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Restoring trust through isomorphism at multinational financial institutions: a matter of boundary permeability

ABSTRACT

Multinational financial institutions (MFIs) are subject to strong isomorphic pressures from the institutional environment. MFIs need to assess appropriate approaches to comply with the desired behaviour of the foreign subsidiaries in the host country societies, without jeopardizing the desired behaviour of the parent company in the home country societies. Therefore, identification of organizational boundaries and developing trust through managing boundary permeability is critical to MFIs. Our results show that restoring trust at all levels of the global financial system is widely recognized as a priority by managers of MFIs, through a range of self-imposed measures and supervisory enforcement of globally coordinated regulations. Further, active management of boundary permeability that determines the degree of isomorphism with host country societies can assist MFIs in fostering legitimacy in both home and host countries. We propose a framework that structures the analysis of the formal and informal rules in the institutional context, including government policy, legal system, cultural dimensions and social capital.

Keywords: MFIs, isomorphism, intracorporate isomorphism, boundary permeability, management control, trust

INTRODUCTION

The recent financial and economic crisis prompted a public debate on the functioning of the global financial system and the relevance of trust (Asmussen, 2012; Brown, 2009; Roth, 2009; Trichet, 2010; Tumpel-Gugerell, 2008; Wells and Gostelow, 2009). At the core of the debate are the roles played by the multinational financial institutions (MFIs) and their relationships with the customers on the one hand and the public on the other. Relationships are in essence built on trust because of relational risks inherent in transactions (Nooteboom, 2007). High levels of trust help reduce transaction costs (Howorth and Moro, 2006). Relationships that are not based upon trust, but on rules and regulations result in increased transaction costs since they need to be negotiated and agreed upon, and if necessary enforced based upon a legal framework (Fukuyama, 1995). Increased transaction costs are detrimental to business and economic growth. Governments across the world have formulated policies and implemented regulatory reforms, while the importance of trust in the financial system for the global economy is a concern at supranational level. The G20 and Financial Stability Board (FSB) recognize that mutual trust is required in the capability of local regulatory authorities to implement common regulatory standards (Carney, 2014; G20, 2014).

The institutional context in which MFIs operate has significantly changed, including the rules of the game on human interaction, which can be prohibited or permitted under specific conditions (North, 1990). In order to prosper in the changed business environment, MFIs need to better understand the new regulations and increase internal and external commitments by incorporating, through isomorphic mechanisms, the patterns of change that are considered legitimate for the specific environment (DiMaggio and Powell, 1991; Meyer and Rowan, 1991). MFIs are subject to strong isomorphic pressures from the institutional environment. According to Powell (1988) this type of environment requires "skilful management of boundary relations and conformity to the normative codes of the relational networks in which it participates" (cited Westney, 2005: 61). Effective boundary management aims to ensure a "fit between its [an organization's] internal structures and processes and the characteristics of its environment" (Ghoshal and Westney, 2005: 8). Further, since multinational corporations (MNCs) operate in several countries, the institutional context differs for

each host country (Ghoshal and Westney, 2005; Westney, 2005). MNC subsidiaries are subject to formal and informal isomorphic forces from both the parent company, as well as the societies in which they operate (Birkinshaw, 2000; DiMaggio and Powell, 1991). Contingency-based research on MNCs provides analytical frameworks to assess alignment of MNCs' strategies and behaviour with their business environments both at parent company level in the home country, as well as foreign subsidiary level in the host countries (Bartlett and Ghoshal, 2002; Chenhall, 2003; Lawrence and Lorsch, 1967; Prahalad and Doz, 1987). In line with institutional and contingency theories, MFIs need to assess the most appropriate approach to be considered legitimate in both home and host countries. Das and Teng (1998: 494, italic added) regard this kind of behaviour as "*desired behavior*" which can enhance trust relationships. For MFIs to build and develop trust with external stakeholders, identification and management of organizational boundaries is important. Boundary permeability, as a particular structural property of organizational dynamics, helps MFIs to improve their management of isomorphism, as boundaries "exert a centripetal force on the entity [MFI] in order to hold the system together" and simultaneously "exert a centrifugal force on the entity by allowing the system to come apart enough to receive input from outside and to provide output for other systems" (Alderfer, 2011: 136-137).

This paper, mainly based upon the first author's Doctor of Business Administration research project, focuses on the interaction of MFIs and the institutional context in which they operate. We argue that selective isomorphism through a choice on boundary permeability can assist in restoring trust in MFIs. The paper is organized as follows. Firstly, we offer extent literature review of MFIs, which are the principal unit of analysis for the purpose of this paper, with an emphasis on the relevance of trust, isomorphism and boundary permeability for operating in a regulated financial system. This is followed by proposing an analytical framework. After a description of our research methods, we present the results. Finally, in conclusion we discuss our results in relation to the proposed framework and offer direction for future research.

TRUST AND MULTINATIONAL FINANCIAL INSTITUTIONS

Multinational financial institutions

MNCs can be traced back to ancient history, while the first MFIs appeared during the Middle Ages (see Wilkins, 2005). As Chandler and Mazlish (2005) point out, definitions on MNCs differ in perspective (e.g. geographical presence, private vs. public ownership, type of forms and practices). For this paper, the UNCTAD definition as cited by Roach (2005: 24) will be used: "an entity composed of a parent enterprise that controls the assets of entities in countries other than its home country plus the foreign affiliates of that parent enterprise". Within the MNC organizational structure, the interdependence between the headquarters and its overseas subsidiaries is a key characteristic (Kostava and Roth, 2003). This interdependence varies according to the models of MNCs, namely international, multinational, global and transnational (Bartlett and Ghoshal, 2002). Due to the MNCs' global business expansion and their complex organizational structure, the corporate governance of MNCs is increasingly under scrutiny. Sun, Stewart and Pollard's (2011: 17) definition of corporate governance ("a systemic set of legal, cultural and institutional arrangements, which determine how the corporation is governed, for what purpose and for whose interests") focuses on the various stakeholders of a corporation. Stakeholders of MNCs include both home and host country regulatory authorities. As Birkinshaw (2000) contends, the growing influence of MNCs can even overshadow nation states on the development of their economies. Chandler and Mazlish (2005) argue that MNCs do not jeopardize the authority of nation states, but acknowledge that the trans-border nature of their activities create challenges from a governance and regulatory perspective. They refer that MNCs have dealt with this matter through an effort towards greater transparency. Roach (2005) elaborates that transparency and accountability to all stakeholders form the basis for alignment of the behaviour of MNCs with society at large. He concludes that this alignment with the objectives of all stakeholders will not only require self-imposed actions at MNCs, but also national and international regulations.

Due to the specific role of MFIs in the economic development of home and host countries (Green, Kirkpatrick and Murinde, 2005), increased scrutiny as regards transparency and accountability is required. While according to Jones (1995), MFIs

were historically seen as a contributing force to the society of a host country (see Wilkins, 2005), the consequences of the recent crisis demonstrated that this positive influence should no longer be taken for granted. The public debate on the crisis has emphasized the notion of trust at various levels, ranging from the financial system at large to financial institutions, such as banks. Roth (2009: 1; 4) argues that "a *certain* level of trust in and approval of the market economy is an important ingredient in ensuring the smooth running of the economic, political and social system", but that "...citizens have been confronted with the fragility of their economic systems and their strong dependence on mutual trust". At the height of the crisis, a representative from the European Central Bank contended that "building, preserving and valuing trust is not an unattainable ideal, but one that can be concretely translated into business objectives and practices" (Tumpel-Gugerell, 2008: 2). In response to the crisis, Brown (2009: 2) defended the overhaul of regulatory systems, emphasizing that "banks cannot assume that trust will return without significant change".

International regulatory systems

Supervisory authorities have pursued reforms of national and international regulatory systems, while objectives for increased trust have been stated at supranational level. The G20 and FSB recognize that, first of all, mutual trust is required in the capability of local regulatory authorities to successfully implement common regulatory standards. As Carney (2014: 1; 3-4), the chairman of the FSB, points out in his letter on financial reforms to the G20 Leaders for their November 2014 summit, "the world's largest banks threatened the stability of the global system and their public bail-outs undermined both market discipline and a sense of fairness in our societies". He states that, after the phase of implementing measures to strengthen regulatory standards across the world, to mitigate systemic risk in the financial system and to end the notion of "too big to fail in the banking sector", the FSB continues to assess risks and vulnerabilities in the financial system, but also aims to "promote a system based on mutual trust and co-operation". Carney clarifies that by "building mutual trust, we can realize fully the benefits of an open, integrated and resilient global financial system". Furthermore, he elaborates that mutual trust depends on the consistency of local implementation of a common set of minimum international standards, as well as the capability of each country to deal with specific matters related

to its financial system and an increased deferral to local regulatory authorities in each jurisdiction. Carney contends that these standards need to "be implemented fully, consistently and in a timely way". This message of persistence and consistency is reinforced by the G20 Leaders (2014: 2) in their joint statement on the Brisbane Summit, referring that "critical work remains to build a stronger, more resilient financial system" and concluding that "the task now is to finalise remaining elements of our policy framework and fully implement agreed financial regulatory reforms, while remaining alert to new risks".

Trust in MNCs

Fukuyama (1995: 26) views trust as "the expectation that arises within a community of regular, honest, and cooperative behavior, based on commonly shared norms, on the part of other members of that community". Literature on trust in international joint ventures assists in gaining a deeper understanding on the afore-mentioned expectation of behaviour. Madhok (2006: 32) argues that "trust is the perceived likelihood of the other [actor] not behaving in a self-interested manner". Therefore, trust does not reflect the actual likelihood of behaviour, which according to Das and Teng (1998: 494) is a matter of control mechanisms, but rather the "*perceived* probability of desired behavior". They define trust as "the degree to which the trustor holds a positive attitude toward the trustee's goodwill and reliability in a risky exchange situation". Literature identifies various dimensions of trust, including the notions of interpersonal and systemic trust (see Roth, 2009). While interpersonal trust represents a reflection on individuals, systemic trust indicates the confidence in institutions and the mode of production in a country.

The afore-mentioned definitions on trust raise several issues that need to be considered with respect to trust in the relationship between MFIs and the communities in which they operate. Firstly, MFIs deal with a number of different communities in host countries, as acknowledged in the literature on the institutional context of MNCs (e.g. Guillén and Suárez, 2005; Westney, 2005). Secondly, the commonly shared norms, that Fukuyama refers to, depend on the culture in each country and community. Culture is defined by Schwartz (2007: 34) as "a rich complex of meanings, beliefs, practices, symbols, norms and values prevalent among people in a society". Thirdly, the meaning

and levels of trust vary from country to country (Zaheer and Zaheer, 2006), which can also be linked to cultural differences. The next section focuses on trust that arises from isomorphism with the institutional context of MFIs.

DEALING WITH ISOMORPHIC PRESSURES AT MULTINATIONAL CORPORATIONS

Fostering trust through isomorphism

The institutional context can be described by applying concepts from North (1990) and Scott (2008). According to North (1990), institutions determine the restrictions on human interaction, including actions that are prohibited as well as permitted under specific conditions. These constraints can be either formal or informal rules, jointly providing a structured and efficient basis for relationships. Scott (2008) distinguishes regulative, normative and culturally-cognitive pillars of society that are based upon different mechanisms. The regulative pillar focuses on coercive mechanisms (rules, laws and sanctions), while the normative pillar prescribes socially accepted behaviour and the cultural-cognitive pillar reflects the mimetic mechanism of creating a shared reference of meaning. The normative and cultural-cognitive pillars deal with the informal rules and the regulative pillar addresses the formal rules of society. According to institutional theory, an organization enhances the chances for survival by applying isomorphism, i.e. by incorporating patterns that are considered legitimate for the specific environment, resulting in increased internal and external commitment (DiMaggio and Powell, 1991; Meyer and Rowan, 1991). DiMaggio and Powell (1991: 66) view institutional isomorphism as a "process of homogenization" among organizations and refer to Hawley's (1968) characterization of isomorphism as a "constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions". They elaborate on the notion of institutional isomorphism by concluding from literature (Carroll and Delacroix, 1982; Aldrich, 1979) that "organizations compete not just for resources and customers, but for political power and institutional legitimacy, for social as well as economic fitness". Since trust arises from "...the trustee's goodwill and reliability in a risky exchange situation" (Das and Teng, 1998: 494), it can be argued that isomorphic pressures that result in increased legitimacy also foster trust. As Scott (2008: 61) claims, "legitimate

organizations are those established by and operating in accordance with relevant legal or quasi legal requirements". If MFIs are in compliance with these requirements, the "*perceived* probability of desired behavior" (Das and Teng, 1998: 494) as assessed by stakeholders also should increase accordingly. In line with the afore-mentioned pillars of society, three types of isomorphism (coercive, mimetic and normative) can be distinguished.

DiMaggio and Powell (1991: 67) clarify that coercive isomorphism "results from both formal and informal pressures exerted on organizations by other organizations upon which they are dependent and by cultural expectations in the society within which organizations function". Organizations respond to the formal legal and technical pressures from governments (e.g. environmental regulations) by changing the organizational structure and behaviour (e.g. adopting technology that protects the environment). DiMaggio and Powell (1991: 68) refer to Meyer and Rowan's (1977) argument that "as rationalized states and other large rational organizations expand their dominance over more arenas of social life, organizational structures increasingly come to reflect rules institutionalized and legitimated by and within the state". DiMaggio and Powell (1991) contend that organizations also impose common policies and procedures on their subsidiaries (e.g. standard operating procedures, reporting requirements). Van der Stede (2003) refers to this type of coercive isomorphic pressures as "intracorporate isomorphism". Examples at MFIs are accounting policies and corporate requirements to comply with anti-money laundering laws in home and host countries.

The immediate response to the crisis, from both governments as well as parent companies, was exercising further "coercive authority". Das and Teng's perspective (1998: 495) implies that there are conceptual limitations to the impact of coercive isomorphism on the level of trust: "because trust involves a positive attitude about others' motivations, conceptually, it is not about influencing and affecting others' behavior but is about believing that others will perform whatever serves the trustor's best interests, even in the absence of control". Moreover, uncertainty in the business environment also increased significantly during the crisis, which fosters a second type of isomorphism. DiMaggio and Powell (1991: 69-70) state that "uncertainty is also a powerful force that encourages imitation", resulting in mimetic isomorphism in order for "organizations…to model themselves after similar organizations in their field that they perceive to be more legitimate or successful". It should be noted that "the modeled

organization may be unaware of the modeling or may have no desire to be copied". MFIs may foster mimetic isomorphism at foreign subsidiaries to quickly achieve an adequate degree of legitimacy in host countries. Although this approach to implement a similar organizational structure and behaviour according to local benchmarks may be effective in countries with strict regulatory requirements, a debate could be held whether the similarity of business models at MFIs contributed to the crisis. The third type of isomorphism reflects "normative pressures" based upon mechanisms of professionalization (e.g. through university education, professional networks). DiMaggio and Powel (1991: 70-73) claim that "professions are subject to the same coercive and mimetic pressures as are organizations". They conclude by referring to Perrow (1974) that professionalization may result in "a pool of almost interchangeable individuals", whose common approach may reduce differences in "organizational and professional behavior" across different organizations. It can be questioned whether normative pressures at MFIs also impacted the crisis since e.g. investment bankers reflect a highly professionalized group of employees. DiMaggio and Powell (1991) contend that these isomorphic processes arguably enhance the efficiency of organizations, but may improve effectiveness (e.g. staff recruitment).

Multiple institutional contexts: home and host countries

The institutional context differs for each host country in which the MNCs' national subsidiaries are located (Ghoshal and Westney, 2005; Westney, 2005). Birkinshaw (2000) contends, by referring to Bartlett and Ghoshal (1989), Prahalad and Doz (1987) and Westney (1994), that MNCs' subsidiaries are subject to isomorphic forces from both the parent company as well as the societies in which they operate. Contingency-based research on MNCs provides analytical frameworks to assess alignment of the desired behaviour both at parent company level in the home country, as well as foreign subsidiary level. Chenhall (2003: 160) summarizes contingency-based literature on management control systems, stating that managers attempt "to adapt their organizations to changes in contingencies in order to attain fit and enhanced performance". These contingencies vary e.g. from environment and technology to culture. Chenhall refers that Lawrence and Lorsch's framework (1967) on differentiation and integration contributed to contingency-based research. Further, according to Bartlett (1986), the theoretical development on MNCs also built on the

foundation of the differentiation and integration logic (see Ghoshal and Westney, 2005). More specifically, Ghoshal and Westney (2005: 3) argue that Prahalad's (1975) "integration and responsiveness" framework (enhanced by Doz, 1979 and Bartlett, 1979) identifies "forces for global integration" and "national differentiation". These forces can be seen as isomorphic pressures aimed at increasing legitimacy within the institutional context of MNCs in home and/or host countries. Westney (2005: 59) clarifies that the transnational MNC as mentioned above "is not subject either to strong home or host country effects", consistent with Perlmutter's (1969) notion of geocentric MNCs. Trompenaars and Woolliams (2003) propose a framework for MNCs to deal with cross-cultural differences between home and host countries (reconciling universalistic and particularistic approaches). Van der Stede (2003) focuses on the notion of "intracorporate isomorphism" as a result of parent company effects (convergence) versus the adjustment of management control systems to the local culture (divergence). He argues, by referring to Granlund and Lukka (1998), that intracorporate isomorphism towards uniform management control systems has not been subject to extensive research. As Roach (2005: 37) describes, a recent school of thought in corporate governance addresses a focus on "internalizing the externalities", providing stakeholders the formal or informal opportunity to influence MNCs' behaviour. Since the various isomorphic pressures can be identified, they conceptually can be assessed at the boundaries between the internalities and externalities. Ghoshal and Westney (2005) contend that organizations need to effectively manage the exchanges that occur at the boundary between the organization and the environment. The next section will deal with managing isomorphism at the boundaries that separate MFIs from the institutional context in home and host countries.

MANAGING BOUNDARY PERMEABILITY WITH RESPECT TO FORMAL AND INFORMAL RULES

Isomorphism: a choice on boundary permeability

Westney (2005: 61) quotes Powell (1988) on his statement that the MNCs' context, subject to multiple isomorphic forces, requires "skilful management of boundary relations and conformity to the normative codes of the relational networks in which it participates". Alderfer (2011: 136-137; 142) offers a theory on intergroup

dynamics within organizations that can assist in the management of the boundaries between MFIs and the institutional context (i.e. formal and informal rules) in host countries. In his view “boundaries separate an entity from its environment, they exert a centripetal force on the entity in order to hold the system together”. Simultaneously, boundaries “permit exchanges between an entity and its environment, they exert a centrifugal force on the entity by allowing the system to come apart enough to receive input from outside and to provide output for other systems”. He defines boundary permeability as “the ease with which energy, information, and matter enter and leave a focal group”. Applying Alderfer’s framework to the foreign subsidiaries of MFIs, management control systems can be underbounded, optimally bounded or overbounded for the state of the local environment. Boundaries with low permeability (relatively overbounded) safeguard a subsidiary in an unstable institutional context, while increased boundary permeability (relatively underbounded) allows a subsidiary to thrive in a benevolent context. Optimal boundary permeability maximizes the likelihood for a foreign subsidiary to survive and prosper in a specific institutional context. A high degree of boundary permeability implies that the foreign subsidiary is subject to strong local isomorphic forces, while relatively closed boundaries foster intracorporate isomorphism.

The institutional context characterized by assessing formal and informal rules

Guillén and Suárez (2005) review theoretical perspectives on characterizing the institutional context. Their approach that describes the political economy of foreign direct investment in a host country can be analysed together with the approach on comparative corporate legal traditions, resulting in an assessment of formal rules. Further, their analysis on cross-cultural frameworks assists in assessing informal rules in society, which can be complemented by the notion of social capital (see Fukuyama, 1995). Guillén and Suárez’ research is consistent with Zucker’s (1986) components of the institutional basis of trust: “the legal, political, and social systems that support the monitoring and sanctioning of social behavior” (see Zaheer and Zaheer, 2006: 22).

It can be argued that the formal rules of the institutional context in a host country, as characterized by government policy and the prevailing legal system, determine the regulative pillar of society.

Formal rules

Guillén and Suárez distinguish two relevant properties of government policy: approaches towards development (export oriented vs. import substitution) and towards MNCs (permissive vs. restrictive). The combination on both dimensions determines the perspective on MNCs (e.g. partners vs. necessary evils), as well as the prevailing type of organizations (e.g. small and medium sized companies vs. state-owned corporations). Moreover, the type of government policy impacts the MFI's institutional context, with emphasis on the characteristics of the regulatory systems in home and host countries. Comparative corporate legal traditions have been extensively studied (e.g. Mattei, 1997; Juriglobe, 2008), but the classification as proposed by La Porta et al. (1998) has been widely acknowledged. Guillén and Suárez emphasize the implications of La Porta et al.'s dimensions on protecting investor and creditor rights for corporate governance, ownership and financing structure. La Porta et al. (1998) distinguish five categories of legal systems, ranging from English and French to German, Scandinavian and the former socialist systems. The strength of investor/creditor protection and respective enforcement provide additional measures for assessing the benevolence of the formal rules in the host country of MFIs.

Informal rules

The informal rules of society characterize the normative and culturally-cognitive pillars of society. Several comprehensive frameworks have been developed on cultural dimensions (e.g. Hofstede and Hofstede, 2005; Inglehart-Welzer, 2010; Schwartz, 2007; Trompenaars and Woolliams, 2003). Based upon Schwartz' definition on culture, an analysis of cultural dimensions can lead to conclusions on both the normative (norms and values) and cultural-cognitive pillars (shared meaning). While any of the cultural analysis frameworks can be applied, Inglehart and Welzer's (2010) cultural map allows a straightforward interpretation on two statistically relevant dimensions (traditional vs. secular-rational and survival vs. self-expression values). Inglehart and Welzer calculated scores on both dimensions for a range of countries, based upon data from the World Values Survey, which resulted in a cultural map that groups countries with similar scores. The first dimension represents the relative importance of religion, while

the latter reflects the evolution towards post-industrial societies in which self-expression is associated with an active participation in economic and political matters. Examples of groups of countries are “Protestant Europe” (e.g. Sweden, oriented towards self-expression and secular-rational values) and “Latin-America” (e.g. Brazil, oriented towards traditional values and relatively neutral on the survival / self-expression dimension).

According to Fukuyama (1995: 10), shared norms and values foster trust within a community and provide a basis for social capital, which is defined as “the ability of people to work together for common purposes in groups and organizations” (a concept developed by Coleman, 1998, cited by Fukuyama). Fukuyama (1995: 62) distinguishes three types of sociability (“family and kinship”, “voluntary associations outside kinship” and “the state”), which also can be linked to the prevailing type of economic organizations. The measurement of levels of interpersonal and systemic trust provides insight in the available social capital in a host country. Linking the concept of management control systems (Chenhall, 2003; Langfield-Smith, 1997; Van der Stede, 2003) with the integration-responsiveness framework and boundary permeability, we propose a conceptual framework depicting a choice on boundary permeability which can lead to functional or dysfunctional outcomes at home (parent company) and/or host country (subsidary), as shown in Figure 1 below.

------Insert Figure 1 about here------

The developed theoretical framework allows MFIs to assess the formal and informal rules in the society of a host country, so that it can decide on the degree of required isomorphism on both dimensions.

RESEARCH METHODS

Data collection was conducted through semi-structured elite interviews (Bellamy, 2011) for which purposive sampling was applied (Silverman, 2010). The interview guides included for a specific phase of the project questions on “critical

incidents", a term defined by Flanagan (1954) (see Bryman and Bell, 2007). The analysis of critical incidents allowed the identification and confirmation of themes underlying the research questions through in-depth insights in incidents at MFIs. Data and evidence were collected between September 2010 and March 2013 through 25 semi-structured interviews with 21 participants. The interview participants (see appendix) were mainly active in the financial sector (18) and who were predominantly based in North America, Western and South-Eastern Europe (16). In order to enhance external validity of the research findings, additional interviews were conducted with professionals from other geographies (2 participants from Africa and Middle East) or active in other heavily regulated sectors (3 participants from the chemical and logistic sector). The secondary data sources included datasets on cultural dimensions from Inglehart and Welzer (2010; Wave 5), on dimensions of trust (as described by Roth, 2009) from World Values Survey (2012) and on characteristics of legal systems from La Porta et al. (1998). Data analysis was performed with a range of tools, including Autoform (Nottingham Trent University application), Nvivo, Word and Excel and SPSS. Nvivo coding at nodes was used to confirm identified dimensions and consistency, while SPSS was applied for a specific part of the research project on boundary permeability.

ANALYSIS AND FINDINGS

The need and challenge to restore trust

Institutional theory offers insight on aligning the "*perceived* probability of desired behavior" (Das and Teng, 1998: 494) of MFIs with the expectations of stakeholders in home and host countries. Restoring trust in the financial sector has been a significant challenge, as also recognized by an interview participant who questions the capability of financial institutions *"to regain easily the trust of consumers and consequently of the supervisory authorities"* (Participant 14).

Senior managers acknowledge that trust from customers and the public at large in MFIs is perhaps even more important than merely complying with coercively imposed regulations. An interview participant in the research project refers that during the crisis:

"The biggest breach in trust has been between the banks and the general public… many banks in fact come to the conclusion now that losing the trust of ... their clients is probably even more of an issue of concern than… the reinforced controls that they now experience from the local supervisors" (Participant 17).

Formal rules are important yet insufficient

Roach's perspective (2005) that the alignment of MNCs' behaviour with the objectives of all stakeholders requires self-imposed initiatives as well as additional regulations, is supported by an interview participant:

"The financial sector… will continue to promote adjustment of behaviour through self-regulation, but I am convinced that [it] will prove to be insufficient and that the government will impose further regulations… The general feeling is too negative in society, which means that even very well structured points of view are not considered to be acceptable [by stakeholders]" (Participant 14).

He furthermore underlines that the implementation of these regulations aimed at strengthening the financial system requires a joint effort of MFI and regulators:

"... I think that the financial sector needs to take responsibility to react in the most appropriate manner [to stricter regulations]. I am an advocate for very strong supervisory authorities that have the capability to fulfil that role, [and that] are very professional in order to enter a dialogue [with MFIs]" (Participant 14).

The crisis has demonstrated that coercive isomorphism at MFIs has not been sufficient to avoid major breakdowns in corporate governance. Coercive isomorphism to enforce compliance with regulations is always an option for authorities, but the question arises whether this is satisfactorily effective to restore trust in the financial sector. An interview participant clarifies this point:

"Of course, I can't predict twenty years into the future, but during the next five years regulations will become stricter. …Certain events occurred that are now being regulated, ...it is an easy solution to implement rules that you can tick-off, but it won't be the real solution; we are dealing with a culture that needs to change, which you can't change just through regulation" (Participant 10).

Informal rules

Comments from an interview participant illustrate the importance of assessing informal rules (e.g. cultural dimensions and social capital) for boundary management:

> *"If you are going in a country where… trust, confidence is not high…, and you may not know that, so if you think about that... the social fabric of the society, then you can come to some very important conclusions"* (Participant 16).

> *"… at the end of the day, if you work in a country [where] you can't really trust the people…then you are going to close the boundaries. If you are working in a country [where] you know people are trustworthy, almost would say with high principles, then you can certainly open the boundaries much more"* (Participant 16).

Normative isomorphism

As DiMaggio and Powell (1991) point out, isomorphic pressures are not mutually exclusive. This perspective is illustrated by a quote from an interview participant which reflects a combination of coercive and normative isomorphism:

> *"Professional behaviour in [country A] is very [much] regulated; ... there is a number of additional regulations that you have to comply with, and therefore… that basically translates ... into management controls to make sure that that [professional behaviour] is actually happening in compliance with the regulations"* (Participant 2).

Isomorphism and managing boundary permeability

Since isomorphic pressures can be either formal or informal in nature, an MFI needs to assess the boundary permeability of the institutional context on formal and informal rules. It can be argued that optimal boundary permeability on both dimensions does not only foster legitimacy but also trust of stakeholders.

An interview participant emphasizes the relevance of these dimensions for the perception that stakeholders have of the corporate behaviour of MFIs:

"When you talk about government policy, legal systems, governance and so forth, you are talking about issues that ... are very [much] linked to reputational risk, [which] ...has to do with ...the breakdown of rules that ... should not be broken and will affect the company in terms of the way people look at it" (Participant 6).

The importance of consistent corporate behaviour is acknowledged by a number of participants, which can be linked to the notions of transparency and accountability:

"I think [that] as an acknowledgement that management has a responsibility, ... the corporate structure, here and abroad basically is much more, interested in assuring the shareholders and the investors, as well as the community, that management is doing a responsible financial job" (Participant 11).

"I think that the first requirement ... is to create transparency… in all their control systems, to create transparency in its financial statements, to create transparency in the way we apply ... rules and regulations, transparency in the way we operate locally" (Participant 17).

The emphasis on transparency and accountability is also reflected in the internal and external communication strategy of MFIs:

"You have to explain a lot as a company; external communications have become more and more important [than] a couple of years ago, in order to explain why you choose to do something, or choose to do something in a different way, or choose not to do something" (Participant 17).

"I insist everywhere that, as a matter of principle, we are fully transparent…and we always have only one approach on the type of management controls at our international subsidiaries…, which also avoids surprises" (Participant 14).

It should be noted that MFIs need to ensure consistent corporate behaviour across both home and host countries in order to meet stakeholder expectations:

"[If] the way you act in one country from a moral perspective differs completely from a country in another part of the world; ... [then] you simply cannot explain that …to your stakeholders in your home country" (Participant 17).

He elaborates that local management needs to understand the requirements at both subsidiary and parent company level:

"…a lot of these local managers …apply local rules or regulations...and… are completely surprised…that their local operation run by them, in a locally acceptable manner, is scrutinized and is heavily attacked by stakeholders in the home country of a company" (Participant 17).

A structured assessment of the formal rules in home and host countries may assist in determining the most appropriate manner to "internalize the externalities".

A choice of market entry

Finally, MFIs may desire to, but are not obliged to operate in certain host countries. A comment from an interview participant underlines the importance of government policy for the nature of the institutional context in which MFIs operate:

"…in the practice of business, there are two principal factors that come into force …, considering the entry into a business relationship. Those two factors which are somewhat equivalent, but may vary in emphasis as time goes on are: economics and political. To the extent that, on a cross-country basis, both the political and the economic [factors] are in balance and positive, the growth of business between the countries ... becomes greater" (Participant 11).

An interview participant phrases the importance of assessing the institutional context as follows:

"It would be to the benefit of the corporation…that goes to a foreign country, to know beforehand ... what is the impact of the cultural and informal rules, or even the formal rules of the country" (Participant 20).

He elaborates that:

"You might even come up with something that is completely conflicting with your basic rules and principles. And, that could lead you to the decision to change your mind and not enter the market" (Participant 20).

This view is shared by another interview participant, underlining the importance of consistent corporate behaviour across home and host countries:

> *"If the morals in the host country are…too far apart from the morals that they [MNCs] have to comply in their home country, then they simply decide to stop the operations in the host country"* (Participant 17).

DISCUSSION AND CONCLUSION

The recent crisis has triggered a debate about the governance of the global financial system, with a focus on the trust of key stakeholders in the financial sector. At the national level, governments have proceeded with regulatory reforms. At the international level, the importance of trust in the financial system has been further emphasized by supranational bodies (e.g. FSB, G20). However, restoring trust between MFIs and their public and private stakeholders is a complex matter because of the nature of trust. MFIs, as large MNCs, can influence the economic development of some countries and can even create challenges to their ability to implement reforms. As a result, restoring trust cannot be achieved simply by complying with government regulations without adequate changes in organizational behaviour within MFIs and adjustment of their trust relationship with key stakeholders in both home and host countries. Two themes stand out from our analysis and findings that contribute to our understanding of the trust relationship that enables or impedes MFI subsidiaries' performance in the host country environment. The first is institutional isomorphism, which reflects a process of institutional and human interactions according to formal and informal rules and constraints. The second is intracorporate isomorphism within the MFI, reflected in the level of boundary permeability of management control systems that enables and limits the impact of institutional isomorphic pressures.

Our findings show that formal rules are important yet insufficient. The initial response to the crisis from governments and parent companies resulted in more coercive authority, through more stringent banking regulations and internal procedures. The aim to achieve institutional isomorphism through coercive formal rules and normative regulations cannot be accomplished without the process of informal mimetic isomorphism through human interactions between MFIs and their key stakeholders. For

MFIs, restoring trust with their customers and the public at large through mimetic isomorphism and intracorporate isomorphism is equally important as compliance with coercively imposed regulations. MFIs need to reinforce relationships with their key stakeholders through the identification and management of the boundaries. Managing boundary permeability requires MFIs' management control systems to be sensitive to the host country institutional environment, including social capital and cultural dimensions. On the one hand, a lower degree of boundary permeability, i.e. relatively overbounded, helps MFIs to safeguard a subsidiary in an uncertain institutional context with unstable regulatory regimes and unclear institutional isomorphism. But conflict may occur when the host government attempts to exercise more coercive rules. On the other hand, a higher degree of boundary permeability, i.e. relatively underbounded, allows MFIs' subsidiaries to prosper in a benevolent environment. However, the relationship between MFIs and the host government can be jeopardized if and when the environment and context changes. This leads to our notion of striking a balance between institutional and intracorporate isomorphism, as reflected in consistent corporate behaviour across home and host countries (e.g. on transparency and accountability) and strengthened relationships between MFIs and supervisory authorities in the application of national and international regulations.

That being said, MFIs have options to choose whether to have subsidiary operations in certain countries; a matter of market entry choice. MFIs may desire to, but are not obliged to operate in certain host countries if the institutional context offers a less appropriate environment for a balance between institutional and intracorporate isomorphism.

Limitations and implications

This paper stems from a larger research project of the first author's doctoral research. Therefore, the nature of literature and data is richer than what we have applied in this paper. The original research questions were stated from slightly different perspectives. We have managed to separate the theme of restoring trust through institutional and intracorporate isomorphism at MFIs' subsidiary level from the research at a number of levels of the global financial system. As a result, we may have achieved the depth of analysis at the expense of a more integrated view. Another limitation is the

generalizability of our findings. By adopting a qualitative research method we have explored the richness of primary data and depth of participants' responses, but the interviews are primarily confined to a limited number of MFIs and their subsidiaries in selected countries. Nonetheless, our theoretical development and empirical findings do offer generalizable results for the financial sector in general and for MFIs in particular. Optimization of boundary permeability between the MFIs as well as their subsidiaries and key institutional stakeholders in both home and host countries is critical for building and restoring a trust relationship. This insight adds value to our understanding of literature on the widely studied concept of institutional isomorphism. Further, we also contributed in reviving research on the under-researched notion of intracorporate isomorphism, which requires further research in the future.

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APPENDIX

Interview participant	**Location**	**Industry focus**	**Seniority**
1	North America	Financial sector	Middle management
2	North America	Logistics sector	Top management
3	North America	Chemical industry	Top management
4	Middle East	Financial sector	Middle management
5	North America	Financial sector	Top management
6	Western Europe	Financial sector	Top management
7	Western Europe	Financial sector	Top management
8	Western Europe	Chemical industry	Middle management
9	South Eastern Europe	Financial sector	Top management
10	Western Europe	Financial sector	Top management
11	North America	Financial sector	Top level external advisory
12	Western Europe	Financial sector	Middle management
13	Western Europe	Financial sector	Middle management
14	Western Europe	Financial sector	Top management
15	Western Europe	Financial sector	Middle management
16	Western Europe	Financial sector	Top management
17	Western Europe	Financial sector	Top management
18	Western Europe	Financial sector	Middle management
19	Africa	Financial sector	Top level external advisory
20	South Eastern Europe	Financial sector	Top management
21	South Eastern Europe	Financial sector	Middle management

FIGURE 1 BOUNDARY PERMEABILITY AND INSTITUTIONAL ISOMORPHISM