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The double-edged sword effect of political ties on performance in emerging markets: The mediation of innovation capability and legitimacy

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Abstract

To improve our understanding of the bright side and the dark side of political ties and determine the processes linking political ties to firm performance in emerging markets, we investigate the underlying mechanism of political ties' effects from the perspective of dynamic capability theory and institutional theory. We posit that reduced market-focused innovation capability and strengthened legitimacy mediate the effect of political ties on firm performance. In addition, to capture the nature of the relationship between political ties and performance, we adopt a contingency perspective in our examination of the moderating roles of legal enforceability and competitive intensity. Specifically, we suggest that legal enforceability buffers the negative impact of political ties on market-focused innovation capability but mitigates the positive impact of political ties on firm legitimacy. Moreover, competitive intensity enhances the positive impact of market-focused innovation capability and firm legitimacy on firm performance. We test our hypotheses using a survey with 362 respondents in China. In conclusion, our findings provide important insights into how Chinese firms effectively utilize political ties to improve their performance.

Keywords Political ties · Performance · Market-focused innovation capability · Legitimacy · Double-edged sword effect

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Building political ties is a prevalent marketing strategy in emerging markets (Heirati & O'Cass, 2016; Ismail Jr et al., 2013; Zhou et al., 2014). Many scholars have examined the use and results of this strategy by testing the impact of political ties on firm performance, and they have reached a consensus that political ties constitute a double-edged sword with respect to firm performance. That is, political ties have the potential to improve performance (Peng & Luo, 2000; Peng & Zhou, 2005; Zhou et al., 2014) but also run the risk of eroding performance (Chen & Wu, 2011; Hadani & Schuler, 2013; Li & Sheng, 2011; Li, Zhou, & Shao, 2009). To provide insights to help firms exploit political ties, scholars have further examined the boundary conditions of the impacts of political ties on firm performance. For example, Sheng, Zhou, and Li (2011) found that political ties lead to greater performance when government support is weak and technological turbulence is low, and Zhang, Tan, and Wong (2015) indicated that the effect of political ties on firm performance is contingent upon firms' choice of innovation activities to pursue.

Understanding how political ties are connected to performance can also help firms effectively use these ties. With such an understanding, firms may use political ties more effectively by keeping a watchful eye on the mediators of the political ties-performance nexus. However, based on a comprehensive literature review (see Table 1), we find that research on the underlying mechanism of the link between political ties and performance is still nascent. Specifically, from the perspective of dynamic capability theory and transaction costs economics, research indicates that political ties facilitate performance by improving firms' adaptive capability and reducing transaction costs (Gu, Hung, & Tse, 2008; Lu et al., 2010; Zhu, Su, & Shou, 2017), but there is no research (with the exception of Guo, Xu, & Jacobs, 2014) integrating institutional theory to test the mediating effect of legitimacy on the political ties-performance nexus. More importantly, most studies have focused on the mediators of the positive impact of political ties on performance but neglected the mediators that can explain why political ties erode firm performance.

To fill these research gaps, we investigate the underlying mechanism of both sides of the effect of political ties by integrating dynamic capability theory and institutional theory. Specifically, we simultaneously examine the mediating effects of market-focused innovation capability and legitimacy on the impacts of political ties on performance. We posit that on the one hand, political ties facilitate a firm's legitimacy, which in turn increases its performance; on the other hand, political ties inhibit a firm's market-focused innovation capability and erode its performance.

To fully map the dual effects of political ties, we also consider the moderating mediation of institutional and market factors. In particular, we posit that legal enforceability, which refers to the perceived legal protection of a company's financial interests in a business transaction (Cai, Jun, & Yang, 2010; Luo, 2007; Zhou & Poppo, 2010; Zhu, Su, & Shou, 2017), buffers the negative effect of political ties on innovation capability but mitigates the positive effect of political ties on legitimacy. In addition, competitive intensity enhances the positive impacts of market-focused innovation capability and firm legitimacy on firm performance. Figure 1 shows the conceptual model. Based on a survey completed by 362 respondents in China, most of our hypotheses are supported.

Table 1 Empirical research on the political ties-performance nexus: a brief summary

Representative Publications	Underlying Mechanism	Major Findings
Hillman, Zardkoohi, and Bierman (1999)	N/A	When a link is established between a firm and the government through personal service, firm performance will be positively affected.
Peng and Luo (2000)	N/A	The positive relationship between political ties and performance differs among firms with different (1) ownership types, (2) business sectors, (3) sizes, and (4) industry growth rates.
Peng and Zhou (2005)	N/A	The positive relationship between political ties and performance tends to weaken over time.
Fan, Wong, and Zhang (2007)	N/A	Firms with politically connected CEOs underperform those without politically connected CEOs by almost 18% based on three-year post-IPO stock returns and have poorer three-year post-IPO earnings growth, sales growth, and change in returns on sales.
Boubakri, Cosset, and Saffar (2008)	N/A	They find that politically connected privatized firms underperform their non-connected counterparts by examining the impact of the political connections of board directors on the accounting performance of newly privatized firms.
Gu, Hung, and Tse (2008)	Channel and responsive capability	Guanxi can enhance market performance through strengthening channel capability and responsive capability.
Li, Zhou, and Shao (2009)	N/A	Political ties impede the positive effect of a differentiation position on foreign firms' profitability. Moreover, foreign firms' profitability suffers when they increasingly rely on the heavy use of political ties.
Lu et al. (2010)	Information acquisition and adaptive capability	The study combined the RBV with the capability-building perspective of rent creation and found positive mediating effects of information acquisition capability and adaptive capability on the impacts of managerial ties on performance.
Li and Zhou (2010)	Resource acquisition capability	Managerial ties improve performance through an institutional advantage (i.e., superiority in securing scarce resources and institutional support).
Chung (2011)	N/A	The interaction between market orientation and political guanxi is proposed to be negatively associated with financial and strategic performance.
Sheng, Zhou, and Li (2011)	N/A	Political ties lead to greater performance when general government support is weak and technological turbulence is low.

Table 1 (continued)

Representative Publications	Underlying Mechanism	Major Findings
Li and Sheng (2011)	N/A	Ties with government officials are more salient with regard to enhancing performance for more entrepreneurially oriented and younger firms. In addition, these ties fail to provide performance benefits to firms when high demand uncertainty exists or when the level of technological turbulence is high.
Wang et al. (2013)	Resource acquisition capability	The study argued that the role of external resource acquisition is a salient mediating mechanism through which political ties influence firm performance.
Hadani and Schuler (2013)	N/A	Firms' political investments are negatively associated with market performance, and cumulative political investments worsen both market and accounting performance.
Zhou et al. (2014)	N/A	The positive role of ties with the government (i.e., political ties) declines over time; technology capability positively interacts with political ties in fostering performance.
Guo, Xu, and Jacobs (2014)	Policy support & opportunity recognition	These findings uncover two fundamental mediating mechanisms that can translate political ties into firm performance: institutional support and institutional entrepreneurial opportunity recognition.
Zheng, Singh, and Mitchell (2015)	N/A	Local political ties buffer firms from threats to their survival, particularly for firms with weaker prior performance, and enable sales growth but only for stronger performing firms; central political ties do not provide buffering or enabling benefits.
Zhang, Tan, and Wong (2015)	N/A	The positive effect of political ties on performance is enhanced when firms pursue a higher level of exploratory innovation. In contrast, a higher level of time investment in political ties could be wasteful and even harmful when firms pursue a higher level of exploitative innovation.
Zhu, Su, and Shou (2017)	Marketing capability & partners' opportunism	The study integrated dynamic capabilities and relational governance theories to indicate that increased firm adaptive capability and reduced opportunism mediate the contribution of positive ties to firm performance.
Yan and Chang (2018)	N/A	While a firm's political connections to a focal government with decision-making authority enhance performance, connections to a rival government competing with the focal government harm performance, particularly when the rivalry is intense. Firms can neutralize the negative effect from this political rivalry by using direct or indirect connections to a constraining government with power over the focal government.

Conceptual framework

Political ties refer to the extent to which managers cultivate interpersonal relations with government officials at various levels of administration and regulatory organizations, such as tax bureaus and commercial administration bureaus (Peng & Luo, 2000; Sheng, Zhou, & Li, 2011). In emerging economies such as China, underdeveloped legal frameworks and pervasive institutional transitions necessitate a strategy centered on developing political ties (Guo, Xu, & Jacobs, 2014; Ismail Jr et al., 2013; Li, Zhou, & Shao, 2009; Peng & Luo, 2000). However, in previous empirical works, the reported effects of political ties on firm performance are contradictory (Li, Poppo, & Zhou, 2008; Wang et al., 2013). To reconcile the mixed results, some researchers have suggested that the value of political ties may be contingent on important contextual factors (Wang et al., 2013; Wu & Chen, 2012; Zhou et al., 2014). For example, Li, Poppo, and Zhou (2008) found that political ties increase domestic firms' performance but decrease the profitability of foreign firms in China. Peng and Luo (2000) pointed out that the impact of political ties on firm performance is stronger for firms in low-growth industries than for firms in high-growth industries. Sheng, Zhou, and Li (2011) suggested that government support negatively moderates the relationship between political ties and firm performance.

However, new advances in research on political ties suggest that political ties are not very likely to convert directly into performance. Converting mechanisms for explaining how managerial ties are materialized into performance have attracted increasing attention (Guo, Xu, & Jacobs, 2014; Wang et al., 2013; Zhu, Su, & Shou, 2017). For example, recently examined mediators include firm capabilities (Gu, Hung, & Tse, 2008; Lu et al., 2010; Zhu, Su, & Shou, 2017), resource acquisition (Wang et al., 2013), and institutional advantage (Li & Zhou, 2010). These reports enrich our understanding of the underlying mechanisms of the relationship between political ties and performance but merely focus on the bright side of political ties. In fact, an increasing number of studies have pointed out that political ties are not always beneficial to firm performance (Gu, Hung, & Tse, 2008; Li, Poppo, & Zhou, 2008). For instance, some studies have indicated negative effects of political ties on innovation capability (Wu, 2011; Yu et al., 2016), but the mediating effect of innovation capability on the relationship

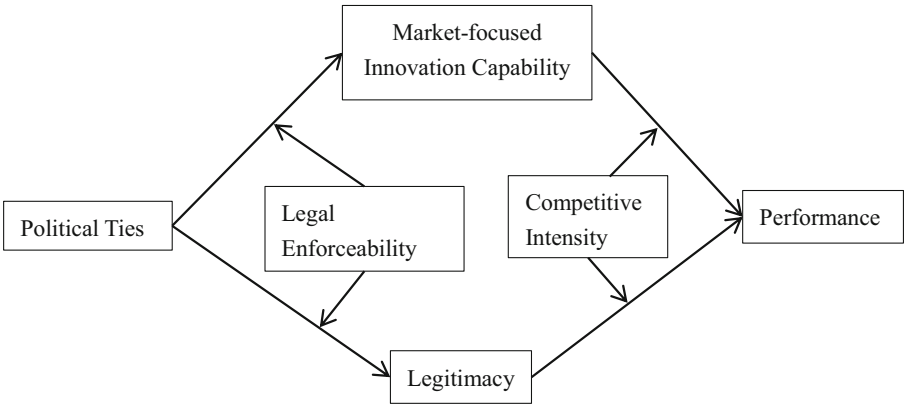

Fig. 1 Conceptual model

between political ties and performance has seldom been examined in the extant literature.

Further, using institutional theory, scholars have provided insights into how political ties work to improve performance from the perspective of legitimacy (Guo, Xu, & Jacobs, 2014; Peng & Luo, 2000; Sheng, Zhou, & Li, 2011; Zhu, Su, & Shou, 2017). However, scant research examines the mediating effect of legitimacy on the political ties-performance nexus. Thus, to fill these gaps in the literature, we integrate dynamic capability theory and institutional theory to discuss the dual effect of political ties on performance.

The mediating effects of market-focused innovation capability

Innovation capability refers to a firm's ability to integrate key capabilities and resources to successfully stimulate innovation, and it is a key driver of sustainable competitive advantage (Zhou, Gao, & Zhao, 2017). Innovation capability enables firms to cope with environmental changes and improve their performance during different phases of the business cycle, especially in today's fast-changing environment (Jiménez-Jiménez & Sanz-Valle, 2011; Zhou, Gao, & Zhao, 2017). The innovation literature finds that innovation capability occurs in innovation processes, which include technique-focused innovation capability and market-focused innovation capability (Damanpour, Walker, & Avellaneda, 2009; Foroudi et al., 2016).

Market-focused innovation capability refers to the competence to apply collective knowledge, skills, and resources to innovation activities to adapt to changes in customer demand and create added value for customers (Hogan et al., 2011). Firms with higher market-focused innovation capability can more easily address the changing demands of their clients and are better able to exploit new market opportunities (Jansen, Bosch, & Volberda, 2006; Sorensen & Stuart, 2000). Consequently, market-focused innovation capability can help a firm attain superior performance by obtaining a greater market share and/or customer loyalty (Hogan et al., 2011; Ngo & O'Cass, 2013).

However, market-focused innovation capability may be negatively affected by political ties. First, firms benefiting from political ties are likely to lack incentives to develop market-focused innovation capability due to the path-dependence effect. For these firms, previous benefits from political ties enhance managers' confidence in their political ties and encourage them to reinvest in building and maintaining their relationships with government officials rather than adapting to customers' changing demand (Chen & Wu, 2011; Wu, 2011). A historical path usually also fosters a vested interest group that may include key firm managers (Greve & Seidel, 2015). They may block the transformation of their profit model from political ties to market demand because it may challenge the perceived benefits.

Second, firms relying on political ties are likely not to have an appropriate culture to foster market-focused innovation capability. Market orientation refers to an organizational culture facilitating market-focused innovation capability (Zhou, Yim, & Tse, 2005). A firm with market orientation can obtain the necessary intelligence from its target customers and competitors (which in turn leads to a better understanding of customer preference changes and competitor strategic moves) and thus foster its market-focused innovation capability (Laforet, 2008). However, firms relying on

political ties prefer to accommodate or yield to the government's goals. An orientation towards the government instead of towards the market impedes a firm's efficiency in responding to market change and in turn suppresses the firm's market-focused innovation capability.

Third, firms relying on political ties are likely to lack the necessary resources to develop market-focused innovation capability. Building and maintaining political ties likely consumes a firm's internal resources. For example, a firm may spend time and financial resources to engage in fulfilling politically oriented goals (e.g., increasing employment levels) (Li, Zhou, & Shao, 2009; Sheng, Zhou, & Li, 2011). Even worse, firms must offer money or other forms of compensation to obtain key resources and favorable treatment from their government (Li, Zhou, & Shao, 2009; Wu, 2011). Thus, in a limited resource setting, efforts devoted to developing political ties compete with time and resources devoted to tracking market demand (Zhang, Tan, & Wong, 2015) and in turn impede the improvement of market-focused innovation capability.

We therefore propose that political ties have a negative effect on firm performance by eroding market-focused innovation capability.

H1 Market-focused innovation capability has a negative mediating effect on the link between political ties and firm performance.

The mediating effects of legitimacy

Legitimacy is "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995). There are two elements of legitimacy that can influence the beholders' support for a firm, namely, pragmatic legitimacy and moral legitimacy (Handelman & Arnold, 1999). Pragmatic legitimacy rests on the self-interested calculations of a firm's direct stakeholders (Suchman, 1995), such as customers, suppliers, distributors, and shareholders. As long as firm stakeholders perceive that the firm's actions increase their own welfare, the firm obtains pragmatic legitimacy (Handelman & Arnold, 1999). In return, a firm with pragmatic legitimacy has a greater market share and revenue because of customer satisfaction and identification, and it also has fewer financial, production and transaction costs since it obtains its partners' trust and cooperation (Suchman, 1995; Wu, 2011).

Moral legitimacy refers to beholders' positive normative evaluation of a firm based on the firm's actions taken to increase the welfare of the community and society (Suchman, 1995), such as donations, environmental protection, and poverty relief. Unlike pragmatic legitimacy, moral legitimacy rests on a judgment derived from altruistic motivation, so a firm with moral legitimacy can obtain more word-of-mouth references and suffer fewer boycotts in the case of a critical incident. In general, legitimacy can improve firm performance by increasing revenue, cutting costs, and avoiding risk.

In terms of the type of beholder, Dacin, Oliver, and Roy (2007) distinguish legitimacy into four dimensions: relational legitimacy, social legitimacy, market legitimacy and investment legitimacy. "Firms that are perceived as attractive and capable partners accrue relational legitimacy" (Dacin, Oliver, & Roy, 2007). This means that a

firm with higher relational legitimacy is regarded as a high-quality partner by other firms. Thus, relational legitimacy may improve firm performance by reducing transaction costs with other firms. Social legitimacy is linked to corporate social responsibility. Firms with social legitimacy are expected to conform to societal rules, such as providing quality-assured and safe products and employing resource-conserving and environmentally friendly strategies. Therefore, firms with social legitimacy may perform well because of their high moral legitimacy. Market legitimacy can be established through acquiring rights or qualifications to operate in a specific market and by ensuring endorsement and receptiveness from the government, customers, or suppliers (Dacin, Oliver, & Roy, 2007). This implies that a firm with market legitimacy should have legitimate operation licenses and a wealth of business experience in a specific market. A firm with higher market legitimacy is likely to enter more markets or to have the ability to obtain more orders, which results in higher performance. Investment legitimacy refers to "the worthiness of a firm's business activities and strategic decision in the eyes of corporate investors, such as the parent firms' board of directors, executives, venture capitalists and shareholders" (Dacin, Oliver, & Roy, 2007, P177, 3rd paragraph). With more confidence in a firm and its business activities, investors are more likely to reinvest in working capital and/or fixed assets; meanwhile, the recognition of strategic decisions by the board of directors and executives reduces firm decision costs. Lower financial costs and decision costs are both important factors for firm performance.

A firm can acquire legitimacy by networking with the government (Li et al., 2014; Peng & Luo, 2000) because political ties send beholders a signal that the firm has the ability and the motivation to satisfy their pragmatic and moral expectations. First, as mentioned, political ties can provide firms with access to scarce resources, information and preferential treatment (Li et al., 2014; Zhou & Li, 2007). Firms with these advantages are more likely to develop the ability to provide quality products and services at reasonable prices, which is consistent with customer welfare and satisfies customers' pragmatic expectations. Second, for a firm's investors, suppliers and distributors, political ties imply that the focal firm will likely help them obtain a superior return on their investment or avoid risk by means of key resources obtained from and protection by the government. The signal of improved welfare meets the pragmatic expectations of firm partners.

Third, improving the welfare of the community and society is an important task of the government, and the government often needs the help of firms to achieve these objectives. A firm with political ties usually has to accommodate the government's demands, so the firm is more likely to participate in activities that benefit the public, thus satisfying its beholders' moral expectations. For example, a firm with high levels of government ownership is expected to pursue corporate social responsibility in accordance with government policy, such as infrastructure development and the resolution of unemployment challenges (Li & Zhang, 2010).

In summary, due to the role the government plays in economic and social activities, political ties can enhance firm legitimacy by sending authoritative signals to beholders (including consumers, partners and the general public), which helps improve firm performance. Thus, H2 states the following:

H2 Legitimacy has a positive mediating effect on the link between political ties and firm performance.

Political ties have both a negative effect and a positive effect on firm performance through eroding innovation capability and fostering legitimacy, respectively; however, these dual effects depend on institutional and market contexts (Sheng, Zhou, & Li, 2011; Zhu, Su, & Shou, 2017). Thus, to enrich our understanding of the political ties-performance nexus and the mediating effects of innovation capability and legitimacy, we consider the contingent effects of institutional and market factors on the mediation.

Moderating effects of legal enforceability

Legal enforceability, which refers to the perceived legal protection of a company's financial interests in a business transaction, is a reflection of the formality of laws and regulations, independent law enforcement, and the public's cultural tradition and attitudes towards laws (Child, Chung, & Davies, 2003; Zhu, Su, & Shou, 2017). The problem of uneven legal enforceability between different regions is one of the most prominent features of emerging markets (Qian et al., 2017). Specifically, in China, where legal institutions are inadequate, firms find it difficult or expensive to follow normal legal processes to gain protection against ineffective punishments and unlawful or unfair competitive behaviors; thus, weak legal enforceability disrupts the economic order and fails to give firms adequate legal protection (Sheng, Zhou, & Li, 2011; Zhu, Su, & Shou, 2017).

We posit that weak legal enforceability increases the restraining effect of political ties on market-focused innovation capability for the following reasons. First, weak legal enforceability leads to an increase in government power in protecting a firm's activities (Li, Zhou, & Shao, 2009; Zhou & Poppo, 2010). Under these circumstances, the pivotal role of political ties in helping firms attain adequate support, favorable policies and privileges that shelter them from unlawful behavior is strengthened (Peng & Luo, 2000; Zhu, Su, & Shou, 2017), which in turn reassures managers of their political ties. As a result, firms prefer to (re)invest more money or other resources in building and maintaining their relationship with the government rather than developing their market-focused innovation capability (Wu, 2011). At the same time, leveraging the political power of government officials enables firms to more easily safeguard potential victims of unlawful and unethical behaviors (Li et al., 2012), again reinforcing managers' commitment to the *status quo* (Geletkanycz & Black, 2001). Thus, decision makers are more willing to forego investing in market-focused innovation capability in favor of strengthening their political ties with the government.

Second, government interventions in a business's operations may decrease the costs of legal actions against unlawful behaviors in an environment with weak legal enforceability (Zhou, Gao, & Zhao, 2017; Zhou & Poppo, 2010). Thus, the greater their dependency on the government to gain access to supporting transactions and preventing unlawful competition, the more pressure firms face from the government (Chen & Wu, 2011; Warren, Dunfee, & Li, 2004). As a result, firms' strategies are more likely to

follow the commands and goals of the government, such as increased employment, fiscal health, regional development, and social stability. When political orientation rather than market orientation is likely to become a dominant culture, firms are challenged in developing their market-focused innovation capability. Consequently, we posit H3 as follows:

H3 The greater the degree of legal enforceability is, the weaker the negative effect of political ties on innovation capability.

Legal enforceability also decreases the positive impact of political ties on a firm's legitimacy. Logically, legal enforceability relates to the degree to which the legal system can protect individual and organizational rights and how well it supports the effectiveness of contract enforcement (Peng & Zhou, 2005; Qian et al., 2017). When legal enforceability is high, it is not necessary for firms to obtain government protection with the aid of political ties. In general, legal enforceability depreciates political ties. Thus, in an environment with a high degree of legal enforceability, a firm's direct stakeholders are less likely to believe that a firm with political ties is more competent in increasing their welfare; thus, political ties are not a major cause of pragmatic legitimacy.

In addition, efficient formal institutions limit government intervention in firm operations, even in a firm with political ties (Zhou, Gao, & Zhao, 2017). In deciding whether to engage in activities that benefit the public, a firm operating in an efficient formal institutional environment is likely to act based on its own judgment rather than based on pressure from the government (Peng, 2003). Thus, if formal institutions are well developed, political ties no longer positively influence the normative evaluation of a firm by beholders, and a firm does not obtain moral legitimacy due to its relationship with the government.

In contrast, if formal institutions are not well developed, beholders (including customers, investors, partners, and the public) value political ties and in turn endow firms that have political ties with more legitimacy. Thus, we offer the following hypothesis:

H4 The greater the degree of legal enforceability is, the weaker the positive effect of political ties on legitimacy.

Moderating effects of competitive intensity

Competitive intensity refers to the degree to which customers have alternative supply sources, which in turn influences whether they are less dependent on a particular supplier (Cannon & Perreault, 1999). Emerging markets usually experience an increase in private enterprises during an economic transition from a centrally planned economy to a market economy, which renders competitive intensity one of most fundamental variables reflecting the task environment. Consequently, we consider competitive intensity a moderator and argue that it can enhance the impact of market-focused innovation capability and firm legitimacy on firm performance.

As one of the most important dynamic capabilities, market-focused innovation capability represents the extent to which a firm introduces new products, new processes, and new systems required for adapting to changing markets, technologies and modes of competition (Dougherty & Hardy, 1996). Intense competition elevates consumers' power in the market, which implies that customer satisfaction becomes imperative for improving performance (Jaworski & Kohli, 1993; Murray, Gao, & Kotabe, 2011). Market-focused innovation capability enables firms to better satisfy customers' changing needs, so the importance of market-focused innovation capability is more salient in highly competitive markets than in minimally competitive markets. Intense competition erodes firm performance due to greater rivalry, which often leads to imitation (Chen, Lin, & Michel, 2010), price wars, promotion competition, and higher advertising costs (Auh & Menguc, 2005; Cui, Griffith, & Cavusgil, 2005). Market-focused innovation capability enables firms to build differentiation advantages through product and service innovation and reduce the cost of operations through process and management innovation, which in turn protects firm performance from aggressive competition.

In addition, competitive intensity accelerates market dynamism, which often results in market performance becoming nonlinear and less predictable (Eisenhardt, 1989). In such a market environment, firm performance relies much less on existing knowledge and much more on rapidly creating situation-specific new knowledge. Existing knowledge can even be a disadvantage if managers overgeneralize from past situations (Argote, 1999). A firm with greater market-focused innovation capability is likely to acquire and exploit new technology and knowledge to improve its performance in a dynamic market.

In sum, firms with high market-focused innovation capability can better translate competitive threats into beneficial opportunities; thus, intense competition in markets often results in firms placing a premium on innovation (Sirmon, Hitt, & Ireland, 2007). We therefore predict the following:

H5 The greater the level of competitive intensity is, the stronger the positive effect of market-focused innovation capability on performance.

As mentioned, legitimacy brings more revenue and lower costs to a firm through customer satisfaction, partner trust and cooperation, and public word-of-mouth. However, when competitive intensity is low in the industry, a firm that lacks sufficient legitimacy may perform well if its customers have no alternative options to satisfy their needs and wants, i.e., "customers are stuck with the organization's products and services" (Jaworski & Kohli, 1993).

Competitive intensity not only reduces customer dependence on a particular supplier but also leads to perceived equalization regarding the quality of the products and services of different suppliers. This equalization then complicates differentiation based on aspects related to a firm's core offering. In such cases, legitimacy, especially moral legitimacy, may be a useful tool to differentiate a firm from its rivals (Ven & Jeurissen, 2005), and a firm with more legitimacy has a competitive advantage. We therefore predict the following:

H6 The greater the level of competitive intensity is, the stronger the positive effect of legitimacy on performance.

Methods

Sample and data collection procedures

We obtained data for this study through a survey in central-western China and southeastern China. An English-language version of the questionnaire was prepared first and then translated into Chinese through a double back-translation process (Hoskisson et al., 2000; Li, Poppo, & Zhou, 2008). We controlled survey quality in the following ways. First, we promised each respondent about USD $1.5 for each valid questionnaire as an incentive. Second, to ensure that respondents were qualified, they were required to report their job position (e.g., general staff, junior manager, middle manager, and senior manager) in the firm. Since our questionnaire was related to the firm's strategic activities, we excluded general staff from the sample. Furthermore, some respondents were excluded based on their answer to the question "Which business activities are you familiar with in the company?"

Since all questionnaire measures except the scales for legitimacy were drawn from previous studies, data were collected in two phases. The data from first phase was used to conduct exploratory factor analysis (EFA) for legitimacy and the data from second phase was used to conduct confirmatory factor analysis (CFA) for all reflective scales and hypotheses testing. During the first phase, in-depth interviews were used to generate an initial item pool. With the help of the alumni association of a large university in China, we received 58 valid questionnaires from top managers. In the second phase, a formal questionnaire including legitimacy (13 items) and other constructs in our research were sent to the MBA Alumni Community of a university in China, and we asked alumni working in company managerial positions to provide information. Ultimately, 362 valid questionnaires were collected. Table 2 shows the characteristics of the samples.

Measures

Legitimacy Following rigorous methods (Gerbing & Anderson, 1988), we developed a measurement for legitimacy. In the first stage, in-depth interviews with five experienced entrepreneurs and three professors in marketing were used to generate an initial pool of 22 items and an assessment of content validity. After that, we asked 80 top managers to evaluate their companies by completing the 22-item questionnaire. Based on 58 valid questionnaires, the Kaiser–Meyer–Olkin measure of sampling adequacy was .797, suggesting that factor analysis was appropriate. In the third step, an EFA was undertaken, and the analysis generated five factors with eigenvalues greater than one (together explaining 73.306% of the total variance; see Table 3). The items in the first four factors had a clear meaning, so according to the legitimacy definition of Dacin, Oliver, and Roy (2007), we could easily categorize them as relational legitimacy, social legitimacy, market legitimacy, and investment legitimacy. However, three items

belonging to the last factor had different meanings, which meant that it was difficult to categorize the last factor. Given that this factor explained only 5.928% of the total variance, we deleted the unnamed factor from the formal scale. In addition, we removed six items from the measurement model due to weak loading or cross loading (Hogan et al., 2011). Table 3 shows the formal scale including the 13 items.

To further assess the factor structure of the legitimacy scale, a CFA was conducted. Specifically, the second-order construct operationalization with four first-order factors (relational legitimacy, investment legitimacy, social legitimacy and market legitimacy) was tested using 13 items of legitimacy. Table 4 shows that the measurement model fit the data satisfactorily.

Political ties and performance The measures of political ties and performance are both four-item structures and adopted from Sheng, Zhou, and Li (2011). The measure of political ties captures the interpersonal relationship between managers and officials at various levels of government and regulatory organizations, such as tax bureaus, state banks, and commercial administration bureaus, and the scale also reflects substantial resources invested by firms in building relationships with government officials. The scales of performance consist of four items: sales growth rate, market share growth, profit growth rate, and return on investment compared to major firm competitors over the past year.

Table 2 Profiles of the sample companies

Sample Characteristics	The First Phase ($N = 58$) **Percentage**	The Second Phase ($N = 362$) **Percentage**
Industry		
Finance and insurance	36.3%	27.3%
Manufacturing	17.2%	24.3%
Wholesale and retail trade	8.6%	8.8%
IT	6.78%	10.76%
Comprehensive	5.08%	3.18%
Real estate	3.4%	5.38%
Other	22.64%	20.28%
Number of Employees		
<200	51.85%	32%
200–1000	20.37%	28.8%
1000–5000	16.67%	17.3%
>5000	11.11%	21.9%
Ownership		
State owned	37.9%	30.1%
International joint venture	8.6%	5.2%
Private	27.6%	39.0%
Foreign wholly owned enterprises	17.2%	18.0%
Other	8.7%	7.7%

Table 3 Exploratory factor analysis for legitimacy

Scale items	Validation sample (N = 58)				
	Factor loadings				
	1	2	3	4	5
Relational legitimacy					
Our firm is well recognized by partners.	.784				
Our firm has been rated as a high-quality partner by other firms.	.768				
Compared with other firms, it is easier for our firm to establish further cooperation with high-quality partners.	.735				
Our firm has more successful collaborative experiences than other firms.	*.563*		*.511*		
Our firm has established alliances with other firms perceived to be socially responsible.	*.554*				
Our firm enjoys greater discretion and a wider set of partner choices in making partner selection decisions in alliances.	*.535*	*.528*			
Our firm exhibits norms of equity, trust, and an orientation toward mutual gain in prior cooperation experiences.	*.524*				
Social legitimacy					
Our firm has been considered in compliance with social rules and expectations by public interest groups, local communities and consumers.		.903			
Our firm is well recognized by the public.		.884			
Our firm has formed a socially responsible image in the eyes of public interest groups, local communities and consumers.		.857			
Compared with other firms, our firm has more experience in cooperation with high-quality firms.	*.570*	*.575*			
Market legitimacy					
Our firm has a wealth of business experiences in the market.			.860		
Our firm's activities in the market are generally recognized by customers.			.845		
Our firm has the right to conduct business freely in the current market owing to our qualification-related permits issued by the government.			.740		
Our firm has a positive reputation and is highly recognized by consumers.			*.576*		
Investment legitimacy					
Our firm's business activities receive lengthy and intense resource investment from internal proponents.				.842	
The board of directors, corporate executives, venture capitalists, and/or shareholders of our firm have sufficient confidence in our firm's business activities.				.752	
Our firm's business activities are worthwhile in the eyes of corporate insiders, such as the parent firm's board of directors, executives, venture capitalists and shareholders.				.739	
Our firm's business activities have received internal endorsement.				.702	

Table 3 (continued)

Scale items	Validation sample (N = 58)
	Factor loadings
Unnamed factor	
Our firm has used environmental actions and policies to produce and operate.	.643
Our firm has secured government contracts.	.533
Our firm's business activities have been recognized by stakeholders.	.526

A set of 13 items was retained after exploratory factor analysis for the next step of the scale development process. The unnamed factor was deleted because of its lower explained variance and ambiguous meaning. Other items in italics were deleted due to cross-factor loading or lower factor loading

Legal enforceability and competitive intensity Legal enforceability, reflecting the extent to which the legal system can protect firms' business interests, was assessed based on a four-item scale from Zhou et al. (2010). Competitive intensity, as a traditional environmental factor, was captured by a mature five-item scale from Jaworski and Kohli (1993).

Market-focused innovation capability Market-focused innovation capability refers to the ability to satisfy a market's changing demand (Damanpour, Walker, & Avellaneda, 2009), which includes the ability to provide clients with new services and products (or the ability to solve clients' problems in innovative ways) and the ability to implement innovative marketing programs. Drawing on Hogan et al., (2011), we used a nine-item scale to capture the extent of firms' ability in client-based innovation activities and marketing-based innovation activities.

Control variables To isolate potential confounding effects, we controlled for the following variables. 1) Firm age, which has an effect on the relationship between innovation and performance (Chen et al., 2014). We used the logarithm of the number of years the firm has been in operation to run a regression model. 2) Firm size, as measured by the natural logarithm of the number of firm employees (Sheng, Zhou, & Li, 2011). 3) Subsidiary, as defined by the answer to the question "Is the firm part of a larger firm?" because a subsidiary is likely to suffer interference from firm headquarters, which may affect firm performance (Birkinshaw, Hood, & Young, 2005). 4) The amount spent by the firm on research and development activities in the last three years, which affects future firm performance (Wu, 2011). 5) Export intensity (the percentage of export business to total sales) because firms with high levels of export intensity are more likely to attain legitimacy by adopting positive environmental strategies (Wu & Ma, 2016) and achieve better performance by improving their innovation capability (Smith, 2014).

Construct reliability and validity

We conducted a CFA to assess the reliability and validity of the reflective measure. Given the limited sample size, we divided the set of scales into two subgroups (Hewett

Table 4 Measurement properties of the legitimacy scale

Scale items	Validation sample (N = 362)			
	Factor loadings	Cronbach's α	CR	AVE
Legitimacy		.947		
Relational legitimacy		.933	.912	.780
Our firm is well recognized by partners.	.901			
Our firm has been rated as a high-quality partner by other firms	.923			
Compared with other firms, it is easier for our firm to establish further cooperation with high-quality partners	.816			
Investment legitimacy		.927	.928	.763
Our firm's business activities obtain lengthy and intense resource investment from internal proponents	.882			
The board of directors, corporate executives, venture capitalists, and/or shareholders of our firm have sufficient confidence in our firm's business activities.	.914			
Our firm's business activities are worthwhile in the eyes of corporate insiders, such as the parent firm's board of directors, executives, venture capitalists and shareholders.	.914			
Our firm's business activities have received internal endorsement	.776			
Social legitimacy		.908	.931	.818
Our firm is well recognized by the public.	.931			
Our firm has formed a socially responsible image in the eyes of public interest groups, local communities and consumers.	.901			
Our firm has been considered in compliance with social rules and expectations by public interest groups, local communities and consumers.	.880			
Market legitimacy		.850	.861	.675
Our firm has a wealth of business experience in the market	.894			
Our firm's activities in the market are generally recognized by customers.	.844			
Our firm has the right to conduct business freely in the current market owing to our qualification-related permits issued by government	.717			
Overall fit: $\chi^2 = 182.966$, normed $\chi^2 = 2.999$, TLI = .964, CFI = .972, RMSEA = .074; SRMR = .038				

All factor loadings are significant ($p < .05$)

AVE average variance extracted; *df* 61; χ^2 chi-square; *normed* χ^2 χ^2/df; *TLI* Tucker–Lewis index; *CFI* comparative fit index; *RMSEA* root-mean-square error of approximation; *SRMR* standardized root mean residual; factor loadings the completely standardized parameter estimates

& Bearden, 2001). The first measurement model included only legitimacy. The second measurement model included the remaining five factors: political ties, market-focused innovation capability, legal enforceability, competitive intensity, and firm performance. The first measurement models fit the data satisfactorily (χ^2 (61) =182.966, $p < .01$; TLI = .964; CFI = .972; SRMR = .038; RMSEA = .074). The second measurement models also fit the data satisfactorily (χ^2 (290) =564.221, $p < .01$; CFI = .969;

TLI = .965; SRMR = .033; RMSEA = .051). All factor loadings for each construct were significant ($p < .01$). The composite reliability and AVE from all focal constructs (see Table 3 and Appendix) exceeded the .70 and .50 benchmarks, respectively. Thus, the measures demonstrated adequate reliability and convergent validity.

We assessed the discriminant validity of the measures in two ways. First, the AVE of each construct exceeded the squared correlation between construct pairs, demonstrating discriminant validity between the latent factors (Fornell & Larcker, 1981). Second, according to chi-square difference tests for all paired constructs, the restricted model (correlation fixed at 1) was significantly worse than the freely estimated model (correlation estimated freely). Specifically, minimum $\Delta\chi^2$ (1) =8.30, $p = .00$, in support of discriminant validity.

Common method bias

In addition to implementing procedural controls for the survey, such as anonymous submission and minimization of the ambiguity of the measurement items, we conducted a test of common method variance by using the marker variable assessment technique approach recommended by Lindell and Whitney (2001). We added a variable regarding the geographical distance between the company and the province capital as the MV marker, which had no significant relation with the variables in our study (Lindell & Whitney, 2001). None of the significant correlations became insignificant after adjustment among the important constructs (see Table 5). Therefore, common method bias was unlikely to be a serious concern.

Results

We used bias-corrected bootstrapping (5000 samples taken from the data set) to test the mediating effects of innovation capability and legitimacy (Preacher & Hayes, 2008) (Table 6). We found that the indirect effect of political ties on performance via market-focused innovation capability was significant (supporting H1),

Table 5 Descriptive statistics and correlations

Variable	Mean	S.D.	1	2	3	4	5	6
1. Legal enforceability	3.838	2.111		.165**	.060	.201**	.435**	.247**
2. Competition intensity	3.997	2.149	.168**		.041	.280**	.302**	.193**
3. Political ties	4.461	1.856	.066	.053		−.138**	.117*	.024
4. Market-focused innovation capability	4.299	1.804	.201**	.278**	−.138**		.448**	.497**
5. Legitimacy	5.234	.979	.435**	.318**	.132*	.444**		.432**
6. Performance	4.065	1.960	.250**	.206**	.037	.495**	.443**	
7. Geographical distance	336.0	128.3	.007	.110*	.046	−.002	.129*	.078

*p < .05; **p < .01 (two-tailed)

N = 362. Zero-order correlations are below the diagonal; adjusted correlations for potential common method variance (Lindell & Whitney, 2001) are above the diagonal

Table 6 Mediating effects of innovation capability and legitimacy

Sample size	Model	Political ties→ firm performance			
		Product of coefficients		Bootstrapping 95% CI	
		Point estimate	SE	Lower	Higher
Full sample ($N = 362$)	Indirect effects				
	Total	−.021	.029	−.083	.033
	Market-focused innovation capability (MIC)	−.051	.021	−.096	−.015
	Legitimacy (LE)	.030	.015	.007	.066

5000 bootstrap samples

with a point estimate of −.051 and a 95% confidence interval (CI) of (−.096, −.015), which excludes zero. Likewise, the indirect effect of political ties on firm performance via legitimacy was significant (providing support for H2), with a point estimate of .030, 95% CI (.007 to .066).

In H3, we predicted that the direct effect of political ties on market-focused innovation capability would be moderated by legal enforceability. We found that the indirect effect of political ties on performance via market-focused innovation capability was significantly moderated by legal enforceability: the index of moderated mediation was .020, with a 95% CI (.001 to .043), which excluded zero (Table 7). Meanwhile, the results of Model 3 (Table 8) indicate that the coefficient of political ties × legal enforceability was significant and positive ($\beta = .051$, $p < .05$), and as indicated by the results of Model 2 (Table 8), the coefficient of political ties was significant and negative ($\beta = -.320$, $p < .01$). Figure 2 indicates that political ties were less negatively related to market-focused innovation capability with high legal enforceability ("high" defined as one standard

Table 7 The results of moderated mediation tests

Sample size	Moderator	Mediator	Political ties→ firm performance			
			Product of coefficients		Bootstrapping 95% CI	
			Index	SE	Lower	Higher
Full sample (N = 362)	Legal enforceability	Indirect effects				
		Market-focused innovation capability (MIC)	.020	.011	.001	.043
		Legitimacy (LE)	−.017	.008	−.035	−.005
	Competitive intensity	Indirect effects				
		Market-focused innovation capability (MIC)	−.007	.004	−.018	−.001
		Legitimacy (LE)	.001	.003	−.005	.009

Table 8 Regression results

Variables	Innovation capability			Legitimacy		
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Intercept	4.296*** (.087)	4.356*** (.265)	5.275*** (.517)	5.234*** (.047)	4.304*** (.132)	3.599*** (.254)
Firm age	.148 (.091)	.159* (.089)	.157* (.089)	−.096* (.050)	−.076* (.045)	−.074* (.044)
Firm size	.110 (.088)	.121 (.086)	.100 (.086)	.110** (.048)	.108** (.043)	.124*** (.043)
Subsidiary	.075 (.090)	.084 (.088)	.079 (.087)	.066 (.049)	.058 (.044)	.061 (.043)
R&D input over the last three years	.622*** (.096)	.571*** (.095)	.555*** (.095)	.327*** (.052)	.275*** (.047)	.287*** (.047)
Export intensity	.209** (.096)	.224** (.094)	.223** (.094)	0041 (.052)	.058 (.047)	.059 (.046)
Political ties (PT)		−.140*** (.046)	−.320*** (.099)		.055** (.023)	.194*** (.048)
Legal enforceability (LE)		.147***(.041)	−.113 (.132)		.178*** (.020)	.379*** (.065)
PTxLE			.051** (.025)			−.039** (.012)
R^2	.169	.215	.225	.170	.330	.350
ΔR^2		.047***	.009**		.160***	.019**

$N = 362$. * $p < .1$, ** $p < .05$, *** $p < .01$ (two-tailed tests)

deviation (s.d.) above the mean) than with low legal enforceability (defined as one s.d. below the mean). Thus, we found support for H3.

H4 predicted that the direct effect of political ties on legitimacy would be moderated by legal enforceability. As shown in Table 7, we found that the indirect effect of political ties on performance via firm legitimacy was significantly moderated by legal enforceability, with a moderated mediation index value of −.017 and a 95% CI (−.035 to −.005), which excluded zero. We also found (Model 6 in Table 8) that the coefficient of political ties × legal enforceability was significant and negative ($\beta = -.039$, $p < .05$) and that the coefficient of political ties was significant and positive (Model 5 in Table 8; $\beta = .194$, $p < .01$), thus supporting H4. This result is confirmed in Fig. 3: political ties were less positively related to legitimacy when legal enforceability was high (1 s.d. above the mean) than when legal enforceability was low (1 s.d. below the mean).

H5 predicted that the impact of market-focused innovation capability on firm performance would be moderated by competitive intensity. We found that the indirect effect of political ties on performance via market-focused innovation capability was significantly moderated by competitive intensity (Table 7), with a moderated mediation index value of −.007, 95% CI (−.018 to −.001), which excludes zero. As indicated by our results for Model 6 in Table 9, the coefficients of market-focused innovation capability × competitive intensity were significant and positive ($\beta = .054$, $p < .01$). Figure 4 shows the moderated effect of competitive intensity on the market-focused innovation capability-performance nexus; specifically, market-focused innovation

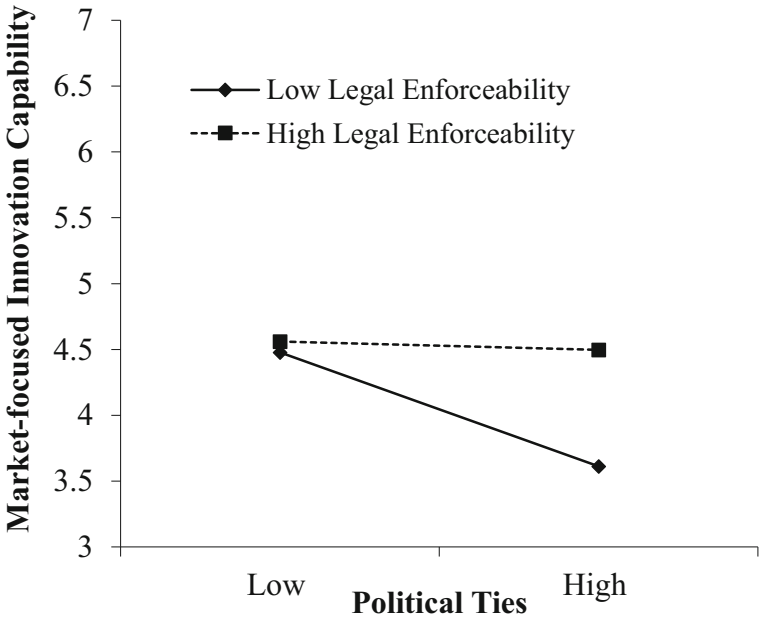

Fig. 2 The interactive effect of political ties and institutional development on market-focused innovation capability

capability was more positively related to performance when competitive intensity was high (1 s.d. above the mean) than when competitive intensity was low (1 s.d. below the mean). Hence, we found support for H5.

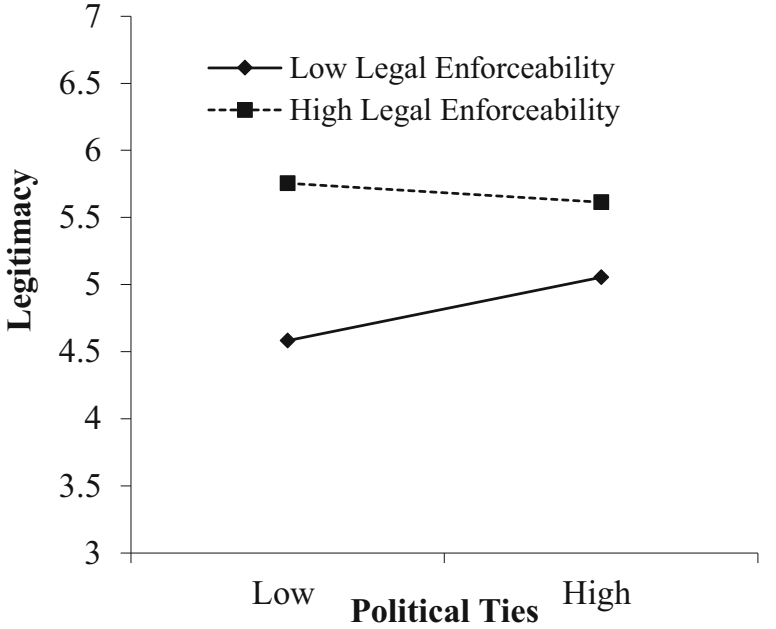

Fig. 3 The interactive effect of political ties and institutional development on legitimacy

Table 9 Regression results

Variables	Performance					
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Intercept	4.070*** (.097)	3.920*** (.255)	−.213 (.538)	1.686** (.694)	.949 (1.113)	.829 (1.073)
Firm age	−.071 (.102)	−.070 (.102)	−.084 (.091)	−.109 (.092)	.002 (.096)	−.072 (.091)
Firm size	.107 (.099)	.105 (.099)	.011 (.088)	.068 (.089)	.023 (.094)	.024 (.089)
Subsidiary	.127 (.100)	.125 (.100)	.066 (.089)	.097 (.090)	.086 (.094)	.080 (.089)
R&D input over the last three years	.552*** (.108)	.554*** (.108)	.167*** (.103)	.239** (.102)	.300*** (.107)	.165 (.103)
Export intensity	.162 (.107)	.162 (.108)	.064 (.096)	.067 (.097)	.137 (.101	.064 (.096)
Market-focused innovation capability (MIC)			.390*** (.057)	.263** (.103)		.195* (.117)
Competition intensity (CIT)				−.197* (.112)	.017 (.259)	−.270 (.250)
MIC x CIT				.052** (.024)		.054** (.027)
Legitimacy (LG)			.452*** (.105)		.633*** (.202)	.372* (.221)
LG x CIT					.005 (.047)	.008 (.051)
Political ties (PT)		.033 (.053)	.054 (.048)	.130 (.103)	−.130 (.108)	.033 (.105)
Legal enforceability (LE)				.203 (.136)	−.093 (.148)	.048 (.142)
PT x LE				−.016 (.025)	.033 (.027)	.003 (.026)
R^2	.120	.121	.318	.311	.245	.333
ΔR^2		.001	.198***	.191***	.121***	.213***

$N = 362$. * p < .1, ** p < .05, *** p < .01 (two-tailed tests)

H6 predicted that the impact of legitimacy on firm performance would be moderated by competitive intensity. As shown in Table 7, we found that the indirect effect of political ties on performance via legitimacy was not significantly moderated by competitive intensity, with a moderated mediation index of .001 and a 95% CI (−.005 to .009), which included zero. We also found (Model 6 in Table 9) that the coefficient of legitimacy × competitive intensity was not significant ($\beta = .008$, $p > .100$); thus, we did not find support for H6. This may be because competitive intensity has opposite impacts on the implied performance of customer satisfaction and customer identification as induced by firm legitimacy. Specifically, intense competition exposes customers more frequently to more competitive offerings, which may result in customers revising their expectations (Mehta, Chen, & Narasimhan, 2008). Thus, satisfied customers in a

more competitive market are less willing to pay than customers in a less competitive market. In contrast, competitive intensity may enhance the impact of customers' identification on their willingness to pay. Previous research has offered support for this suggestion. For example, Haumann et al. (2014) found that customer identification reflects the extent to which a customer perceives overlap between his or her identity and that of an organization (Bhattacharya & Sen, 2003); thus, highly identified customers confronted with a high level of competitive advertising, to maintain self-consistency, are likely to accentuate the advantages of the offerings of the focal company with which they identify and devalue the competitive offerings.

Discussion and conclusion

Drawing on dynamic capability theory and institutional theory, we investigated how political ties play dual roles in an emerging market. Our results suggest that political ties have a metaphorical double-edged sword effect on firm performance in emerging economies; political ties can erode performance by inhibiting market-focused innovation capability, but they can also facilitate performance by enhancing firm legitimacy. In addition, we found that this dual effect is conditional on the institutional environment (legal enforceability buffers the negative impact of political ties on market-focused innovation capability but mitigates the positive impact of political ties on firm legitimacy), and the market environment, i.e., competitive intensity, is an important market factor that enhances the impact of market-focused innovation capability on firm performance.

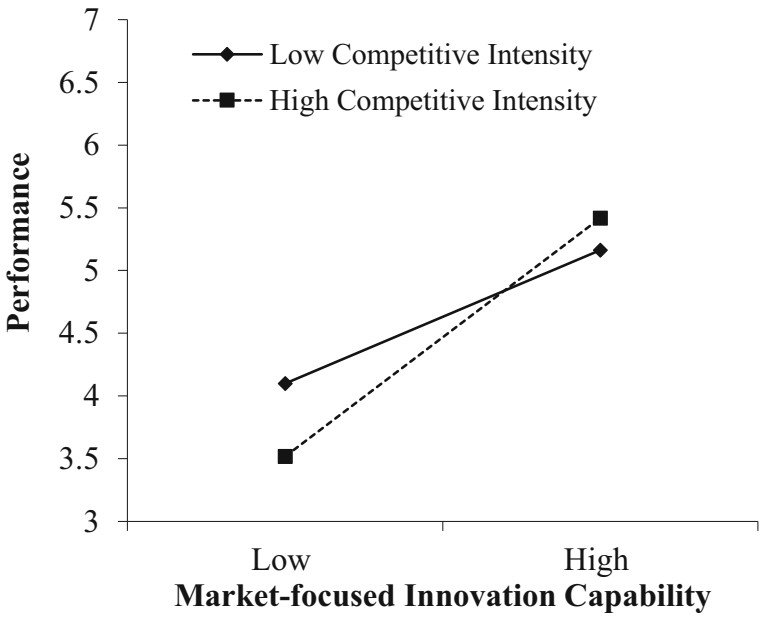

Fig. 4 The interactive effect of market-focused innovation capability and competitive intensity on performance

Theoretical contributions

Our results contribute to the existing scholarly literature on political ties in the following ways. First, our study explored the political ties-performance nexus by examining the intermediate role of market-focused innovation capability and legitimacy. Unlike studies that shed light on only the positive underlying mechanism of the political ties-performance nexus (Guo, Xu, & Jacobs, 2014; Zhu, Su, & Shou, 2017), we provide insight into the bright side and the dark side of political ties simultaneously.

Second, we provide information on fundamental mediating mechanisms by testing the mediating effect of legitimacy in the relationship between political ties and performance. Extant research has provided insights into how political ties work to improve performance from the perspective of legitimacy (Peng & Luo, 2000; Sheng, Zhou, & Li, 2011). However, little if any research has examined the mediating effect of legitimacy on the political ties-performance nexus. We found that political ties can facilitate firm performance by sending beholders a signal that the firm has the ability and motivation to satisfy their pragmatic and moral expectations; consequently, our work constitutes a meaningful attempt to explain how political ties translate into firm performance from the perspective of institutional theory.

Third, our results suggest that the mediating effect of market-focused innovation capability and legitimacy depends on the institutional and market contexts. Thus, from a process-based perspective, our findings contribute to an enriched understanding of the relationship between political ties and performance. For example, we can explain why the impact of political ties on firm performance decreases with the improvement of legal enforceability; our results suggest that this occurs because legal enforceability buffers the erosion of political ties on innovation capability but mitigates the positive impact of political ties on legitimacy. In addition, we found that the impact of market-focused innovation capability on performance is positively associated with competitive intensity, which also explains why the positive impact of political ties on firm performance is not salient in a highly competitive market (Li, Poppo, & Zhou, 2008).

Furthermore, we developed a multi-dimensional measurement for legitimacy based on the insight of Dacin, Oliver, and Roy (2007). Specifically, we measured legitimacy from four dimensions: relational legitimacy, social legitimacy, market legitimacy and investment legitimacy. Compared with previous literature, the scale of legitimacy in our study provided a more detailed and insightful reconceptualization of the legitimacy construct.

Managerial implications

Our work has important implications for managers conducting business in emerging economies. First, we found that while political ties increase firm performance by fostering firm legitimacy, they erode firm performance by limiting market-focused innovation capability. This finding suggests that managers should be cautious in building political ties; specifically, seeking political ties would be an appropriate strategy for a firm without enough legitimacy (e.g., a foreign firm) but not a good choice for a firm that operates in an intensive competitive market because competitive intensity values market-focused innovation capability.

Second, we showed that legal enforceability decreases the negative influence of political ties on market-focused innovation capability but mitigates the positive impact of political ties on legitimacy. This result suggests that when formal institutions exist, a firm hoping to exploit political ties should keep an eye on its market-focused innovation capability in order to prevent those political ties from eroding its market-focused innovation capability.

Limitations and future research

Our results are subject to certain limitations that also suggest directions for further research. First, our results are context specific; thus, a natural extension would be to examine the roles of political ties in other transition economies. Second, we examined only legal enforceability and competitive intensity to determine the dominant mediator between political ties and performance. Additional studies should be conducted examining other factors, such as information verifiability, market uncertainty and organizational learning.

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Appendix

Table 10 Construct validity and item description

Construct and source	Description	Factor loadings
Performance (Sheng, Zhou, & Li, 2011) Cronbach $\alpha = .910$; CR = .910; AVE = .718	Our firm's overall performance compared with major competitors over the past year on	
	1. Sales growth rate	.753
	2. Market share growth	.823
	3. The growth rate of profit	.916
	4. Return on investment	.889
	(1 = "far below competitors," and 7 = "far above competitors")	
Political ties (Sheng, Zhou, & Li, 2011) Cronbach $\alpha = .944$; CR = .943; AVE = .804	1. Top managers at our firm have maintained good personal relationships with officials in various levels of government.	.834
	2. Top managers at our firm have developed good connections with officials in regulatory and supporting organizations such as tax bureaus, state banks, and commercial administration bureaus.	.917
	3. So far, our firm's relationship with regional government officials has been good.	.890

Table 10 (continued)

Construct and source	Description	Factor loadings
	4. Our firm has spent substantial resources in building relationships with government officials.	.943
Legal enforceability (Zhu, Su, & Shou, 2017) Cronbach $\alpha = .934$; CR = .917; AVE = .736	In our business operations,	.898
	1. the legal system protects our interests.	
	2. the legal system ensures that we can get our money back.	.909
	3. the legal system ensures the accuracy of suppliers' delivery.	.853
	4. the legal system prevents us from being cheated.	.763
Competitive intensity (Jaworski & Kohli, 1993) Cronbach $\alpha = .935$; CR = .936; AVE = .744	1. Competition in our industry is cutthroat.	.788
	2. There are many "promotion wars" in our industry.	.881
	3. Anything that one competitor can offer, others can match readily.	.883
	4. Price competition is a hallmark of our industry.	.834
	5. One hears of a new competitive move in our industry almost every day.	.921
Market-focused innovation capability (Hogan et al., 2011) Cronbach $\alpha = .956$; CR = .956; AVE = .707	1. Provide our clients with services/products that offer unique benefits superior to those of competitors	.780
	2. Solve clients' problems in very innovative ways	.793
	3. Provide innovative ideas and solutions to clients	.784
	4. Present innovative solutions to our clients	.836
	5. Seek out novel ways to tackle problems	.910
	6. Develop "revolutionary for the industry" marketing programs for our services/products	.896
	7. Adopt novel ways to market our firm	.796
	8. Innovate with our marketing programs to keep ahead of the market	.868
	9. Implement innovative marketing programs	.892

All items, unless specifically indicated, use Likert scales (1 = "strongly disagree" and 7 = "strongly agree").

CR composite reliability; *AVE* average variance extracted

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