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How MNCs' perceive and respond to the Polish institutional environment

Abstract: The article discusses the significance and role of institutional analysis in building up competitiveness of the economy and evaluates condition of the Polish institutional system from the viewpoint of foreign investors. It also analyses an impact of the Polish institutional environment on the status, structure and activities of MNCs operating in Poland. Preliminary results of empirical studies conducted by the author in 20 Polish manufacturing subsidiaries of MNCs are shown and discussed here.

The paper begins with a short presentation of what institutions are, what constitutes an institutional environment and discusses the difficulty and importance of its appropriate creation. The next section is a short description of the main features of the Polish institutional environment. Analyses of some empirical data are in the last part of the paper; these concern opinions of MNCs about operating in Poland and information about their internal structure and organizational practices in comparison with analogous sister companies operating in other host markets.

Keywords: institutions, institutional analysis, institutional environment, Poland, multinational companies, subsidiaries.

Jel codes: F2, P3, L2.

1. Institutional environment: its elements and significance to the country's competitiveness

All theoretical trends dealing with institutions in the economy (e.g. old institutionalism and new institutional economics), organizational theory and sociology emphasize a significant impact of institutions on the functioning of economic actors. Institutions, however differently defined and examined, are the rules we create and follow in our life. Institutions reflect regularities in repetitive actions, customs and rules that provide a set of incentives and disincentives for individuals¹ or they can be defined as macro-

¹ D. North, *The New Institutional Economics*, Journal of Institutional and Theoretical Economics 142/1986, 231.

level abstractions of rationalized and impersonal prescriptions². They create a tunnel which restricts full rationality of economic actors³. Institutions shape our (not only) economic preferences, influence perception of economic values and other economic actors, determine the whole process of decision making and, in a way, our effectiveness⁴. They also form the way a certain market operates, so they shape both the environment of economic entities and the framework of an organization.

Institutional environment is created by a complex system of regulations, customs and practices which directly or indirectly influence certain behaviours of entities. Thus the institutional environment of economic entities consists of:

- formal institutions: all kinds of legal-administrative regulations; prohibitions, restrictions, commands or privileges. Institutions formalized in this way contain a description of circumstances in which a given regulation is used, the extent of sanction/relief and the procedure of executing this regulation (according to R. Scott it is a regulatory dimension of the institutional environment)⁵.

² This is a typical definition for new institutionalists of organizational theory. Institutions originate from certain scripts of behaviour, categorizations or rules, not necessarily rational but becoming ingrained when repeated without any reflection. A human being in the institutional organizational trend resembles a passive individual entangled and somewhat bound by environment and its regulations. An economic actor strives for environmental legitimization in his/her desire to adapt to the rules of this environment. Adhering to routines, duplicating patterns, favours institutionalization but at the same time is also a source of structural inertia, thus changes (e.g. in an organization) occur rarely and they are frequently of incidental character, more creeping than stepping and often superficial. Revolutionary, fundamental changes occur when e.g. an institutional system of a higher order breaks down. For more see e.g. *The New Institutionalism in Organisational Analysis*, ed. W.W. Powell, P.J. DiMaggio, The University of Chicago Press, Chicago 1991.

³ According to H.A. Simon, regarded as a precursor of studies on limited rationality of economic actors, economic activity takes place in a kind of “tunnel” of restrictions within which the entity has a freedom of choice. J. Wiśniewski mentions two groups of limitations of an entity’s rationality. The first one is connected with tendencies in the development of market economy and imperfections of market mechanism (e.g. no access to perfect information, barriers to entry). The second group is limitations connected with the features of entities making economic decisions. In both groups institutions play a significant role: legal and administrative regulations, customs, habits, moral code, etc. For more on the subject of limited rationality see, among others H.A. Simon, *Rationality in Psychology and Economics*, (in): *Rational Choice. The Contrast between Economics and Psychology*, R.E. Hogarth, M.W. Reder (ed), The University of Chicago Press, Chicago and London 1987; J. Wiśniewski, *Polimorfizm zasady racjonalnego gospodarowania. Teoretyczne studium komparatywne*, The Publishing House of Nicholas Copernicus University, Toruń 1996, pp. 25-27.

⁴ This is a common view shared by all institutionalists; those from sociology, organization theory and economics: Veblen, Coase, Williamson, Hennart, Ostrom, Shepsle, Riker, Selznick, Scott, Powell, DiMaggio etc. For a good comparison of differences between those fields and scientists – how they see influence of institutions on actors’ behavior, see P.J. DiMaggio, W.W. Powell, *Introduction*, in: *The New Institutionalism*, op.cit, and U. Pagano, *New Institutionalism and the Diversity of Economic Institutions*, CASE – CEU Working Papers Series, Warsaw, December 1998.

⁵ See three pillars of institutional environment: W.R. Scott, *Institutions and Organisations*, Sage, Thousand Oaks 1995, p. 35 and following.

- informal, but commonly known practices, habits in a given environment which frequently do not exist in a written form and are not as univocal as institutions of regulatory sphere. The actors, however, know the risks involved when the fixed norms of behaviour are violated:
 - norms resulting from e.g. obligations, perception of social roles, stemming from moral standards functioning in a given society or the so-called sense of appropriateness, i.e. from the common belief that in a given situation requires a given behaviour. This type of institutions can be defined more precisely and assume the form of e.g. guidelines or codes of practice or they may function as unwritten scripts of behaviour in the so-called collective awareness of a community (according to R.Scott this is a normative dimension of institutional environment).
 - norms resulting from e.g. the acceptance and recognition of a given way of behaviour as a professional, more effective one. Institutions of a cognitive dimension of the institutional environment (as defined by W.R.Scott, quoted above) find their origin in the activity of a broadly understood group of experts recognized in a given environment. It is them who determine the new ways of conduct and institutionalization of this conduct occurs through imitation and mimetic behaviour.

The related literature of the new institutional economics analyses above all formal institutions; character and stability of political and legal-administrative sphere of the economy (e.g. regulations concerning the freedom to conduct economic activity, tax system). The impact of these elements on the functioning and effectiveness of the market is fairly obvious. Acts on economic activity, development of financial markets and regulations concerning the transfer of profit, tax and administrative burdens define the range of freedom and effectiveness of the functioning of economic entities. For multinational enterprises it is important to have as much freedom on the host market as their local counterparts, although multinationals would obviously desire more institutional privileges than the local entities (e.g. several years long tax holiday)⁶. The analysis also covers adjustment of the local legal solutions to international standards as such standardization reduces transaction costs. Another important aspect of the analysis is stability of law which guarantees security and encourages long-term investment.

The analysis of formal institutions embraces not only their contents and stability but also effectiveness of executing the established norms since they influence the volume of transaction costs. An efficient system of execution eliminates the propensity to cheat and reduces transaction costs because a potential crook will inevitably

⁶ The author of this article, however, holds a view that such privileges lead to distortion of the market mechanism. Regulations concerning the economic activity should not discriminate against any group of economic entities, including the local ones.

bear the consequences of his opportunistic behaviour⁷. Moreover, efficient execution of the established institutions increases the citizens' level of confidence in the state and this in turn enhances legitimization of the standards established by this state. Social confidence concerns not only the state but, even more, business partners. A perception of the business partner, his/her integrity and future conduct influences the level of transaction costs. If we represent a market where it is commonly believed that the other party only waits to take unfair advantage of us and make money at our expense then we will have to devote more time and energy to protect ourselves against such opportunistic activities and, therefore, the costs will be higher.

In order to obtain a full picture why a given market operates in this and not the other way, apart from formal regulations, one has to understand informal institutions and the sources of their origin in general, namely the culture of a given nation, its history, moral standards or ideology. Formal institutions cannot be established regardless of the nature of informal institutions in a given area. It is possible to create any number of various legal regulations and enforce them by means of an efficient executive apparatus but the absence of social approval for "ideologically alien" or incomprehensible rules gives rise to objections and formation of informal institutions evading such a law. According to an interaction thesis, formulated by S. Pejovich, mutual interactions between formal and informal institutions have a decisive and favourable influence on the costs of transactions and, consequently, on economic stability and growth⁸. Formal institutions which originate from informal institutions have much bigger chances for social approval, observance and stability. Such a pattern of establishing formal institutions is much more likely to obtain social legitimization of the elites who create institutional order. The analysis of informal institutions in the form of customs and beliefs is therefore of tremendous significance for the construction of an effective system of formal institutions and, simultaneously, for the competitiveness of a country's economy.

The quality of the existing institutional structure is path dependent, so it is influenced by the past: history and culture of a given country, and the present: different interests of the market participants, market complexity, and above all, an ability to research the market shown by the governing elites and those elites' capability to create and enforce adequate institutions. The latter two factors seem to be of key importance for building up an institutional order fostering the future economic growth of a country and its citizens⁹. The more divergent motivations of market participants,

⁷ See also D. North, *Institutions, Ideology and Economic Performance*, CATO Journal, Vol. 11, Issue 3/1992, pp. 477-478.

⁸ S. Pejovich, *The Effects of the Interaction of Formal and Informal Institution on Social Stability and Economic Development*, Journal of Markets and Morality, 1999, No. 2, p. 164 after: J. Godłów-Legiędź, *Transformacja ustrojowa z perspektywy nowej ekonomii instytucjonalnej*, Ekonomista 2/2005, p. 180.

⁹ One can ignore the most clear signals of the market or motivations of its participants and establish institutions protecting only the interests of a narrow group of decision makers.

the more desired are high moral standards of decision makers who should make every effort to satisfy various needs of different social groups. High complexity of the market in terms of number of industries within the economy, positions in their life cycle, their globalization - proneness and interdependencies between them require determining different state involvement in industry development and devising suitable institutional governance programs. Choosing the level of state involvement in the economy is regretfully not only subject to rational decision making but is very often a result of ideological fights and political bargaining. Apart from this, there is still a big discussion between theorists of strategic management and political economy protagonists on what creates competitive advantage of a nation: is this a result of the market and firms' behaviour that constitutes an appropriate branch structures and high value added chains¹⁰ or is this because of the existence of suitable governance structures that coordinate the market in a way that provides appropriate structures of industries and helps to create high value added chains¹¹. The answer is not simple and universal at the national level: it seems whatever model of institutional arrangement we choose it brings certain benefits and costs for various actors, so it should always be a result of a serious analysis and social debate. The institutional arrangements should also be rather industry than nation tailored¹², what then raises a problem of coordination of those arrangements at the national level. The difficulty in building appropriate institutional order grows even more when the country suffers from incompatibility between regulatory and structural spheres as well as from an unfavourable structure of each of them.

Building an institutional order is a costly process and those costs cannot be reduced by using the idea of benchmarking. It is very hard to copy ready made solutions of other countries which might have been done in the case of some structural solutions, because this is "path dependent"; the solutions of today were made on the assumptions of tomorrow and experiences from yesterday. Each country has its own path; it can have goals similar to those in other countries, but it cannot refrain from its past. People brought up in a different environment use different thinking patterns to interpret the reality. These are made of myths, dogmas, ideologies and

¹⁰ For detailed discussion see e.g: M. Porter, *The Competitive Advantage of Nations*, Free Press, New York 1990; J. Barney, E. Zajac, *Competitive Organizational Behavior: Toward an Organizationally Based Theory of Competitive Advantage*, Strategic Management Journal, 15/1994, pp. 5-9.

¹¹ For detailed discussion see e.g.: D. North, *Institutions, International Change and Economic Performance*, Cambridge University Press, Cambridge 1990; C. Oliver, *Sustainable Competitive Advantage: Combining Institutional and Resource Based Views*, Strategic Management Journal, Vol. 18/1997, pp. 697-713; L. Weiss, J. Hobson, *States and Economic Development; A Comparative Historical Analysis*, Polity Press, Cambridge 1995.

¹² See more: A. Griffiths, R. Zammuto, *Institutional Governance Systems and Variations in National Competitive Advantage: An Integrative Framework*, Academy of Management Review, October 2005, Vol. 30 (4), pp. 823-842.

“half- baked theories”¹³, therefore the patterns of their conduct and objectives may be different. Those thinking patterns provide the grounds for informal and formal institutions. Thus it cannot be expected that institutional solutions applied in one country will be fully appropriate for another one.

2. Polish institutional environment: a short description

As has already been mentioned, building up an institutional order is a very difficult task, evolutionary by nature. If it is to be carried out extremely fast, being an element of restructuring of the total political and economic system, one should certainly expect errors, failures and distortions. Creating an effective and market oriented institutional framework is a very difficult task in the country which had for planned economy system and socialist ideology for nearly 50 years.

Poland was the first CEE country to break from the socialist system and the forerunner of economic and political reform. Mazowiecki's non-communist government moved quickly to establish a market economy. This took the form of the Balcerowicz Plan which focused on a stabilisation programme to deal with inflation and regulation of government finances, and the creation of conditions appropriate to the emergence of competitive markets through the privatisation of state assets and attempts to attract FDI. The Polish restructuring programme was focused predominantly on the adoption of an economic, rational model based on neo-classical liberal orthodoxy. Key features of this rational economic model can be summarised as:

- financial restructuring, or the reform of financial institutions to provide effective sources of external finance for investment and a market in which ownership change can take place e.g. privatisation of banks and infrastructure, fiscal reforms, social security reforms,
- structural change – at the macro level – the reform of government administration to remove excessive and unpredictable taxation, uncertain policies, arbitrary bureaucratic intervention and corruption, and at the micro level – the removal of subsidies, tax leniency, soft bank lending along with mass privatisation and the development of mechanisms of corporate governance,
- technological restructuring – to enable the Polish economy to ‘catch up’ with advanced capitalist economies, FDI and foreign trade were and still are seen as important mechanisms for achieving technological restructuring which also has implications for changes in work organisation and styles of management.

Introducing such a shock therapy came along with total ignorance of the fact

¹³ A.T. Denzau, D.C. North, *Shared Mental Models: Ideologies and Institutions*, KYKLOS, 1994, vol. 47, Issue 1, p. 3.

that transformation is a complex social process in which the institutional, socio-technical and behavioural foundations of the society need to be restructured and they definitely will not be equally rapid and radical. The main assumption was that it is enough to introduce the magic of the market and everything else would follow: the society would be re-made on the basis of a free market economy¹⁴. This assumption proved to be wrong: although it is possible to introduce formal institutions within a short time, under a simultaneous restructuring of the whole economic and political system, it is extremely difficult to ensure high quality, durability of the implemented solutions and, which is highly improbable, their coherence with informal institutions.

The Polish formal institutional deal is still in the phase of transformation. This is only partly due to the fact that the scope of changes was multifaceted and multilayered and that Poland joined the European Union and still has to adjust to various EU regulations. Poland gradually improves its image internationally in terms of economic performance and freedom, but still a lot of work has to be done. According to Heritage Institute, the ranking of Poland (Index of Economic Freedom) changed from 3,51 in 1995 to 2,49 in 2006¹⁵, which means that we are now placed in the category of “mostly free countries”. Poland obtained the best score (1) for its monetary stability, but lowered its final result by scoring 3,5 for informal market and 3 for weak property rights protection and blurred regulations¹⁶.

Stability and effectiveness of the Polish institutional deal could be much higher¹⁷ though, and one of the reasons for such a situation is that the governing elites have not worked out and followed a clear political vision concerning the extent and way of the state’s involvement in the economy. This vision was quite clear at the beginning of the 90s but it proved to be too orthodox in some parts: a too restrictive stabilization programme and liberalization of the foreign trade caused the “flood of import”, which resulted in a rapid fall in sales of domestic products, collapse of many state enterprises, sudden and unexpected rise in unemployment and inhibition of domestic investment¹⁸. It had to be modified, but we still cannot decide how we should do

¹⁴ See also comments of H. Radice, *Organising Markets in Central and Eastern Europe: Competition, Governance and the Role of Foreign Capital*, in: *Industrial Transformation in Europe*, E. Dittrich, G. Schmidt, R. Whitley (eds.), Sage, London 1995, p. 107.

¹⁵ The best category is free country (scores from 1 to 1,99), followed by mostly free (2-2,99), mostly unfree (3-3,99) and the worst category is repressed (4-5).

¹⁶ For more see www.heritage.org.

¹⁷ Most of new EU members have better score in this 2006 index: Czech Republic (2.10), Lithuania (2.14), Slovak Republic (2,35), Slovenia (2,31), Hungary (2,34).

¹⁸ For a broad discussion about shock therapy and its results see e.g.: D. Lipton, J. Sachs, *Creating a Market Economy in Eastern Europe: The Case of Poland*, Brookings Papers on Economic Activity 1990, No. 1; J. Winiecki, *Post-Soviet-type Economies in Transition: What Have We Learned from the Polish Transition Programme in its First Year?* *Wirtschaftliches Archivum* 1990, Nr. 4; M. Ellman, E.T. Gaidar, G. Kołodko, *Economic Transition in Eastern Europe*, P.H. Admiral (ed.), Blackwell, Oxford,

it, which results in a conviction that Poland is not governed, but administered¹⁹. The lack of a clear strategy how to govern a country contributes to a creation of a “soft country”²⁰, characterized by a low level of social discipline, ineffectiveness in law execution, overwhelming corruption, and lawlessness of bureaucratic apparatus.

All those symptoms of a “soft country” are visible in Poland, but it cannot be claimed that this is only due to the lack of strategic vision. It is hardly likely that an institutional order will be stable and effective when the direction and rate of transformation differs considerably from the expectations of market participants. It is obvious now that expectations of the effects of a new political and economic order were too high and ideal. The sense of stability and security during radical changes at the macro level is always seriously shaken, but the shock therapy seriously injured public trust in the sense of transformation. In 1989, 93% of Polish citizens believed in better future, this trust diminished in the following years and has not reached this level until today²¹. The paradox in Poland was that the force which seriously helped to introduce free market – economy was trade union “Solidarity”, so it was hard for the workers who had joined this movement to believe that they could be victims of their own success. Idle promises of “another Japan”²² did not say anything about losing jobs and long – term unemployment. The myth about ideal future faded away when confronted with the labour market; many people suddenly realized that their qualifications were no longer satisfactory.

According to A. Giza – Poleszczuk, Poland is now a society of two vectors and two categories of people. On one side, there is a cosmopolitan, modern, well educated, well – off Polish society and at the other end of the vector there is highly marginalized, traditional and rural Poland²³. This dichotomy is confirmed by many

England 1993, s. 1-91; M. Gorynia, *Polska polityka przystosowawcza w latach 1990–1993*, „Gospodarka Narodowa” 1994, nr 2; M. Gorynia, W. Otta, *Polska polityka przystosowawcza w latach 1990–1996*, Ruch Prawniczy, Ekonomiczny i Socjologiczny 1997, nr 3; L. Balcerowicz, *Socjalizm, kapitalizm, transformacja*, Wydawnictwo Naukowe PWN, 1997; D.K. Rosati, *Polska droga do rynku*, PWE, Warszawa 1998.

¹⁹ See: M. Marody, J. Hausner, *Miękki kraj*, *Polityka* 2000, No 50.

²⁰ The expression “soft country” comes from G. Myrdal, *ibidem*.

²¹ The year 1989 was uniquely high, as regards general mental state of the Polish society and the level of social optimism. It dropped considerably in the late 90s. The worst year was 2001: 51% of population feared the future (comparing to 40% in 1989, and 41% in XII.2005), 26% did not believe in any improvement (comparing to only 7% in 1989, and 19% in XII.2005). As it can be observed, results improve gradually, but are far from positive and those for 1989. See: *Samopoczucie Polaków w latach 1988–2005, komunikat z badań*, Warsaw, December 2005, CBOS, www.cbos.pl.

²² Lech Wałęsa, in one of his spontaneous but insufficiently thought out speeches promised that Poland after transformation would resemble Japan; a country that was then considered a symbol of technical world mastership and economic miracle.

²³ A. Giza-Poleszczuk, *Brzydkie kaczątko Europy, czyli Polska po czternastu latach transformacji in: Zmiana czy stagnacja? Społeczeństwo polskie po czternastu latach transformacji*, M. Marody (ed.), Wydawnictwo Naukowe Scholar, Warszawa 2004, p. 265.

sociological surveys: transformation extrapolated the Polish society into those who benefited from this process and those who suffer from it; these are especially older people, from the country or small towns in the eastern part of Poland, living below the line of poverty. Those groups also have a different system of values and behave differently: people who suffer from transformation are more traditionally oriented towards home, family and religion and behave quite passively, whereas the cosmopolitan part are more market-oriented, open to international cooperation, often questioning traditional values and being more active²⁴.

This stratification and a growing number of people dissatisfied with the effects of transformation was reflected in the results of recent parliamentary and presidential elections in Poland, where such populist parties as “Samoobrona (Self-defense)” and Liga Polskich Rodzin (League of Polish Families) gained considerable social approval and now form the government together with PIS (Law and Justice). These results prove definitely that a large part of the society is tired of aggravating non-steerability of the state and a lack of considerable improvement in their living standard. It is very probable that in the slogan “law and justice” they wanted to see a chance of diminishing the scale of corruption in Poland and settling accounts with those who benefited from transformation using legal loopholes and political connections.

Although corruption is an inevitable phenomenon, existing in each country, its increase above some “natural level”²⁵ becomes a clear signal of the dysfunction of the state as a creator of institutions and is a direct obstacle to economic growth. The analysis of correlation between the index of economic freedom and the indices of corruption in highly developed countries provides the grounds for the conclusion that the higher the level of economic freedom the lesser the probability of corruptive practices which are not treated as the source of the problem but rather as a symptom of over-regulation of the economy, absence of the rule of law or the existence of a large state-owned sector. However, the studies on interdependencies between the level of corruption and economic freedom in the countries under systemic transformation conducted by J. Godłów-Legiędź do not reveal such univocal correlation. The author points out that a high level of corruption in these countries may not only be the symptom of absence of economic freedom but also a factor hindering liberalization of the economy and its growth. Although the thesis about a close correlation between economic freedom and the level of corruption seems to be true in the long run, in the short run, under the lack of appropriate informal institutions, including respect for property and adequate market culture, the increased

²⁴ Ibidem, p. 268.

²⁵ It is impossible to univocally define such a natural level of corruption. It is well-known that such an indicator should oscillate around zero (according to methodology accepted by Transparency International it should approach the level of 10).

level of economic freedom may result in the increased level of corruption²⁶. Such a statement explains why in the Polish, free market economy the level of corruption is very high. The latest report of Transparency International shows that corruption in Poland has reached the level of 3.4²⁷. This indicator is the same in such countries as Burkina Faso, Lesotho, Egypt, Croatia or Saudi Arabia. For the sake of comparison the indicator for Estonia is 6.4, for Slovenia - 6.1, Hungary - 5.0, Lithuania - 4.8, the Czech Republic - 4.3, Slovakia - 4.3., Latvia - 4.2. Less corrupted than Poland are e.g. Bulgaria (4.0), Columbia (4.0), Mexico (3.5) or Turkey (3.5).

The most corrupted circles in Poland include politicians, party activists, local self-government members, members of parliament, members of the Senate (64% of responses)²⁸, judges and prosecutors (42 %) and government officials (39%). Such results indicate not only a deep crisis of citizens' confidence in the state²⁹ (which, as has been mentioned above, increases transaction costs), but leads to the conclusion that the shape of formal institutions in a corrupted country favours interests of narrow social groups closely linked with the ruling elites.

Such a state of affairs does not encourage economic entities to make serious investment decisions, although it does not stop economic activities. Luckily for the economy it takes very many extremely insensible formal institutions to entirely hinder its growth³⁰. Such a situation explains a high rate of structural transformation and economic growth of the country under persisting institutional ineffectiveness.

3. Assessment of Poland's institutional environment by MNCs

Studies carried out by CBM INDICATOR in December 2005 at the request of the Polish Agency of Information and Foreign Investment concerned foreign investors'

²⁶ J. Godłów-Legiędź, *Korupcja a wolność gospodarcza w krajach transformacji ustrojowej*, Gospodarka Narodowa 11-12/2004, pp. 35-48.

²⁷ Indicator 10 denotes a country where corruption is virtually at zero level, indicator 0 - a totally corrupted country. According to the report of 01. 02.2006 the least corrupted countries are : Iceland (9.7), Finland (9.6) and the most corrupted are Chad and Bangladesh - indicator 1.7. The whole, latest report (the year 2006) can be found on Transparency International's website.

²⁸ Studies conducted by CBOS in June 2004 "Postrzeżenie korupcji w Polsce - komunikat z badań", www.cbos.pl.

²⁹ Another survey shows however, that trust in public institutions grows; in 2006 61 % of Polish citizens declared that they do not trust: political parties (comparing to 2004, with 72%), parliament (in 2006 - 54%, in 2004 - 67%), courts (in 2006 - 51%, in 2004 - 60%) and government (in 2006 - 40%, in 2004 - 68%). For more results see: *Zaufanie w sferze prywatnej i publicznej a społeczeństwo obywatelskie, komunikat z badań*, CBOS, Warsaw, February 2006, www.cbos.pl.

³⁰ Such were the conclusions of, among others, M. Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation and Social Rigidities*, Yale University Press, New Haven 1982, p. 175.

opinions on the conditions of their activities in Poland³¹. They prove that the main motives for expansion onto the Polish market are of structural nature. The most significant motives to take up economic activity are as follows:

1. size of the Polish market³²,
2. cost of labour³³,
3. prospects of economic growth³⁴,
4. qualifications of workforce,
5. supply of workforce³⁵,
6. opportunity to reduce manufacturing costs³⁶,
7. legal security,
8. low taxes,
9. membership in the EU.

As it is shown by the studies, foreign investors indicate that the most important motives to start activities on the Polish market are of market or cost dimension. Factors of institutional character are also important but they are not the most significant when making a decision to expand onto the Polish market. However, it should be emphasized that the absence of appropriate formal institutions hinders expansion even when the structure of the markets is most attractive. We have to bear in mind that formal regulations effectively discouraged foreign entities from setting-up subsidiaries in socialist Poland. Creating adequate legal and administrative regulations was then a necessary, though absolutely insufficient, condition for the foreign companies to start economic activities; it provided information that the economy is open to the inflow of foreign capital. Such a fact is perceived as an invitation to enter a given host market, however, it is not a motive for expansion in itself. Establishment of formal institutions facilitating foreign entities' operations is an indispensable gate for expansion onto a given market, although it does not guarantee that these regulations will function effectively. Certainly one cannot expect it in a country which is undergoing rapid changes in its entire political and economic macrostructure. However, it is justified to expect the increase of adaptation effec-

³¹ The report was published on the PAIiIZ website: www.paiz.pl.

³² In the years 1993 and 1995 it ranked second as regards significance and in the years 2000 and 2003 as third. See: studies conducted at the request of PAIZ (now PAIiIZ) in the years 1993, 1995, 1997, 2000, 2003 on the same subject (see also the PAIiIZ Internet archives. Comments on the results of the studies can be found e.g. in: W. Karaszewski, *Bezpośrednie inwestycje zagraniczne, Polska na tle świata*, Toruń 2004, pp. 238-248.

³³ For the last five years it has ranked second motive for expansion as regards significance, in the years 1995 and 1997 it was the most important motive, whereas in 1993 it ranked third.

³⁴ In comparison with the years 2000, 2003 it fell from the first to the third position.

³⁵ In the studies for 1993-2000 the 4th indicator in the order of importance; in 2003 – the 5th position.

³⁶ In the studies for 1993-2000 the 5th indicator in the order of importance; in 2003 – the 4th position.

tiveness of formal institutions. Unfortunately, improvement of formal institutions, which consists mainly in the simplification of procedures, their adjustment to international standards and raising the efficiency of enforcement apparatus, is still too slow. W. Karaszewski presents interesting results of his own studies concerning the years 1990-1999. The aim of these studies was to investigate to what extent the expectations of foreign investors in Poland were met as compared with their motives for expansion. It turns out that if the motive for expansion was factors of structural character, both of market and cost nature, all these expectations were fulfilled, although to a different degree³⁷. Worth mentioning is the fact that almost all expectations concerning institutional factors, such as lower tax burden, lower number of administrative obstacles or longer working hours were not fulfilled³⁸.

The assessment of legal regulations concerning activities of foreign capital in Poland was and still is generally negative. According to the quoted studies conducted by CBM INDICATOR, only every third respondent regarded them as appropriate (35% of the responses). However, it should be emphasized that such a percentage of positive responses shows a significant growth in the number of foreign entrepreneurs who are satisfied with the legal solutions in our country as compared with the year 2002 when this number amounted to mere 7.2%. Two facts undoubtedly influenced the increase in the number of positive opinions: an act on economic freedom passed in 2004 (over fifty per cent of the respondents perceive it as a favourable factor for the operation of foreign entities in Poland) and harmonization of the Polish law connected with Poland's entry into the European Union.

It is not surprising that Poland's entry into the EU is generally seen as a positive phenomenon (nearly 73% of the respondents) because it confirms that Poland was able to meet the criteria, both structural and institutional, to become an EU member and that our country decided to pursue a defined path of political-economic development including adjustment of its legislation to the EU norms. Poland's accession to the EU has increased credibility of our country in the eyes of the present and potential foreign investors and trade partners and caused simplification of supply and purchase procedures inside the Community (liquidation of customs barriers).

Despite the fact that satisfaction with the state of legal regulations is growing, the studies indicate many areas which need improvement. There still exist significant obstacles to the economic activity of foreign entities, such as:

- difficulties with starting activities due to necessity of preparing documents and observance of complicated registration procedures (51% of the respondents),

³⁷ Complete fulfillment of expectations was marked as (+1) and total non-fulfillment of expectations as (-1). The results of studies are as follows: lower labour costs (+0.58), creating new markets (+0.47), certainty of retaining the existing markets (+0.37), lower prices of raw materials and semi-finished products, power (0.09). For more on this subject see: W. Karaszewski, *op.cit.*, pp. 240-241.

³⁸ Lower tax burden (-0.18), elimination of administrative barriers (-0.24), longer working hours (-0.03), smaller barriers to imports (-0.14). *Ibidem*, p. 241.

- bureaucracy (45.9% of the respondents),
- frequent changes in regulations (44.6%),
- contents of regulations in force (assessed negatively by 42.1% of the respondents),
- long period of waiting for administrative decisions (40.1%)³⁹.

All these shortcomings prove that formal institutional solutions are dysfunctional.

4. The behaviour of MNCs in Poland – preliminary studies

Multinational corporations are institutional hybrids: they create new, international institutional frameworks of the environment in which they operate and possess the elements of many institutional environments in their structure and strategy. Efforts to maintain coherent structure and strategy on the world scale often result in imposition of organizational solutions by headquarters on their subsidiaries and divisions (coercive isomorphism). The headquarters' tendency to standardize organizational solutions is caused by the willingness to use competitive advantages achieved on the home market and by the willingness to work out a homogenous identity of the entity. In their attempts to standardize the conditions of operating on the international scale, MNCs also exert pressure on the governments of host countries so that they create adequate and worldwide formal institutions. MNCs are also influential members of non-government organizations which, in turn, are responsible for generating and spreading isomorphic behaviour of normative character.

On the other hand a multinational corporation, like any other economic entity, tries hard to be perceived as friendly by the environment where it operates, which results in de-institutionalisation of its internal structure and strategy⁴⁰. Propensity to environmental legitimization is caused by a typically economic calculation: an entity which understands and complies with the rules of the game functions more effectively in a given environment. When a given market differs institutionally from those where a multinational corporation has been operating so far, it is necessary to grant its branches some autonomy indispensable to work out and implement strategies and structures which differ from the general pattern but are appropriate for the local markets. With this autonomy subsidiaries are more flexible in their activities on the local market but headquarters lose some of its control and power. This loss of control and rise of the subsidiaries' autonomy is even greater when the host

³⁹ The results from previously quoted INDICATOR studies, December 2005.

⁴⁰ D. E. Westney, *Institutional Theory and Multinational Corporation, w: Organization Theory and the Multinational Corporation*, S. Ghoshal, D.E. Westney (eds.), Palgrave Macmillan, New York 2005, pp. 51.

market is considered as strategically important in terms of its structural and institutional traits; market size, high potential rise in demand, favourable law regulations, cheap resources etc.

Ensuring effectiveness of the functioning of a multinational enterprise as a whole under the situation when the links with its subsidiaries operating on institutionally “exotic” markets are loosened, can be carried out in two ways: by strengthening co-ordination and integration⁴¹ links and by creating in the minds of managers the so-called “matrix thinking”⁴² which takes into account and tries to meet the interests of the corporation as a whole, with a simultaneous necessary adjustment of their operations to the requirements of the local environment. As a cost of abandoning standardization and a potential risk of losing control, the extent of autonomy will be directly proportional to structural attractiveness of the host market. A structurally attractive host market is the one which contributes significantly to the growth of the value of a multinational as a whole, e.g. by large and constantly increasing demand or low costs of manufacturing.

Analysis of MNCs opinions about Polish institutional environment shows that this market is perceived as structurally attractive, but requires certain local knowledge of how to overcome bureaucratic obstacles and deal with ubiquity of corruption. This suggests that Poland should be treated as institutionally different from the analogous environment in host countries of MNCs (especially those from the USA or Western Europe), which could then lead to differences in the strategy and structure of the Polish subsidiaries in comparison with analogous companies in other host countries.

Studies conducted by the author in the manufacturing subsidiaries of 20 multinationals operating in Poland⁴³ indicate that multinational corporations observe

⁴¹ Coordinating/integrating instruments may be divided into four groups: socialization, formalization, centralization and communication mechanisms which, apart from coordinating and integrating function, play a supporting role for the instruments from the remaining three groups. For more see: K. Kim, J.H. Park, *Integrating Distinctive Manufacturing Competence Globally: Its Effect on Business Performance*, *Multinational Business Review*, Spring 2000, vol. 8 (1), pp. 87–98; J.I. Martinez, J.C. Jarillo, *The Evolution of Research on Coordination Mechanisms in Multinational Corporations*, *Journal of International Business Studies* 1989, 20 (3), pp. 489–514; B. Stępień, M. Sulimowska-Formowicz, *Konkurencyjność przedsiębiorstw międzynarodowych – poszukiwanie źródeł przewagi*, w: *Perspektywy i kierunki rozwoju*, J. Schroeder (ed.), The Poznań University of Economics Publishing House, Poznań 2006, pp. 19–40.

⁴² C.A. Bartlett, S. Goshall, *Matrix Management: Not a Structure, a Frame of Mind*, *Harvard Business Review* 1990, vol. 68:4, pp. 138–145; C.A. Bartlett, S. Goshall, *Managing Across Borders: Transnational Solution*, Harvard Business School Press, Boston 1998, p. 176.

⁴³ The research included 20 manufacturing subsidiaries of multinational corporations of the world (80%), or European (20%) range of activity. Each of those enterprises has been operating on the Polish market for over 5 years and most of them appeared in Poland due to the buyout of the local enterprise. Industrial sectors represented by the studied corporations are as follows: processing of plastics, manufacturing of packaging, building materials, gaskets, window frames, etc, manufacturing of machinery,

some institutional difference of the Polish market, which is proved by a generally higher autonomy of the Polish subsidiaries than that indicated by the policy of the corporations they are part of (see Table 1).

A bigger than standard range of autonomy granted to the Polish subsidiaries may result from the fact that the main or regional headquarters of the concerns perceive the Polish market as unknown and thus most probably different from the ones where they have been operating⁴⁴. As it has been mentioned above, effective activity on such a market requires loosening of the ties between the headquarters and a subsidiary operating on this market. Loosening of these ties and granting wider autonomy to the Polish market is observed in trading and marketing activities as well as in the current financial policy. As much as 44% of the Polish subsidiaries indicated that they enjoyed full freedom of decisions in creating promotional activities and 38% conduct these activities on the basis of partner negotiations and arrangements with the main or regional headquarters⁴⁵. Subsidiaries enjoy similar freedom e.g. in defining target groups of customers: nearly half of the studied entities have the so-called free hand in this respect (47% of the responses) and 24% pursue their trade policy in partnership agreement with the headquarters. The freedom of trade activity is also proved by the possibility of making decisions as regards tailoring the products to the local conditions (35% of the subsidiaries enjoy full freedom of decision making and another 35% make their decisions after partnership negotiations with the headquarters). The results are totally different if we analyse the range of subsidiary's autonomy as regards marketing and trade activities within the whole concern (See Table 1). These considerable discrepancies between the levels of autonomy can be explained by the fact that the Polish market is still treated as new, unknown but attractive and growing (See Table 2) therefore it seems reasonable to believe that the local managers know the market better than expatriates from the headquarters and to allow them to gain a bigger and bigger share of this market. However, these results should be treated with caution and they represent the respondents' opinions rather than the real standard. What is very important here, answers concerning similarities and differences between operations of a Polish subsidiary and the so-

equipment, technical and electronic parts and components, manufacturing of cosmetics, foodstuffs, stationery and home furnishings. The results of studies presented in this article show how much organizational solutions applied in the Polish subsidiaries are similar to those applied in other units of the corporations and what are the possible reasons for such a situation. It should be underlined however that the research in question is still in progress, therefore the results presented in this paper should be regarded as preliminary, concerning only the initial group of 20 enterprises and the conclusions formulated here require further verification. Data presented in Tables 1,2, and 3 come from 20 enterprises but not each question in the questionnaires was filled by all enterprises, that is why the results in % do not show multiples of 5%.

⁴⁴ The term "perception" is used deliberately here because perception of phenomena may not have too much in common with reality.

⁴⁵ None of the Polish subsidiaries is the regional headquarters.

called standard in the whole MNC were based mainly on the respondents' experiences in foreign sister companies operating either in Western Europe or in North America. Majority of respondents did not have substantial knowledge about the nature of operational strategies in the subsidiaries based in the Far East Asia, Africa or South America, so the basis for comparison was not really the whole MNC, but only European and North American part of its domain.

The results in Table 2 show fairly big significance of the Polish subsidiaries in the structures of the concern, which additionally strengthens this quite big level of autonomy. This significance, however, has nothing to do with institutional distance, but is a mixture of structural attitudes of the Polish market (such as size, location, cheap workforce etc.) and effectiveness of local workforce. Table 2 shows that the studied subsidiaries well deserve trust of their headquarters thanks to the fact that their effectiveness is higher than in similar subsidiaries and their sales results are higher than the targets set by the concerns. A high level of autonomy and significance can also be correlated with geographical location of the Polish subsidiaries. For many of the studied multinationals the Polish subsidiaries are a bridgehead for further expansion to the Eastern markets which are perceived as even more different and "exotic" than the Polish market. Due to geographical proximity and similar experience of the last few decades, it is assumed that the Polish managers will quickly adjust to the realities of these markets and in order to act effectively they need a lot of freedom. Neither are the current financial activities controlled by headquarters to such an extent as indicated by the standards of the concerns. The respondents justify this situation with the so-called specificity of the Polish market correlated with a high level of trust bestowed on the Polish subsidiaries. The current levels of working capital result to a large extent from the relations established with customers and suppliers and these in turn are, at least partly, a result of the local, commonly believed as binding, periods of mercantile credits granted. A higher than the standard one level of autonomy as regards financial activities may also result from the complexity of the Polish tax law and the act on accountancy which are not only complicated and thus unclear but change frequently, therefore it is hard to control them thoroughly. On the other hand, however, adjustment of the Polish regulations to international standards is frequently carried out through forcing the Polish subsidiaries to apply the so-called double accountancy, but this sphere does not relate so much to the freedom of conducting current financial activities as to corporate standardization of various organizational practices.

Table 3 shows the degree of work standardization in the Polish subsidiaries in comparison with analogous companies within MNCs. As it can be seen from the Table, the most standardized practices include quality systems (93% of subsidiaries in the sample), controlling procedures (nearly 70%) and financial planning (about 60%). Polish managers and workers conform to those standardized regulations because they find them effective. Polish employees in subsidiaries of multinational

enterprises generally regard those companies as more professional and more effectively managed than their local counterparts⁴⁶. Thus they are willing to follow organizational solutions implemented in those organizations, which is a symptom of both normative and cognitive isomorphism shown by the Polish staff.

Apart from rational reasoning, there may be other reasons for this high acceptance and duplicating organizational solutions worked out and applied in a multinational corporation. One of these reasons is undoubtedly a high level of unemployment in Poland. The necessity to satisfy basic needs effectively weakens the willingness to manifest the lack of acceptance for different organizational and cultural standards because such an attitude could lead to job losses. The results show that employees of the studied enterprises are sometimes afraid to openly question the sense of some organizational practices enforced by headquarters because it may lead to job losses. Another reason for such conformity can be low safeguarding distance of the Polish people. The safeguarding distance is a historically shaped defined system of behaviours which prevents identity and culture from being undermined or damaged. Each society creates such a distance: own patterns and processes of cultural adjustment and protective barriers against changes. The bigger the safeguarding distance, the greater is cultural identity and lesser proneness to changes. According to W. Head, a big safeguarding distance is caused by, among others: clearly defined moral standards of a society, where violation of these standards is condemned, high self-discipline, formalization of class relations and social roles or high esteem for formal institutions in the form of widely understood law⁴⁷. As it was shown above, moral standards of the Polish society are shaken by ubiquity of corruption and cultural dichotomy of the nation, social classes and roles are still being shaped and considerable distrust in government, jurisdiction system and parliament indicates that respect for formal institutions is low. Poles' new identity is not defined yet and therefore it is difficult to manifest it clearly. From the viewpoint of multinational enterprises it is a positive phenomenon because it makes the market more attractive and diminishes the cost of adapting their strategy and structure. The absence of clear cultural barriers, however, can raise some concern about the future shape of our country's identity and culture, but this is not a subject of this article.

High conformity of the Polish workers to rules established by MNCs headquarters does not mean however, that all organizational practices are standardized in the Polish subsidiaries. Some of them, like documentation flow or internal, non-production work procedures show no considerable pattern of organization: some subsidiaries have their own local regulations while others have those areas highly standardized. The reason for such dispersed results may lie in a mode of entry, pe-

⁴⁶ This is also confirmed by other studies; see e.g. D. Stuglik, *Wpływ bezpośrednich inwestycji zagranicznych na zmiany strukturalne w przedsiębiorstwie*, Raport z badań, *Gospodarka Narodowa* Vol. 5/6, 2002.

⁴⁷ W. Head, *Adaptive Sociology*, *The British Journal of Sociology* 1961, March.

riod of operation on the Polish market and restructuring philosophy of a particular MNC. Brownfield investments involve taking over the company with its own management system which is often quite different from the one that is required. Changes of this system are time consuming, so older subsidiaries could report a higher level of standardization in this area than the younger ones, but this is only an assumption that should be further investigated. It is also noteworthy that those areas can be differently perceived by MNCs headquarters: if standardization of documentation flow or some non – production work procedures were crucial to effective coordination and management, then subsidiaries could expect bigger pressures from headquarters on regulating this area according to MNC’ s standards. The results could indicate then that universal regulation of those areas within the whole MNC is not always considered as important.

Table 3 also shows that organization of distribution network is left to local managers (27%), however with the need to follow general rules of a corporation (40%). Explanation for such a situation is similar to this given above when the level of autonomy was discussed. The Polish subsidiaries are also quite different from their sister companies when it goes about organization of HRM area. Salaries, motivational system and training are adjusted to local needs, regulations and payment levels and reflect MNCs’ standards only in terms of general rules. The grounds for such organization are fairly obvious: one of the reasons MNCs based their subsidiaries in Poland was cheap labour force and there is no reason not to benefit from this.

Table 1. Differences in the range of autonomy between standard organization of a concern and activity of the Polish manufacturing subsidiaries

Type of activity	Standard of a concern		Polish subsidiary	
	No / slight autonomy of subsidiary	Considerable/ total autonomy of subsidiary	No /slight autonomy	Considerable/ total autonomy
Freedom of conducting marketing activity	65%	35%	18%	82%
Freedom of conducting trading activity	69%	31%	29%	71%
Current financial policy	56%	42%	44%	56%
Human resources management		100%	20%	80%
Supplying activity	60%	40%	59%	41%

Source: Author’s own calculations.

Table 2. Significance of Polish subsidiaries for the analyzed MNCs

	Slight	Average	Great
Significance as regards current volume of sales	6%	41%	53%
Significance as regards future volume of sales	6%	23%	71%
Significance due to geographical location	6%	19%	75%
Significance due to characteristics of local staff (e.g. cheap labour, structural unemployment, etc.)	0	44%	56%
Significance due to accessible raw materials	63%	31%	6%
Significance as regards production potential, subsidiary's resources	19%	37%	44%
Significance due to unique achievements of subsidiary (efficiency, productivity, creativity, fast response to market needs, etc.)	12%	19%	79%
Significance due to competitive position on the Polish market (e.g. biggest share, highest growth in market share, etc.)	6%	37%	56%

Source: Author's own calculations.

Table 3. Degree of work standardization in Polish subsidiaries in comparison with analogous companies within MNCs

Obszar	The same system in all subsidiaries	System differs only in some minor details	System is different in subsidiaries but the main rules are the same	Totally different system
Frequency and content of financial and production plans	43,5%	19%	37,5%	
The content and frequency of plans' control, frequency of reports procurement	44%	25%	31%	
Documentation flow	37,5%	19%	31%	12,5%
The content of training plans and way of training	13%	20%	47%	20%
Quality system	36%	57%	7%	
Distribution system in a local market	13%	20%	40%	27%
Internal work procedures	8%	38%	54%	
Wages, salaries at the same work position			57%	43%
Additional bonuses for workers (e.g. additional insurance, company cars, fitness club membership etc)		7%	57%	36%

Source: Author's own calculations.

5. Conclusions

Each country needs to carefully examine its institutional environment in order to improve its functioning: to raise the quality of life of its citizens and competitiveness of the economy. Studies should include both formal and informal institutions because only their harmonized activities contribute to the creation of effective institutions and higher level of social confidence. They are of particular importance for the countries which carried out radical transformations in all the spheres of their macrostructure. A profound and comprehensive analysis of institutional environment should be a starting point for the improvement of the regulatory sphere of the Polish economy. Although the formal institutional framework, securing freedom of economic performance is already established in Poland, this framework needs mastering and clarifying. Radical improvement of the executive, administrative and judicial apparatus seems to be a priority as it will certainly reduce a pathogenic phenomenon of corruption and will help to regain social trust in the state. Better efficiency of the executive apparatus leads to reducing opportunistic behaviour and such a tendency facilitates gradual simplification of legal and administrative regulations. Transparency and clarity of legal regulations also lead to reduction of transaction costs and better effectiveness of economic activities on such a market.

All those distortions in the institutional framework are well noticeable for MNCs. They emphasize the structural attitudes of the Polish market but notice serious shortcomings of the institutional sphere which improves gradually, but too slowly than expected. It is interesting that although the Polish formal institutions are assessed by multinational entities as still unsatisfactory and improving too slowly, the layer of the so-called institutional distance is not a serious barrier to expansion nor does it hinder their future functioning on the Polish market. In order to function smoothly in the environment where rules of economic game are somewhat blurred by corruption, incomprehensible laws, and hyped bureaucracy, MNCs grant the Polish subsidiaries greater autonomy than to their sister companies. The Polish workforce, perceived as flexible and well educated, seems to equalize institutional obstacles not only outside companies but also inside them, by modifying and adjusting organizational practices to the local needs, where it is justified (such as creating and managing local distribution systems, adjusting internal work procedures or training programmes) and conforming to other standardized procedures such as quality systems controlling procedures and financial planning. Features of the institutional deal make this market somewhat exotic and therefore greater autonomy and a certain level of adjustment is needed, but informal institutions and local culture do not seem to disturb MNCs to operate in a standardized and highly effective way in such crucial areas as production, controlling and finance. It is also worth mentioning that all respondents from the questioned subsidiaries want to have an even greater level of standardization at least in two areas: salaries levels and bonuses programmes but they are aware that is highly improbable in the near future.

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