Radical Institutional Change: Foreign Firms Strategic Responses to Regulatory Punctuations in Emerging Markets

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This paper offers theoretical and empirical insights about the strategies and characteristics of foreign banks operating in an emerging market, which suffered radical transformations in its business landscape during the 1990's and the early 2000s. The results demonstrate foreign banks from countries with stronger commercial ties to the focal emerging market, a higher degree of internalization, and more aggressive lending practices (in the focal market) outperformed and or outlasted foreign banks with weaker commercial ties, lower degrees of internalization, and less aggressive lending practices.

INTRODUCTION

The ability to understand the external environment has been long recognized as a key determinant of organizational performance (Porter, 1990). In the last few years, however, profound transformations of the business landscape took place due to globalization and technological advances (Hitt, Keats, and DeMarie, 1998). Therefore, it has been suggested that successful organizations would be those with the ability to adapt to radical change (Richardson, 1996; Volberda, 1996).

While the importance of radical change has been recognized (e.g., Meyer, Brooks, and Goes, 1990; Gersick, 1991, 1994; Wollin, 1998; Sabherwal Hirschheim, and Goles, 2001), firm strategies and characteristics that facilitate or hamper firm performance, under radical change, have not received the same attention (Keister, 2002). In addition, because emerging economies[1] have experienced a more radical transformation in their business landscapes, examining firms operating in these regions should allow us to better identify the causes behind a successful or failed (radical) adaptation. For instance, according to Peng and Heath (1996), the old institutional rules of the communist system became useless under the new environment. Similarly, after major liberalization policies carried out by most Latin American governments during the 1980s and 1990s, foreign multinational firms suddenly could enter the Latin American markets after 50 plus years of government protectionism (Sheahan, 1987, 1997; Toulan, 2002). In turn, this abrupt policy change forced domestic[2] firms to quickly adapt to the new landscape.

The strategic management and international business literatures have produced a wealth of research gauging the actions and strategic shifts of large multinational corporations (e.g., Luo & Peng, 1999; Ferrier, 2001). However, this research has emphasized performance comparisons between foreign multinational and domestic firms, largely overlooking the performance differences among foreign multinational firms competing in a third host market (Rangan & Drummond, 2004). For instance, Doh (2000) recognized the scarcity of studies on firm-level responses to privatization, while Hoskisson, Eden,

Lau, and Wright (2000) commented on the need to study the larger institutional context on individual firm responses.

The present study addresses these gaps in the literature by examining how a particular type of radical change, namely a radical institutional change or regulatory punctuation, [3] affects foreign multinationals in emerging markets. In so doing, the study explains why despite regulatory punctuations' normally positive effects on foreign firms, there are some foreign firms that performed poorly. This research also explores whether there are certain "universal" firm strategies or firm characteristics that enable some foreign firms to better align with the new business landscape (after a regulatory punctuation).

In sum, the goal of the paper is to give answer to the following research questions: Why are some foreign firms more likely to outlive other foreign firms, during regulatory punctuations in an emerging host market? Why are some foreign firms more likely to outperform other foreign firms, during regulatory punctuations in an emerging host market?

THEORY & HYPOTHESES

The following hypotheses seek to identify the successful strategic responses and characteristics of foreign firms adapting to regulatory punctuations. In so doing, the hypotheses compare foreign firm vs. foreign firm as follows: (1) Commercial distance, (2) international diversification, and (3) market and non-market capabilities.

Commercial Distance
The Strategic Management and International Business literatures have largely overlooked the performance differences among foreign MNEs competing in a third host market (Rangan & Drummond, 2004). However, in light of the profound transformations of the business landscape of the last few years, competition among MNEs in emerging markets is becoming more pervasive (Rangan & Drummond, 2004). Emerging markets have moved from protectionism (e.g., Latin America) or central planning policies (e.g., Russia) towards market-oriented policies (Sheanan, 1987, 1997; Spicer, McDermott, and Kogut, 2000). Because this policy shift effectively changes the 'rules of the game' in several emerging markets, firms operating in these markets had to adapt quickly in order to survive.   Institutions, defined by Scott (1995: 33) as "cognitive, normative, and regulative structures and activities that provide stability and meaning to social behavior," reduce uncertainty by providing dependable and efficient frameworks for economic exchange (DiMaggio & Powell, 1991). However, during revolutionary periods, such as the ones brought about by regulatory punctuations (e.g., commercial liberalization policies), following old institutional rules could become useless as these rules rapidly lose legitimacy (Peng & Heath, 1996). Seemingly, under these conditions, following old institutional rules no longer lessen uncertainty, as they are no longer the consensus for efficient economic exchange.

Zaheer and Mosakowski (1997) found that under financial market deregulation, local firms are more likely to exit the market than foreign firms. Ataullah and Le (2004) found that after liberalization, the performance of foreign banks in Pakistan and India was higher than that of Pakistani and Indian banks, respectively. Judging by these results, the rule change (after liberalization) did not affect foreign MNEs as much as it did domestic firms. Perhaps, because the policy change signified a move towards market-oriented economic policies, MNEs did not experience as much uncertainty as their domestic peers since MNEs already knew how to operate under market-oriented conditions[4]. While the literature demonstrates that foreign MNEs outperformed domestic firm after liberalization (e.g., Zaheer & Mosakowski, 1997), which implies a sharp decrease on liability of foreignness (LOF), we are yet to know why some foreign MNEs outperformed other foreign MNEs, after liberalization.

Eden and Miller (2004) identify institutional forces as key drivers of LOF. According to these authors, legitimacy and institutional distance explain how MNEs adjust to the 'rules of the game' or business environment of the host-country (i.e., adjust to the host-country's unfamiliarity, relational, and discriminatory hazards). However, during a regulatory punctuation, emerging market institutions are in a state of flux. According to Gersick (1991), during a punctuation (i.e., a revolutionary period), firms try to

adapt to a new set of environmental (or institutional) rules. Yet, because this change is not part of a life cycle, end-states are unknown. Under these uncertain circumstances of evolving institutionalization, where new rules for economic exchange are being tested and selected, carefully gauging how institutions evolve should allow foreign MNEs to better adapt to the new environmental rules. In other words, Eden and Miller's (2004) assertion that institutional distance explains the MNEs ability or inability to adapt to the new 'rules of the game' of a host country, should become even more important during regulatory punctuations.

Rangan and Drummond (2004) found support for the notion that foreign MNEs from institutionally closer host nations would outperform their competition – i.e. those which home nation has stronger ties to a focal host nation. For instance, they mention that the Dutch Unilever and the American Procter & Gamble, two equally large and powerful MNEs, dominate each other in Europe and North America, respectively. According to them, this is because the Netherlands have stronger ties with European host-nations than America does, while the US has stronger ties with their North-American neighbors than the Netherlands does.

Following this rationale, it seems MNEs from countries with closer commercial ties to the target host market are better aligned to the host market's business landscape (Rangan & Drummond, 2004). It is also apparent that after liberalization, some institutions from emerging markets began to collapse as protectionist and central planned economic policies were substituted by market-oriented policies (Peng & Heath, 1996). Because foreign MNEs had experienced operating under these conditions, foreign MNEs outperformed domestic firms during this regulatory punctuation (e.g., Ataullah & Le, 2004). However, because new institutions in emerging markets would probably evolve slowly and would not become exact replicas of those from developed markets, MNEs from countries with stronger commercial ties to the target host market should be in a better position to align to the evolving institutions of the focal host market.

Cultural distance has often been used in the international business literature. For instance, Blomstermo, Sharma, and Sallis (2006) used cultural distance to investigate foreign market entry modes. However, we side with the arguments espoused by Shenkar, Luo, and

Yeheskel (2008), were they offer the concept of cultural friction as the substitute metaphor for cultural distance. The concept is intriguing because it implicitly considers culture, but within a context of power relations. We believe commercial distance does reflect the importance of globalization and how it reduces country barriers (Hitt, Ireland, and Hoskisson, 2002), which in turn affect both cultural systems and power relations between MNEs and focal host country. Thus, we posit that commercial distance better captures the strength of ties among countries and their firms. Following this explanation, we hypothesize the following:

Hypothesis 1a. Among foreign MNEs competing in an emerging host market, MNEs from countries with lower commercial distance to that host market country will be more likely to survive (not exit the industry) than MNEs from countries with higher commercial distance to that host market country.

Hypothesis 1b. Among foreign MNEs competing in an emerging host market, MNEs from countries with lower commercial distance to that host market country will outperform MNEs from countries with higher commercial distance to that host market country.

International Diversification

The topic of international diversification has gained favor among corporate diversification scholars (e.g., Delios & Beamish, 1999; Hitt, Hoskisson, and Ireland, 1994). Because international diversification strategies seek to leverage firm-specific capabilities or ownership advantage (Dunning, 1977), Geringer, Tallman, and Olsen (2000) argue that higher international diversification should be preferred as long as MNEs can preserve their ownership advantage. Hitt, Dacin, Levitas, and Arregle (2000) suggest that because MNEs are likely to have a higher number of learning experiences than local emerging market firms, MNEs should possess higher absorptive capacity (Cohen & Levinthal, 1990). Thus, it follows that

MNEs can profit from international diversification not only through their ownership advantage (Dunning, 1977), but also through increasing their learning experience repertoires.

Previous studies find that international diversification is positively related to firm performance, albeit not linearly (e.g., Geringer, Beamish, and Acosta 1989; Hitt, Bierman, Shimizu, and Kochhar, 2001). According to Delios and Beamish (1999), the positive effect of international diversification on firm performance comes as a result of possessing superior resources and the ability to develop new technological expertise. For instance, Kim, Hwang, and Burgers (1993) argue the more internationally diversified a firm is, (i.e., 'the more multinational'), the greater the opportunities to leverage its resources and increase its performance. However, the extant literature has yet to test the link between MNE's international diversification and the performance of its subsidiary in a focal emerging market. In other words, do more internationally diversified MNEs hold an advantage over less diversified ones when entering a new (emerging) market? Do all countries increase the MNEs ability to succeed in a certain host market equally?

Important to the context of the present study, radical institutional changes are likely to create the need for new organizational designs (Baum, Korn, and Kotha 1995). Thus, under these circumstances, organizations might need to change their current business archetype (Gersick, 1991). According to Greenwood and Hinings (1988, 1993) organizations facing regulatory punctuations will seek to reconfigure their business archetype based on their learning experiences or repertoires. Because during these periods organizations try to make sense of the evolving business landscape (Gersick, 1991), it follows that firms with larger business repertoires should adapt quicker. In other words, more internationally diversified firms[5] (i.e., firms with larger repertoires) should be quicker to identify the proper business archetype for that particular market based on their previous experiences. However, a caveat is considered. Perhaps larger repertoires only increase firm's performance when it is localized in a particular region (e.g., Western Europe, Latin America). Following this explanation, we hypothesize the following:

Hypothesis 2a. *Among foreign MNEs competing in an emerging host market, more internationally diversified MNEs, within a particular world region, will be more likely to survive (not exit the industry) than less internationally diversified MNEs, within a particular world region.*

Hypothesis 2b. *Among foreign MNEs competing in an emerging host market, more internationally diversified MNEs, within a particular world region, will outperform less internationally diversified MNEs, within a particular world region.*

Market Capabilities

Hitt et al. (2000) acknowledge the superior technological capabilities and intangible assets of MNEs compared to those of emerging market firms. However, amongst foreign MNEs, under presumably equally superior capabilities, it is unclear if aggressive market oriented growth strategies would result in a competitive advantage. Hitt et al., (1999) suggest that MNEs entering new markets need to quickly obtain certain resources or develop certain capabilities to remain competitive. Moreover, because non-market capabilities take time to develop, foreign MNEs emphasizing growth strategies may choose to leverage their resources and capabilities (i.e., superior technology, intangible assets) as quickly as possible, seeking to outmaneuver their foreign counterparts. This is perhaps even more relevant in an environment where an industry is radically changing. Thus, it should follow that "aggressive" market oriented MNEs would be better positioned to capitalize in their resources and capabilities (and develop new ones quicker) than their less aggressive counterparts. Following this explanation, we hypothesize the following:

Hypothesis 3a. *Among foreign MNEs competing in an emerging market, those following more aggressive market oriented growth strategies (i.e., aggressive lending practices) will be more likely to survive (not exit the industry) than MNEs following less aggressive market oriented growth strategies (i.e., aggressive lending practices).*

Hypothesis 3b. *Among foreign MNEs competing in an emerging market, those following more aggressive market oriented growth strategies (i.e., aggressive lending practices) will outperform MNEs following less aggressive market oriented growth strategies (i.e., aggressive lending practices).*

METHODOLOGY

The Mexican banking industry suffered several regulatory punctuations during the 1990s. These punctuations came in the form of reprivatization and market liberalization policies, which dramatically altered the industry's landscape. Thus, the Mexican banking industry's radical institutional transformation presents an excellent opportunity to study the characteristics and strategies of successful foreign firms adapting to regulatory punctuations in emerging markets. The database consists of all multinational private commercial bank' subsidiaries operating in the Mexican banking industry from 3/1991 to 3/2004. Data was collected quarterly from the bulletins issued by the (Mexican) National Commission of Banking. The bulletins have all the financial data available for both foreign multinational and domestic banks operating in Mexico, such as loan portfolio, net income, assets, market share, etc. This financial information also allowed us to calculate other measures such as the aggressiveness index, and to identify when a bank entered or exited the industry. Other non-financial information used in this dataset was retrieved from several scholarly articles on the subject (e.g., Guillen and Tschoegl, 1999; Mailander, 1999; Ortiz, 1994).

Dependent Variables

Survival (Foreign MNEs & Local Firms). Following Cox (1972), we created a "life table" of subject-time units where the dependent variable is the hazard or probability that a bank exits the Mexican banking industry in a given quarter (3/1991-3/2004). Thus, the banks at risk were those operating in the Mexican banking industry during that period. The hazard of exiting the industry starts when a bank enters the industry after its reprivatization. Consequently, the banks' ability to survive (not exit) the industry is measured in quarters (1-52). In turn, the dependent variable is named NuQuarters, as it records the number of quarters between when the bank first enters the Mexican banking industry (i.e., starts the risk period) and when the bank either exited or was censored (from quarters 1 to 52). The NuQuarters variable is used in combination with the variable Exit. Exit records whether the event actually occurred, that is, whether a bank exited the industry (Exit=1) in a given quarter or was censored (Exit= 0). For this dataset, only 15% of the foreign multinational banks (dataset) exited the industry during the same period.

Performance (Foreign MNEs). While using the same dataset and quarterly data, we used return of equity (ROE) as our dependent variable to measure foreign MNE performance.

Independent Variables

Commercial distance. Commercial distance is measured by using country foreign direct investment (FDI). That is, the inflows of FDI from foreign country X to host country Y is used as a proxy for commercial distance. The higher, the FDI from country X to country Y (i.e., Mexico) the lower the commercial distance. Commercial distance is the result of dividing the net FDI outflows from country Y to the host country (i.e., Mexico) by its total FDI outflows. For instance, America's FDI to Mexico divided by its total FDI outflows in 1995 equaled 3.7%. There are nine countries of origin represented in the sample (i.e., USA, UK, Spain, Netherlands, Germany, France, Japan, Switzerland, and Canada).

International Diversification. Because Bankscope does not report the revenues of a bank at a country or regional level, an entropy measure cannot be calculated. Barkema and Vermeulen (1998) use the number of foreign countries where a bank has subsidiaries as a proxy for the level of international diversification. Accordingly, we use the number of Latin-American countries where these foreign MNEs had banking operations (without considering Mexico) as a proxy for international diversification.

Aggressive Growth Strategies, AGS. The AGS index illustrates whether a bank is aggressively expanding its loan portfolio, in relation to other banks in the industry. Thus the AGS index is the result of dividing the banks' market share in loans by their market share in equity, and then multiplied by 100.

This index [(market share assets/equity) * 100] reflects a bank's relative aggressiveness; the higher the index the higher the bank's aggressiveness. For instance, a bank's index of two hundred means that relative to the industry, this bank is loaning twice as much as a bank with similar equity levels. We used the overall foreign banks assets and equity figures to measure market share.

Control Variables

Size (Top 1000 Banks of the World). Zaheer and Mosakowski (1997) used the Top 200 banks of the world (reported by the Banker) as a control variable. This variable is important because it controls for overall size, reputation, and the overall performance of the bank. In other words, this variable controls for the possible positive (or negative) effects of a bank's international franchise. The Banker's ranking factors include: strength, size, soundness, profits, performance, BIS capital ratio, and NPL to total loans (see Appendix D). For this study, we expanded the measure to include the actual ranking (1-1000), instead of creating categories. Banks' outside the top 1000 ranking received an arbitrary ranking of 2000.

Statistical Models

Survival. About the specific models used in this paper, we used the Exponential, Weibull, and Gompertz models according to how the time is to be entered the equation. Allison (1984) notes that the exponential model implies that a hazard is constant over time, which mean that logarithms of the survival function (ln (S (t)) are linearly related to time t. In other words, the exponential model assumes that the subjects studied (i.e., the banks) are no more likely or less likely to fail towards the end of the observation period than they were at its star. The exponential model can be expressed by the following equation:

$$\log h (t) = a + b1X1 + b2X2$$

The Weibull model allows the log of hazard to increase or increase linearly with the log of time (Hamilton, 1998) and can be expressed by the following equation (where c is a constant that can be positive or negative):

$$\log h (t) = a + b1X1 + b2X2 + c \log t$$

The Gompertz model is appropriate to use when a hazard increases with time (Cleves, Gould and Gutierrez, 2004) and can be expressed by the following equation:

$$\log h (t) = a + b1X1 + b2X2 + ct$$

To determine the suitability of the model, we first ran the Weibull distribution model because it provides information about the distribution shape parameter p. According to Cleves et al. (2004), a *p* value of 1 corresponds to an exponential model where the hazard does not change with time. A *p* value >1, on the other hand, indicates that the hazard increases with time, and thus, that the Gompertz model is the appropriate model to be used. Finally, if *p* value <1, then the hazard decreases with time and thus indicates that the Weibull model is the appropriate model to use.

The use of a maximum likelihood approach was preferred over the partial likelihood approach (i.e., Cox model) mainly because the Cox model is unable to model variables that predict success perfectly. This is because the partial likelihood estimation is a product of likelihoods for all events that are observed to occur; whereas the maximum likelihood estimation is a product of the likelihoods for all individuals in the sample (not only the ones that occurred). Furthermore, the hazard models utilized in the present study are best suited to measure the effect of radical change and firm strategy for domestic firms. This is because 2 out of 3 banks exited the industry during the period of analysis. We believe is close to futile to examine financial performance under these circumstances. On the other hand, for foreign MNEs the ratio of exits to no exits was about 2 out of 14. Thus, we also conducted a longitudinal analysis of firm performance.

Performance

We used cross section time-series linear model using random[6] (within) regression estimators[7] (See Certo and Semadeni, 2006 for a good review on the use of these types of models). We did conduct the corresponding Hausman test (Thomas et al., forthcoming) and the random effects model was the appropriate one to use (P>chi2 = 0.81). Likewise, we conducted a cross section time-series linear model using generalized least squares[8]. To conduct these tests the same database was utilized.

TABLE 1
DESCRIPTIVE STATISTICS

	Mean	SD	1	2	3	4	5	6	7
1. Exit	0.01	0.08	1.00						
2. NuQuarter	15.03	9.75	0.06	1.00					
3. ROE	-1.96	37.83	-0.04	-0.05	1.00				
4. Liberalization	0.85	0.36	-0.02	-0.38*	-0.11*	1.00			
5. Bankers_Ranking	129.84	401.32	-0.02	-0.03	-0.05	-0.02	1.00		
6. Commercial Distance	4.14	3.46	-0.05	0.16*	-0.03	0.06	0.19*	1.00	
7. International Diversification	3.15	3.32	0.01	0.05	0.23*	0.00	-0.26*	-0.10*	1.00
8. Aggressive Growth Index	57.00	65.20	-0.07	0.16*	0.21	-0.12*	-0.02	-0.13*	0.14*

N= 644; * p<0.05

RESULTS

Table 1 shows means, standard deviations, and correlation coefficients. The variables test our hypotheses regarding commercial distance, international diversification, and aggressive market growth and their relationship on firm performance and survival. This dataset consists of one observation per foreign bank per quarter for the years of 1994-2004 (# foreign banks=26; time-subject observations or # of periods at risk=644). The time period does include attrition and accretion changes. Potential multicollinearity between variables was checked and controlled.

Survival

To test hypotheses 1a, 2a, and 3a, we ran the Weibull (distribution) method. The Weibull Table (not shown) displays the Weibull distribution shape parameter p, which has a value of 3.99 and is statistically significant (p< 0.01). A p value > 1 indicates the hazard increases with time, and that the Gompertz distribution is the appropriate one to use (Cleves et al., 2004; Hamilton, 1998). The fully specified model (Table 2) contains one control variable (Top 1000 banks of the world or 'Bankers Ranking') and three independent variables, namely: commercial distance, international (regional) diversification (or number of Latin-American countries with banks- 'NLACOWB'), and aggressive growth index.

TABLE 2
GOMPERTZ DISTRIBUTION; DEPENDENT VARIABLE = EXIT

	Hazard Ratio	SE	Coeff	SE	P > z
Control Variables					
Bankers Ranking	1	0	0	0	0.57
Independent Variables					
Commercial Distance	0.61	0.13	-0.49	0.22	-0.02*
International Diversification	0.94	0.78	-0.06	0.08	-0.44
Aggressive Growth Index	0.77	0.1	-0.26	0.12	-0.04*
intercept			-3.42	1.25	-0.01**
gamma	0.11	0.05	0.11	0.05	0.03*

N = 644
Wald χ^2 = 16.23
Prob > χ^2 = 0.01**

Numbers of subjects = 26
Numbers of failures = 4
† $p<0.10$, *$p<0.05$, **$p<0.01$, ***$p<0.001$

Performance

To test hypotheses 1b, 2b, and 5b, Table 3 presents the same specified model from Table 2. However, Table 3 presents the results from two statistical models that measure performance (not survival). These statistical models are both cross-sectional time-series linear models. The first is a cross-sectional time-series generalized least squares model, while the second is a cross-sectional time-series using random effects[9] (within) regression estimators.

TABLE 3
CROSS SECTIONAL TIME SERIES

	GLS			Random Effects		
	Coeff	SE	P > t	Coeff	SE	P > t
Control Variables						
Bankers Ranking	0	0	0.98	0	0.01	0.96
Independent Variables						
Commercial Distance	0.14	0.42	0.75	-0.55	0.49	-0.26
International Diversification	2.31	0.45	0.00***	2.12	0.61	0.00***
Aggressive Growth Index	0.11	0.02	0.00***	0.09	0.04	0.04*
intercept	-15.96	3.02	-0.00***	-10.76	5.75	-0.06

N = 644; 644
Wald χ^2 = 59.90 ; 22.87
Prob > F = 0.00*** ; Prob > χ^2 = 0.00***

Numbers of subjects = 26
Numbers of failures = 4-38
† $p<0.10$, *$p<0.05$, **$p<0.01$, ***$p<0.001$

Overall, the theoretical model of foreign MNEs strategies and characteristics is generally supported by the data. We present the statistical evidence of each hypothesis in turn.

Hypotheses 1a and 1b suggest foreign MNEs from countries with lower commercial distance to the host market (i.e., Mexico) will outlast and outperform (respectively) those MNEs from countries with higher commercial distance. To test these hypotheses, we used FDI as a proxy for commercial distance. As shown in Table 2, the commercial distance variable is statistically significant. The FDI hazard ratio equals 0.61 (p<0.05), which means that for every percentage point of FDI increase, the hazard of exiting the industry decreases by roughly 39% (i.e., 100 * (0.61-1.00) = -39%). Therefore, the argument that

banks from countries with lower commercial distance to the host market (i.e., Mexico) are less likely to exit the Mexican banking industry is supported. For the relationship between commercial distance and foreign firms' performance, Table 3 shows the commercial distance variable to be not statistically significant. These results only support hypothesis 1a.

Hypotheses 2a and 2b suggest a positive relationship between international diversification and firm survival and performance (respectively). This means that foreign banks that own banks in more Latin-American countries will outlast and outperform foreign banks that own banks in fewer Latin-American countries (in the focal emerging market). Table 2 shows the hazard ratio for this variable (NLACOWB) is 0.94 and it is not statistically significant ($p < 0.44$). In contrast, Table 3 shows this variable to be statistically significant in both cross-sectional time series models ($p < 0.00$). This means that while international diversification does not affect foreign firm survival, it does positively affect foreign firm performance. The results strongly support hypothesis 2b.

Hypotheses 3a and 3b imply that MNEs that follow more aggressive market growth strategies would outlast and outperform (respectively) their less aggressive foreign counterparts. According to Table 2, the aggressiveness index variable is significant. The hazard ratio is 0.77 ($p<0.04$), which means that every percentage point increase in the aggressiveness index decreases the likelihood of exiting the industry by 23% (that is, $100 * (0.77-1.00) = 23\%$). Likewise, Table 3 shows statistical significance for both cross sectional time series models ($p < 0.00$ and $p < 0.05$ respectively). These results strongly support both hypotheses 3a and 3b.

DISCUSSION & CONCLUSIONS

It is worth noting that studies about strategic responses of either multinational or domestic firms operating in emerging markets, when the rules of business have changed so radically, have been scarce. Thus, the present study contributes to the business literature by addressing these gaps. Particularly, this research explains why, despite regulatory punctuations' normally positive effects on foreign firms, there are some foreign firms that perform poorly.

In answering our first research question, the present study demonstrates that banks from countries with closer commercial ties to the host market (i.e., Mexico) and banks that engage in more aggressive growth strategies, namely aggressive lending practices, were more likely to survive regulatory punctuations in an emerging host market. Because liability of foreignness research has largely overlooked the performance differences among MNEs competing in a third host market, this finding contributes to the liability of foreignness literature by identifying the existence of a country of origin liability effect (due to commercial distance).

About our second research question, commercial distance was found to have no effect in foreign firm performance. International diversification had a positive effect on foreign firm performance. Thus, it seems foreign MNEs can transfer their acquired knowledge from different countries through out a world region. The aggressiveness index was also related to foreign firm performance.

Several researchers have suggested that successful organizations will be those with the ability to adapt to radical change (e.g., Richardson, 1996; Volberda, 1996). However, comprehensive studies about which firm strategies and characteristics better help organizations to successfully adapt to radical change are scarce.[10] In this sense, this research contributes to the extant literature by extending current organizational theories when considering the effect of radical institutional change. For instance, while punctuated equilibrium provides a good "environmental" explanation about a firm's need to adapt to radical change, it does not suggest how firms should adapt to this change. However, by providing an explanation on how firms supposed to adapt to this radical change, this study had expanded the theoretical implication of the punctuated equilibrium model. Similarly, the present paper provides a theoretical extension to liability of foreignness by finding that not all foreign firms face the same liability of foreignness. Lastly, RBV is also extended by this research, as RBV is found to have implications for emerging markets firms that are different from foreign developed market firms.

Limitations and Future Research

As with most studies, the present research has limitations that must be noted. First, the degree to which these results can be generalizable to the experience of other foreign firms operating in other emerging markets needs to be considered. While emerging markets are not homogenous (Hoskisson et al., 2000), the regulatory punctuations (e.g., liberalization, privatization) faced by foreign and emerging market firms operating in them have commonalities. For instance, several streams of literature (e.g., economics, political science, management) suggest that these regulatory punctuations were widespread. Thus, it might be possible to conclude that these findings can be generalizable to other emerging markets, or to the Latin-American region at the very least, because this study is conducted in Mexico. For example, the present study may have useful implications for the banking industry in the People's Republic of China, which is currently undergoing a similar regulatory punctuation involving deregulation, privatization and liberalization.

Second, that all firms come from the banking industry might be a limitation. However, it is also worth noting that several international business studies have been conducted using financial institutions as their sample. This is particularly clear in those studies testing liability of foreignness (Miller & Parkhe, 2002; Zaheer & Mosakowski, 1997). Moreover, regulatory punctuations in the 1980s and 1990s often took place at the industry level as government deregulated, privatized and liberalized industries that historically had been under strong government regulations, such as telecommunications, banking and public sector utilities. Nonetheless, for both the first and second limitations, future research should investigate more industries in more than one country.

Another limitation of this study is the measurement of some of the variables. However, it is also worth mentioning that conducting empirical research in emerging markets adds another degree of difficulty. These difficulties were apparent in the use of a categorical variable (0-2) to measure international diversification for domestic banks. Although, more fine-grained measures would have been preferred, the availability (or lack of) archival sources made this task unattainable. Yet, we anticipate the potential effect on the results to be even more positive had we attained more-fine grain measures. This is because the variable became more statistically significant when we changed the measurement from a dummy variable ($p>.041$) to a categorical variable ($p>0.024$).

This study also brings out interesting issues that raise various other new questions for future research. For instance, drawing from the underlying theories used, this study identifies that liability of foreignness is not the same for all foreign firms. As Eden and Miller (2004: 196) put it, the main disadvantage of an international firm when going abroad is being a "stranger in a strange land." However, this study shows that some lands are indeed *stranger* for some strangers. Thus, it would be interesting to explore if these differences in liability of foreignness change with time. Does it necessarily decrease with time? Or, are there certain conditions under which it can be enhanced? Are these results different without a (regulatory) punctuation?

Besides finding that banks from countries with closer commercial ties to the host market are more likely to survive, the present study finds that foreign banks that lend more aggressively are more likely to survive. Also, our study finds that international (regional) diversification and aggressiveness allow foreign banks to perform better that their less aggressive counterparts. Thus, it follows that aggressive growth strategies along with bank familiarity with the host country environment were successful strategies for this set of banks. This is an interesting finding because it is counterintuitive in that the results show that it pays to take bold measures in desperate (not so stable) times. However, it is unclear if other factors facilitated the success of these aggressive strategies. In other words, perhaps for more diversified banks it is easier to implement aggressive strategies. It might be that in so doing, these banks are in fact reducing their company-wide risk. Thus, future research should test for interaction effects. Likewise, it would be interesting to find how aggressiveness affects other types of firms. Do aggressive strategies only benefit banks? Should an aggressiveness index be developed for non-financial firms?

In following with the topic of aggressive responses, this study finds that for (emerging market) domestic firms, aggressive (loan) growth strategies relate negatively to firm survival during regulatory punctuations. Sachs et al. (1996) find that (emerging market) countries that experienced lending booms,

as a result of liberalization, were more likely to suffer currency crises. In this sense, it would be interesting to test if aggressive growth strategies have negative effects on firms from countries that experience lending booms (e.g., Mexico). Do aggressive policies affect banks from countries that did not experience lending booms? Future research should strive to obtain answers to these questions.

ENDNOTES

1. As defined by Hoskisson et al. (2000, p. 249) "Emerging economies are low-income, rapid growth countries using economic liberalization as their primary engine of growth. They fall into two groups: developing countries in Asia, Latin America, Africa, and the Middle East and transition economies in the former Soviet Union and China."
2. Throughout this paper, the words domestic and local are used interchangeably to refer to firms that are owned by the citizens (investors) of a particular emerging market.
3. Following Haveman et al. (2001: 254), regulatory punctuations are defined as those discontinuities originated by "sudden and extensive shifts in state constraints on business operations."
4. These arguments are consistent with the presence of a liability of localness (Perez-Batres and Eden, 2008; Jiang and Stening, 2013).
5. This statement assumes firm manageability (Hitt et al., 2002) and the maintenance of the firm's ownership advantage (Dunning, 1977).
6. Xtreg function in STATA
7. Please note the cross sectional time-series linear model uses ROE as its dependent variable.
8. Xtgls function in STATA
9. The Hausman Test was conducted ($p<0.81$). Thus, the random effects model is preferable to the fixed effects model.
10. Notable exceptions are: Hitt et al. (2004), Rangan and Drummond (2004), and Toulan (2002).

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