ownership strategies. We report a number of important outcomes that offer some useful implications for scholars and managers investigating CG mechanisms from an international perspective. The impact of ownership concentration on the foreign equity ownership strategy in an emerging country context differs significantly from that in a developed country context. This implies that the emerging country context is a critical determinant of CG effects.

The findings suggest that the ownership concentration has no effect on the equity ownership of EC MNEs in their foreign subsidiaries. Consistent with relevant literature (Demirag & Serter, 2003; Kula, 2005), we find that Turkish MNEs exhibit a highly concentrated ownership structure like many firms from emerging countries. The largest shareholders of Turkish MNEs (CONCEN) have nearly half of ownership. However, contrary to previous research, there is no main effect of the largest shareholders on equity ownership strategies of Turkish MNEs. In this context, we cannot explain the risk aversion of CONCEN in an emerging country using only an agency perspective.

However, when we add the moderating effects of three institutional distances to the analysis, Turkish MNEs having high CONCEN are less likely to prefer risk-taking at high regulative (REGDIST), normative (NRMDIST) and cognitive institutional distance (COGDIST). That is, when REGDIST, NRMDIST or COGDIST of Turkey and the host country is high (viz., the regulative, normative or cognitive environment of the host country is not similar to Turkey), Turkish MNEs with high level of CONCEN choose a lower level of equity stake in their subsidiaries.

Overall, the findings reveal that the main determinant of MNEs' equity shareholding in their subsidiaries is not institutional distance *per se*. Institutional distance has a moderating effect rather than a direct effect on the link between the CG mechanism and entry strategies. This study provides strong evidence that regulative, normative and cognitive distances affect the strength of the interaction between ownership concentration and equity ownership of MNEs. These findings are at odds with those of previous studies focusing on DC MNEs (Kostova & Zaheer, 1999; Gaur & Lu, 2007; Trevino, Thomas, & Cullen, 2008). In comparison with DC MNEs, the EC MNEs with large shareholders prefer a low equity ownership in their subsidiaries because of risk avoidance. It is preferable for an EC MNE to involve an indigenous partner that is knowledgeable about the host country regulative environment, thereby being more likely to select an equity ownership mode with a lesser control (Xu et al., 2004). This study suggests that the EC MNEs' equity ownership strategies are more influenced by the moderating impacts of regulative and normative distances than by cognitive distance. The host country regulative environment perhaps is the easiest for MNEs to monitor, understand and accurately interpret since regulative institutions are codified and formalized in rules and procedures (Kostova & Zaheer, 1999), whereas the cognitive pillar is often tacit and difficult to comprehend (Boyacigiller, Goodman, & Phillips, 2004).

5.1. Contributions, limitations and future research

We make several contributions. First, most prior studies in CG literature have neglected the links between CG mechanisms and foreign entry strategy. This study extends the relevant literature by investigating equity ownership from the viewpoint of CG considered in terms of ownership concentration. Second, we systematically investigate foreign market equity ownership decisions of EC MNEs. Consequently, this study makes an important attempt in enhancing our understanding of

how CG mechanisms of EC MNEs differ from DC MNEs with regard to functionality and operationalization. Third, this may be considered the first study to analyze both the direct and the moderating impacts of institutional distance on ownership concentration and EC MNEs' equity ownership of subsidiaries. The moderator variable of institutional distance strengthens the link between ownership concentration and equity ownership of EC MNE subsidiaries. That is, when the institutional distance is high, the link between ownership concentration and the equity ownership level of Turkish MNEs in their subsidiaries becomes negative.

The findings have implications for practice, especially for emerging country foreign investors and managers. The effects of CG mechanisms on equity ownership of EC MNEs differ from those of DC MNEs, with significant differences between FDI strategies of DC MNEs and those of EC MNEs from the viewpoint of ownership concentration. Managers of MNEs should take these cross-country CG mechanism differences into consideration if they want to be successful in the risk management of their overseas subsidiaries.

This study is subject to some limitations that should be acknowledged when evaluating the findings. First, our sample is confined to Turkish MNEs. Further studies of other EC MNEs would help to better understand how CG mechanisms and institutional distance matters. Another limitation is that we focus on ownership concentration as a CG mechanism. However, board structure and top management team characteristics including commitment to risk tolerance and personal attributes are also important factors determining the international strategy of the firm, which should be addressed in future research.

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Control Variables
- International diversification
- Unrelated product diversification
- Country risk
- Corruption distance
- Subsidiary size
- Sector of subsidiary
- Emerging country

Ownership Concentration
- Proportion of the largest shareholder in the parent

H_1

Foreign Equity Ownership Strategies
- The parent company's proportion of equity shareholding in its subsidiary

H_{3a}
H_{3b}
H_{3c}

Institutional Distance
- Regulative distance
- Normative distance
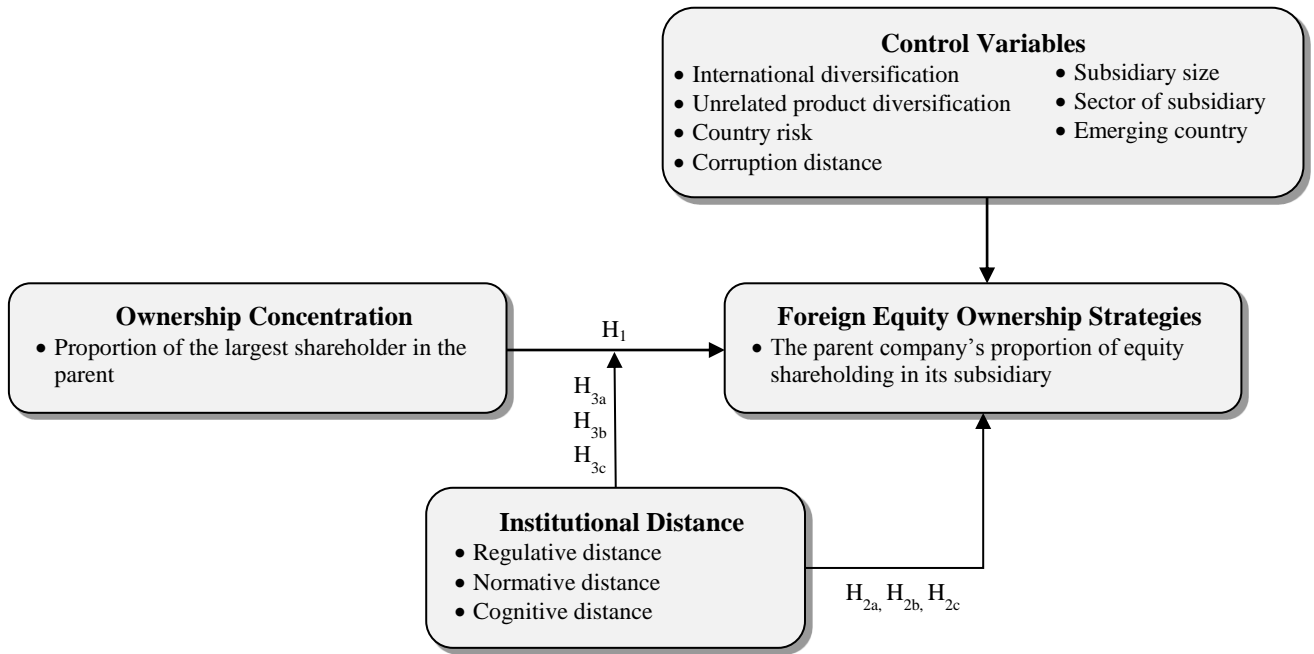- Cognitive distance

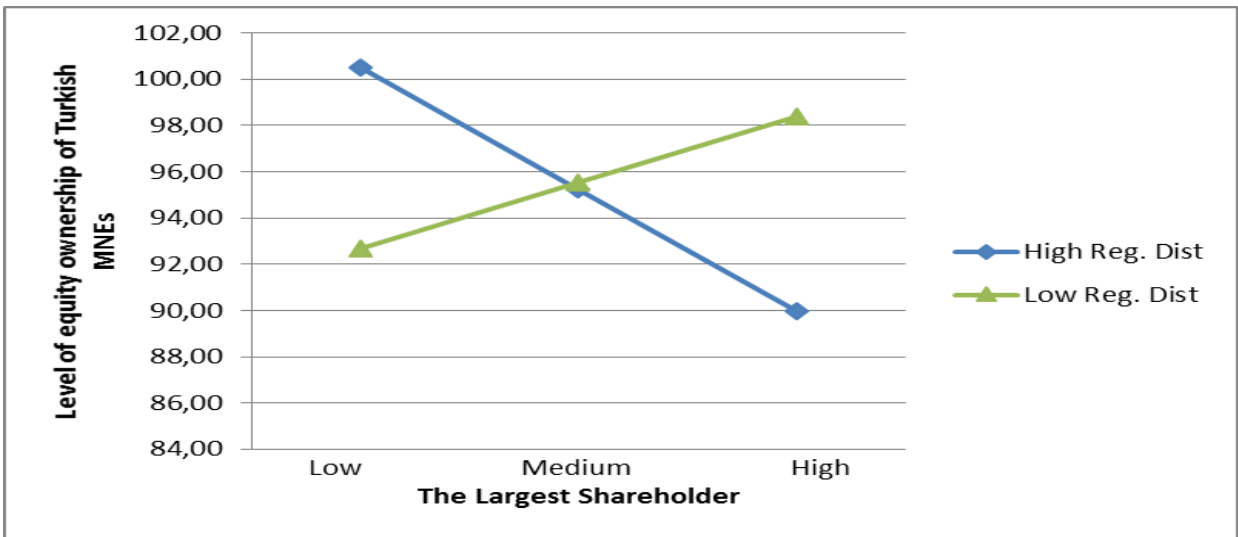H_{2a}, H_{2b}, H_{2c}

Fig 1. Research framework

Fig. 2a. The interaction between CONCEN and REGDIST

Fig. 2b. The interaction between CONCEN and NRMDIST

Fig. 2c. The interaction between CONCEN and COGDIST

Table 1. Descriptive statistics and correlation matrix

Variables	Mean	SD	Min.	Max.	1	2	3	4	5	6	7	8	9	10	11	12	13
1. EQOWN	78.54	26.88	1.00	100	1												
2. CONCEN	49.76	20.29	19.3	97.92	0.12*	1											
3. INTDIVER	0.43	0.35	0.03	1.00	-0.33**	-0.32**	1										
4. UNREDIV	0.33	0.47	0.00	1.35	-0.35**	-0.23**	0.31**	1									
5. SUBSIZE[a]	7.23	6.62	1.70	123.39	-0.04	-0.08	-0.03	0.04	1								
6. SECTOR (MAN)	0.29	0.45	0.00	1.00	0.06	0.28**	-0.16**	-0.21**	-0.03	1							
7. SECTOR (TER)	0.37	0.48	0.00	1.00	-0.09	-0.29**	-0.04	0.22**	0.09	-0.50**	1						
8. COUNTRISK	73.69	7.03	57.20	89.50	-0.06	-0.09	0.05	0.16**	0.03	-0.29**	0.29**	1					
9. CORDIST	0.99	0.57	0.04	2.02	-0.02	-0.01	-0.03	-0.02	0.01	-0.16**	0.33**	0.66**	1				
10. EMRGCON	0.53	0.49	0.00	1.00	0.07	0.04	-0.09	-0.12*	0.04	0.24**	-0.22**	-0.70**	-0.64**	1			
11. REGDIST	2.69	1.23	0.70	5.24	-0.04	-0.05	-0.01	0.09	-0.02	-0.24**	0.34**	0.87**	0.82**	-0.73**	1		
12. NRMDIST	2.94	1.62	0.58	5.79	-0.05	-0.05	0.01	0.08	-0.04	-0.26**	0.33**	0.81**	0.83**	-0.84**	0.90**	1	
13. COGDIST	2.13	0.82	0.27	3.36	-0.05	-0.02	0.09	0.09	-0.06	-0.27**	0.27**	0.72**	0.77**	-0.88**	0.79**	0.86**	1

Notes:
EQOWN: Equity ownership, CONCEN: The largest shareholder, INTDIVER: International diversification, UNREDIV: Unrelated product diversification, SUBSIZE: The size of the subsidiary, SECTOR (MAN): Manufacturing sector operated, SECTOR (TER): Tertiary sector operated, COUNTRISK: Country risk, CORDIST: Corruption distance, EMRGCON: Emerging country, REGDIST: Regulative distance, NRMDIST: Normative distance, COGDIST: Cognitive distance.

* $p < 0.05$; ** $p < 0.01$.

[a] SUBSIZE/million Turkish lira

$N = 355$

Table 2. The regression results

Variables [a]	Main effects						Interactive effects		
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**	**Model 7**	**Model 8**	**Model 9**
Control variables									
Parent company level									
INTDIVER	-0.25**	-0.27**	-0.26**	-0.27**	-0.27**	-0.27**	-0.26**	-0.26**	-0.28**
UNREDIV	-0.27**	-0.26**	-0.28**	-0.26**	-0.26**	-0.26**	-0.28**	-0.27**	-0.27**
Subsidiary level									
SUBSIZE		-0.03	-0,03	-0.03	-0.03	-0.03	-0.02	-0.02	-0.02
SECTOR (MAN)		-0.07	- 0.05	-0.07	-0.07	-0.07	-0.07	-0.08	-0.08
SECTOR (TER)		-0.08	-0.06	-0.08	-0.08	-0.09	-0.08	-0.07	-0.08
Host country level									
COUNTRISK			0.02						
CORDIST			-0.03						
EMRGCON			0.01						
Predictor variable									
CONCEN	-0.02	-0.03	-0.04	-0.03	-0.03	-0.04	-0.04	-0.04	-0.05
Moderator variables									
REGDIST				-0.01			-0.01		
NRMDIST					-0.03			-0.02	
COGDIST						0.01			0.01
Interactive effects[b]									
REGDIST * CONCEN							-0.15**		
NRMDIST * CONCEN								-0.14**	
COGDIST * CONCEN									-0.09*
F	24.82**	12.93**	8.24**	11.06**	11.09**	11.05**	11.04**	10.91**	10.11**
Adjusted R^2	0.17	0.17	0.16	0.17	0.17	0.17	0.19	0.18	0.17

Notes:

EQOWN: Equity ownership, CONCEN: The largest shareholder, INTDIVER: International diversification, UNREDIV: Unrelated product diversification, SUBSIZE: The size of the subsidiary, SECTOR (MAN): Manufacturing sector, SECTOR (TER): Tertiary sector, COUNTRISK: Country risk, CORDIST: Corruption distance, EMRGCON: Emerging country, REGDIST: Regulative distance, NRMDIST: Normative distance, COGDIST: Cognitive distance.

[a] Standardized regression coefficients are reported.

*$p < 0.05$; **$p < 0.01$.

N = 355