# INTEGRATING INSTITUTIONAL THEORY WITH MARKET ORIENTATION TO STUDY SMEs IN TRANSITION ECONOMIES: A CONCEPTUAL MODEL

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***Abstract.*** *The presence of a market orientation is a universal concept which defines the extent to which a customer focus is evident in organizational practices and culture. The concept has been examined extensively in for-profit entities in developed economy settings and has also been found to be of value in transition economies. We contend that transition economies are by definition in a state of change at the institutional level and that this changing dynamic is significantly influential on organizations embedded in its context. However, although noted in previous research results, the inclusion of institutional drivers in market orientation models has not been well developed. This paper presents theoretical and research-based support for a conceptual model which includes the address of relevant institutional drivers of an organization's development and presence of a market orientation. Given the important contributions of SMEs in transition economies, we focus our discussion on this organizational type. Specifically, we present a conceptual model and eight propositions suitable for a comprehensive research agenda of SMEs in transition economies. The propositions present that a significant relationship exists between the extent to which institutions support market orientation practices, and management's recognition and emphasis of market orientation in an organization. We also propose that market-oriented governance and the embrace of a market culture in an organization provides additional support for the presence of market orientation.*

***Keywords:*** *market orientation; transition economy; institutional theory; SMEs; organizational change.*

## Introduction

The presence of a market orientation in an organization is based on the competitively strategic participation of its actors across all functional areas to identify and address customer needs (Day, 1994). A market orientation presence has been found to be positively related to organizational performance (e.g. Kirca, Jayachandran & Bearden, 2005; Jaworski & Kohli, 1993; Slater & Narver, 1994). The research stream over the past 25 years includes the exploration of its presence in multiple organizational forms including for-profit, not for profit and public sector organizations, as well as diverse economic settings (Barberis, Boycko, Shleifer & Tsukanova, 1996; Kirca, Bearden & Roth, 2011). And, while there are variations of the model (Deshpandé, Farley & Webster, 1993; Kohli & Jaworski, 1990; Narver & Slater, 1990), the common presentation is a relationship between key internal antecedent conditions such as leadership, and organizational dynamics and systems, and the presence of market orientation (Kirca et al., 2005; Lancaster & Velden, 2004). That is, the focus has been to identify *what* internal conditions lend toward the presence of a market orientation.

Not surprisingly, as is the case with the development of any research stream, the market orientation literature also presents noted shortcomings. Kirca et al. (2005) encourage a better understanding of *how* market orientation antecedents interact by way of exploring contextual differences. There is also a lack of longitudinal study which leads to the inability to capture the dynamics of change (Gebhardt, Carpenter & Sherry, 2006), as well as an absence of theory development which considers the role of external environment conditions in developing a market orientation (Gebhardt et al., 2006; Qu & Ennew, 2005). While external environmental conditions in an established market driven economy may not be a significant driver in the development of a market orientation, as suggested by Qu and Ennew (2005) organizations in transition economies may have a greater sensitivity to external conditions as there is a shift from a centrally planned to a market-oriented economic structure (World Bank, 2016).

The prominence of business organizations operating in transition economic settings, which account for one-third of the world's population, has increasingly played an influential dynamic in global trade (World Bank, 2016). The transition is exemplified through the implementation of privatization agenda emphasized during the later portion of the 20th century and continuing into the 21st century (Althaus, 2016; Desai &Wheeler, 2016; Ramamurti, 1999). Tushman, Newman, and Romanelli (1986) describe privatization as a "frame breaking" change strategy, while Ramamurti (2000) presents that successful privatization is dependent on factors such as the quality of market-supporting institutions which are simultaneously in a state of flux. These conditions suggest that the state of *external institutional* level drivers may be of particular interest to enrich understanding of a market orientation in organizations embedded in this context. Further, sensitivity to institutional level changes in transition economies may be especially relevant for small and medium-sized organizations (SMEs) which oftentimes do not enjoy a continuation of state subsidy as compared to larger more monopolistic organizations, but are found to be the main competitiveness generators ( e.g. Ahrend & Martins, 2003; Mackic, Peric & Soric, 2014; McIntyre, 2001). Thus, the purpose of our paper is to present a conceptual research model focused on SMEs in transition economies.

Given a gap in theoretical development, we consider using a middle range theory approach. In particular, we consider the meta-analysis findings of Kirca et al. (2005) for relevant perspective derived from market orientation literature, and the presentation of Greenwood and Hinings (1996) for relevant external environment perspective derived from institutional theory. Specifically, our presented conceptual model and eight propositions are intended to provide a research agenda platform to examine the influence of external institutional drivers of the presence of market orientation in an organization by addressing the following questions 1) How do relevant external institutional drivers impact the development of a market orientation in a transition economy SME?, 2) What is the relationship between relevant external institutional drivers and internal antecedents of market orientation in a transition economy SME?, and 3) What is the relationship between key inter-organizational constructs and the presence of a market orientation in a transition economy SME?

We begin our discussion with a literature review of market orientation theory. We then present a brief discussion of relevant institutional theory perspective integrated with the prevailing market orientation model as the basis for the presentation of eight propositions. We conclude with a brief discussion of how the model would be applied to a comprehensive research agenda.

## Literature review

### *Market orientation theory*

For-profit organizations typically focus attention and activities on customers to gain competitive advantage, and thus market orientation became the basis for the development of marketing thought (Tworoger, Voges & Barnes, 2010). Over time market orientation has gained prominence as an approach which can be beneficial when embraced by the organization as a whole (Slater & Narver, 1994). Multiple perspectives of the market orientation construct have been presented (Kirca et al., 2005). Market orientation was conceptualized as a three-dimensional behavioral activity comprised of intelligence generation, intelligence dissemination and responsiveness to market conditions (Kohli & Jaworski, 1990). It was also conceptualized as a culturally derived concept oriented toward both customer and competitors in the market (Narver & Slater, 1990). Market orientation has also been identified as an effective cultural form acting as an element of cohesion in organizational performance (Gebhardt et al., 2006; Narver & Slater, 1990).

Studies of market orientation have included frameworks which address its relationship with antecedents, organizational outcomes, and moderating conditions. Jaworski and Kohli's (1993) frequently cited model tested the relationship of a multi-dimensional market orientation construct (Kohli & Jaworski, 1990) with three categories of antecedents, 1) top management, 2) organizational systems, and 3) inter-departmental dynamics. Their work along with others produced mixed support for the moderating impact that external factors of environmental turbulence, competitive intensity, and technological turbulence can have on the relationship between market orientation and performance (Kirca et al., 2005). Further, the meta-analysis provided for differences in the strength of the market orientation – performance relationship depending on the types of measures used, the type of firm, and cultural context of employees.

As anticipated by Kohli, Jaworski and Kumar (1993), extensions of market orientation studies to less traditional business settings (i.e., non-profit and public sector, transitioning economy nations) indicate that market orientation is also a viable construct related to these organizations' performance. Vazquez, Alvarez, and Santos (2002) found that a market orientation is present in a Spanish non-profit organization although there was a noted need for a modified market orientation scale to capture the differences in non-profit outcome focus as compared with for-profit organizations. Likewise, Balabanis, Stables and Philips (1997) and Cervera, Molla and Sanchez (2001) found the presence of a market orientation in non-profit organizations. Kok and Driessen (2012) found in their study of the transition from public to private sector operation of Dutch housing associations that the most important antecedents associated with the presence of a market orientation are related to the change capacity factors of 1) process improvement control and 2) top management emphasis. And, Barberis, Boycko, Shleifer and Tsukanova (1996) identified the presence of a market orientation in privatized Russian organizations.

Qu and Ennew (2005) explored the development of market orientation in the transition economy China and concluded that although actions of managers in these organizations are relevant, the more influential is the external conditions found in governmental policy regulations which support product quality and customer protections, as well as market-based ownership structure. Li, Sun, and Liu (2006) applied institutional theory to capture the role of government control and the transition to formalized corporate governance of state-owned enterprises in China and found a relationship between market orientation and organizational performance. Farley and Deshpandé (2005) in their study of the presence of a market orientation in Russia noted that while both China and Russia have undergone economic transition, the extreme and long-term central planning systems in Russia and higher degrees of political uncertainty at the time of their study contributed to findings that the presence of market orientation is weaker. Stan, Boush, Barb and Sebastian (2006) consider the potential inability of customer's skills to effectively appreciate a market orientation in transition economies because of the insufficient supporting institutional frameworks.

Kirca, Bearden, and Roth (2011) examined the presence of market orientation implementation in global subsidiaries of U.S. companies and found a positive relationship between the subsidiary's level of market orientation and company headquarters. They found a positive relationship between the subsidiary's level of market orientation and market-supporting institutions in its host country. They also found that subsidiary manager's identification with headquarters positively moderated the strength of the relationship between the host country's market supporting institution and the subsidiary's market orientation. Further, they found that the greater the cultural distance between the home country (U.S.) and the host country the more accentuated the role of the host country's market supporting institutions to the presence of the subsidiary's market orientation. The study offers an insightful illustration of the complex impact that external global conditions can have on the presence of a market orientation in an organization.

Studies have also tested the validity of the two most popular instrument scales used to measure the presence of market orientation in an organization (Ellis, 2006; Rojas-Mendez, Kara & Spillan, 2006; Ward, Girardi & Lewandowski, 2006). The MARKOR scale follows the market orientation model of Kohli, Jaworski and Kumar's (1993) instrument (i.e. intelligence generation, intelligence dissemination and responsiveness), while the MKTOR scale follows the market orientation model developed in 1990 by Narver and Slater (i.e. customer orientation, competitor orientation and inter-functional coordination). As surmised by Roersen, Kraaijenbrink and Groen (2013) although the market orientation concept has universal potential, most research has been conducted in developed economies with established free market business environments suggesting that modification of survey instruments to recognize knowledge limits in understanding the market orientation concept in transition economies would be beneficial. In all, informal institutional contextual settings such as culture, as well as formal institutions are seen as critical in the ability of an organization to identify and address market needs (Webb, Ireland, Hitt, Kistruck & Tihanyi, 2011). Thus, we contend in transition economies there is credible evidence to argue that external institutions, as well as cultural and knowledge tendencies toward the value of market-oriented practices are significant influences on the presence and development of a market orientation in an organization.

***The role of institutional context***

Although a full discussion of institutional theory is beyond the scope of this paper, the initial orientation of the theory was toward answering the question, "why are organizations the same" (e.g. Di Maggio & Powell, 1983). There is an underlying assumption that organizations adapt in order to survive (e.g. D'Aveni, 1994). The primary focus of the theory's tenets is on *relevant* institutional level context infusing values and beliefs (i.e. ideological templates) into organizational behaviors (Meyer & Rowan, 1977; Meyer, Scott & Deal, 1983). The process of adoption evolves from acceptance of the legitimacy of the institutions (e.g. government and regulatory agencies, professional associations) to subsequent mimetic and isomorphic behaviors which evolve to converge into acceptable organizational behaviors (DiMaggio & Powell, 1983). Over time, institutional theory applications have advanced to also consider, "what occurs when there is institutional level change?" (e.g. Greenwood & Hinings, 1996). Interest shifted to consider the impact of the type of institutional change, as well as the pace and scope of the change effort. Two *types* of change were identified, 1) *radical:* a significant shift from one institutional template to another, and 2) *convergent*: a less abrupt shift within the same institutional template. The *scale* and *pace* of change addressed the period of upheaval and adjustment to new conditions and is characterized as ranging from *revolutionary:* wide and fast change, to *evolutionary:* narrow and slow change. In our discussion we are focused on *radical* change as we contend that in transition economies there is a "frame-breaking" shift from one institutional template to another; namely a shift from a centrally planned to a market-oriented structure.

Greenwood and Hinings (1996) broached the topic in response to recognition of the complexity of political and regulatory institutional changes in current environments. As such, they specifically addressed the impact of radical change resulting in a break up of interpretive schemes used to assess an organization's context; that is they presented that "… organizations are structures which are institutionally derived." (Greenwood & Hinings, 1996, p.1028). They proposed that change may vary across institutional sectors due to the extent to which the sectors are coupled and/or are insulated from ideas practiced amongst sectors. Further, inconsistent cues across sectors are also seen as creating the potential for variation of organizational behavior in the sector. Finally, the incidence of radical change and pace of change may vary within institutional sectors because organizations vary in their internal dynamics; namely, there may be resistance to change.

Their process model delineates the adoption and practice of related behaviors as organizations change their organizational templates based on *prevailing* institutional context (in contrast with *past* institutional context). Specifically, while organizations are embedded in the same dynamic institutional context leading toward an isomorphic need to change in order to survive (Oliver, 1991), organizational differences in *precipitating* and *enabling* conditions lend toward different organizational responses. If the prevailing template is recognized as an advantage by actors within the organization a shift to this template is likely to occur. If power structures, namely executive action within the organization support the new behaviors, the culture will ultimately change. Over time, reciprocal exchanges lead to enforcement of mimetic, normative and coercive processes within the prevailing institutional context solidifying the change experience. Greenwood and Hinings (1996) contend that in the early phase of institutional change the technical aspects of the change are more important; and, over time institutional pressures become more prominent.

Seo and Creed (2002, p.224) further develop a theory on the impact of institutional change and provide a clearer focus on "when and how embedded actors individually and collectively come to the conscious point…where they recognize the need… for collective action to change existing institutional arrangements". Recognizing the complexities and inconsistencies of social behavior patterns, they argue that the change process results in a *praxis* defined as "… a particular type of collective human action, situated in a given social-historical context, but driven by the inevitable by-products of that context -social contradictions" (Seo & Creed, 2002, p.230). That is, although institutional change may occur, the outcome may not be what is intended because of the inability for fundamental realignments in frames of reference and logic for action. This conundrum is proposed to be particularly relevant in transition economies where the organizational template may not know by its actors and a 'learning effort' is required. In the absence of suitable institutional templates to mimic, actors may resort to old known routines for behavior (Newman, 2000).

## A conceptual model and propositions

The following discussion presents an argument for eight propositions which reflect an integration of relevant institutional theory perspective with the market orientation model validated by Kirca et al. (2005). Figure 1 is an illustration of the model. In brief, the model recognizes the relationship between relevant institutional context and the process of developing a market orientation in an organization as portrayed by relationships between key actors, organizational dynamics, and organizational systems. The model integrates three main points from institutional theory. First, in the external environment, as suggested by Greenwood and Hinings (1996) there is the presence of multiple vertically and cross- integrated institutional sectors, namely, 1) regulatory, 2) professional support and 3) political which provide cues and basis for the legitimacy of a new archetype or organizational template. When these sectors, in which organizations are embedded present consistent favorable market-oriented characteristics it is expected that a positive environmental setting exists for change to a market-oriented archetype (delineated as 'new archetype"). Second, given that the new archetype is considered to be legitimate (which assumes that the old archetype is considered not to be legitimate) there will be a *precipitating* dynamic of market orientation recognition by top management in the organization (Greenwood & Hinings, 1996). That is, top managers serve in an initiator role to foster the development of a market orientation in an organization. Further, as discussed by Seo and Creed (2003) and Newman (2000), we propose that the recognition of a market orientation is the result of a learning effort or adaptive response by top managers, who are primarily

responsible for the survival of the organization. If the cues from the institutional sectors are confused or obscure the ability for top manager recognition is hindered, and the potential for the organization to develop a market orientation is diminished. Thus, we present the following four propositions for consideration:
Proposition 1: There is a positive relationship between a country's market orientation regulatory policies and an organization's top management's market orientation recognition.

Proposition 2: There is a positive relationship between a country's market orientation professional support institutions and an organization's top management's market orientation recognition.

Proposition 3: A country's political uncertainty negatively impacts the relationship between a country's market orientation regulatory policies and an organization's top management's market orientation recognition.

Proposition 4: A country's political uncertainty negatively impacts the relationship between a country's market orientation professional support institutions and an organization's top management market orientation recognition.

We also propose a *precipitating* condition within the organization's dynamics. That is, the potential of resistance toward change to a market orientation can be assessed based on the extent to which actors throughout the organization value a market culture. Greenwood and Hinings (1996) assert that if actors within an organization are supportive of the status quo, change to the new archetype will not occur. This is especially relevant for SMEs in transition economies. Research indicates that cultural distance from developed economy settings challenges the ability for an understanding and acceptance of market orientation practices (e.g. Kirca et al., 2005). Given that market orientation by definition embraces an organizational-wide presence we include this perspective in the model. Thus, we present the following proposition for consideration:

Proposition 5: An organization's market culture is positively related to its market orientation

Third, as the potential for embracing a new archetype is supported through *precipitating* dynamics, *enabling* dynamics are also engaged to provide an ability to successfully implement the new archetype. In this regard, an organization's governance structure is considered to be an important source of enabling dynamic by providing support for a *capacity for action* by way of providing market-oriented skills and resources (Greenwood & Hinings, 1996). We propose that top management is the point that market orientation recognition and supportive governance converge. This convergence is proposed to unleash the potential for a market-oriented *emphasis*; a construct identified in the traditional market orientation model. Further, as top management plays a significant role in the organization's cultural orientation (Schein, 1985) we also propose that there is a subsequent shift to a market-supporting culture throughout the organization. Thus, we propose the following three propositions for consideration:

Proposition 6: The market-oriented governance of an organization is positively related to its top management market orientation responsiveness.

Proposition 7: The top management market orientation responsiveness is positively related to top management market orientation emphasis.

Proposition 8: The top management market orientation emphasis is positively related to the organization's market culture.

In summary, our conceptual model and eight propositions are intended to present that when there is a positive gain in each of three arenas (i.e., (i) market orientation in institutional sectors, (ii) market orientation antecedent conditions in the organization, and (iii) capacity for change to a market orientation) the result is a development/presence of a market orientation in the organization. Our focus in this discussion has been on SMEs in transition economies. However, we consider that these external institutional drivers may be influential in any economic setting undergoing change.

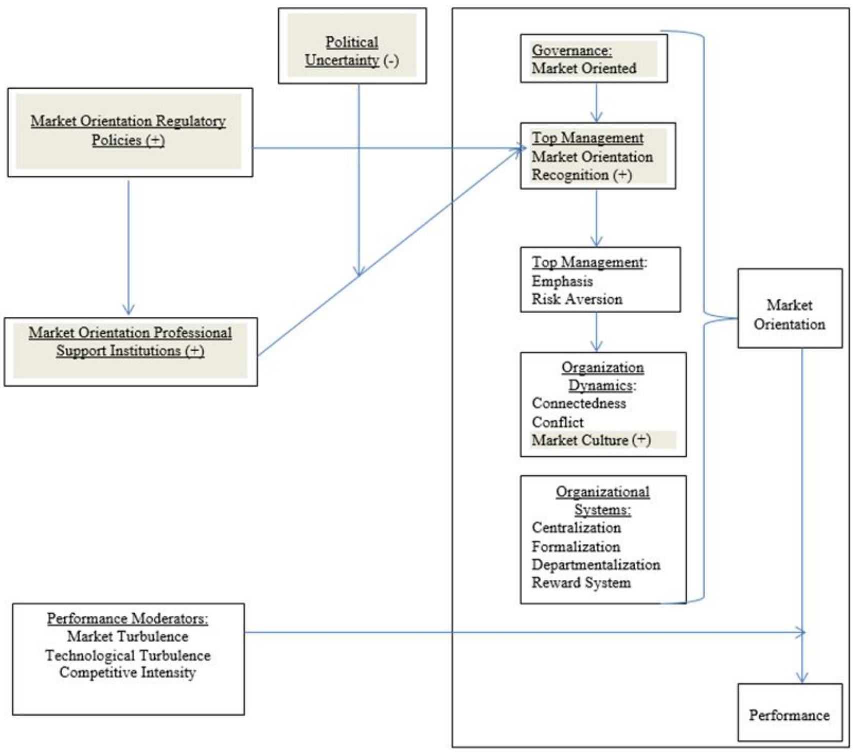


***Figure 1. Market Orientation in Transition Economy SMEs: A Conceptual Model (propositions are shaded)***

## Conclusion

We suggest that the next stage of the study is the development of a comprehensive research agenda. First, given that mid-range theoretical approach in the development of the model and the lack of direct empirical study, we suggest that the first phase of study employ a qualitative investigation. For example, exploring with open-ended question format the potential existence of 'market ignorance' as raised by Roersen et al. (2013), as well as exploring the role of supporting professional organizations in constrained regulatory and political settings as noted by Kshetri (2009) would be of value.

Second, although not directly presented in the model, we propose that while all organizations in transition economic settings experience radical change, each would experience differing levels of revolutionary/evolutionary change contingent upon the timing and relevant political and economic agenda. Further, as suggested by Greenwood and Hinings (1996) the potential for successful change may vacillate between emphases on the technical aspects of institutional conditions in the early stages of transition to an emphasis on institutional pressures to promote isomorphic behaviors in later stages. Also, as observed by Kirca et al. (2005) relevant industry sector characteristics (i.e. manufacturing vs. service) may impact the level of a market orientation. Thus, we suggest that careful consideration of controlling for county level and industry level contingencies be employed.

An organization's archetype is derived from its associated external institutional environment (Greenwood & Hinings, 1996). The ability for an organization to survive is predicated on its ability to adapt to oftentimes changing contextual forces (D'Avini, 1994). Organizational actor responses may vary depending on which institutional context they are aligned with, and to what extent they are coupled with their institutional context. We contend that especially in transition economies there is by definition a *radical* or fame breaking change as seen by shifts in support of organizational archetypes by key institutional sectors. We acknowledge that SMEs are pivotal in not only their success but also the success of transition economies of which they are a member.

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