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## **The Role of Formal Method of Handling Conflicts in Company's Foreign Relationships**

### **Abstract**

The aim of this paper is to assess the role of the formal method of handling conflicts occurring in company's foreign relationships.

The assessment is performed taking into consideration the complex character of conflicts and ambiguous role of formal procedures in the process of resolving conflicts. That is why, in order to achieve the aim of the paper, quantitative as well as qualitative study has been undertaken. Results of the quantitative study has indicated dependency between formalization and frequency of conflicts in company's relationships with partners operating in an international environment. Outcomes of qualitative research are complementary to the quantitative study by providing some insightful information and explaining in a more detail way the role of formalization in handling conflicts in company's foreign relationships.

**Key words:** conflict handling, formalization, foreign relationships

### **Introduction**

What is the best way to resolve a conflict occurring in relationships with external partners of a company operating in an international environment? Should it be handled in a formal or an informal manner?

Existing research identifies both positive as well as negative aspects of formalization. On one hand formalization can be associated with a high predictability and efficiency of organizational management. Moreover, it decreases the probability of misinterpreting responsibilities assigned to different roles in organizations which can result in avoiding conflicts. It is also said to increase commitment in business relationships (De Clercq, Dimov, & Thongpapanl, 2013). On the other hand, formalization is believed to restrict possibilities to adapt your own strategy to the needs of relationship. It could also inhibit partner's commitment as well as hamper developing cooperation beyond borders specified in agreement. Therefore, by some (Vlaar, Van Den Bosch, & Volberda, 2007), it is said to cause conflicts.

The existing ambiguity is especially important in the case of companies operating in an international market where the risk of misunderstanding and conflict is high. There is a couple of reasons proving that the risk of conflict in the internationalization process is high. Firstly, because of cultural distance relationship's partners do not understand each other so well as in case of cooperation with local entities. Secondly, operations in an international market are often more costly than in case of a local one. Thirdly, companies in the internationalization process often have to develop relationships not only with buyers and suppliers but also other types of entities.

While in the literature concerning conflict developed in company's foreign relationships there is a stream referring to informal governance mechanism such as trust, commitment or flexibility, the formal side needs a thorough attention (Aulakh & Gençtürk, 2008).

### **Literature background**

In industrial marketing research conflict has a specific meaning (Zhang, Finch, & Geiger, 2012). It can be understood as “a process in which one party perceives that its interests are being opposed or negatively affected by another party” (Lee i in., 2017). In order to avoid or resolve the existing conflict, companies use formal as well as informal mechanisms (Noémi Piricz & Tibor Mandják, 2012). Formal mechanisms refer to firm’s rules, procedures or policies and informal mechanisms are ad hoc activities undertaken by conflicting sides (Tidström & Hagberg-Andersson, 2008). By definition formalization is a set of behavior and responsibilities granted to specific roles which can be exemplified in form of agreements as well as procedures regulating business relationships (Mysen, Svensson, & Payan, 2011).

Different streams existing in the literature (such as transaction cost economics, agency theory and contract theories) have all underlined the fact that formalization is necessary in order to successfully manage interorganizational relationships (Vlaar i in., 2007). Formalization creates a framework for relationship’s development. However, when the set of behavior and extent of responsibilities granted to specific roles in relationship is unbalanced, there is a risk of conflict. Some authors (Newman, 2011) claim, that conflicts are an inseparable element of business relationship so it is an issue how they can be handled by a company, specifically in the international context. In such a situation firm’s foreign activity is bounded to a highly complex, unstable and dynamic environment and each interaction represents a potential source of a conflict (Pfajfar, Rašković, Brenčič, & Shoham, 2010).

In the literature both formal and informal methods of handling conflicts are exposed. But to the best of our knowledge there are often contradictory opinions on their real influence on conflicts’ elimination or at least reducing conflict’s negative impact in company’s foreign relationships (Lee i in., 2017; Tidström & Hagberg-Andersson, 2008; Vaaland, 2001). We have assumed that especially in company’s foreign relationships conflicts should be handled effectively by using a formal method. That is why the aim of the paper is to assess the role of the formal manner of handling conflicts occurring in company’s foreign relationships.

### **Methodology**

In order to achieve the aim of the paper a two-stage research procedure has been carried out. First a quantitative study was conducted and then it was complemented by a qualitative one. The reason for conducting a quantitative study before the qualitative one was to verify that formal methods help handling conflicts. Because of the ambiguity of research perspectives on this matter which occurs in the literature this issue needed to be settled. This fact was of utmost importance in case of companies in the internationalization process. While both international environment as well as handling conflicts are characterized by high complexity, the interdependency occurring between these two issues needed to be clarified. Therefore the aim of the quantitative study was to determine the links between a formal manner of resolving conflicts and frequency of conflicts occurring in relationships with different entities in the internationalization process. Data used for the purpose of analysis has been obtained in September 2015 from companies located in Poland, operating in international markets. With the use of a database (Kompas Poland) a random sample of companies has been selected and a research survey has been sent (via mail and e-mail) to 1748 companies. Starting point for quantitative study were answers obtained from representatives of 278 companies analyzed with the use of a computer statistical program (SPSS).

In order to provide an in-depth perspective to study dependency between formalization and conflicts in relationships with foreign partners a qualitative study has been carried out as the second step of performed procedure. Results of qualitative study served as complimentary to the ones obtained from the quantitative study. In order to gather information, face-to-face interviews were carried out in 2016 with the use of a standardized questionnaire consisting of open-ended questions. The questions concerned the type of company's activity, relationships developed with other entities, as well as the course of the internationalization process. In total 19 open questions were asked among which issues important in the context of formalization and conflicts such as decision-making manner, way of resolving conflicts, degree of trust and openness to cooperation were concerned. Interlocutors were top managers representing 30 companies (differing in size, structure, form of ownership and industry) located in Poland, operating in international markets. Each interview was recorded and a transcript has been prepared. Starting point for qualitative study were answers obtained from representatives of 9 companies.

## **Results**

In order to assess the influence of formalization on conflicts occurring in company's foreign relationships a quantitative study has been performed. Two groups of companies have been identified. Taking into consideration answers to a question about attitude towards formalization of handling conflicts in foreign relationships. The first group of companies perceives a formal method of handling conflicts as the most relevant one in foreign relationships, while the second one indicates a non-formalized manner as an optimal method to solve conflicts in relationships with foreign partners. It has to be underlined that in case of both groups of companies only severe conflicts were considered. They are understood as a threat for the existence of a given foreign relationships and even for the company itself (Duarte & Davies, 2003; Plank & Newell, 2007). They were perceived by the investigated companies as an important factor influencing their competitive advantage. Using the two identified groups of companies the frequency of conflicts has been assessed. Both questions (the one about formalization as well as the one about frequency of conflicts) were based on a 5-point Likert scale. Answers to both questions have been analyzed from the perspective of the two identified groups of companies. Results of performed analysis are presented in fig. 1.

Taking into consideration information presented in fig. 1, one can observe two interesting facts. Firstly, in case of companies characterized by formal method of handling conflicts most often there are rare conflicts. Secondly, in case of companies characterized by non-formal method of handling conflicts, conflicts are more common. These facts suggest that formalized method of handling conflicts decreases the frequency of conflicts.

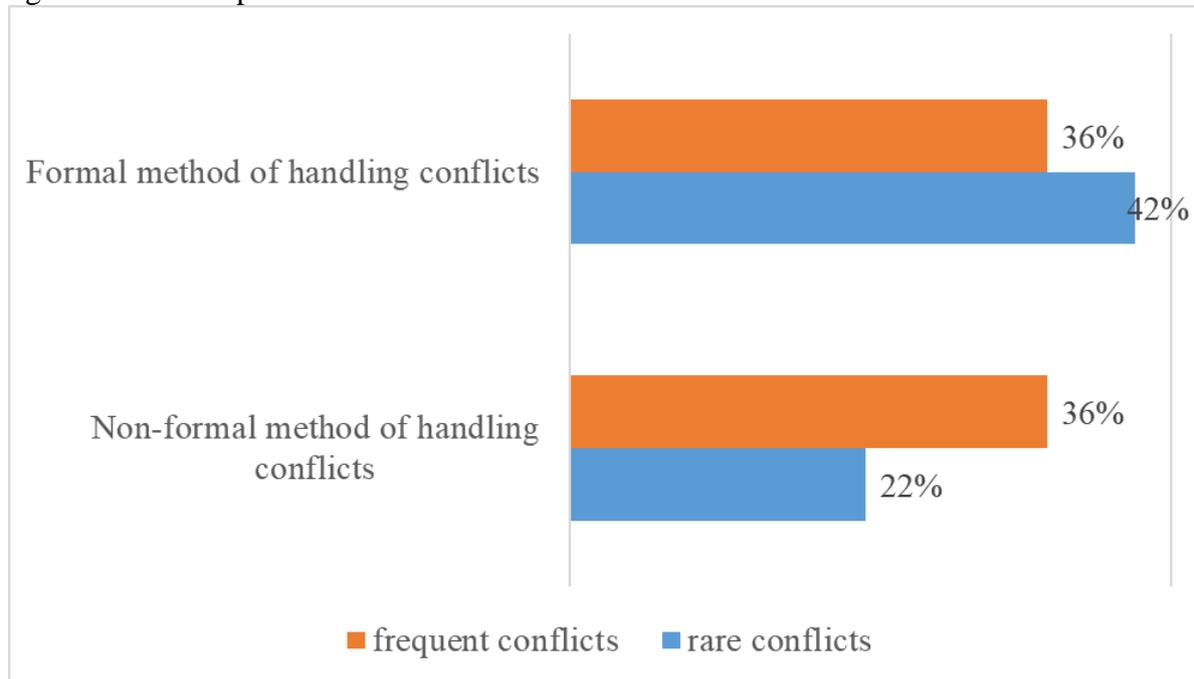
In order to statistically verify the significance of identified interdependencies a correlation analysis has been performed. Results of correlation analysis are presented in tab. 1.

Information presented in tab. 1 confirms the existence of a statistically significant correlation. It proves, that formalized way of resolving conflicts decreases the frequency of conflicts occurring in relationships with external partners of a company operating in foreign markets. Although correlation exists, the interdependency between formalization and conflicts in the internationalization process is a highly complex issue. Therefore, in order to further investigate the research problem, additionally to quantitative study a qualitative one has also been performed.

In order to perform a qualitative study transcripts of interviews with representatives of 30 companies have been thoroughly analyzed. The text was scanned in search for key words such as "conflict", "formalization" and their variations. In result 9 interviews were identified as the ones matching the research problem. Taking into consideration results of the qualitative study

a few interesting observations on formalized manner of resolving conflicts occurring in relationships with external partners in the internationalization process need to be mentioned.

Fig. 1. Relationship between attitude towards formalization and conflicts



Source: (own elaboration).

Tab. 1. Correlation between attitude towards formalization and frequency of conflicts

Correlations			
		Frequency of conflicts	Formalized way of resolving conflicts increases competitive advantage
Frequency of conflicts	Pearson Correlation	1	,256**
	Sig. (2-tailed)		,000
	N	278	278
Formalized way of resolving conflicts increases competitive advantage	Pearson Correlation	,256**	1
	Sig. (2-tailed)	,000	
	N	278	278

\*\* . Correlation is significant at the 0.01 level (2-tailed).

Source: (own elaboration).

Firstly, formalized way of resolving conflicts causes some additional effects. These are:

- strengthening existing relationship,
- helping to resolve the existing conflict,
- being a substitute for lack of openness to resolve the existing conflict.

Secondly, some conflicts (especially less serious ones) require an informal way of solving the problem.

Thirdly, sometimes (even in situations strictly defined in a formal manner) company has to take the blame on itself in order to maintain the relationship.

Fourthly, effectiveness of resolving conflicts depends on trust.

Fifthly, when, instead of high formalization, a conflict occurs it is a serious problem for the existence of a relationship.

Sixthly, resolved conflict determines the strength of company's future position in a relationship.

Seventhly, the most important exemplification of formalization in context of resolving the conflict is company's organizational culture.

## Conclusions

Although existing literature does not agree on using either informal (Rundh, Camén, & Gottfridsson, 2009) or formal manners (Vlaar, Van den Bosch, & Volberda, 2006) to resolve conflicts, results of the study performed in the paper suggest the latter way, especially when a company has to handle serious conflicts. Formalization can contribute to positive resolution of conflicts occurring in company's foreign relationships. Not only does it reduce the possibility for a conflict to occur, but also helps to settle it down. However, results also suggest, as it was pointed out by some authors (Vaaland, 2001), that formalization is supplemented with informal ways of dealing with conflicts.

The paper contributes to existing research by broadening the framework for discussion about conflicts occurring between company and its external partners in the international environment. Results of the quantitative study prove that formalized way of resolving conflicts decreases the frequency of conflicts occurring in company's foreign relationships. Results of qualitative study add further value by identifying more detailed dependencies between formalization and handling conflicts in foreign relationships. Information presented in the paper could be also useful for representatives of business practice by helping them to understand the nature of successful conflict management.

However, much of the field of formalized resolution of conflicts in the internationalization process still remains unexplored. A possible direction for future research is the proper extent of formalization at different stages of the internationalization process in order for the conflict to be resolved. Moreover, researching conflicts with specific types of entities in the internationalization process, not only importer-exporter relationships (Aulakh & Gençtürk, 2008), might be fruitful. Finally, it would be interesting to identify to what extent a method of handling conflicts (formal/non-formal) depends on conflicts' nature (serious ones versus minor ones called day-to-day problems). Such issues seem to be interesting research problems taking into consideration results of the study presented in the paper which points out an inseparable interdependency between formal and informal methods of handling conflicts.

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