

# A Study on the Impact of Institutional Distance and Cultural Distance on International Trade in the Post-Epidemic Era

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doi:10.56397/JWE.2022.12.02

## Abstract

Institutional and cultural factors, as endogenous variables affecting trade development, determine the scale and direction of a country's foreign trade development. This paper hopes to understand the impact and mechanism of institutional distance and cultural distance on international trade activities by analyzing the literature on the impact of institutional distance and cultural distance on international trade, so as to provide solutions for the business model of global trade companies as much as possible.

**Keywords:** institutional distance, cultural distance, international trade, post-epidemic era

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## 1. Introduction

With the deepening of global economic integration, the content, methods and channels of international trade have undergone profound changes. Since the outbreak of the new crown epidemic, it has spread rapidly around the world, which has had a huge impact on the international trade and economy, directly affecting the economies of the world's most important North American trade circle, EU trade circle and East Asian trade circle. When enterprises of various countries actively participate in the competition of the global value chain, they are also faced with drastic changes in

the external business environment such as foreign politics, economy and culture, and the uncertain risks of global trade are increasing.

Institutional and cultural factors, as endogenous variables affecting trade development, determine the scale and direction of a country's foreign trade development. Theoretically speaking, the influence of institutional distance and cultural distance on trade is bidirectional, which not only inhibits the development of foreign trade, but also promotes the growth of foreign trade; affects the flow of resources. The institutional distance and cultural distance between a country and other

countries will affect the further development of the country's foreign trade. In reality, it is even found that institutional distance and cultural distance are important reasons for trade conflicts between countries. This paper hopes to understand the impact and mechanism of institutional distance and cultural distance on international trade activities by analyzing the literature on the impact of institutional distance and cultural distance on international trade, so as to provide solutions for the business model of global trade companies as much as possible.

## 2. Overview

This paper sorts out the literature on the impact of institutional distance and cultural distance on international trade, systematically sorts out the relevant theoretical researches on institutional distance and cultural distance, and selects a part of the literature to focus on analyzing its research problems, data sources and research methods.

## 3. Literature Review

### 3.1 *The Theory of Institutional Distance and Cultural Distance*

Institutional economics was developed on the basis of classical economic theory. In order to patch up the gap between classical economics and reality, institutional economics scholars revised mechanical theoreticalism and introduced the concept of institution into economic theory (Douglas North, 2002). North (1994) believes that an institution is a rule that can constrain or motivate a series of behaviors in social life, including formal institutions and informal institutions. Formal system refers to a series of code of conduct stipulated in the form of legal provisions in society, which has a clear guiding and normative role in the behavior of people or groups; informal system refers to behavioral habits gradually formed in society. Supported by factors such as values, beliefs, cultural traditions, etc. In North's dichotomy theory, institutional distance mainly refers to formal institutional distance, and cultural distance refers to informal institutional distance.

### 3.2 *Research on the Influence of Institutional Distance and Cultural Distance on International Trade*

Me'on & Sekkat (2008) divided products into manufactured products and non-manufactured

products, and studied the impact of different systems on the export of different products. Finally, it is found that the export value of a country's manufactured goods is significantly positively related to the country's institutional differences, while the export value of non-manufactured goods is significantly negatively related to the country's institutional differences.

Chen Lili and Gong Jing (2014) studied the relationship between institutional factors and bilateral service trade based on panel data of bilateral service trade flows between 49 countries. The results showed that the institutional distance between the two countries is not conducive to the development of bilateral service trade.

Studies such as Bojnec & Ferto (2015) show that institutional differences have a significant negative impact on the bilateral trade scale of agricultural products.

Liu, AL, et al. (2020) found through their findings that institutional distance has a significant negative impact on China's foreign trade, and institutional distance has a greater impact on China's trade with countries along the "Belt and Road" than cultural distance.

### 3.3 *Method and Empirical Research on the Influence of Institutional Distance and Cultural Distance on International Trade*

Liu Dexue and Sun Bowen (2019) constructed an econometric model based on the cross-country panel data of 81 countries from 1995 to 2014 through a classical gravity model and added variables that reflect bilateral institutional differences, and conducted empirical test analysis. The data source is mainly from the Index of Economic Freedom database released by the World Heritage Foundation, which includes the institutional quality of 81 countries in 20 years from 1995 to 2014. The data includes a total of 13 specific indicators, including law enforcement, government size, regulatory effectiveness, market opening, and overall institutional level, which are scored from 0 to 100, covering almost all the connotations of economic institutions. The empirical results are mainly carried out through basic regression and endogenous processing, and the mechanism analysis of the influence of institutional distance on trade development is

carried out through the mediation effect model, estimated results and correlation tests. The study finally concluded that through the narrowing of economic institutional distance, a certain degree of trade costs will be reduced, and trade freedom will be improved, so that the negative impact of economic institutional distance on bilateral trade will also be reduced.

In the context of global integration, Jingjing Huang (2015) discusses the impact of institutional environment differences in different dimensions on the adoption of customer engagement strategies by companies from the perspective of institutional theory and uncertainty management, and then on the long-term multinational business performance of companies. The data source mainly comes from the questionnaire survey on the heads of multinational enterprises and business projects. Jingjing Huang (2015) theoretically used a combination of literature research and deductive derivation to construct different aspects of the uncertainty of transnational operations under the influence of institutional distance. The method of factor analysis is used to test the reliability and validity of the data, and then the descriptive statistical analysis method is used to preliminarily organize and analyze the research data, using the hierarchical regression analysis method to test.

In the context of ongoing Sino-US trade frictions, and cultural differences between countries have become an important factor affecting international trade, Xi Jiancheng and Wang Lujian (2021) empirically test China and other countries through integrated panel data from 2008 to 2017. The impact mechanism and effect of national cultural heterogeneity on manufacturing exports. The research question of this paper is mainly to study the mechanism and effect of cultural heterogeneity affecting manufacturing exports. By theoretically constructing an analytical framework of cultural heterogeneity affecting international trade, it examines the impact of cultural heterogeneity on international trade. In addition, the application of digital technology is included in the study of the impact of cultural heterogeneity on international trade, which expands the theoretical understanding of the impact of culture on trade. The data sources are the United Nations Commodity Trade Statistics Database (UN

Comtrade, World Bank World Governance Index (WGI), World Bank World Development Index (WDI), etc. The study concludes that cultural heterogeneity helps to increase the scale of manufacturing exports, but the application of digital technology weakens the positive effect on manufacturing exports.

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