

**THE DYNAMISM OF *GUANXI* IN COMPANY PERFORMANCE  
IN CHINA**

By

Irene Y.M. Yeung  
B.A., University of Windsor, 1986

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## APPROVAL

Name: Irene Y.M. Yeung  
Degree: Master of Business Administration  
Title of Thesis: The Dynamism of *Guanxi* on Company Performance in China

Committee Chair: Dr. Mark Wexler  
Professor  
Faculty of Business Administration  
Simon Fraser University

Supervisory Committee:

---

Dr. Rosalie L. Tung  
Senior Supervisor  
Professor  
Faculty of Business Administration  
Simon Fraser University

---

Dr. Carolyn P. Egri  
Assistant Professor  
Faculty of Business Administration  
Simon Fraser University

---

Dr. Patricia M. Howard  
Associate Professor  
School of Communication  
Simon Fraser University

Date Approved: July 5 '95

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**Author:** \_\_\_\_\_  
(signature)

IRENE YEUNG  
(name)

JULY 26, 1995  
(date)

## EXECUTIVE SUMMARY

The objective of the current research study was to assess the impact of *guanxi* (personal connection) on company performance in China. It also aimed at formulating a strategy which would enhance business success through the practice of *guanxi*.

The research was conducted in both Canada and Hong Kong. The executives of nineteen Chinese and non-Chinese companies were invited to participate in the qualitative research study. Personal interview was conducted with each respondent to solicit his/her mentality on the *guanxi* construct.

### Research Findings

Although *guanxi* has been cited by the literature and business practitioners in China trade as a key success factor, it is revealed that *guanxi* is only a necessary condition for entering the China market, but insufficient for ensuring long-term business success for investors. The preliminary role of *guanxi* is confined to exploring business opportunities and opening channels for investors in China when they first enter the market, because the local Chinese are too conservative to have business with outsiders. At the mature stage of business establishment, technical competitiveness takes precedence over *guanxi* in gaining long-term business success for investors.

In establishing *guanxi* relations, it is found that achieved *guanxi* bases function equally well for investors in establishing *guanxi* relations. That is, investors can utilize hired intermediaries as the initial step to establish *guanxi*, since they are newcomers to the Chinese society. But investors should aim at entangling into the *guanxi* networks of the Chinese so that more common attributes can be cultivated through continuous interaction, and to strengthen their *guanxi* with the local Chinese.

In *guanxi* maintenance, it is disclosed that offering short-term gains is a strategy which is essential in the initial stage of *guanxi* building in order to gain a chance for *guanxi* establishment. However, it is inadequate in nurturing stable and strong *guanxi* ties, due to its incapability to fulfill the perpetual instrumental function of *guanxi* and to nourish particularistic ties with the Chinese. It is proposed that nurturing long-term mutual benefits, cultivating personal relationship, building trust and tendering favors are the four collaborative successful *guanxi* building techniques which can cultivate strong *guanxi* relations. The integrated approach is underlined by the five fundamental dimensions of *guanxi*. They are instrumentalism, personal relations, trust, reciprocity and longevity.

It is highlighted that *guanxi* ties have to be both relevant and effective. Building weak *guanxi* relations with appropriate authorities or cultivating strong *guanxi* ties with irrelevant

parties are equally deficient, since they cannot elicit the desirable *guanxi* benefits embodied in good *guanxi* relations.

Investors are advised to incorporate a long-term perspective when considering China business requests. Profit-making will only be realized in the long-term balance sheet rather than for individual business transactions. This is because the favors tendered today will incur immediate loss but they will provide handsome rewards in future since the Chinese tend to reciprocate. The reciprocation entails an accumulation of *renqing* which will be at the disposal of investors when they are in hard times in future.

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# CHAPTER 1

## INTRODUCTION

### 1.1 THE PROMINENCE OF *GUANXI* IN CHINA

China, since the embarkment of Open Door Policy in 1978, has emerged as an awakening giant on the Asian horizons. It thundered the world by its super economic performance of 12.5% GNP growth rate in 1992, as compared to the 4-6% growth rate of the Four Asian Tigers. (World Bank 1992) Being perceived as a golden opportunity for success, China has become the target for business expansion by foreign powers. However, failures have been reported by non-Chinese firms that have tried to establish a foothold in the oriental market. One of the most cited reasons for frustration is the lack of *guanxi* in China.

*Guanxi*<sup>1</sup> (connections 關係), a general term for social networking in China, is pivotal at all levels of societal functioning and in all kinds of dealings in the oriental country, be they social, business or political. *Guanxi, renqing*<sup>2</sup> (human feelings 人情)

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<sup>1</sup> The transliteration system used in this thesis is in accordance with the pin-yin system which follows the Beijing pronunciation of standard Northern Chinese. The four key Chinese terms (relations, human feelings, face and reciprocity) are translated as "*guanxi*", "*renqing*", "*mianzi*" and "*bao*" respectively.

<sup>2</sup> There is no unified English translation of "*renqing*". Some use its literal meaning and label it as "human feelings". (Gold 1985, L.S. Yang 1957, M. Yang 1994) Some stress its sentimental component and translate it as "affection". (Chu & Ju 1993, Jacobs 1979) Others emphasize its social element and put it as "human obligation" (Chu & Ju 1993, King 1991) or "favor". (Hwang 1987) The diversified translations reflect the very fact that there is no single English word which captures the rich meaning of "*renqing*". The different translations mentioned above are the various dimensions of the Chinese concept "*renqing*". For more in-depth explanation, please refer to the section on "Rule of *Renqing*" under "Operating Concepts of *Guanxi*".

In this thesis, the translation based on the literal meaning (human feelings) is used in order to avoid making bias against any specific dimension of *renqing*.

and *mianzi* (face 面子), are regarded as key building blocks of the Chinese culture. The three elements are viewed by anthropologists and sociologists as fundamental sociocultural concepts which shape the social behavior and cognitive thinking of the Chinese (King 1991).

The significance of *guanxi* was revealed in a comprehensive study by Chu and Ju (1993) conducted in mainland China in 1988. Its research target was the local Chinese in Shanghai and Qingpu (a rural county outside Shanghai). Both urbanities and rural dwellers were invited to participate in the research. Of the 2000 respondents, an overwhelming majority (92.4%) confirmed the importance of social connections in daily living. Only 7.5% negated its significance. It was found that younger people placed greater emphasis on *guanxi* than older folks. Forty-six percent of young people believed in the importance of *guanxi*, as compared to only 35.1% of the latter group. *Guanxi* is so prominent in China that it leads scholars to term the arts of establishing and managing *guanxi* as "*guanxixue*", (relationology 關係學) (Gold 1985, King 1991), or the "Chinese gift economy" (Yang 1989, 1994).

In the business arena, there is a well-accepted 'motto' among non-Chinese investors in China: "Whom you know counts more than what you know." It implies that how well one is connected is of utmost importance because *guanxi* determines the success of business negotiations in China. It is not only the products that make the deal, but also the relationship (de Keijer 1992). In a qualitative study by Ai (1994), it was discovered that Canadian companies which had developed good connections with Chinese local parties achieved higher levels of business performance than firms which had not. It is often assumed by the Chinese that foreigners who do not establish *guanxi* with local parties are not serious about doing business in China, and these foreigners will be facing greater difficulties in their Chinese business operations (Griffiths 1986).

The impact of *guanxi* is also apparent in Chinese politics. As Lucian Pye has commented, *guanxi* is the "key ingredient of faction" (Pye 1992: 213). This is echoed in

Jacobs' study of *guanxi* in Taiwanese political alliances. In this study, the *guanxi* pattern observed among overseas Chinese in Taiwan closely resembled that in mainland China. It was found that *guanxi* played an important role in voting patterns, as the vast majority of votes were cast on the basis of *guanxi* (Jacobs 1979). Similar research findings were supported in another study by Bosco (1992) which postulated that factional leadership and mobilization were contingent upon *guanxi*.

## 1.2 DE-EMPHASIS ON *GUANXI* IN RESEARCH

Ironically, despite its importance in societal functioning and business success in China (Campbell 1989, de Keijer 1992, Frankenstein 1991, King 1991, Pye 1992, Yam 1993), little attention has been given to *guanxi* by both business and social researchers. Prior to 1994, no empirical study had examined the relationship between *guanxi* and business performance. Instead, some attempts had been made to investigate "*guanxi*" in relation to overseas Chinese politics in Taiwan, in the hope that these investigations of related concepts would reveal some hidden facets of the "*guanxi*" construct (Bosco 1992, Jacobs 1979, Pillsbury 1978).

Chu and Ju (1993) conducted a comprehensive study to explore the different aspects of the Chinese culture with one focus on *guanxi*. However, this study did not make any in-depth analysis of the construct. Since the study was not conducted in a business context, but used a purely sociological perspective, no correlation was made between *guanxi* and business operations. Such a correlation was first made in Ai's (1994) study which touched on the relationship between *guanxi* and business performance. Yet, the researcher did not operationalize the *guanxi* construct since the focus of the study was on examining the overall business strategies in China, therefore the specificity of *guanxi* still remained unknown. For instance, will *guanxi* be more influential in specific types of industries? Or at specific investment locations?

The first research study which undertook to investigate primarily the concept of *guanxi* was conducted by K. Xin and J.L. Pearce in 1992 (Xin & Pearce 1994). Executives of thirty-two local companies in China were interviewed. Interviewees were requested to identify 8 to 10 business connections that were most helpful to them in solving business problems. They were asked to evaluate each *guanxi* relation on five different dimensions. Research findings were as follows:

1. *Guanxi* relations were important to interviewees in doing business in China.
2. Interviewees asserted that *guanxi* relations were useful as a defense against threats.
3. They disagreed that *guanxi* building was based on gift giving.
4. They confirmed that trust was an essential element in *guanxi* building.
5. They agreed that *guanxi* relations were more social than work related.

This study was an initial attempt to explore the hidden dimensions of *guanxi*. However, as acknowledged by the two researchers, the study was small and preliminary. It neither provided any sound psychometric measures of the *guanxi* construct, nor gathered any data on the relationship between company performance and *guanxi*. More methodologically vigorous research is required to explore the dynamics of *guanxi* and its impact on business performance.

The neglect of *guanxi* by researchers is attributable to four types of obstacles in exploring the Chinese construct:

1. Hurdles in data collection

Enormous difficulties exist in obtaining adequate data for empirical research in China for two reasons. First, China had not been opened to the outside world until 1978. Non-Chinese researchers did not have any opportunity to observe Chinese behavior before then (Jacobs 1979). Second, there is a severe lack of information for doing empirical research due to bad record keeping within China (Rhoads 1976).



## 2. Difficulties in cross-cultural understanding

Non-Chinese social scientists have a hard time in understanding the peculiar Chinese concepts underlying the *guanxi* construct (Jacobs 1979). In addition, *guanxi* is often condemned as a sordid form of favoritism and nepotism. Both non-Chinese and modern Chinese sociologists are reluctant to explore the 'inferior' construct. Hence, little explicit research has ever been done on the subject (Pye 1992).

## 3. Sensitivity of the research topic

Great difficulties have been encountered by researchers in soliciting data on *guanxi*, even when they have decided to explore the construct. This is because *guanxi* relations are regarded as a personal asset by the Chinese. They are reluctant to talk openly about *guanxi* relations to someone whom they do not trust, especially when it involves questionable payment. The high sensitivity of the subject hinders the collection of valid and reliable data and reduces the success of the study (Xin & Pearce 1994).

## 4. Under-development of social research

Although China has been opened to the West since 1978, the development of social research is in its infancy after the long seclusion. As a result, there is a lack of research skills to conduct in-depth explorations of complex social constructs (Fox 1987).

In view of the ignorance regarding *guanxi* and its potential impact on business operations, this thesis has three objectives:

1. To explore the nature of *guanxi* and its underlying concepts;
2. To examine its impact on business performance;
3. To formulate a strategy to enhance business success through the practice of *guanxi*.

The forthcoming exploration is divided into five parts. It starts with a review of the literature with special emphasis on the nature of *guanxi* and the art of *guanxi*. It is followed by the proposed research model and hypotheses. Research design and methodologies are documented in the next chapter. The research findings and discussion are segmented into

five different respects, namely, the relative importance of *guanxi* in attaining long-term business success in China; *guanxi* establishment; hidden dimensions of *guanxi* and ways of *guanxi* maintenance; the relative importance of five factors in the dilemma of *renqing*; and *guanxi* networking. The research exploration is ended with managerial implications and conclusions.

## CHAPTER 2

### NATURE OF *GUANXI*

To understand the impact of *guanxi* on China, one needs to first comprehend the nature of *guanxi*. What is *guanxi*? What are its key characteristics? How has it evolved in China? How is it different from social relations in Euro-centric cultures? This chapter is devoted to examining the different facets of *guanxi* in order to answer the above questions.

#### 2.1 IDENTITY OF *GUANXI*

*Guanxi* is a term loosely describing social relations in China. According to *Shu* (1947), the Chinese meaning of "*guan*" is either "to connect" or "a gate/pass that can be closed" (Yang 1994:49). "To connect" is to build a linkage between two independent individuals. "To make a gate" is the ability of individuals to control the in-flows and out-flows of their substance (e.g., possessions, time or efforts) in social transactions. Consequently, "*guanxi*" implies the social relations that enable individuals to make transactions in their favour.

Strictly speaking, *guanxi* does not represent all kinds of social relations in China. It is restricted to only a certain type of connections. Two schools of thought have developed regarding the type of relations that *guanxi* denotes. They are the discrete nature school and the mixed quality school. Both schools of thought admit that there are different types of social relations in the Chinese society<sup>3</sup>. The school of discrete nature suggests that the

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<sup>3</sup> "The Chinese society" is a general term which may denote any societies that are dominated by Chinese inhabitants, e.g., Taiwan or Hong Kong. Since the scope of the research study is mainly on China, thus the meaning of the term is restricted to the community in mainland China. The same principle is applied to other similar terms in the thesis such as "the Chinese culture" or "the Chinese". They denote the traditional culture and the local nationals of mainland China respectively.

different categories are mutually exclusive and are independent of one another. Conversely, the supporters of the mixed quality school argue that the different types of relations are not discrete in nature; rather, they are fused with one another in reality (DeGlopper 1978, Hwang 1987, Jacobs 1979).

Ambrose King (1991), a reputable Chinese sociologist, is an advocate of the discrete nature school. He proposes that there are two distinct types of exchange relations, namely economic exchanges and social exchanges, and *guanxi* relations flourish in social exchanges.

### **2.1.1 Social Exchanges (Mixed Tie)**

According to King (1991), *guanxi* is embedded in social exchanges. The medium of transaction in this category is *renqing* which is similar to favors exchanged in Eurocentric cultures. The differentiating criterion between economic and social exchanges is the association with the donor. In Yang's (1989, 1994) terminology, an economic transaction is a commodity exchange which has a clear separation between the object transacted and the donor. It is an objective quantitative exchange of objects without any involvement of a qualitative dimension in the interaction. In contrast, a gift exchange (social exchange) is a qualitative relationship between the donor and the recipient. The transaction is governed by the quality of relation between the two parties involved rather than by the material utilities of the objects exchanged. Full ownership over the gift transacted is accomplished only when the recipient has repaid the social debt owed to the donor by the acceptance of the gift. Hence, a bond is developed between the parties through the medium of a gift (Yang 1989, 1994).

One prominent characteristic of social exchanges is unspecified obligations which do not detail the exact value of the transaction. Individuals may have expectations of reciprocated favors by others, yet they cannot bargain the timing, format and value of repayment. This is described by Hwang (1987) as the "dilemma of *renqing*".

In social exchanges, the operating guideline is the rule of *renqing* which delineates the obligation of helping members in the same social network when they are faced with difficulties. The incentive motivating individuals to fulfill the obligation is the anticipation of reciprocity. [More detailed discussion of *renqing* is given under the section on "Operating Concepts of *Guanxi*".]

King (1991) postulates that social exchanges are distinct from economic exchanges, and that the two categories are mutually exclusive. He argues that individuals try to discern the types of relations without mixing the constituent components of the two categories. For instance, in a study of rural China, villagers preferred making business transactions in a market town which was miles away rather than selling at front doors. This was because the relationship with buyers in the market town was impersonal and would not be fused with any qualitative element of social exchanges (King 1991).

Nevertheless, the proposition of the discrete nature of relations is subject to reconsideration based on the findings of DeGlopper's (1978) research. In his study of Lukang (a city on the west coast of Taiwan), it was discovered that people, ideally, preferred to have discrete categories of social connections such as business, kinship or neighborly relations. While each group had its own set of principles, satisfactions and problems, in reality, the different categories tended to fuse with one another to a certain extent (DeGlopper 1978). For example, personal relationships may exert the utmost influence in business transactions at the appropriate time.

In support of DeGlopper's argument, Hwang suggests that social exchanges based on *renqing* are, in fact, a mixture of two 'discrete' categories: the instrumental tie (economic exchange) and the expressive tie (Hwang 1987).

### **2.1.2 The Instrumental Tie (Economic Exchanges)**

In economic exchanges, there is a clear delineation of contract terms, costs and price values. The medium of transaction is monetary rewards or goods of equivalent value in the barter trade. The entire exchange process is characterized by a gain-loss calculation based on market rationality. It dictates that one should maximize one's profits/benefits with minimum cost. In the course of interaction, no emotional element is required (King 1980, Blau 1989).

Hwang (1987) asserts that economic exchanges which are defined by the instrumental tie adopt an equity rule for interaction. The equity rule suggests that individuals should be repaid in proportion to their own contribution. In order to achieve profit maximization, objective cost-benefit analysis is dominant in economic exchanges. Hence, the transaction is perceived as a means to attain personal goals and the relationship is basically temporary and unstable and will terminate when the transaction is over.

### **2.1.3 The Expressive Tie**

The expressive tie is a relationship that incorporates the "feelings of affection, warmth, safety and attachment" of the parties involved (Hwang 1987:949). The need rule is the operating guideline. It dictates that the need of others is the foremost consideration governing individuals' behavior. In contrast with the instrumental tie, the goal of establishing an expressive tie is the tie itself rather than a means to accomplish other goals. Consequently, the expressive tie is a permanent and stable social bond between individuals.

Hwang argues that social exchanges are combinations of both instrumental and expressive ties. He terms the integrated category as the "mixed tie", and defines it as "a relationship in which an individual seeks to influence other people by means of *renqing* (human feelings) and *mianzi* (face)" (Hwang 1987:952). As opposed to the instrumental tie which is a one-time transaction with a stranger, a long-term specific relationship will be

developed in the mixed tie. The personal element arises from the fact that both parties have to maintain the relation, and their behavior in the relation will influence the evaluation of them by others who are also in the same network. Yet, the affection component is never as strong as that in the expressive tie. The mixed tie will last only as long as the personal interests of both parties are satisfied in the relation.

Within the three categories (instrumental tie, expressive tie and mixed tie), the term "*guanxi*" seems to be applicable only to the mixed tie for three reasons. Firstly, the mixed tie is predominantly affected by the rule of *renqing*. As noted in the literature, *renqing* is an essential element of *guanxi* relations in China.

Secondly, in doing business in China, the *guanxi* relations between non-Chinese investors and local parties resemble the peculiarities of the mixed tie: specific and instrumental. *Guanxi* relations are specific because they will not be developed universally between any non-Chinese and local parties. The matching between two parties is contingent upon the congruence of their goals. Only those parties that have complementary goals will develop business relations. Both parties are willing to maintain the relations because of the expected mutual profits to be gained from business co-operation. This cultivates the particular and personal essence in the relations. However, *guanxi* relations will not be maintained if the personal interests of either party are not satisfied. Hence, the relations are, to certain extent, an instrumental tool to advance personal goals.

Thirdly, in Hwang's psychological model of *guanxi*, neither the instrumental nor the expressive tie embodies the essential elements of *guanxi*. The determinant of instrumental ties is market rationality which pays no attention to maintaining long-term relationships as required by *guanxi* relations. As for the expressive tie, the utilitarian consideration which is a primary feature of *guanxi* is reduced to a minimum. Consequently, it may be fair to say that *guanxi* is cherished only in the mixed tie.

If the above analysis is accepted as valid, then the focus of this research study should be on the mixed tie where *guanxi* is embedded. Thus, the scope of the following discussions and analyses will be confined only to this category, but not to the expressive and instrumental ties.

## 2.2 CHARACTERISTICS OF *GUANXI*

Many sociologists and anthropologists have attempted to define the nature of *guanxi*. Some qualify it as "particularistic ties" between individuals (Jacobs 1979, King 1980 & 1991, Parsons 1968), while others view it as a kind of social networking (Hwang 1987, King 1991, Liu 1993, Yang 1994). However, Chien Chiao, a Chinese anthropologist, argues that both propositions are inadequate to capture the full and complex meaning of *guanxi* in China. He defines *guanxi* as "a status in which a person(s) or an organization(s) interacts with another person(s) or organization(s), and in which they are mutually affected and enjoy mutual gains (Chiao 1982:345)".

Chiao proposes three different attributes that characterize the "*guanxi* status". The following is an attempt to define the different facets of the construct, based on Chiao's propositions.<sup>4</sup>

### 1. Ego-Centric Nature

Chiao (1982) suggests that *guanxi* is "ego-centric". This means that *guanxi* development is at the mercy of the ego of individuals. The ego is a part of individuals' conscious minds which controls their cognitive thinking and outward behavior. It identifies and initiates *guanxi* building with its selected targets. The ego maintains *guanxi* in the direction of attaining desired *guanxi* benefits. Consequently, the ego can

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<sup>4</sup> Because of different classification of attributes, the attributes listed in this thesis are slightly different from Chiao's original proposal.



be perceived as the "social engineer" of *guanxi* which dictates the growth of *guanxi* relations amongst individuals.

The attribute of the "ego-centric nature" embodies two different characteristics of *guanxi*, namely the voluntaristic ability and the particularistic value.

**Voluntaristic ability:** Individuals have the capability to build *guanxi* at their own discretion. In China, social relations can be classified into two types: in-born prescribed (e.g., father-son) and voluntarily constructed (e.g., friends). The voluntaristic ability of *guanxi* exhibits itself in the latter type, with the ego being the "architect" of any social relations beyond the realm of prescribed familial structure.

Indeed, the ego is at the heart of *guanxi* building, because it is the ego which defines the roles for individuals and which initiates social communication with others. It has prime control on the continuation of relations, since no relation can be maintained without the ego's consent. For instance, the ego of A identifies B as the supplier, and concludes that good *guanxi* relation has to be built with B, if A wants to have a stable supply of raw materials in his Chinese business operations. Hence, A starts to cultivate a connection with B. Yet, such *guanxi* relation can only be built if the ego of B allows it to develop. The relation will definitely collapse if B rejects A and closes off all communication channels. Consequently, *guanxi* building is "an ego-centered social engineering of relation building" (King 1991:79).

In constituting the voluntaristic ability of *guanxi*, a great deal of autonomy is attached to the ego in deciding with whom to associate and how to interact. This leads to the second characteristic of the ego-centric attribute: particularistic values.

**Particularistic values:** According to Parsons and Shils, particularistic values are defined as attributes that are "attached to objects by their particular relations to the actor's properties" (Blau 1989:266). Particularistic values, as opposed to universalistic standards<sup>5</sup>, are attributes that are specific and contingent upon the

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<sup>5</sup> Universalistic standards are general features that are common to all

relations amongst individuals. That is, the type or closeness of relationship between two individuals will govern their behavior towards each other, which will, in turn, either strengthen or weaken the relation. Hence, there is a mutual effect between individuals' relationship with and their behavior towards others. The better the relation between two individuals is, the more positive and rewarding the individuals' actions towards each other are, and hence the greater effect it has on strengthening the relation; or vice versa.

As observed by King (1991:76), *guanxi* relations in China are "a form of interpersonal relationship which is predominantly based on particularistic criteria." Pushing the point even further, Talcott Parsons (1968:551) argues that "the whole Chinese social structure accepted and sanctioned by the Confucian ethic was a predominately 'particularistic' structure of relationship." The above two propositions of *guanxi* are supported by many sociologists and anthropologists (Alston 1989, Chiao 1982, Jacobs 1979, King 1991, Parsons 1968, Pye 1992, Yang 1994). They highlight that *guanxi* relations are developed with specific individuals whom, for particular reasons, have been selected by the ego for further relationship development. This is a manifestation of the particularistic values.

The particularistic nature of *guanxi* is also supported by Clyde Mitchell's (1969) idea of personal networking.

## 2. **Personal Networking**

Clyde Mitchell suggests that "the point of anchorage of a network is usually taken to be some specified individual whose behavior the observer wishes to interpret" (King 1991:68). Thus, with whom a relation is developed is at the mercy of an individual's will. When two or more relations are formed around an individual, then a personal network is created. This network is an informal one based on personal

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people without giving special treatment to any particular persons.

relationships and mutual interests (Liu 1993). Its scope stretches far beyond the realm of formal organizational structure.

Personal networking is constituted by positioning the ego at the center, and around it are individuals with whom the ego has particular social ties (Hwang 1987, Yang 1994). This very pattern of personal networking is applicable to every person in the network. It means that each person has his/her own network of social relations, with the ego at the center and others on the periphery. This leads to the situation in which a large portion of an individual's personal network intersects the periphery of others' networks, thereby resulting in an extremely complicated and overlapping system of social relations.

The social network in China has been described as "*guanxi huan*" (關係環) by some scholars (Chiao 1982, Gold 1985). "*Huan*" is a Chinese word for a 'ring' or 'circle'. "*Guanxi huan*" is a network of *guanxi*, signifying a boundary within which individuals are bound together by social ties. The individuals circumscribed by the "*huan*" are called "*guanxihu*" (*guanxi* household 關係戶), since they frequently interact and are indebted to one another for favors as if they were members of a large family.

Despite the fact that indebtedness for favors is diffused to everyone in the *guanxi* network, the obligation to repay favors is embedded only in dyadic relationships, especially when a chain of favors is activated in which more than one intermediary is involved. For instance, A requests B to do a favor for C who intends to solve the problem for D who is, in fact, the final beneficiary in this chain of favors. In this case, B consents to commit the favor for A due to his/her personal tie with A, rather than the relationship with either C or D whom B may not even know. In turn, A seeks assistance from B because of his/her *guanxi* with C, but not with D. As a result of this chain of *guanxi* transactions, D is obliged to repay the favor to C who is indebted to A who owes the favor to B. The rationale is that the favor provided is based on the

personal *guanxi* between the requester and the resource allocator rather than on their relationships with the final beneficiary, who may be a stranger to both of them. Hence, because of the obligation to respond to the requests of *guanxihu*, the social networks of the requester's *guanxi* members are the resource base to accomplish tasks. However, the obligation to repay favors is confined to the immediate person in the chain to whom the request is made; and thereby it is embedded at a personal level. This has an important implication for *guanxi* development in the business field. No *guanxi* relations are established between corporate entities on a formal, unit-to-unit basis. Instead, *guanxi* is developed based on the personal tie between the representatives of corporate entities. As one of the respondents in Yang's field study commented, "when the personal relationship between representatives of two units deteriorates, ....., then the two units can no longer have anything to do with each other" (Yang 1994:105).

Indeed, individuals are embedded in webs of social relations which have become an essential part of their lives. The social webs are embroidered with two features: connective essence and pluralistic identifications.

**Connective essence:** There is a great fluidity of *guanxi* networking in China. The social web of relations is highly expansive due to the connective essence of *guanxi*. Two *guanxi* networks can be easily blurred together by a person familiar to both sides. For example, B is introduced to A by Z who is a friend of both parties. The introduction leads to two immediate effects on *guanxi* networking. B who was formerly an outsider of A's social network is now located inside it. At the same time, A also becomes part of B's social network as well. The effect of the relationship between A and B is to interlink their respective social webs. In this case, A indirectly becomes a 'friend' of C who is situated in B's social network. This means that A is associated with every individual inside B's social web, and A himself becomes a part of these individuals' networks. Consequently, the networks of A, B, C and many

others are inter-connected thereby constituting a very complex, indistinguishable social web (Chiao 1982).

According to Liang (1989), there is no definite boundary for each *guanxi* network, since the group boundary is infinitely flexible and expandable because of the connective essence. Liu Pin-yen, a reputable Chinese scholar, has written a vivid description of the *guanxi* network. "If you touch a person, it will unexpectedly affect a large number of persons.... There are complicated and overlapping relations between and among people, weaving a thick and tight social web" (King 1991:64).

With the connective essence of *guanxi* networks, individuals often have pluralistic identifications.

**Pluralistic identifications:** This is the identification of individuals with multiple groupings. As individuals are integrated with several different networks, their social webs are exponentially enlarged. The integration enables them to be located at a more advantageous position for personal gains, since more individuals are now at their disposal in the expanded network. Pluralistic identifications with multiple groups are perceived as a means to increase individuals' resources for personal interests, because of the requirement of mutual obligation in *guanxi* system.

### 3. **Mutual Obligations**

The *guanxi* network is interdependent in nature. When individuals are integrated into the web, they are socially obliged to respond to the requests of members in the same network. *Guanxi* connotes a commitment of involved parties to the relations; that is, they are supposed to share their resources and are obliged to help one another in an unlimited manner (Alston 1989, King 1980 & 1991, Pye 1982 & 1992, Yang 1994). As Lucian Pye claims, "each can tax the other and expect automatic special consideration" (Pye 1982:89).

Nevertheless, the unlimited demands are reciprocal. *Guanxi* rules that anyone who fails to return favors will be condemned as untrustworthy and will lose his/her reputation in all connected networks (Alston 1989, Blau 1989). When individuals give 'special consideration' to others, they are making 'social investments' in *guanxi* relations. These investments will yield proportionate returns in the future. The idea of social investment implies the quantitative value and instrumental flavor of *guanxi*.

**Quantitative value:** *Guanxi* relations have high quantitative value, in terms of the number of favors provided and the degree of difficulty involved. According to King (1980), there is a balance sheet of social investments in the minds of individuals. Its objective is to keep an account of the ins and outs of social investments, so that individuals will not be socially indebted to others. However, it is hard to maintain a balance in social exchanges because reciprocated actions always elicit unbalanced status. Consequently, the balance sheet, in fact, involves perpetual entries of social transactions among individuals, and the *guanxi* network is by nature "unlimited exchanges of favors" (Pye 1982). It gains the reputation of being the "Chinese gift economy" which consists of "personal exchanges and circulation of gifts, favors and banquets" (Yang 1989:35). The gift exchanges are mainly for the pursuit of calculated social ends of individuals. This highlights the instrumental flavor of *guanxi*.

**Instrumental flavor:** The objective of complex networking in *guanxi* is to have mutual gains. Chiao (1982) proposes that the construction of *guanxi* is mainly to fulfill utilitarian objectives. The instrumental nature of *guanxi* is confirmed by Alston (1989), Chu & Ju (1993), Gold (1985), Hwang (1987), King (1991), Liu (1993), Pye (1982 & 1992) and Yang (1989, 1994).

In Chu and Ju's study (1993), it was revealed that 71.7% of respondents voted for utilizing *guanxi* connections as the preferred means to advance personal interests or to handle problems. Only 19.6% opted for following normal bureaucratic channels which were assumed to be more inefficient in problem solving. In Yang's field study,

her respondents revealed that "*guanxixue* is using people." (Yang 1994:51) They admitted that *guanxi* relations were built primarily on self-interest. They would terminate the relations with those *guanxihu* (*guanxi* households) in whom they have lost utilitarian interests.

The pragmatic interests can be career advancement, access to scarce resources, or permission for restricted privileges. These goals will be more easily attained if individuals have built *guanxi* with authorities that have such resources at their disposal. In return, individuals will provide favors in other forms. Hence, the relationship is sustained by continuous advancement of personal gains for both parties.

The utilitarian emphasis in *guanxi* overshadows any emotional element fostered in the relations. The *guanxi* network will collapse and the relationship will wither if there is no mutual gain for involved parties. One factor leading to such a desperate situation is refusal or inability to return favors. The bond among individuals will then be weakened and the web will disintegrate if nothing remedial is done.

#### 4. **Dynamism**

The last major attribute of *guanxi* is dynamism. Chiao (1982) suggests that *guanxi* relations have to be sustained through continuous interaction between parties. The relationship should not be static. It should always be under constant reinforcement so that it can be kept alive and useful. Accordingly, it is a long-term nurturing process requiring enormous patience and time. This goes hand in hand with the long-term orientation of the Chinese.

**Longevity:** There is a Chinese saying: "Time will reveal the heart of the person." Relationships have a longevity dimension in the Chinese culture. As a manifestation of this long-term orientation, *guanxi* takes years to build and consolidate. The potential of certain *guanxi* may not surface in immediate future, but it may be of great use in the years to come.

In this fashion, every *guanxi* relationship is perceived by the Chinese as a 'stock' to be put away in times of peace. The 'stock' will then be at their disposal in times of trouble.

Ego-centricity, personal networking, mutual obligations and dynamism are the four cardinal features of *guanxi* relations. They function in collaboration to promote the unique characteristics of *guanxi* in China.

*Guanxi* is a social engineering of relations governed by the ego of individuals. Very often, individuals exercise the voluntaristic ability to build *guanxi* ties with particular others who are beyond the realm of prescribed familial structure. They select specific individuals with whom they want to associate.

As two individuals are connected, the social networks of their *guanxihu* are integrated as well because of the connective essence of *guanxi*. It contributes to the formation of indistinguishable, complex personal networks. The intricate *guanxi* networking will be maintained until individuals voluntarily detach themselves from the entangling social webs. However, in China, individuals would seldom take this approach due to the great implication brought by mutual obligation.

The rule dictates that individuals are obliged to respond to the requests of members in the same *guanxi* network. Hence, the entanglement of social webs of various *guanxihu* is, in fact, an enlargement of the resource base for individuals to mobilize resources such that more *guanxihu* are now at their disposal in the expanded network to fulfill their interests. Breaking a relationship with an individual does not only mean the loss of *guanxi* tie with that particular person, it entails a cutoff with the person's *guanxihu* as well. This leads to a great shrinkage of one's own *guanxi* network, together with a reduction of resource base for the individuals involved.

As a result, one can conclude that individuals have the voluntaristic ability to choose with whom they desire to have *guanxi*. But when they consent to be in the *guanxi*



network, they have to comply with the rule of mutual obligation and be responsive to the requests of their *guanxihu*. Compliance will bring them substantial benefits which fulfill the instrumental function of *guanxi*. The pragmatic gains earned is one of the main objectives for individuals to engage in complex *guanxi* networks. Individuals often identify themselves with multiple groupings because pluralistic identifications are perceived as a means to increase the individuals' resources for personal gains.

In addition to instrumental benefits, *guanxi* relations are dynamic and need to be nourished by continuous interaction among *guanxi* members. Constant reinforcement is a manifestation of the longevity of *guanxi*, as it takes prolonged time to consolidate relationships with the Chinese.

These four unique characteristics of *guanxi* originate from the idiosyncratic environment in which the Chinese culture is nurtured. Further, these idiosyncrasies are a function of Confucianism which is the root of the *guanxi* system.

## **2.3 ORIGIN AND BUILDING CONCEPTS OF GUANXI**

According to S.M. Liang, a reputable Chinese scholar adept in Chinese culture, a culture owes its origin to the ideology of the nation which governs its orientation. In China, it is Confucianism; in Euro-centric cultures, it is Judeo-Christian ideology. The two different ideologies dictate two opposite directions of the two cultures: role relations and familism in China, individuality and team orientation in Euro-centric cultures. (Liang 1989, Yang 1994)

### **2.3.1 Role Relations and Familism in Confucianism**

#### **2.3.1.1 Role Relations**

Confucianism has been the predominant ideology governing the cognitive thinking and the moral values of the Chinese for over three thousand years. Its fundamental

objective is to achieve harmony through maintaining a differentiated but complementary order instituted by "Heaven" (i.e. the omnipotent Creator) (King 1980 & 1991, Liang 1989, Parsons 1968, Yang 1994). The graded social order is the framework for societal functioning in the Confucian world. Hence, the duty of a man is to accept and preserve the harmonious equilibrium, as the Confucian philosophy stipulates a "dignified adaptation to a tradition order" (Parsons 1968:548).

Being in a society presided over by hierarchical order, Confucianism views that individuals, instead of being isolated discrete entities, are living in a world of relational construction. The strand of relations associates individuals to their surrounding environment in an orderly fashion which constitutes the harmony of the universe. Its aim is to prevent any disturbance to the prescribed order by observing moral ethics which delineate the hierarchical relations and their associated duties that a righteous man should abide by. This is the "*wu-lun*" ( 五倫 ).

"*Lun*" means differentiated ethics or graded relations. "*Wu-lun*" means the five cardinal hierarchical relations in Confucianism. They are father-son, husband-wife, brother-brother, friend-friend and ruler-subject. Each *lun* carries with it a set of moral claims and ethics. This has two implications: hierarchical differentiation and a particular kind of relations established between individuals. That is, the kind of relations individuals have with particular others will lock them into a specific hierarchical status which defines their social roles and moral obligations in the relations. For instance, individuals should be loyal to their ruler; and a son should have filial piety for his father.

In this fashion, the essence of Confucianism is role relations and obligations amongst individuals. Once the kinds of relations have been determined, the role obligations are then clear, and individuals should act accordingly (King 1980 & 1991, Liang 1989, Parsons 1968). Confucianism stipulates that personal identity is established by individuals' interaction with others around them. It focuses on the relations amongst individuals rather than on the individuals themselves (Liang 1989, King 1980 & 1991,

Parsons 1968, Yang 1989). As Parsons (1968:547) has commented: "Confucius conceived the whole of society as a network of such personal relationships and his injunction to each was to see that his conduct was right in his own relationships." This concept has laid the foundation for the obligatory character of today's *guanxi* system.

The contemporary *guanxi* network is, in fact, a system of indebtedness and obligations through role relations. The role of a member of the *guanxi* network is to observe the relations with other in-group members and to fulfill obligations by responding to their requests. Such obligatory requirements may sound alien to non-Chinese who have been educated in Euro-centric cultures which emphasizes individuality rather than role relations. Yet, role obligations may provide a clue for non-Chinese who want to survive in the *guanxi* system of China.

In addition, Confucianism also provides an impetus for the accentuation of insider/outsider identity in *guanxi* and its overwhelming attention to familism.

#### 2.3.1.2 Familism

Among the *wu-lun* (five cardinal relations), special emphasis is placed on family, since three of them are concerned with familial relationships. There is a Chinese saying reflecting a hierarchy of goals to be achieved by a hero: "Settle the family, govern the nation and conquer the universe." This indicates the relative importance of family before the nation and the universe in the Chinese culture. The family has been the basic survival unit in the Chinese society leading some to comment that China is based on "utilitarian familism" (Redding 1990). The prominence of family stems from two aspects of the Chinese culture. The first is the stress on relations in Confucian teachings. In old China, life was centered around the family. It was the seeding bed where individuals were nourished and where they spent most of their time. Throughout their lives, individuals interacted mostly with family members and relatives. Therefore, the dominant type of relations for individuals was familial.

The second aspect of Chinese culture is the relative absence of the "society" concept. The concept of "society" or "community" is foreign to the Chinese culture (Liang 1989, Liu 1993, Redding 1990, Yang 1994). As opposed to Euro-centric cultures which stress community life, the Chinese shift their attention towards familial dependence. The Chinese society is conceived of as comprised of various families rather than countless individuals. The family is viewed by the Chinese as a shelter where individuals can share family abundance and be protected from outside fluctuations. Hence, the family has been termed "the walled castle" (Liu 1993).

With the overwhelming stress on familial structure, the family displays a high degree of collective solidarity that is impermeable by outsiders. The familial identity creates a common solidarity and integrative ties that unify family members to varying degrees. Hence, the social matrix of Chinese society can be perceived as a set of concentric circles (Redding 1990, Yang 1994). Situated at the core is the family with which the individual is significantly identified. Surrounding the core is the lineage group which is perceived as an extension of the family. On the periphery are non-family members who fulfill special needs for the individual, e.g. his/her teacher. The more distant the circles, the weaker are the ties, and the fewer are the role obligations that will be assumed.

Anyone who lies outside these circles will be treated as an intruder if he/she approaches the concentric premises. Interaction with out-group members is generally filled with suspicion and fear. There is no role requirement assigned for out-group members, since they are not locked into any status within the hierarchical system. In contrast, interaction with in-group members within the circles is bathed in trust and sharing. At the same time, in-group members have to fulfill role obligations. Consequently, the identity of being an in-group or out-group member profoundly influences interactions amongst individuals.

Given the peculiar social matrix of the Chinese and the salience of in-group and out-group identity, non-Chinese (who want to achieve business success in China) have the

challenge of shedding the label of "outsiders" in order to be embraced into at least the outer circle of the social matrix. Inclusion will not only enable non-Chinese to be perceived as part of the 'big family', it will also require them to assume role obligations in the hierarchical system, thereby enabling them to enjoy the abundance of the *guanxi* network.

### **2.3.2 Individuality / Team Orientation in Judeo-Christian Ideology**

In contrast to the relational construction of persons in China, the Euro-centric cultures stress individuality and team orientation which are deeply rooted in Judeo-Christian ideology. Three aspects of the Judeo-Christian religion constitute an environment that is not appropriate for the nourishment of the *guanxi* system in the Chinese mode (Liang 1989, Yang 1994).

#### **1. Individuality**

Judeo-Christian ideology views every individual as a discrete and complete entity who is independent of each other. Compared to the Chinese, individuals in the Euro-centric cultures prefer more autonomy and less interference from others in their lives. Hence, there is a greater focus on individuals rather than role relations and moral obligations as is the case of the Chinese culture.

#### **2. Team Orientation**

One of the main ordinances of Judeo-Christian ideology is "Love thy neighbor as thyself" (Matthew 22:39). In the Judeo-Christian world, everyone is supposed to be brother or sister to others. There is no dividing line between individuals, collective groups, or nations; thus there is no in-group/out-group identity. This is detrimental to the breeding of *guanxi* relations. The ordinance collapses the boundary of the "walled castle". The familial identity is extended universally to everyone, such that individuals are strongly identified with the community. This furnishes an impetus for the team orientation in Euro-centric cultures.

### 3. Revolutionary force

Judeo-Christian ideology declares that God is the absolute truth. He is above the universe. Any human worldly order is inflicted with defects and thus should be overthrown to prepare for the coming of the Kingdom of God on Earth. Hence, Judeo-Christian ideology represents a revolutionary force to the imperfect worldly order, rather than a mere acceptance of prescribed order as Confucianism does (Parsons 1968).

The differences between the Chinese and Euro-centric cultures stem from the different orientations imposed by these two ideologies. As guided by Confucianism, the Chinese culture focuses on role relations, thus the society is "*guanxi benwei*" (relation-based 關係本位). In contrast, Euro-centric societies are governed by Judeo-Christian ideology. Revolving around individual autonomy and team orientation, Euro-centric societies are "*geren benwei*" (individual-based 個人本位) or "*shehui benwei*" (society-based 社會本位). According to Liang (1989), these different orientations are two sides of the same coin. With the de-emphasized role of family, individual identity and team orientation gain dominance in Euro-centric cultures. On the other side of the coin is Chinese culture's over-emphasis on familial structure which overshadows the functions of individuality and team orientation.

Figure 1: A Comparison on the Focus Between the Chinese and the Euro-Centric Cultures.

(Source: S.M. Liang, The Essential Features of Chinese Culture. Hong Kong: Joint Publishing (H.K.) Co. Ltd., 1989, pp. 78.)



- Note:
- 1) The size of labels indicate the importance of elements in respective cultures.
  - 2) The arrow represents the direction of influence and relationship.
  - 3) The dotted line denotes a weaker relationship and influence.

The overwhelming focuses on role relations and familism in Confucianism constitute the origin of *guanxi*. However, the smooth functioning of *guanxi* relies on four other operating concepts in Confucian philosophy.

## 2.4 OPERATING CONCEPTS OF *GUANXI*

The operation of *guanxi* rests upon four concepts in Confucianism, namely the notion of *shu* (forgiveness), the norm of *bao* (reciprocity), and the rule of *renqing* (human feelings) which embraces the principle of *li* (ethics).

#### 2.4.1 Notion of *Shu* (Forgiveness 恕, )

The Confucian norm of interpersonal relationships begins with the notion of *shu*. Some scholars translate "*shu*" as "forgiveness" (Yang 1957, Hwang 1987). However, it seems that "forgiveness" cannot fully capture the deep meaning of *shu*. The essence of *shu* is "Do not do unto others that which you would not wish done unto you. Do unto others as you wish done unto yourself." This is equivalent to the Golden Rule of "Do unto others as you would have them do unto you." The highest ideal of *shu* is to merge one's individual identity with that of others, so that people will treat others the same as they would treat themselves. This would contribute to the attainment of personal harmony which is the objective of Confucianism. Forgiveness is only one aspect of *shu* which describes how individuals should respond to the mistreatment by others.

Embedded in the notion of *shu* is the norm of *bao* which serves as a safeguard against *guanxi* abuse.

#### 2.4.2 Norm of *Bao* (Reciprocity 報 )

According to Mauss (1967), there are three kinds of obligations in social exchanges. They are the obligations to give, to receive and to repay (King 1980). This is the core meaning of *bao* (reciprocity) which stipulates that individuals should return what other fellow members have given to them, both positive and negative. The rationale for such reciprocal actions is the belief that there is a cause-and-effect relationship (Yang 1957, Yang 1994). It is anticipated that individuals will receive returned favors equivalent to the favors they have done for others, or they will suffer revenge when they have tricked or mistreated others. This is dictated by the notion of *shu*, because everyone should treat others as if one was treating oneself. In addition, individuals dislike being indebted to others in social transactions, so there is a tendency towards reciprocity (Blau 1989).

Favors bestowed in social transactions are identified as "social investments" since a handsome rate of return is expected (Gold 1985, Yang 1957). As the term "investments"



implies, favors may not be responded to immediately, repayment may be postponed until some future time. Temporary indebtedness is tolerable in the Chinese culture because of the long-term orientation in interpersonal relationships and balance in social exchanges among individuals. However, such balance will not be realized if *guanxi* relations are to be maintained, for a balance of social exchanges will mean a termination of *guanxi* relations among individuals. To the Chinese, relations are built upon the reciprocity of favors and continuous interactions. Each interaction will elicit an unbalanced status in social exchanges, thereby allowing individuals to continue reciprocal relations. A balance will lead to an ending of reciprocity and the basis for further social interaction. Consequently, the social transactions are perpetual continuations of the long-term balance sheet which registers the relationship among individuals. The norm of *bao* is deeply inculcated in the minds of the Chinese. In Chu and Ju's (1993) study, 82.1% of respondents considered it important to repay kindness received from others.

Once the notion of *shu* and the norm of *bao* are understood, it is easy to comprehend the heavy emphasis on reciprocity in the *guanxi* system. Reciprocity works in accordance with the equality rule which demands that resources be distributed equally among all members in the social network in order to preserve personal harmony in interpersonal relationships. Distributing resources equally is the best way to minimize interpersonal conflicts if members need to interact on a continual base (Hwang 1987). Consequently, it is important for individuals to reciprocate favors to in-group members of the same *guanxi* network.

Favors reciprocated in *guanxi* are known as "*renqing*" in China. The Chinese will bestow favors according to the rule of *renqing* which is the guiding principle in *guanxi*.

### 2.4.3 Rule of *Renqing* (Human Feelings 人情 )

J.H. Weakland comments that "the system of reciprocal aid in Chinese life centered around the concept of *renqing*" (King 1991:74). *Renqing* is paramount in the Chinese

culture. After institutional law and morality, it is one of the three sociocultural concepts that regulates the social behavior of the Chinese.

What is *renqing*? There is no element in Euro-centric cultures that is equivalent to *renqing* in Chinese; nor is there a single English word which captures the rich meaning of "*renqing*". This is reflected in the diversified English translations of the Chinese concept. Some use its literal meaning and label it as "human feelings" (Gold 1985, Yang 1957, Yang 1994). Some stress its sentimental component and translate it as "affection" (Chu & Ju 1993, Jacobs 1979). Others emphasize its social element and regard it as "human obligation" (Chu & Ju 1993, King 1991) or "favor" (Hwang 1987). The different translations mentioned above are the various dimensions of the Chinese concept "*renqing*". Fundamentally, it can be conceptualized on three different dimensions: human feelings, social capital, and social norm.

#### 1. Human Feelings

This is the literal meaning of *renqing*. "*Ren*" (人) means people in Chinese, and "*qing*" (情) means affection. Thus, the two together imply the emotional responses towards other individuals (Gold 1985, Yang 1957, Yang 1994). If individuals empathize with others and understand their emotional responses in daily encounters, they are judged to have *renqing*. Conversely, if individuals are indifferent to others' emotions, they are criticized as not knowing *renqing*.

In the past, some scholars confused *renqing* with *gan-qing* (Fried 1969, Gold 1985 and Jacobs 1979). Yet, the two elements differ on the social dimension. In Chinese, the literal meaning of *gan-qing* (感情) is the affection and emotional commitment of individuals towards others (DeGlopper 1972, Gold 1985, Jacobs 1979, Yang 1994). It is only the sentimental component of an interpersonal relationship. Thus, it is personal, as contrasted to the social nature of *renqing* (King 1991). *Renqing*, as rendered by Yang (1957:292), is human feelings which "covers not only sentiment but also its social expressions such as the offering of congratulations or condolences or the

making of gifts on appropriate occasions." Consequently, *renqing* is underlined with a great sense of social obligations in the interaction with others, whereas *gan-qing* is fully embraced under the meaning of affection.

In line with the above reasoning, Fried (1969) contends that *renqing*<sup>6</sup> is the quality of interpersonal relationship which varies in warmth and intensity. It is different from 'friendship' in Euro-centric cultures in three respects. Firstly, friendship is based on mutual affection and sympathy, but *renqing* is dependent on specific common interests which are the personal goals of parties involved. There is much less warmth and affection, and more formality of contact. Secondly, friendship is devoid of any element of exploitation, whereas *renqing* has a high degree of instrumentalism. *Renqing* is maintained only as long as the personal interests of individuals are satisfied. Thirdly, in the strongly hierarchical Chinese society, friendship is only cherished between individuals on the same social level. *Renqing*, instead, is the primary technique that bridges the gap in social status of two unrelated individuals, and allows a relation to develop between different social levels (Fried 1969).

## 2. Social Capital

In the context of social exchanges, *renqing* can be interpreted as a kind of resource that can be transacted in the course of interaction. It can be a gift or favor for a particular individual. Hence, it embodies a high degree of particularism and a medium level of concreteness, as demonstrated in Foa and Foa's (1976) model which depicts the different dimensions of *renqing*.

*Renqing* ranks high on the dimension of particularism, meaning that it is promoted among selected individuals rather than universally associated with everyone in the

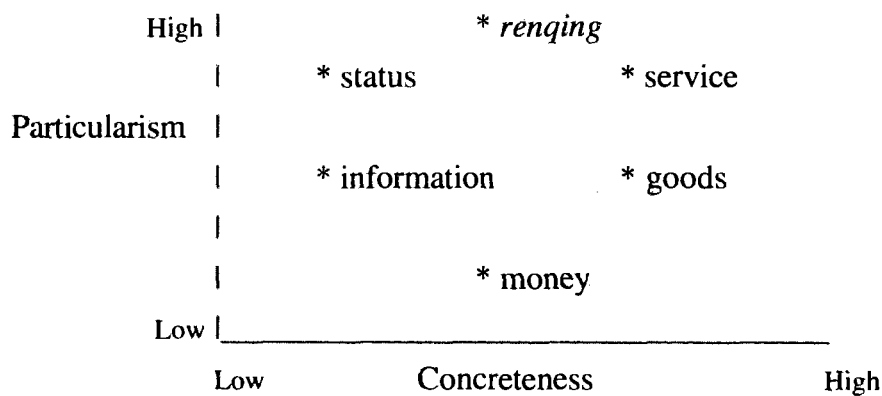
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<sup>6</sup> In the original article, the word used is "*gan-qing*" instead of "*renqing*". Yet, it is defined as something more than sentimental affection. It has less warmth and more formality of contact with a recognized degree of exploitation. The three qualities coincide with the definition of "*renqing*" in this thesis. Hence, it is taken as "*renqing*" here.

personal network. On the other hand, *renqing* is located at the center on the dimension of concreteness. This implies that it encompasses substantive materials such as goods and services as well as abstract components such as affection. This abstract aspect of *renqing* accounts for the enormous difficulties which need to be surmounted in calculating its exact value (Hwang 1987).

Figure 2: The properties of *renqing* as social capital

(Source: K.K. Hwang, "Face and Favor: the Chinese Power Game." *American Journal of Sociology*, 1987, Vol. 92, No. 4, pp. 955.)



### 3. Social Norm

From the perspective of Chinese sociology, *renqing* denotes a set of uncodified social norms that regulates the behavior of individuals in the Chinese society (Chu & Ju 1993, Hwang 1987, King 1980 & 1991, Liu 1993, Yang 1994). If personal harmony is the prime objective of interaction<sup>7</sup>, it delineates the proper rules of conduct

<sup>7</sup> A detailed discussion on how to be "ren" is presented in the article by Wen Shao-Yih in the Symposium on the Character of the Chinese: An Interdisciplinary Approach, edited by Li Yih-Yuen and Yang Kuo-Shu. Taipei: Institute of Ethnology, Academia Sinica, 1972.

for how individuals should behave in accordance with their specific status and their relationships with others, It is on this dimension that the principle of *li* (ethics) is embraced.

#### 2.4.4 Principle of *Li* (Ethics 禮 )

"*Li*" is sometimes translated as propriety (King 1991). Yet, it is much more than conformity to the prevailing standards of social behavior. According to the Book of Rituals (one of the four Confucian classics), *li* signifies the cosmological order used to preserve the sacred order instituted by Heaven, thereby it has a large moral component. Ethics set the guidelines for interpersonal relationships among individuals who are obliged to observe role obligations in the hierarchical society. Yet, the binding force is moral and ethical rather than legal (Liu 1993).

When individuals are locked into defined positions in the hierarchy, they have every moral responsibility to fulfill the role requirements and associated obligations. The fulfillment of role obligations is "*li*". Hence, it can be conceived that "*li*" is the knowing of and acting on prescribed rules of behavior by individuals; whereas the prescribed rules of behavior are implicitly governed by the notion of *shu* and norm of *bao*. Consequently, the principle of *li* defines the social ethics of individuals in the community. This implies a special feature of *li*; it is socially defined.

The moral code of conduct is adjusted constantly as the social definition of ethics evolves over time. What is considered as immoral by the conservative standard in the past may be seen as ethically appropriate in modern times. By the same token, what is regarded as corrupt in Euro-centric cultures may be totally acceptable in the Chinese culture. A good illustration is unofficial questionable payments which are a common phenomenon in the Chinese business arena. To the Chinese, the unofficial payment is a fee paid for the extra "personal" service to accomplish the request. However, this may be interpreted as

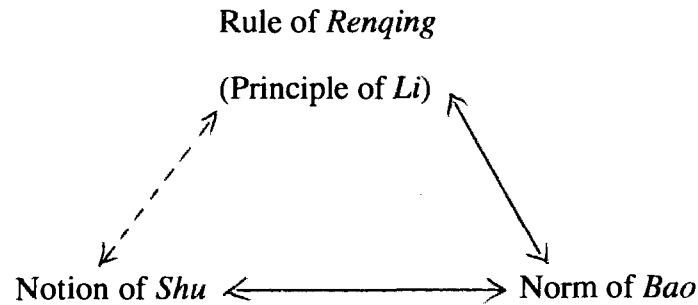
corruption under the business legislation of Euro-centric cultures. Accordingly, *li* is a function of the evolution of social ethics and the circumscribing culture.

In conclusion, the notion of *shu*, the norm of *bao*, the rule of *renqing* and the principle of *li* are the basic operating concepts of *guanxi*. The principle of *li* is embodied in the rule of *renqing* which stipulates role regulations for individuals with an emphasis on reciprocity. It means individuals have to respond positively to the requests of in-group members in anticipation of potential reciprocated assistance in the future. As the rule goes, petitioners are obliged to pay back the debts of gratitude when the appropriate time comes. This is clearly stated in the Book of Rites:

"What the rules of propriety (*li*) value is that reciprocity. If I give a gift and nothing comes in return, that is contrary to propriety; if the thing comes to me, and I give nothing in return, that also is contrary to propriety" (Yang 1957: 291).

Hence, the rule of *renqing* and the principle of *li* can be perceived as derivatives of the notion of *shu* and the norm of *bao* (Hwang 1987, King 1980). The former (*renqing* and *li*) are manifestations and rules for daily applications of the two latter underlying principles (*shu* and *bao*). As a consequence of the interplay of the four operating concepts, the *guanxi* system is deeply entrenched in the Chinese society.

Figure 3 : A Diagram Depicting the Relationships Among the Four Operating Concepts of *Guanxi*



- Note: 1) The arrow represents the direction of influence and relationship.  
2) The dotted line denotes a weaker relationship and influence than the bold line.

Reciprocity is mainly concerned with repayment in the future. Its focus is on future enactment of reciprocated favors rather than past actual contribution that petitioners have made for individuals. The future enactment encompasses an element of uncertainty in the repayment. This leads to the dilemma of *renqing*.

#### 2.4.5 Dilemma of *Renqing*

When individuals comply with the rule of *renqing*, they are inevitably faced with the dilemma of *renqing*. It occurs when the repayment of *renqing* is in the unknown future, and there is a high degree of uncertainty as to the value, timing and form of repayment. In resolving the dilemma, individuals will employ a cost-benefit analysis which involves the interplay of five factors (Hwang 1987).

##### 1. Cost to individuals

These include the loss of resources used in assisting petitioners and the opportunity cost that the resources could be alternatively used to help other petitioners who may bring even greater value of repayment.

## 2. Anticipation of reciprocation

This is the estimation of the possibility of reciprocation. It is a function of petitioners' social status and the amount of resources at their command. If petitioners are prestigious persons of high caliber or are reputed for returning favors, the uncertainty in repayment is very much reduced.

## 3. Evaluation by significant others in the same social network

The Chinese live in a relation-oriented society. The relation between two particular individuals is indirectly intertwined with many others that are closely associated with them. Individuals, in refusing the requests of petitioners, have to consider the effects rejections will have on their relations with other people who are connected with the petitioners in the same social network.

## 4. *Guanxi* relations with petitioners

The *guanxi* ties with petitioners is a consideration in the dilemma. Accepting requests will better the relations with petitioners, while rejecting them will erode the ties. Its primary concern is how important the *guanxi* relations with petitioners are to individuals.

## 5. Face of petitioners

Face work is the projection of self-image and the impression management of individuals. It connotes the self-esteem of the Chinese and is "a function of perceived social positions and prestige within individuals' networks" (Hwang 1987:961). Responding to the face work of petitioners is a cardinal way of preserving harmony and improving *guanxi* relations with others (Liu 1993).

In facing the dilemma of *renqing*, individuals will weigh the above five factors against one another to estimate the net gain/loss that a particular *renqing* would bring to them. If there will be a net gain in providing the *renqing*, then a favorable decision will follow. Conversely, if the anticipated cost is greater than the estimated gain, individuals will be inclined to reject the request. They will have to bear all the possible consequences



in declining the *renqing*, e.g., breaking up the *guanxi* connections with petitioners and their significant others.

The foregoing analysis elicits an important message for non-Chinese who do business in China. When they are faced with the requests of Chinese business associates, they have to reorient the linear logic of their cognitive thinking to the spiral logic of the Chinese.

For non-Chinese, the main factor for considering requests is the requests themselves rather than the related implications. They will more often employ straightforward cost-benefit analysis on economic terms in considering requests. Factors evaluated may not include the social evaluation of their decisions by others in the same *guanxi* network, nor past favors bestowed on them by the related others of petitioners. They may be inclined to reject requests if the requests incur net economic losses. However, the rejection may lead to a collapse in *guanxi* development, as the "no" draws a line between them and the Chinese business associates. It is because, according to the Confucian teachings, individuals have to share with and offer help to other in-group members. Rejections may signal to the Chinese business associates that they are not in the same 'big family', and remind them of the identity of non-Chinese as being out-group members.

On the contrary, accepting requests allows non-Chinese to establish a foothold in the *guanxi* circle and be regarded as in-group members. The relations will be continuously cultivated with reciprocated favors between the non-Chinese and the Chinese business associates. Hence, accepting requests will solicit long-term benefits though the requests may incur immediate net economic loss. Consequently, if non-Chinese want to have business success in China, they have to take the Chinese approach and try to detect the underlying connection between matters which seem to be unrelated at the surface. This

will, indeed, enable non-Chinese to participate in the mind games of the Chinese. (Tung 1994)

The *guanxi* system in China is, in fact, a child nourished in the cradle of these four operating concepts. It has been deeply entrenched in Chinese tradition. However, the smooth functioning of *guanxi* was interrupted by political turmoil induced by the Chinese Communist Party (CCP). The political intervention forced interpersonal relationships to undergo a fundamental change which in turn fostered the two dominant features of today's *guanxi* system: instrumentalism and in-group solidarity.

## **2.5 EVOLUTION OF GUANXI IN CHINA**

### **2.5.1 Instrumentalism**

Prior to the 1940s, social relations in China were characterized by friendship and personal commitment. Both characteristics arose from continuous interaction amongst individuals in fulfilling role obligations. However, this harmonious status was vigorously impaired when the Chinese Communist Party (CCP) decided to create a "new socialist man for the new socialist society" and commenced the terrifying Cultural Revolution.

The Revolution had a profound impact on the nature of social relations because it forced social relations to undergo a transformation from trustful friendship to skeptical comradeship. From then onwards, social relations among individuals were deeply colored by instrumentalism and distrust (Gold 1985, Vogel 1965, Yang 1994).

After the CCP had established control over the country in 1949, they launched a series of campaigns aimed at achieving control over people's life. They promoted the ideal of creating a new socialist man for the new society. They selected particularistic social relations as the target of attack because it ran against their advocated comradeship.

Friendship is a particularistic tie in that individuals have specific relations with each other. The relationship is nourished by a bond of personal commitment and trust between the parties involved. Yet, it is against the ideology of comradeship.

Comradeship is a universalistic morality which puts absolute emphasis on equality among individuals. There are no in-group and out-group identifications because all individuals are supposed to be equal and have universal standing in status or in the degree of closeness (Gold 1985, Vogel 1965, Yang 1994). Comradeship is characterized by helpfulness, civility and concern for others. However, the element of helping is given a special meaning. Helping, instead of going along with the will of individuals in need, is to get them to fall in line with the Party's requirement, even if it is against their own free will. This is in fulfillment of the obligation of being a comrade in Communist China (Vogel 1965).

The value transformation of relationships in the Cultural Revolution was accomplished through fear. Fear arose because people were unsure when their sharing in private conversations with friends would be subject to sanction by the Communist authority. Friendship as a relation of confidence and affection declined. Not only were the trustful relationships between friends weakened, the bond among family members was questioned as well. Children were taught how to be dutiful comrades and gave "little reports" on family affairs to their teachers. Hence, the risk was omnipresent and there was a prevailing mood of skepticism among people. This had profound impact on social relationships because individuals were reluctant to share information which might provide undesirable evidence for criticism in future campaigns. Consequently, cynicism became pervasive in social relations which were then viewed only as a tool to advance personal interests, rather than relations of mutual trust and intimacy. (Gold 1985, Yang 1994)

An extreme form of instrumentalism started to emerge in *guanxi* relations after the Cultural Revolution, and it persists in China today. At present, the pragmatic impulse of individuals is to seek personal gain replaces some of the affective elements in *guanxi*

relations. Individuals are related to one another through cash exchanges rather than through affective connections (Gold 1985).

### 2.5.2 In-group solidarity

In addition to the stress on instrumentalism, the value transformation has also heightened the importance of in-group and out-group identity (Gold 1985, Vogel 1965). As opposed to the goal of comradeship which accentuated universality, the great sense of insecurity induced by political pressure drove people, for self-protection, to be very cautious in confiding information or in making any close comrades. Whether individuals would be perceived as in-group members depended on their trustworthiness. Generally, such credibility was found more in family members or relatives than in outside strangers. Hence, the Revolution imposed a dual effect on social relations in China. On one hand, it unwittingly strengthened the solidarity of familial members; but on the other hand, it widened the gap between in-group and out-group members (Redding 1990).

The suspicious mentality of the Chinese was demonstrated in a study on Chinese students in America who were found to have great family loyalty but displayed a higher level of distrust towards strangers (Sue & Kirk 1972). Again, similar findings were revealed in Chu and Ju's study (1993) where 84.5% of respondents admitted that they would not trust strangers until they knew them better. These two research findings suggest the existence of great suspicion in social interaction with out-group members.

In conclusion, the disturbance brought on by the Cultural Revolution had a profound impact on the nature of social relations in China. Not only did it collapse the traditional social order which stressed complementary and hierarchical role relations, it put the domain of social relations on a platform of comradeship based on universalism, and dressed it in a thick coat of instrumentalism and in-group solidarity. The two elements, compounded by the dominance of personal power, economic /social disarray and political

dictatorship, fueled the widespread dissemination of *guanxi* that has already penetrated into every single aspect of life in China.

## 2.6 RATIONALE FOR THE PREVALENCE OF *GUANXI* IN CHINA

The dominance of *guanxi* in the Chinese society can be conceived of as a consequence of four factors: personal power overriding institutional law, political dictatorship, scarcity of material necessities, and the breakdown of social order.

### 1. Personal power overriding institutional law

As discussed in the previous sections, Confucianism stresses the fulfillment of role obligations. The behavior of individuals is dictated by moral ethics specified in the Four Books of Confucianism. The moral codes are not institutional laws that would sanction individuals if they behave against the ethical guidelines. Yet, most Chinese abide by these ethics because they are routes to their ideal--benevolence. Hence, the society is largely "*li-zhi*" (governing by ethics 禮治). From the Confucian perspective, institutional sanction is redundant when every individual follows the moral code. "*Fa-zhi*" (governing by law 法治) is undesirable because it will ruin the harmony in the interpersonal relationships amongst individuals. Consequently, there is a lack of institutionalized tradition in the Chinese culture.

With the de-emphasis on institutional law, the power of influence is shifted to individuals in authoritative positions in the hierarchy who have the power to command resources. Thus, the society has evolved from governing by ethics to "*ren-zhi*" (governing by persons 人治). That is, the persons in power are the executors of law and can make all kinds of judgments in disputes. As a result, the better the relationships individuals have with the persons in power, the more capable they are to advance their personal interests.

With the emergence of personal power in the societal structure, institutional functioning is largely lost. This directly leads to the prevalence of *guanxi* in China (King 1980 & 1991, Liang 1989). The above proposition was confirmed in a research study conducted by Xin and Pearce (1994) in an interior city of mainland China. The executives of thirty-two companies in different industries were recruited to participate the research. A personal interview was conducted with each of the research subjects. The interviewees reported that *guanxi* relations were important to business success because they served as a defense against threats. Their rationale was that China was handicapped by poor market structure and institutional instability. Private companies had to rely on building close *guanxi* relations with powerful figures for obtaining desirable resources and for protection, since both were generally unavailable to them through formal channels (Xin & Pearce 1994). Hence, it can be concluded that, for private companies, *guanxi* relations are a substitute for institutional support in China.

## 2. Political dictatorship by the CCP

With the objective of promoting comradeship, the CCP attempted to eliminate all personal and particularistic spheres in the society. They extended their control to all aspects of life and had full authority over every element of the people. This situation also fueled the use of *guanxi* for self-protection and restricted privileges for the people who had built connections with powerful figures.

## 3. Scarcity of material necessities

China had long been disturbed by internal political upheavals and the Cultural Revolution. The political turmoil had brought tremendous economic disarray to the country. There was indeed a desperate shortage of basic goods and services. Under the bureaucratic control of the CCP, some goods and services were denied to some collective and individual sectors. Thus, it became apparent that *guanxi* connections with privileged officers were an effective, though illegal channel for the deprived individuals to meet their needs (Gold 1985, Yang 1994).

#### 4. Breakdown in social order

Before the Cultural Revolution, the use of *guanxi* to meet personal needs was uncommon. This was because people were taken good care of by the State which provided all basic necessities. However, after the Cultural Revolution, there was a breakdown in the former social order and law. The traditional moral ethics and institutional order were destroyed. The familial and educational systems had been seriously impaired. People felt so insecure with the new state order that they withdrew into their own private sphere of *guanxi* network which served as a buffer to the overwhelming state control. Through practice, the Chinese learned that *guanxi* with the authority was the supreme law which could protect them from the Party's criticism or allow them to gain personal benefits (Gold 1985, Yang 1994).

In conclusion, the Confucian teachings on moral ethics and role relations have laid the groundwork for the development of *guanxi*. The other three factors (economic disarray and breakdown of social order due to prolonged political upheavals, and political dictatorship by the Communist Party) serve as catalysts that accelerate the evolution of *guanxi* in China. They are likened to a team of craftsmen that jointly paint different colors on the *guanxi* construct, and shape it into a unique configuration that differentiates *guanxi* from the social relationships of Euro-centric cultures.

### **2.7 DIFFERENCES IN SOCIAL RELATIONSHIPS BETWEEN THE CHINESE AND THE EURO-CENTRIC CULTURES**

*Guanxi* is reputed to be a unique social phenomenon that is commonly found in China. Its specific features have distinguished it from the social exchanges of Euro-centric cultures. One would wonder how Chinese *guanxi* relations differ from those in Euro-centric cultures.

In conceptualizing the divergence of social relations between the Chinese and the Euro-centric cultures, one would be misled to perceive them as two fundamentally different entities. In essence, there are similarities between the two cultures. A good illustration is the concordance between Chinese *guanxi* and nepotism in Euro-centric cultures. Both share the common feature of having individuals in authority make decisions on job employment or business deals based on familial relations, instead of objective evaluation on task requirements.

Such a commonality indicates that social relations of the Chinese and the Euro-centric cultures originate from a common foundation. In fact, they are positioned on the same continuum with universalism located at one end, and particularism at the other (Hwang 1987). Both types of cultures possess similar ingredients in social exchange behavior, such as reciprocity, obligation, instrumentalism and power differentiation. Yet, the constituting components are of varying degrees in the two types of cultures. This gives rise to the different characteristics of social relations between the Chinese and the Euro-centric cultures.

The following is an attempt to compare the social relationships of the two types of cultures in terms of seven categories: the motives for engaging in social relations; reciprocation in social exchanges; the time orientation; the pattern of power differentiation; the nature of power; the degree of instrumentalism; and sanction practice.

#### **1. Motives : Role Obligations vs. Self-interest**

In the philosophy of *guanxixue*, individuals have the voluntaristic ability to choose with whom they desire to have *guanxi*. But when they consent to be in the *guanxi* network, individuals have to comply with the rule of mutual obligation which is embedded in Confucianism. This originates from Confucian teachings on role obligations which stem from the relational construction of personhood in China. The motives for conforming to the prescribed hierarchical relations are to preserve personal



harmony among individuals and to be "ren" (benevolence 仁 ). These are the highest ideals of Confucianism. They motivate individuals to have unquestioned acceptance of graded relations and compliance with the associated role requirements.

In contrast with the Chinese, the primary motive that governs social behavior in Euro-centric cultures is self-interest. According to Liang (1989), Judeo-Christian ideology views every individual as an isolated entity that is independent of one another. Judeo-Christian religion represents a revolutionary force that challenges the earthly social order with a doctrine of "rational mastery over the world" (Parsons 1968: 549). Its by-product is an emphasis on power which encourages individuals to confront the worldly authority for personal ideals. This leads to the accent on self-interest<sup>8</sup> as a basis for social behavior and for rational decision making (Hwang 1987).

With dissimilar motives, the two cultures have developed very different mentalities regarding reciprocation.

## 2. Reciprocation : Self-loss vs. Self-gain

Under the enchantment of Confucian ideology, the Chinese are governed by the four operating principles in social exchange transactions: the norm of *shu*, *bao*, *renqing* and *li*. [Please refer to the section on "Operating Concepts of *Guanxi*" for detailed discussion.] The four principles aim at directing individuals to the road of "yi" (righteousness 義), a noble ethical standing in Confucianism.

To be a "yi-ren" (a righteous person 義人 ), individuals have to fulfill role obligations and repay favors they have received from others. Yet, they should reject reciprocation by others for the favors they have bestowed. This is in accordance

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<sup>8</sup> It should be specified that the self-interest engaged in networking in Euro-centric cultures is different from the ego-centric *guanxi* building in Chinese culture because of different time orientations. The former element is governed by a short-term perspective which stresses on immediate benefits for actions taken; whereas the latter is underlined by a long-term perspective which accepts delayed rewards for favors given to others.

with the principle of *shu* which centers around role responsibility. As stipulated by the norm of *shu*, it is the responsibility of donors to reject reciprocation, and the obligation of recipients to repay favors. With complementary role requirements on donors and on recipients, personal harmony is within reach. (King 1980)

In the case of reciprocation, it is suggested by Confucianism that reciprocated rewards to donors should be of greater value than the favors bestowed on recipients. The unbalanced reciprocity is also reflected by a Chinese saying: "Reciprocity, in theory, signifies that one person honors some other person a linear foot<sup>9</sup>, and the other person should in return honor him ten feet." (Yang 1957: 291) Repaying ten feet in return for a favor of a linear foot definitely incurs a loss on the part of recipients. Yet, the unbalanced reciprocation falls under the principle of *yi* in Confucianism.

As a consequence, the role requirement of donors to extend help without seeking rewards, and the obligation of making excessive reciprocation by recipients to repay favors, causes losses to individuals involved in social transactions. This stands in great contrast to the self-gain motive of social relations in Euro-centric cultures.

According to Blau's (1989) social exchange theory, there is also an unbalanced reciprocity in social transactions of Euro-centric cultures. However, the tilt of disadvantage is shifted towards the opposing party in the relationship rather than to self. It is suggested that individuals are strained to maintain a balance of social debts, thus they are obliged to reciprocate as the Chinese. However, it is hypothesized that individuals are in a dilemma of waiting for reciprocation. The dilemma will endure until the opposing party makes a greater contribution to stabilize the relationship before it is endangered by non-commitment of either party. Its objective is to enable individuals to assume superior positions in the relations and enjoy more gains at the

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<sup>9</sup> Linear foot is a Chinese linear measurement. One linear foot is equivalent to three feet in Western measuring units.

expense of the opposing parties who make greater contribution. Consequently, self-gain is the primary motive that underlies social interaction in the Euro-centric cultures.

### 3. **Time Orientation: Long-term vs. Short-term Perspective**

Long-term orientation is deeply inculcated in the Chinese culture. It stems from the fact that China enjoyed prolonged stability in the ancient past. The durable peace has induced the Chinese to take a long-term bearing in their mindscape and it underlies the cultivation of *guanxi* relations in China.

Longevity manifests itself in the long-term balance sheet of social interactions which is implanted in the minds of the Chinese. It is to record the ins and outs of social investments among individuals, so that they will not be socially indebted to others. However, the ins and outs will never be balanced because such a status will mean a termination of *guanxi* relations. To the Chinese, *guanxi* ties are built upon the reciprocity of favors and continuous interactions among individuals. Each social transaction will elicit an unbalanced status because it incurs losses to individuals as underlined by the self-loss approach in reciprocation. A balance will lead to an ending of reciprocity and thereby loss of the ground for further social interactions. Consequently, the Chinese aim at maintaining constant social exchanges among individuals in the long-run with each social transaction serving as one of the integrated steps to the continuation of relations between two individuals.

In contrast, social transactions in the Euro-centric cultures are governed by a short-term perspective. Non-Chinese tend to maintain a balance in every interaction, and each social exchange stands on its own with great emphasis placed on the immediate gains from the transaction. It pays only minimal attention to any long-term relationship building. This contradicts the long-term relational orientation of Chinese *guanxi*.

#### 4. Power Differentiation : *Xia* vs. Power

"*Xia*" (俠) is another doctrine of Confucianism. It is similar in meaning to being a 'knight' in the Western sense. A *xia* serves as a bodyguard of *yi* (righteousness). His aspiration is to promote *yi* in the imperfect world and urge every individual to comply with the prescribed order. Hence, in being a *xia*, the individual is supposed to right the wrongs, to help the poor and to punish the wicked. (Yang 1957)

In extending the doctrine of *xia* to social relations, the powerful parties who have greater command of resources will assume superiority in relations and will take up the role of *xia*. They have every obligation to help the weaker parties. Thus, the advantages are tilted towards the inferior parties and allow them to 'victimize' the superiors by calling for special favors which they do not have the ability to reciprocate (Pye 1992, Alston 1989). In return, the superior parties will gain face and reputation of being righteous for the unequal exchanges. Hence, the unbalanced social exchange relations will be maintained perpetually under the work of face. The above pattern of power differentiation is reflected in the complaints of non-Chinese investors about the unreasonable requests of the Chinese in business negotiations. The non-Chinese criticize that the Chinese often press for greater concessions in negotiations by stressing that foreign powers have the obligation to help, since they are superior in economic prosperity and therefore should assume the role of *xia* in business relations.

In contrast, social relations in Euro-centric cultures assume a different pattern of power differentiation. Those who have greater command of resources likewise assume superiority in social relations. However, those who cannot reciprocate favors of equal value are under pressure to defer to their wishes. They have to comply with the superiors' will as repayment for favors received. If such reciprocation is not realized, the relation is bound to be terminated, instead of being maintained through face as in the Chinese culture. The provision of unilateral favors is a means for superior parties to accumulate a capital of compliance which will be at their disposal at

some future time. Hence, the tilt of advantages is placed on the superior parties in social relations.

#### **5. Nature of Power : Personal Power vs. Institutional Authority**

In today's China, little can be accomplished without the use of *guanxi*. Its supremacy is derived from the dominance of personal power over institutional authority. Owing to the overwhelming focus on moral ethics in Confucianism, the Chinese society is largely *li-zhi* (governing by ethics) and has great distaste for *fa-zhi* (governing by law). Hence, there is an absence of institutionalization. The power of influence is shifted onto the persons holding the authoritative positions, and the society evolves to be *ren-zhi* (governing by persons). This leads to the rise of personal power which, together with the accentuation on particularism that favors giving benefits to related others, greatly promotes the practice of *guanxi* in the Chinese society.

Conversely, the Euro-centric cultures give prominence to institutional authority and downplay the use of social connections in commanding resources. Institutionalization is a Euro-centric tradition that installs enduring mechanisms to transmit social norms and values, knowledge and skills from generation to generation (Blau 1989). This gives legitimacy to formalized constitutions that allows organizational functioning to be independent of any individual member and is devoid of any personal influence. Consequently, universalistic rationality is firmly established in replacement of personal power. The effectiveness of using social relations to mobilize resources is submerged under institutional legitimacy.

#### **6. Instrumentalism : Greater Emphasis vs. Less Importance**

As discussed in the previous sections, an extreme form of instrumentalism has been inflicted upon *guanxi* relations by the value transformation of the Cultural Revolution. Compounded by the shortage of material necessities and political dictatorship of the

Communist Party, the Chinese have learned to use *guanxi* as a way of achieving resource re-distribution. The external rewards derived from relations overshadow the nourishment of any emotional affection between individuals.

In contrast, the scope of instrumentalism is much reduced in social interaction of Euro-centric cultures, because of material abundance and political democracy in the society. Material abundance and economic prosperity spare individuals from using illegal channels to secure scarce but desirable resources. In addition, formal institutional channels are available for them to lodge complaints in instances of unreasonable denials. Their complaints are lodged with the government authorities because of the political democracy in Euro-centric societies, as opposed to the political dictatorship in China. Therefore, social relations in Euro-centric cultures are affected by instrumentalism to a much smaller degree.

#### **7. Sanction : Shame vs. Guilt**

One of the salient underlying differences between Chinese and Euro-centric societies is the sanction on deviating behavior by individuals. In the Chinese culture, sanction by shame has long been established. Shame is a sense of disgrace brought on by individuals' awareness of having committed dishonorable deeds. In the Confucian world, the relational construction of personhood requires individuals to be closely related with one another. Their behavior is constantly under the social evaluation of other in-group members in the same network. They are expected to comply with the social expectations on behavior. A deviation from the social norm will be condemned, and shame will be brought onto individuals guilty of the deviated behavior as well as onto their significant others (e.g. parents) Therefore, shame is a social sanction which serves as a control device over individuals' behavior in the Chinese society (Liu 1993). It has been viewed by Confucius as the best regulating mechanism as He commented in Analects (2:3):

"Lead the people with governmental measures and regulate them by law and punishment, and they will avoid wrongdoing but have no sense of honor and shame. Lead them with virtue and regulate them by the rules of propriety (*li*) and they will have a sense of shame, and, moreover, set themselves right." (Yang 1994:227)

By contrast, sanction in Euro-centric cultures rests upon guilt. It comes in the form of an internalized conviction of sin (Liu 1993). Individuals will feel guilty if their behavior has deviated from the absolute standard of morality as stipulated by Judeo-Christian ideology.

### 2.7.1 Business Applications

With dramatic disparities in motives and in the objective of reciprocation, conflicts are bound to emerge when non-Chinese firms operate in the Chinese environment. A common conflict arises from the different perceptions on the role of non-Chinese in business relations. The Chinese presume non-Chinese take the role of *xia* in the economic development of China for two reasons. Firstly, non-Chinese are perceived as experts on market economy, and they should give way to the Chinese who are newcomers to capitalism. Secondly, the Chinese feel that it is the right time for Westerners to repay the old debts of their ancestors who extracted so much from China in the 19th Century by imposing various unfair treaties on them. Hence, the Chinese assume non-Chinese will make a long-term business commitment in China, and expect them to give much assistance in business dealings as well as make great concessions in negotiations. To the Chinese, though the concessions may incur immediate losses on the part of non-Chinese, everyone will benefit in the long-run because stable long-term relationships will then be established between the Chinese and the non-Chinese. This will allow non-Chinese to gain more from *guanxi* relations in the future.

Nevertheless, to non-Chinese, one key objective is to make maximum gain with minimum cost within the shortest possible time span. In line with business practices in their home countries, they aim to make a profit in every business dealing with the Chinese. Long-term relationship building is significantly less of a factor in business decision making, nor is it a consideration for making concessions in negotiations. The pragmatic motive of non-Chinese has been very annoying to the Chinese, since it is in direct opposition to the obligation of *xia*.

Consequently, if non-Chinese want to have business success in China, they have to balance their motive of short-term self-gain with that of long-term role obligations. More attention should be given to their particular role as *xia* in interacting with the Chinese. One way to achieve this is to incur temporary loss in business dealings. Immediate 'sacrifice' is desirable in building relationship with the Chinese, because the Confucian teachings on reciprocation requires 'self-loss'. Yet, the temporary loss is not a failure. It is only one of the integrated steps leading to eventual success in the prolonged exploration of the Chinese business arena. The short-term loss may mean long-term victory in the future when non-Chinese are fully integrated into the Chinese *guanxi* network.

After establishing *guanxi* with Chinese local parties, non-Chinese need to make special efforts in three different respects. Firstly, non-Chinese should find out who the right decision makers are, since China is predominated by personal power instead of institutional authority. One illustration of the prevalence of personal power is the difference in attitudes towards legal contracts. To non-Chinese, a written contract defines the roles and rights of the parties. It is legally binding and restricts any deviating behavior of the involved parties. However, to the Chinese, a written contract is viewed as an organic document which will change as the situation evolves. Because of the supremacy of personal power in China, the binding effect of a contract is generally subject to interpretation by authority figures. As a result, non-Chinese should try to build up their



stature through connections with persons in power rather than by means of institutional authority. The key factor here is to identify who the right decision makers are.

Secondly, non-Chinese should continue to enhance their instrumental utility to the Chinese. Pragmatic gains are the main nutrient for maintaining the life of *guanxi* relations. As noted in the literature and in the field work of Yang (1994), *guanxi* relations are sustained by the continuous advancement of personal gains for both parties. When utilitarian benefits are gone, the *guanxi* relations will wither. Accordingly, the non-Chinese have the mission of cultivating a perception in the Chinese that doing business with non-Chinese is of great importance to the Chinese economy. This can be accomplished through creating new needs for the Chinese and selling products which cater to those needs.

Thirdly, non-Chinese should recognize the importance of social evaluation of their behavior in the *guanxi* network. When non-Chinese have entered into the *guanxi* circle, they are intricately entangled with others through strands of *guanxi* relations. Their actions are under close scrutiny by other in-group members. With the notion of shame in the Chinese culture, any perceived misbehavior of non-Chinese will bring shame to their close Chinese business associates. As a result, the Chinese business associates will weaken *guanxi* relations with the non-Chinese to avoid the shame induced by them. This will tremendously hinder the attainment of business success in China. Consequently, non-Chinese need to evaluate their behavior constantly in accordance with the Chinese social norm, and consider the social evaluation of their behavior in business decision making.

In conclusion, Chinese *guanxi* has been contrasted with the social relations of Euro-centric cultures in the above seven aspects. Yet, it should be remembered that they differ only in relative terms. There are some similarities in social relations between the Chinese and the Euro-centric cultures, even though the two cultures are located at different positions on the same continuum. The unique characteristics of each culture are the natural consequences of the interactions among political intervention, economic development and

social orientation of the nation. In short, the peculiar type of social relations dominating in the Chinese or in Euro-centric cultures is a precious child nurtured in the idiosyncratic environment of each respective culture.

## 2.8 SUMMARY

*Guanxi* is a Chinese construct that represents a special type of social relations which Hwang (1987) has labeled as the "mixed tie". Though it is a combination of both instrumental and expressive ties, *guanxi* has developed unique characteristics. The four special attributes include: (1) an ego-centric nature which encompasses voluntaristic ability and particularistic values; (2) personal networking with connective essence and pluralistic identifications; (3) mutual obligations which imply quantitative quality and instrumental flavor; and (4) dynamism with the connotation of longevity.

The above characteristics of *guanxi* differentiate it from the social relations of the Euro-centric cultures in seven respects: the motives for engaging in social relations; reciprocation in social exchanges; the time orientation, the pattern of power differentiation; the nature of power; the degree of instrumentalism; and sanction practice. The development of *guanxi* owes its origin to Confucian teachings which focus on role relations and familism. These formulate the basic framework in which *guanxi* is operated. Together with the functioning of the four Confucian operating principles (rule of *shu*, *bao*, *renqing* and *li*), the *guanxi* system is firmly established in the Chinese society.

The smooth functioning of the *guanxi* system was however disturbed by the Cultural Revolution, which forced social relations in China to undergo a value transformation from particularistic friendship to universalistic comradeship. The political intervention had intensified the in-group solidarity and the degree of instrumentalism in *guanxi* relations.

## CHAPTER 3

### ART OF *GUANXI*

With the supremacy of *guanxi* at all levels of societal functioning in China, Mayfair Yang (1989:35) has termed the collection of practices associated with *guanxi* as the "art of *guanxi*". Indeed, *guanxi* is an art which requires participants to be extremely tactful in crafting relations, starting with building *guanxi*, maintaining *guanxi* and benefiting utilitarian gains from *guanxi*. The three different stages have been analyzed by Yang (1989, 1994) from the perspective of the microphysics of power at a personal level. She determines that there is a power struggle between the two parties involved in every instance of *guanxi* transaction. This can be conceptualized as five different strategies, namely, transformation, incorporation, moral subordination, appropriation and conversion.

#### 3.1 *GUANXI* BUILDING

In Yang's terminology, *guanxi* building is the **transformation** process in which a basis of familiarity is constructed between two discrete persons for future relationship development. The focus is to bridge the gap between two formerly unrelated individuals so that the outsider can be brought into the inside social circle of the other individual and be perceived as an in-group member. Hence, the insider/outsider dichotomy assumes great importance in the transformation stage which is the overture to any *guanxi* relations.

There are two ways to facilitate the transformation process: group identification and altercasting.

### 3.1.1 Group Identification

*Guanxi* building based on group identification has to depend on the existence of any particularism among parties involved. Particularism manifests itself in the form of attributes that are common to the individuals, so that they have a shared identification. More importantly, shared identification is significant to the individuals so that they are committed to the requests of other in-group members. Hence, this commonality is a base upon which *guanxi* connections are built, and it is termed as the "*guanxi* base" (Jacobs 1979, King 1991). There are two types of *guanxi* bases: ascribed and achieved.

#### (a) Ascribed *guanxi* base

The ascribed *guanxi* base is a commonality that is in-born and indisputable. The two most common types of ascribed *guanxi* bases are kinship and locality.

**Kinship** : Kinship has been cited as one of the most important *guanxi* bases in China (Bosco 1992, Chu & Ju 1993, Jacobs 1979, King 1991, Redding 1990, Yang 1994). Its significance is confirmed by Chu & Ju's study (1993) in which a higher percentage of respondents would offer help to a relative rather than to a friend (70.9% versus 64.3% respectively). Correspondingly, a lower percentage of respondents would reject assistance to a relative rather than to a friend (8.0% versus 11.4% respectively). (Chu & Ju 1993) Similar results were obtained by asking respondents whether they would lend money to a relative or to a friend. [Please refer to Appendix 1 for the comparative research results.] These research findings show that kinship *guanxi* plays a very important role in China and its prominence is derived from the traditional emphasis on family structure.

There are two categories in kinship *guanxi*: agnatic and affinal. Agnatic kinship is composed of immediate family members, e.g., father, son and their wives. Affinal kinship is extended to include the families of nuclear family members, e.g., the family of the father's sisters or that of the son's wife. Thus, affinal kinship is much larger in number and in geographic scope. It is proposed by Jacobs (1979) that agnatic kinship

is more important in politics at village level, while affinal kinship is predominant at multi-village level.

One special feature of kinship *guanxi* is its elastic nature. With the loose definition of affinal kinship, the boundary between in-group and out-group identity is flexible. Familial identification can be restricted to the members of the nuclear family, or it may be extended to include all members of a lineage who share very distant familial associations. It depends on how individuals perceive the definition of 'family' (King 1980, 1991). The common Chinese expression "*zi jia ren*" ( 自家人 ) means "our family people". It can refer to any outsider whom individuals would like to conceive as part of the 'family' ---- an in-group member. The fluid expandable nature of kinship is also found in *guanxi* based on locality.

**Locality :** *Guanxi* based on locality has been ranked by Jacobs (1979) as the most important *guanxi* base in Chinese politics. The particularism shared by individuals is the identification of a common native place. The native place can be a small village, a province or a large region. Hence, its loose definition gives rise to the extensive nature of *guanxi* based on locality.

*Guanxi* relations based on kinship and locality, though embodying an ascribed element, are elastic in nature because of their loose definitions. They allow individuals to have enough flexibility to build relations with many others who should be excluded under a strict definition of 'family'. This highlights the voluntaristic nature of *guanxi* building in China, even within the group of ascribed relations. This flexibility in *guanxi* building is further enhanced in the second category of *guanxi* base: achieved.

(b) **Achieved *guanxi* base**

The achieved *guanxi* base connotes that individuals have shared experience instead of innate commonality. It is voluntarily constructed and its existence is totally at the

will of individuals. There are many types of achieved *guanxi* bases, such as coworkers, classmates, sworn brothers, teacher-student relations and many others (Chiao 1982, Jacobs 1979, Yang 1994). Among these, co-workers and classmates have relatively more influence in *guanxi* building (Jacobs 1979<sup>10</sup>).

*Guanxi* with co-workers is important because individuals tend to identify with their work group, as they spend most of their time in the work place. Co-workers are the ones they interact with most after their immediate family members.

The importance of *guanxi* with classmates is derived from the historical emphasis on education in China. In the past, few students could pass the imperial examination. Those who could do so certainly shared among themselves a sense of superiority which served as a solid base for *guanxi* development.

Both ascribed and achieved *guanxi* bases are significant in *guanxi* building only if they are perceived as important identifications by individuals concerned. The importance of any particular *guanxi* base varies among different individuals and across different cultures. Some individuals may value kinship relations while others may stress classmate connections. Correspondingly, some cultures may accentuate the importance of lineage whereas others may de-emphasize it. Hence, there is no universal standard on the importance of any particular *guanxi* base. In a preliminary attempt, Jacobs (1979) has proposed four key factors that will affect the level of importance associated with each *guanxi* base in relationship building:

1. The hierarchical level in the political system will determine which *guanxi* base has greater importance. For instance, affinal kinship may have higher impact on politics at a provincial level than at a village level.

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<sup>10</sup> An excellent analysis of the different types of achieved *guanxi* is presented in "A Preliminary Model of Particularistic Ties in Chinese Political Alliances: *Kan-ching* and *Guanxi* in a Rural Taiwanese Township" by J. Bruce Jacobs. *China Quarterly*. No. 78 (June 1979). p 237-273.

2. Individuals will allocate various degrees of importance to different *guanxi* types according to their own preference, e.g. kinship may be more significant to person A than to person B.
3. The type of political arena will affect the importance of *guanxi* type in the society. *Guanxi* is particularly prominent in a relational society, but has less impact in a bureaucratic environment.
4. Time will change the degree of importance that has been allocated. *Guanxi* based on classmates had greater effect in old China than in today's communist environment.

The above four factors will shape the pattern of identification. They will determine which relations based on a particular *guanxi* base has greater significance in the relational society. Other than *guanxi* base, *guanxi* connections can also be built by altercasting.

### 3.1.2 Altercasting

Altercasting (Hwang 1987) is a term used for describing the establishment of *guanxi* between individuals who have no ascribed commonality. That is, they do not have any common *guanxi* base for shared group identification. The technique is commonly known in China as "*la guanxi*" (pulling social relationships 拉關係) or "*zou houmen*" (going through the back door 走後門). Altercasting works because of the connective nature of *guanxi* relations.

The basic idea of altercasting is to rearrange a targeted person's networking system in which an individual desires to be included. Hence, the individual must first try to get himself/herself involved in the target's social network. One effective way of accomplishing this is through an intermediary.

An intermediary is a third person who is familiar to both parties and has the capability of making a proper introduction of an outsider to an insider. He/She serves as a cable connection to link two unrelated individuals and merges the boundary of their social networks. When an association has been established through the intermediary, the two

formerly unrelated individuals will behave in accordance with the rule of *renqing*, and treat each other as an in-group member.

The roles of intermediaries are fully revealed in business research. An intermediary is defined by Ai (1994:103) as "an outside individual or entity that helped the Canadian (foreign) company enter the Chinese market for a fee." The significance of the role of intermediary is confirmed in a study by Kearney which revealed that 42% of non-Chinese investors used intermediaries to find partners for joint ventures (de Keijzer 1992).

Generally, the role of intermediary is played by the "members of the third culture". These are individuals who are familiar with the Chinese culture and are willing to bridge the gap between the Chinese and the non-Chinese (Tung 1981). Very often, these individuals are ethnic Chinese who are nurtured in the Chinese environment during their up-bringing, but have also received education in Euro-centric cultures. Hence, they are receptive to both Chinese and Euro-centric perspectives, and have the capability to fulfill the intermediary role which encompasses four major aspects: (a) overcoming the cultural differences between the Chinese and non-Chinese investors; (b) helping non-Chinese investors to establish rapport with the Chinese parties who have doubts about their trustworthiness; (c) preventing non-Chinese investors from making poor decisions due to a lack of familiarity with the China market; and (d) building *guanxi* ties with appropriate authorities for non-Chinese investors (de Keijzer 1992).

The important role played by intermediaries in foreign business operations in China can be attributed to two reasons. The first reason is the desire of non-Chinese firms for quick return on investment. The unique Chinese business environment requires non-Chinese firms to have market-specific knowledge before achieving any success. The knowledge has to be acquired through incremental learning which is a prolonged process involving the long-term commitment of resources. Such enormous investments are undesirable for smaller firms which require quick return for continuous operation. Therefore, building connections through intermediaries serves as a short-cut for non-



Chinese firms to accumulate the required experiential and market-specific knowledge within a short period of time.

The second reason is the emphasis on in-group and out-group identity. In general, interaction with out-group members is filled with suspicion and skepticism while interaction among in-group members is bathed in trust and sharing. The out-group alienation is greatly amplified in Sino-foreign interaction because of the historical invasion of China by foreigners (Shenkar 1990). The long period of seclusion had cultivated fear and an ignorance of non-Chinese on the part of the Chinese. Consequently, it is essential for non-Chinese firms to build relations with the insiders (intermediaries) of the Chinese market for entry.

In business, the direct pattern of linkage is generally preferred because it involves only one intermediary for establishing relations between two individuals. However, the linkage pattern can also be indirect and involve two or more intermediaries. For instance, A wants to be associated with Z. But, there is no one in A's network who is an insider of Z's network. A has to go around and ask assistance from B who has *guanxi* with C who has *guanxi* with D ..... The linkage will go on until A finds Y who is in Z's network. By giving face to Y who gives face to X ..... C who gives face to B, A is eventually connected with Z.

In terms of reciprocation, social indebtedness is embedded only in dyadic relations even in a long chain of linkage. This means that a person is only socially obligated to the next person in the chain, rather than to everybody involved in building the complex linkage (Yang 1994). As in the above example, A is socially indebted to B for building a linkage with Z; and B is obliged to C for helping to obtain the desired linkage with Z for A; and so on. Consequently, tremendous *guanxi* transactions may be involved in a complex indirect linkage, yet social indebtedness is confined only to the next person in the chain.

Both group identification based on commonality and altercasting relying on intermediaries are means to achieve the same end: to build *guanxi* relations with another unrelated individual. The two ways are designed to build a base of familiarity between two unrelated persons and to diffuse the boundary of their social networks. Nevertheless, this is only step one in the *guanxi* management process. The transformation procedure only erects a bridge of connection between two individuals. The success and the utility of the relation still depends on its consolidation.

### 3.2 *GUANXI* MAINTENANCE

In the transformation process, a bridge has been built to link up two unrelated individuals. However, the connection is not a guarantee of success. It has to be constantly reinforced and maintained through continuous social interaction which can be in form of exchanges of gifts, banquets and favors. When a gift has been received or a request for a favor has been granted, four different mechanisms immediately occur in the relationship (Yang 1989). Each is designed to deepen the commitment of both parties to the *guanxi* connection.

The first process is called **incorporation**. This is a "symbolic breaking down of boundaries between persons" (Yang 1989:41). The commodity exchanged or the request granted is identified with the donor or resource allocator respectively, and thereby embodies a personal substance of the donor or resource allocator. Hence, when it is accepted, the personal identity of the donor or resource allocator symbolically intrudes into the personal space of the recipient or petitioner. This will reduce the barrier between the donor and recipient or between the resource allocator and petitioner, thereby breaking down the boundary between the two selves.

The intrusion of personal identity by means of incorporation triggers the process of **moral subordination** which is the second step in the microstruggle of power in *guanxi*

relations. The power struggle manifests itself in the contest for face and in the struggle for moral superiority between the two individuals. Face is cardinal to the personal identity of a Chinese because the personhood of an individual is attained by internalizing the approval of his/her significant others. Thus, Liu (1993:27) defines face as "the individual's assessment of how others close to him see him."

There is a direct relationship between face and power. The greater the face an individual has, the more prestige and power he/she is supposed to possess. Hence, in a social exchange, when a gift is accepted or a request is granted, the face of donor or resource allocator is enhanced, thereby increasing his/her prestige and power as well. This leads to an imbalance of power in the relationship. The donor or resource allocator assumes moral superiority over the recipient or petitioner.

The imbalance of moral status and face in relations leads to the third process: **appropriation**. This is to incorporate the other's personal substance into oneself. After accepting the gift or the favor which symbolizes the personal identity of the donor or resource allocator, the recipient or petitioner is indebted to the opposing party. He/She is then subject to the internalized will of the donor or resource allocator.

In response to the moral inferiority created by the enhancement of face on the part of opposing parties, the recipient or petitioner will try to restore the balance of power by means of **conversion**. Conversion of values takes place when reciprocated action has been made by the 'inferior' side. When the recipient repays the gift accepted by giving out another gift, or the petitioner returns the favor by helping the resource allocator in other ways, the indebtedness in the relation is cleared. A balance of power is resumed by means of reciprocity.

These four micro-physical mechanisms of power struggle depict the operating cycle of *guanxi* relations which will not end after the process of conversion. This cycle will repeat itself when reciprocated actions take place. The second cycle of power struggle

begins when the recipient or petitioner repays the social debt, and there is a change in identity. The individual who was formerly the recipient or petitioner becomes the donor or resource allocator. Conversely, the former donor or resource allocator will be faced with the dilemma of *renqing* and wonder whether he/she should accept the repayment. The decision will be more difficult if the return is of greater value than what he/she has offered in the first cycle. The acceptance of more 'precious' repayment will cause him/her to be indebted to the other party. This is contrary to the objective of maintaining an equilibrium on the balance sheet of *renqing*. Conversion will take place again and the third cycle of power struggle will commence. Consequently, once the bridge of connection has been established after the transformation process, and when the mechanism of incorporation starts off for the first time, it leads to repeating cycles of reciprocity which will never end unless there is a break-up in the relationship. It is this repeating reciprocity that deepens the commitment of each party to the relation, thereby strengthening the *guanxi* connection.

In addition to the continuous exchanges of gifts or favors, *guanxi* connections can also be promoted through multiplex relationships. This is to cultivate more commonalities or more *guanxi* bases when a single-stranded relation has been developed. It can be achieved easily by sending children to the same school or by marriage. The objective is to strengthen the base of familiarity between two parties and to provide a more consolidated support for future *guanxi* development. In this way, multiplex *guanxi* is more resistant to deterioration than single-stranded relations.

For *guanxi* maintenance, the mutual satisfaction of the personal interests of both parties is essential. Relations can be easily broken if either side disappoints the other party in the social exchange processes by excessive demands or by a blunt rejection. Excessive demands will overstrain the delicate relationship and create a tendency of avoidance by the opposing party. A rejection will destroy the sense of dependability and cast distrust in the relation.

### 3.2.1 Dependability

Dependability is essential in *guanxi* maintenance because it denotes the trustworthiness of individuals in the *guanxi* network. As discussed in the previous sections, trust exists only among in-group members who are supposed to fulfill the obligation of responding to the requests of other members in the same network. If individuals abide by the rules of the exchange game and fulfill the role requirements, they are considered as reliable and trustworthy and are entitled to the benefits of *guanxi*. On the contrary, rejections to other members' requests for no valid reason will be judged as unwilling to take up role obligations. Individuals will then be criticized as undependable and will be labeled as outsiders. They will be excluded from the *guanxi* network and lose all *guanxi* benefits.

### 3.3 GUANXI BENEFITS

The accent on instrumentalism implies that *guanxi* relations are a personal system that individuals use for personal goal attainment. It functions chiefly as a way of resource re-distribution by the state (Chu & Ju 1993, King 1991, Redding 1990, Yang 1989, 1994).

Under the state distribution system of China, the CCP has indisputable control over the allocation of resources in the country. This unilateral decision making has created a one-sided dependency of the people on government authority for resource allocation. To counteract the unbalanced state distribution, the people use *guanxi* to secure resources that are denied to them by state decisions. This reconstructs the flow of resources from the privileged class to the deprived group, therefore, the more *guanxi* network individuals have established, the greater relations they have at their command, thus the more advantageous positions they are in to mobilize restricted resources for personal interests.

What types of personal interests do individuals benefit from *guanxi*? Yang (1989, 1994) has postulated four different forms of value:

1. Gift capital

It is comprised of two subcategories: (a) material capital: the monetary resources spent on gifts; and (b) body capital: the labor and time required of individuals to perform favors or prepare gifts.

2. Symbolic capital

It is the accumulation of face, gratitude and social indebtedness which allow individuals to assume moral superiority in relations.

3. Office capital

It is the resources that are denied to individuals, but can be made accessible through having good *guanxi* with the officers in rank.

4. Political capital

It is political security and upward mobility to be attained by being a Party member or powerful official, or by having a good family background<sup>11</sup>.

Among the four types of benefits, it is the symbolic capital which obliges in-group members to engage in the conversion process. Symbolic capital is the key to the treasuries of office and political capital. Both contribute to a mode of resource re-distribution and ultimately allow individuals to enjoy material and body capital from the *guanxi* system.

With its tremendous instrumental value, the practice of *guanxi* has spread like a social epidemic and it penetrates every single aspect of societal functioning in China. However, under the supremacy of *guanxi* connections, a hidden current of condemnation

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<sup>11</sup> The Communist Party of China emphasizes proletarian dictatorship and advocates that the working class hold the leadership of the country which is exercised through the Chinese Communist Party. Hence, those individuals who are born in low working class are considered as having good family background. Conversely, the capitalists, the rich peasants and the counterrevolutionaries are classified as bearing "bad" family backgrounds because of state resentment against the rich and the intellectual. (Tung 1988, Yang 1994)

of *guanxi* relations has surfaced, and a tendency of *guanxi* avoidance has been cultivated in today's China.

### 3.4 GUANXI AVOIDANCE

An article with the title of "The Growing Trend of Today's China: Universalization of Family Affairs" was recently published in a Chinese newspaper (Sing Tao Newspaper 1994). The title itself indicates a growing condemnation of the practice of *guanxi* in China. Toiling against the conventional wisdom which advocates that in-group matters be dealt with in a private and personal fashion, modern young Chinese in mainland China now prefer family affairs to be handled in accordance with universalistic rules rather than by particularistic ties. They are becoming disgusted with the devious use of *guanxi* connections for personal goal attainment which is often in conflict with more universalistic or moral issues.

The negative view of *guanxi* practices is fully revealed in Chu and Ju's study (1993) in which 59.1% of the respondents indicated that "having good outside connections" was the least important leadership attribute. Only 7.8% accepted that it was one of three most important qualifications. With such a negative rating, the index of net importance for *guanxi* relations was reduced to -51.3%. The attitude was found to be more acute among urbanites than among rural inhabitants. 64.7% of urban dwellers voted against *guanxi* relations while only 43.5% of villagers displayed a negative opinion. Correspondingly, only 4.2% of the former group as compared to 17.5% of the latter group agreed that *guanxi* was an important leadership qualification. These surprising research findings endorse the condemnation that has started to gain ground in China.

The negative feelings about *guanxi* practices can be attributed to two causes:

1. Loss of autonomy

With the overwhelming emphasis on role relations, individuals find that they are socially obliged to respond to the requests of fellow members when they have been locked in the *guanxi* circle. The compulsion of social obligations causes them to lose autonomy and freedom. They have no choice but to comply with social rules, even if it is against their own will. The desire of individuals to secure autonomy is confirmed by DeGlopper (1978) who found that the businessmen in Lukang preferred to maximize their freedom of choice and limit the diffusion of personal relations into business functions.

2. Modernization of the country

China is now in a surge of modernization with the aim of pushing the nation from the status of a third world country to the advanced standing of a world power. This can hardly be accomplished if economic transactions and organizational functioning rely mainly on particularistic ties.

With the aim of modernization, out-bound transactions with strangers are definitely desirable to expand the sphere of economic influence and to promote the prosperity of the unit, be it a lineage, a province or a nation. Such massive expansion of exchange transactions is obstructed by the narrow scope of functioning by particularistic ties. Instead, universalistic rationality is required to create a new mode of interaction which can bind together people of different social backgrounds, from different cultures and with different relationships.

Universalism, though anti-personal, can institute a relation of confidence and objectivity in which professional bureaucracy and economic efficiency can flourish. The desire for universalistic ethics is confirmed by Chu and Ju's (1993) study in which an overwhelming majority (92.2%) agreed to the statement that "law brings justice to society". The affirmation of respondents is solid evidence of the common desire of the people in



today's China to embrace universalism in replacement of particularism. The desire is especially strong in modern educated Chinese who believe that *guanxi* connections should not be used as unconditionally as they are now. They reason that more institutionalized modes of behavior should be in place to minimize the dominance of *guanxi* in the society. However, such a de-emphasis of *guanxi* relations can hardly be realized in the near future, given that individuals are indoctrinated with the Confucian ideology of role obligations. They are deeply engulfed in the relational construction of personhood of the Chinese culture.

Nevertheless, the Chinese are now torn between a wish for a universalistic rationality and an existing dysfunctional institutional structure. To solve the dilemma, some individuals resort to other means to reduce the dominance of *guanxi* in their daily encounters. Hwang (1987) has proposed four different methods of *guanxi* avoidance:

1. Individuality incorporation

This is to internalize the element of individuality into a person's behavior. The new attitude places less emphasis on the social evaluation of others in the network. It stresses the essentiality to act on one's own terms, rather than being concerned with face or fear of bringing shame to other in-group members in the case of deviant behavior. However, such a socializing process has to start early in childhood; otherwise, it is hard for a person to incorporate the individualistic idea when he/she has long been nurtured in a relation-oriented environment.

2. Functional compartmentalization

This is to separate specific economic transactions from diffused social exchanges (King 1991). Functional compartmentalization can be achieved by enforcing clear-cut rules which are designed to override the rule of *renqing* in interaction. The new social norms should allow individuals to act in accordance with an equity rule which accentuates individuals' contributions. This will enable the organization to operate in

an impersonal and fair climate. One way of doing this is to adopt the Euro-centric management rule of equity.

### 3. Evasion

This is to have a total separation between self and the relational environment. Dispatching the person to overseas assignment is an example of evasion. When the individual is relocated in an unfamiliar community, the rule of *renqing* will become dysfunctional. It will only operate again when mixed ties have been established between him/her and the inhabitants of the new environment. Yet, it is assumed that the instrumental tie will be promoted instead, because *guanxi* avoidance is the aim of evasion.

### 4. Psychological compartmentalization

This is to compartmentalize the different domains in life on a psychological basis. Different operating rules will be applied to different domains. For instance, the rule of equity is dominant in business functions; while the rule of *renqing* is used in the domain of familial interaction.

## 3.5 SUMMARY

To conclude, *guanxi* is an art which requires individuals to be tactful in crafting relations. The *guanxi* cycle commences with *guanxi* building which is essentially a transformation process. The process will erect a connection between two formerly unrelated individuals and transform the out-group identity of an individual to be an insider of the Chinese community. The connection can be built by two means: group identification and altercasting. Group identification is a process by which commonality is cultivated among individuals. Commonality can be in the form of innate attributes (ascribed *guanxi* base) or shared experiences (achieved *guanxi* base). Altercasting is to establish *guanxi*

relations by rearranging the social networking systems of targeted persons wherein individuals desire to be included. This can be easily achieved by the use of intermediaries.

According to Yang, four different mechanisms evolve in a *guanxi* relation after the transformation process has occurred. They are the processes of incorporation, moral subordination, appropriation and conversion. The four micro-physical mechanisms elicit repeating cycles of reciprocity which will deepen the commitment of involved parties in the *guanxi* relation. Reciprocation, together with dependability, are essential in maintaining *guanxi* ties which are expected to gain great *guanxi* benefits for individuals. There are four major forms of *guanxi* benefits: gift capital, symbolic capital, office capital and political capital. It is the symbolic capital which obliges individuals to be engaged in the conversion process.

Owing to the tremendous *guanxi* benefits, the practice of *guanxi* predominates in today's China. However, a growing condemnation of the devious use of *guanxi* relations for personal goal attainment by modern young Chinese has surfaced. They advocate that universalistic rationality should take precedence over particular ties if the objective of modernizing China is to be accomplished, and if individuals prefer to reserve greater autonomy for themselves.

## CHAPTER 4

### RESEARCH MODEL AND HYPOTHESES

In depicting the social mechanisms of *guanxi*, Bruce Jacobs (1979) and K.K. Hwang (1987) have proposed different models to relate *guanxi* with its associated elements. Each is based on a different perspective with a different focus. Jacobs' preliminary model aims at outlining the relationship between the *guanxi* base and the strength of *guanxi*. Hwang's model focuses on the psychological struggle within individuals in decision making when they are confronted with petitions, and on the consequences of decisions on *guanxi* maintenance. Together, these conceptual frameworks form the basis of the proposed model to be tested.

#### 4.1 BRUCE JACOBS' PRELIMINARY MODEL

There are three main variables in Jacob's model, namely *guanxi* base, affect (*gan-qing*<sup>12</sup>) and the value of *guanxi*. *Guanxi* base is defined as a "commonality of shared identification" upon which *guanxi* can be developed. It is the independent variable in the model, and is measured in terms of its existence. It determines the presence or absence of *guanxi*. It is hypothesized that *guanxi* cannot be developed without a *guanxi* base. However, the quality of *guanxi* depends on the intervening variable, affect (*gan-qing*).

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<sup>12</sup> In the original article, "affect" was translated as "*kan-ching*". It is now re-transliterated as "*gan-qing*" following the pin-yin system, in order to maintain consistency in this thesis.

Jacobs' definition on *gan-qing* follows closely Fried's analysis. As stated in footnote 5, the qualities of *gan-qing* in Fried's work coincide with the definition of *renqing* in the thesis. Hence, the materials associated with *gan-qing* in Jacobs' article are taken as supports for *renqing* to be used in the proposed model.

Jacobs' definition of 'affect' follows the classic analysis of Fried (1969). It is something more than the affective component of a relationship. It has less warmth and more formality of contact with a high intention of exploitation. It is suggested that good affect is required for close *guanxi*. In the model, the strength of *guanxi* is labeled as the value of *guanxi* which is the dependent variable. It is operationalized into three ordinal levels: close, distant and non-existent. The interplay of the three variables (*guanxi* base, affect and value of *guanxi*) constitutes the social mechanisms of the *guanxi* construct. The following is the schematic outline of Jacobs' *guanxi* model which describes various relations among the three variables.

<b><i>Guanxi</i> Base</b> <u>(Independent Variable)</u>	<b>Affect (<i>Gan-qing</i>)</b> <u>(Intervening Variable)</u>	<b>Value of <i>Guanxi</i></b> <u>(Dependent Variable)</u>
Present	Good	Close
Present	Absent	Distant
Absent	Absent	Non-existent

It is hypothesized that close *guanxi* will be cultivated with the presence of a *guanxi* base and good affect. Alternatively, distant *guanxi* will be developed if there is only a *guanxi* base but without any good affect. Lastly, *guanxi* will not flourish without the two required ingredients of the *guanxi* base and affect.

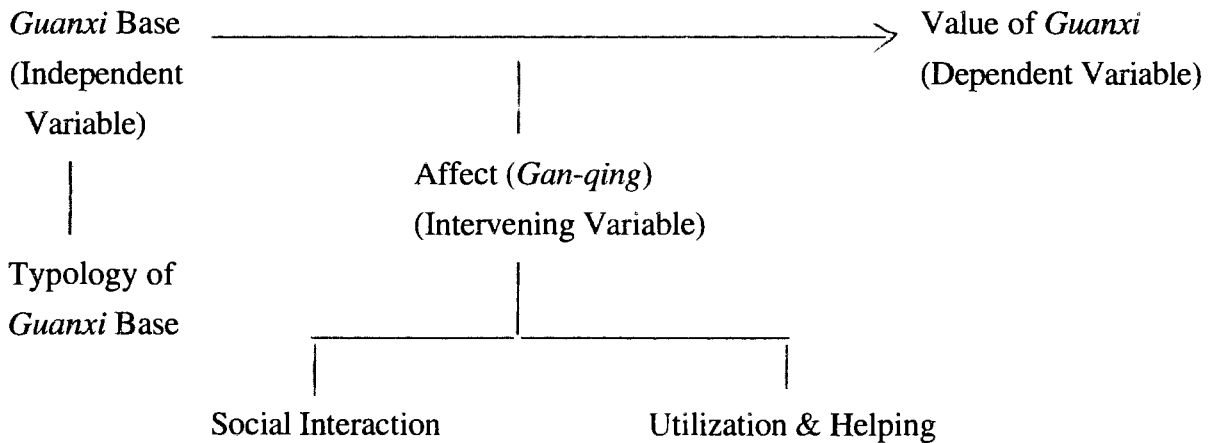
In Jacobs' model, it is postulated that the value of *guanxi* and the occurrence of affect depend on two dynamic processes. The first is the social interaction among parties involved which denotes social functions such as sending gifts and holding banquets. Social interaction is important to the development of close *guanxi*, and *guanxi* will wither without it. The second is the utilization of *guanxi* and the helping of *guanxi* members. They are the two sides of the same coin. Both are essential for fostering affect due to the instrumental nature of *guanxi*. However, individuals will not commit to help if there is no

affect between them and the petitioners. Thus, there is a mutual direct relationship between affect and utilization/helping.

Another element that is important to the maintenance of *guanxi* is dependability. Dependability varies directly with the value of *guanxi*. That is, the closer the *guanxi*, the more reliable the relationships are; or vice versa.

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Figure 4 : Bruce Jacobs' Preliminary Model on *Guanxi* (1979)



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**4.2 K.K. HWANG'S PSYCHOLOGICAL MODEL**

The most important contribution of Hwang's model (1987) is the pioneer postulation of operating rules in different domains of social relationships. Hwang suggests that there are three different types of social relationships. The first is the instrumental tie which is governed by the rule of equity, with an emphasis on the actual contribution of individual members. In this category, decision making is based on market rationality. The second is the expressive tie which is dominated by the need rule. The foremost consideration for decision making is the needs of others. The third is the mixed tie which is a mixture of the two former domains. The decision rule is the norm of *renqing* with a special accent on reciprocity. Hwang hypothesizes that it is in the domain of the mixed tie

that *guanxi* is developed, while the other two categories are not concerned with any *guanxi* building.

Decision making in the mixed tie is complicated by the dilemma of *renqing* which requires resource allocators to weigh five factors: the cost of performing the request; the anticipation of reciprocation; the social evaluation from other people in the same *guanxi* network; one's *guanxi* relations with petitioners; and the face of petitioners. Individuals will accept requests if there is a net gain, but reject the plea in case of a net loss. The decisions made will directly affect *guanxi* development, mediated through the face work of petitioners. Petitioners will lose face in the event of rejection, and they will engage in the actions to save face. In contrast, the face of petitioners is enhanced if the requests are accepted. Acceptance will reinforce the *guanxi* connections between petitioners and resource allocators. Consequently, there is a feedback loop flowing to *guanxi* relations from the decisions of resource allocators.

The two foregoing models have made a tremendous contribution to the exploration of the *guanxi* construct. Jacobs' preliminary model focuses on the initial stage of the *guanxi* cycle: the transformation process. It has a clear postulate on the causal relationship between the *guanxi* base and *guanxi*. It also presents a full discussion of the typology of the *guanxi* base which attaches different degrees of importance to various *guanxi*.

Hwang's model confines itself to the psychological struggle of resource allocators in the face of requests. With the inclusion of face, the model encompasses Yang's four mechanisms for *guanxi* maintenance, namely incorporation, moral subordination, appropriation and conversion. It suggests that there is a close relationship between *guanxi* maintenance and the decision making of resource allocators.

As each model has its own strength and focus, they are together taken to form the base of the proposed model which is a representation of a complete *guanxi* cycle.

### 4.3 BASIC COMPONENTS OF THE PROPOSED MODEL

The proposed *guanxi* model is comprised of three different stages: *guanxi* building, *guanxi* maintenance and *guanxi* benefits.

#### 4.3.1 *Guanxi* Building

Jacobs' preliminary model has provided a solid foundation in this respect, with an emphasis on *guanxi* base in building *guanxi*. However, the *guanxi* base only denotes the process of group identification. It does not cover the full domain of the transformation process.

From the literature, *guanxi* can be established by two means: group identification and altercasting. The means of *guanxi* building based on group identification is applicable to individuals who have already been in the Chinese society. They have built up their own networks and have various attributes for identification.

Nevertheless, group identification is inappropriate for newcomers to the Chinese community because they have no pre-established connections. Since newcomers do not have any attributes which enable them to be identified with other members in the *guanxi* circle, they have no resources to initiate the group identification process. The only alternative for them is altercasting which is presented in Hwang's model. Consequently, both group identification and altercasting are variables under the process of transformation in the proposed model.

In group identification, there are two types of *guanxi* bases: ascribed and achieved. Both types contribute to *guanxi* establishment, and both have their own sphere of commonality.

With the establishment of *guanxi* connections, two-way interaction starts to flow between two unrelated individuals. The newly built relationship has to be constantly nurtured through continuous interaction which is an essential part of *guanxi* maintenance.



### 4.3.2 *Guanxi* Maintenance

*Renqing* is a cardinal element in *guanxi* maintenance. It is cultivated through social interaction. Yet, the scope of social interaction in the proposed model is much larger than that in Jacobs' model. It encompasses the circulation of gifts, banquets and favors, as well as utilization and helping. Utilization and helping are included in the model because they are conceived as part of interaction among individuals.

*Renqing* is highly affected by the element of dependability. As stipulated by Jacobs, dependability denotes the commitment of individuals to the relations. It strengthens *guanxi* relations as well as enhances *renqing*.

*Renqing* is achieved when individuals accept the requests of petitioners after experiencing the psychological struggle in decision making. Therefore, Hwang's model is incorporated in the concept of *renqing*. For the sake of parsimony, only the category of mixed tie is included since it is only in this domain that *guanxi* relations are cherished. Accordingly, only the rule of *renqing* will be tested.

In Hwang's model, face work assumes an important role in *guanxi* reinforcement as the mediating variable. However, face, in itself, is a very complex construct which deserves a whole separate research study.<sup>13</sup> Owing to its complexities, the general concept of face is included in the proposed model, but its detailed mechanisms are excluded. Fortunately, the omission does not invalidate the other mechanisms of *guanxi* in the model. Hence, the feedback loop flows from the decision making of resource allocators through a black-box of petitioners where face work is formerly located in Hwang's model, and then goes on to either strengthening or weakening *guanxi* relations.

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<sup>13</sup> For in-depth discussion of the face concept, please refer to the classic analysis by David Y.F. Ho "On the Concept of Face", American Journal of Sociology 81:867-884, 1976. Hu Hsien Chin "The Chinese Concept of Face", American Anthropology 46:45-64, 1944. Simon Liu "Family, Face and Fate in *Guanxi* Capitalist Societies and Their Business Implications for North American Firms", Unpublished MBA project, 1993.

With good *guanxi* maintenance, *renqing* is greatly enhanced. The end result is the enjoyment of *guanxi* benefits which is the last stage in the model.

### **4.3.3 Guanxi Benefits**

In the proposed model, *guanxi* benefits are conceptualized as the goal attainment of individuals. According to Yang, there are four main types of *guanxi* benefits (gift capital; symbolic capital; office capital; and political capital). However, only gift and office capitals are included in the proposed model because of their objectivity and measurability. Both symbolic and political capitals are too abstract for respondents to grasp as benefits of *guanxi* as well as being too difficult to measure. Therefore, they are excluded from the proposed model. Goal attainment is measured in terms of the form and level of *guanxi* benefits gained.

### **4.3.4 Dynamics of the Model**

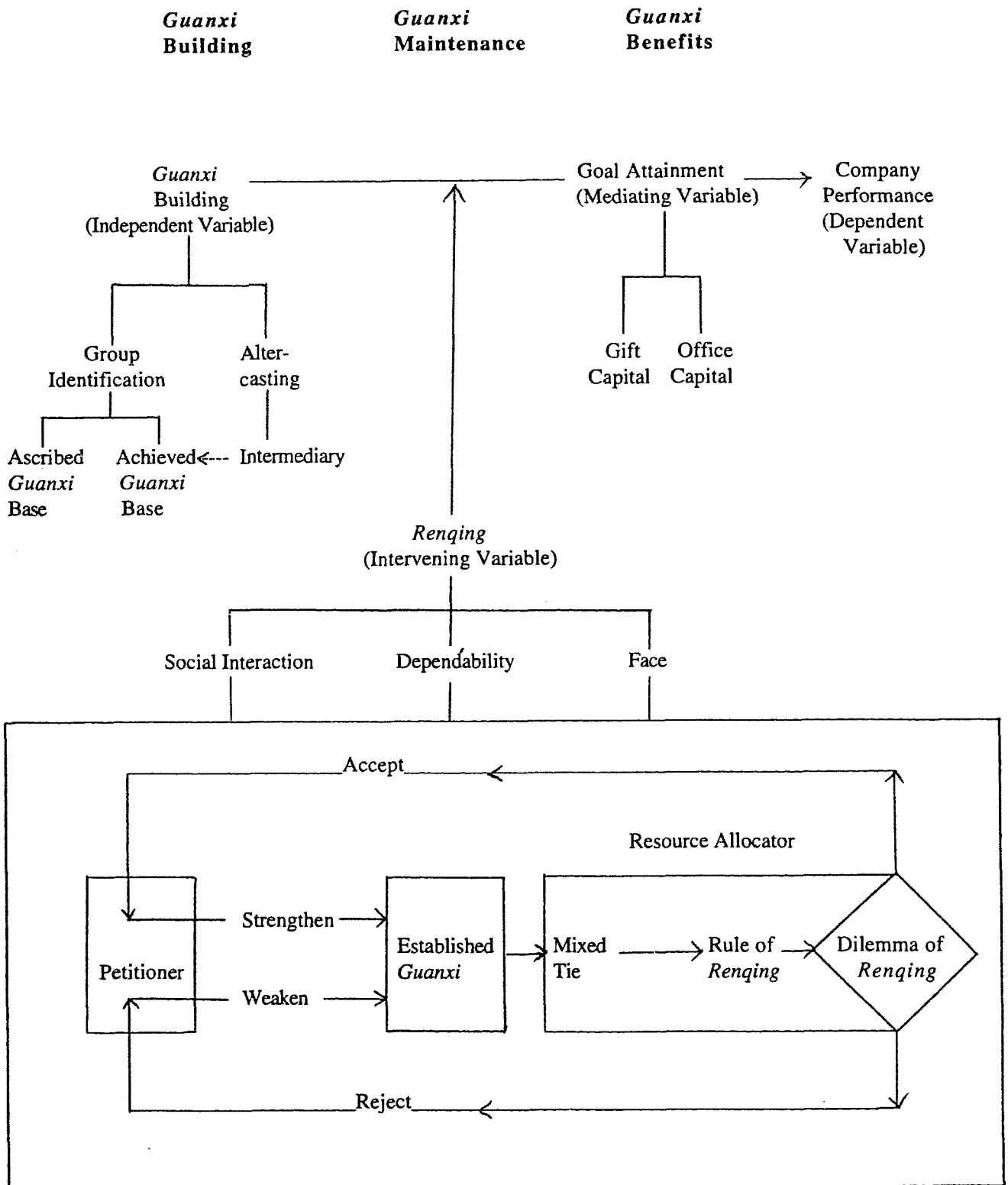
The three primary elements (*guanxi* building, *renqing*, and goal attainment) are the three basic components of the proposed model. *Guanxi* building takes the role of an independent variable. It is affected by group identification and altercasting in the stage of transformation. It determines the level and form of goal attainment (gift and office capitals) through which company performance can be achieved. Hence, goal attainment is the mediating variable and company performance is the dependent variable in the model. However, the simple causal relationship is disturbed by an intervening variable, *renqing*. *Renqing* is accumulated through positive social interaction amongst individuals and it will cherish dependability for individuals who continuously make positive responses to in-group members' requests.

In the face of a petition, the decision made is the end-result of a psychological struggle governed by the rule of *renqing*. Consequently, *renqing* is an element that will affect the level of goal attainment. But, it cannot be treated as another independent variable

because it cannot stand on its own. *Renqing* is a supplementary component of *guanxi* and is fostered only after *guanxi* has been established. It is assumed that there is a positive relationship among the three variables (*guanxi* building, *renqing* and goal attainment). That is, the greater the *renqing* in the relationship, the closer is *guanxi*, and the higher the level of goal attainment.

The foregoing section outlines the basic components and the dynamics of the proposed model. The following discussion will highlight the hypotheses for testing and their relevant managerial implications.

Figure 5: The Proposed Research Model on *Guanxi*



## 4.4 HYPOTHESES AND MANAGERIAL IMPLICATIONS

The objective of this research study is to assess the impact of *guanxi* on business performance and to formulate a strategy which will enhance business success through the practice of *guanxi*. Non-Chinese investors have been chosen as the target audience of the current research since they have been reported to experience tremendous frustration in *guanxi* building. The exploration is conducted at both macro and micro levels with a special emphasis on the micro mechanisms within the *guanxi* construct.

### 4.4.1 Macro Level

*Guanxi* has been well cited in the literature as one of the most important success factors in business operations in China. It would be essential to examine the overall relative importance of *guanxi* on business operations, as compared to other key success factors (e.g. price and product quality). Based on the literature, ten factors have been selected for comparison with *guanxi*. These ten elements have been cited in the literature as important in doing business in China. Hence, it is proposed that:

**Hypothesis 1 : The business practitioners who have been doing business with China think that *guanxi* is the most important factor among the following 11 elements in attaining business success in China.**

The 11 elements are:

- Choosing the Right Business Location
- Choosing the Right Entry Strategy
- Competitive Prices
- Complementarity of Goals
- Familiarity with the Chinese Negotiation Style
- Flexibility in Business Operations in China
- Guanxi* relations with Chinese business associates
- Long-term Business Commitments in China

Management Control in Business Operations in China

Product Differentiation / Quality

Understanding China's Policy and Legislation

Managerial Implications :

If Hypothesis 1 is supported, non-Chinese businessmen should spend a lot of effort and time on *guanxi* building, given that it is the key to business success in China. More importantly, they have to know the effective ways of establishing and maintaining *guanxi*. This will require them to have full understanding of the micro-mechanisms of the construct.

#### 4.4.2 Micro Level

##### 4.4.2.1 Guanxi Building

The *guanxi* cycle commences with *guanxi* building. It is postulated that *guanxi* can be established through group identification and altercasting. It would be interesting to explore the relative effectiveness of the two processes. It is stated in the literature that ascribed *guanxi* bases (e.g. kinship) are more significant than achieved ones. This statement should be tested in an in-depth investigation of *guanxi*.

**Hypothesis 2 : Other elements being equal, ascribed *guanxi* base is more effective than achieved *guanxi* base in establishing *guanxi* relations.**

Managerial Implications :

The primary notion of *guanxi* building is to transform oneself from the identity of an outsider to that of in-group member. Group identification and altercasting are the ways to facilitate such a transformation. For non-Chinese business practitioners who are certainly perceived as outsiders by the Chinese, the most appropriate method is altercasting. Being newcomers to the Chinese society, non-Chinese do not have any commonality for shared identification with the locals. Therefore, altercasting through intermediaries can be regarded as the initial step to establish *guanxi* connections. Yet, it is not the end of the

building process. Altercasting has to be followed by group identification for *guanxi* relations to be consolidated between non-Chinese and the Chinese.

As noted in the literature, non-Chinese are perceived as not being serious about doing business in China if they do not develop long-term personal relationships with local parties. This implies that non-Chinese should eventually entangle themselves into *guanxi* networks if they want to have business success instead of relying totally on intermediaries. This would require non-Chinese to maintain personal presence in China, such as stationing in the oriental country or at least making frequent visits to China. This is because more common attributes for shared identification can be cultivated through continuous social interaction. It allows non-Chinese to create more achieved *guanxi* bases of familiarity so that stronger *guanxi* can be promoted.

The next implication concerns the long-term commitment to *guanxi* building which is proposed to affect business performance greatly. In order to be in-group members, non-Chinese have to know the culture and the rules of the *guanxi* game. This requires patience and persistence to learn incrementally through personal experience in China.

#### 4.4.2.2 Guanxi Maintenance

The most important element for testing in this stage is the direct relationship between *renqing* and goal attainment. However, owing to complexities in the nature of *renqing*, an objective measurement of *renqing* in terms of quality or quantity may not be feasible. As an alternative, the elements which are required to sustain *renqing*, such as social interaction, are investigated.

As suggested in the literature, *renqing* flourishes through social interaction. It is conventional belief that social interaction with the Chinese is cherished by questionable payment, banquets and gift-giving. These activities can be categorized as offering short-term gains to the Chinese, since the benefits are to be consumed within a short period of

time. It is worthwhile to evaluate the effectiveness of these short-term gains in maintaining *guanxi* relations and in attaining business success in China. Hence, it is postulated that:

**Hypothesis 3 : Other elements being equal, the individual will have a higher chance of enhancing corporate financial performance if he/she has employed a strategy of offering short-term gains to maintain *guanxi* relations.**

In the stage of *guanxi* maintenance, individuals are mostly faced with requests from other in-group members. Resource allocators are tortured by the dilemma of *renqing* and will undergo a psychological struggle in the decision-making process presided by the rule of *renqing*. In resolving the dilemma, resource allocators will weigh five factors: the cost in performing the requests; the anticipation of reciprocation; the social evaluation by significant others in the same network; the *guanxi* relations with petitioners; and the face of petitioners. Thus, it is essential to examine the validity of the above postulation.

**Hypothesis 4a : The cost to the individual in performing the request is the most important factor in the decision-making process when considering a request.**

**Hypothesis 4b: The anticipation of reciprocation is the most important factor in the decision-making process when considering a request.**

**Hypothesis 4c: The evaluation of an individual's behavior by significant others in the same social network is the most important factor in the decision-making process when considering a request.**

**Hypothesis 4d: The *guanxi* with the requester is the most important factor in the decision-making process when considering a request.**



**Hypothesis 4e: The face of the requester is the most important factor in the decision-making process when considering a request.**

Managerial implications :

The hypotheses tested in this stage will enlighten non-Chinese on *guanxi* management. If the method of offering short-term gain is confirmed to be effective in cultivating *guanxi* relations, non-Chinese should try to maintain continuous social interaction with their Chinese business associates through the circulation of gifts, banquets and favors. Only in this way will they have higher chances of attaining greater business success.

The hypotheses testing the five factors in decision making are important for non-Chinese to present requests to or reject requests from other in-group members. Knowing the factor that is most salient in Chinese business decision making, non-Chinese can either stress the benefits their requests will bring to that particular factor when they present requests to other in-group members; or downplay the negative effects of rejections on the particular factor.

4.4.2.3 Guanxi Benefits

According to Frankenstein (1991), with whom *guanxi* is developed is important. The key consideration is to establish *guanxi* with the right persons who can give non-Chinese competitive advantages in business negotiations and transactions. Hence, it is proposed that:

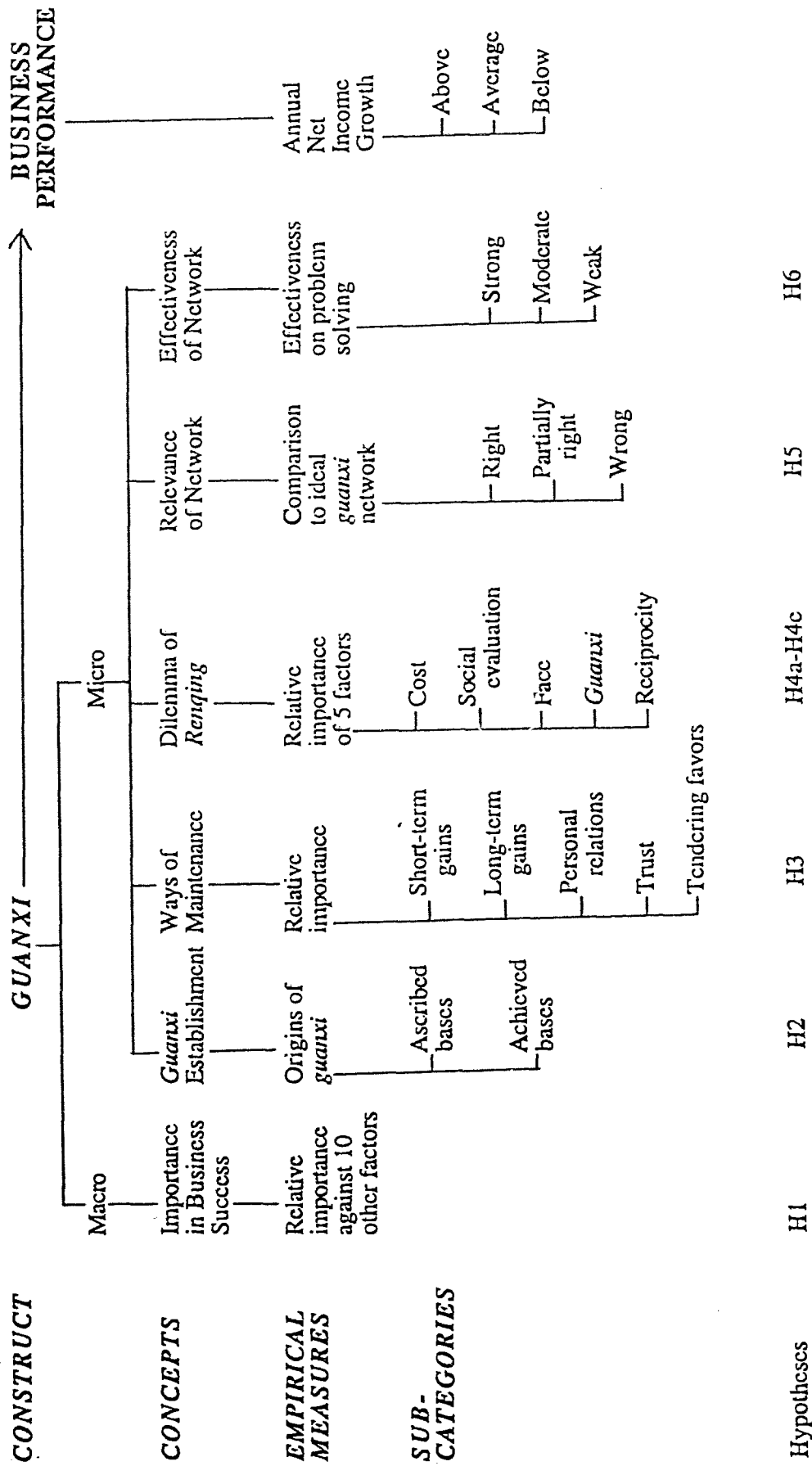
**H5 : Other elements being equal, the firms that have right *guanxi* with Chinese business associates are more successful in enhancing corporate financial performance than firms that do not.**

**H6 : Other elements being equal, the firms that have strong *guanxi* with Chinese business associates are more successful in enhancing corporate financial performance than firms that do not.**

*Managerial implications :*

The most important message for non-Chinese is to source the right route to the *guanxi* benefits they particularly hunger for. The right route means to know the right persons and nurture strong *guanxi* with them. Building weak *guanxi* and cultivating relations with wrong persons will not contribute to the attainment of business success in China. Both right and strong *guanxi* are required to direct non-Chinese investors to the treasury of their desired gains which will lead to higher business performance.

Figure 6 : OPERATIONALIZATION OF GUANXI CONSTRUCT



## CHAPTER 5

### RESEARCH DESIGN AND METHODOLOGY

Little progress has been made in the research exploration of the *guanxi* construct. It is not only because negligible attention was paid to the subject by social science researchers in the past; more importantly, the abstract nature of the construct has impeded social scientists to make any progressive stride in the investigation. Hitherto, the specificity of *guanxi* is still largely unknown and well-defined research concepts of *guanxi* have yet to be established. Hence, the current research is, in essence, an exploratory study with the aim of making inductive analyses of the complex research construct.

#### 5.1 Research Methodology

The technique of qualitative personal interview was selected to conduct the current research for two reasons.

1. *Guanxi* is a very sensitive issue that individuals would have great hesitation to disclose in a mailed survey questionnaire. In fact, individuals find it difficult to discuss *guanxi* relations openly with anyone whom they do not know nor trust. Personal interviews are the preferred approach because interviewers can establish rapport and trust with respondents during the interview sessions so that respondents are more comfortable in releasing sensitive information.
2. Personal interviews facilitate securing in-depth information on research concepts which are inaccessible by quantitative surveys or telephone interviews, thereby greatly enhancing the quality of research findings. This is particularly important in an exploratory study such as this one. It is hoped that the qualitative interviewing

technique would enable the researcher to discover the hidden dimensions of *guanxi* as well as foster new insights into the understanding of the *guanxi* construct.

### 5.1.1 Procedures

Qualitative data were collected through a format of semi-structured interviews. An interview protocol of 36 open-ended questions was developed and administered to each respondent. [Please refer to Appendix 2 for the interview protocol.] The open-ended questions allowed respondents to add any information that was salient to them on specific research concepts. Consistency among various interviews was maintained by asking the same set of questions.

Pilot tests were conducted with the executives of three non-Chinese firms to detect any problems with the interview protocol. After conducting two pretests, revisions were made on the wording of specific questions which were unclear. Some questions were dropped because the two pretest subjects complained the interviews were too lengthy. A third pilot test was administered after revisions in order to ensure the quality of the interview protocol. This was completed with a satisfactory result.

The questions were translated into Chinese by an ethnic Chinese who obtained a Master degree in Communications and was working in the public relations and communications industry in Vancouver. The specific terms of Chinese entities were transliterated by an MBA student at Simon Fraser University who originally came from Beijing (China). This was to insure the appropriateness of the Chinese terminology. The interview protocol was back-translated into English by another ethnic Chinese who was teaching English in a high school in Vancouver. The three steps together were taken to confirm the accuracy of the translation.

## 5.2 Research Sample

The research study was launched from November 1994 through February 1995. All the interviews were conducted in Hong Kong, except three which were conducted in Canada. Hong Kong was chosen to be the location for research interviews for two reasons:

### 1. Requirements of research sample

Since non-Chinese investors were the target audience of the current study, the research sample should possess some resemblance in terms of the key characteristics of *guanxi* building. One of the most salient features of non-Chinese investors was their out-group identity as perceived by the local Chinese. However, the research subjects should also possess in-depth experience in *guanxi* building such that they would provide enlightening insights on the *guanxi* construct. The two restrictive requirements were fittingly fulfilled by the crossvergent identity of Hong Kong people (Ralston, Gustafson, Cheung and Terpstra 1993). Hong Kong people were generally conceived by the local nationals of China as outsiders, even though they were ethnic Chinese. This is because Hong Kong is a genuinely capitalist society which differs fundamentally from Communist China in terms of socio-economic and political systems. However, Hong Kong executives are preferable to non-Chinese investors as research subjects because they know Chinese culture. Hong Kong people are deeply shaped by Confucian values in the same way as the local Chinese, and they closely adhere to some traditional Chinese customs. Hence, Hong Kong is a point of convergence between the Chinese and Euro-centric cultures, and Hong Kong managers are most suitable to be the sample subjects of the current study.

### 2. Accessibility of representative research subjects

Hong Kong is the gateway leading to mainland China. It functions as an intermediary between China and the outside world since an increasing share of foreign investment and business in commodity trade and tourism in China is handled through

Hong Kong (Sung 1991). Thus, Hong Kong was seen as an optimal location for launching the research where a representative sample could be easily recruited.

Research subjects were mainly recruited through the referral of friends and relatives of the researcher. Although true random sampling was sacrificed in this study, sampling bias was largely avoided because there was a wide coverage of research subjects in terms of age, industry type, experience level, ownership type and education level. No specific selection criterion of research subjects was set, except that they had to be currently doing business with China. The wide coverage of potential research subjects was designed to maintain a high external validity of research findings since the current research was an exploratory study rather than a confirmatory analysis.

The only sampling bias that might influence the study's findings is the ethnicity of research subjects. By coincidence, all the research subjects turned out to be ethnic Chinese. This applies to the non-Chinese companies interviewed in both Canada and Hong Kong. The non-Chinese firms employed ethnic Chinese who originated in Hong Kong to handle the China market. Hence, the research findings fully reflect the mentality of Chinese (Hong Kong) on the *guanxi* construct.

Twenty companies were recruited to participate in the research study. Each of the twenty respondents was invited to attend a personal interview of one-and-a-half to two hours. Chinese was used as the medium of communication to capture the full meaning of information solicited in the interviews, since all the research subjects were ethnic Chinese. However, in data analysis, one company was dropped from the study because the respondent was unwilling to disclose information concerning company performance which was a critical variable for data analysis. Therefore, the research findings were derived from the information of nineteen companies only.

The interviewees were either directors, managers or top representatives who headed the China business division in 1994. The research sample was comprised of 11 Hong Kong firms (57.8%), 5 American companies (26.3%), 1 Canadian business operation

(5.3%), 1 German trader (5.3%) and 1 Swedish company (5.3%). The majority of respondents (63.2%) were in the age range of 31-40. Three other interviewees (15.8%) were between 41-50 years old; two respondents (10.5%) were 21-30, and the remainder (10.5%) were over 50 years of age. In terms of education, 10 respondents (52.6%) had university education, while five interviewees (26.3%) had masters degrees. The remainder (21.1%) had completed high-school. Of the 19 respondents, 16 (84.2%) were male and 3 (15.8%) were female.

### **5.3 Financial Performance of Respondents**

Company performance is the dependent variable in the proposed model. It is operationalized by measuring the sales revenue generated by Chinese business operations through the sale of manufactured/imported/exported products in world and/or China markets.

Two sets of financial data were collected from respondents: annual sales growth and annual net income (pre-tax profits) increase. However, only the data on annual net income increase were used for analysis for the following two reasons:

1. It was suggested by respondents that *guanxi* building would involve huge social expenses and questionable payment. The enormous social expenses would definitely inflate the operation cost and thus leave a low profit margin.
  2. The sales volume increase did not necessarily reflect the efficiency of the firm. For instance, Company 7 had an annual sales increase of 30% for the past three years. However, the annual net income growth was only 2% for 1991 and 1992, 0% for 1993 and it had a net loss for 1994. In another case, Company 1 had a decrease in annual sales growth, because of the loss of sales markets in Mexico and Latin America. Yet, the annual net income growth for the company was over 300% for the past three years.
- Consequently, the research findings would have greater validity if the analysis on company performance was mainly based on annual net income growth.



### 5.3.1 Methods of Analysis

In the research model, it is hypothesized that firms which have established a good *guanxi* network in China will attain higher business performance. Higher business performance is determined by comparing the corporate financial results (i.e. annual net income growth) of the nineteen respondents against their corresponding industry norms in China. The industry norms are statistics taken from the China Statistical Yearbook (1991-1994), compiled by the State Statistical Bureau of the People's Republic of China (Beijing). Respondents were then coded in the following categories:

"Above Average" : The company performance was above the industry norm in China.

"Average" : The company performance was at the industry norm in China.

"Below Average" : The company performance was below the industry norm in China.

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Table 5.1: Company Performance of Respondents

Year	Percentage of Annual Net Income Growth (%)						Comparison Results		
	Company Performance			Industry Norms			'91	'92	'93
	'91	'92	'93	'91	'92	'93	'91	'92	'93
Company 1	300	300	300	22.92	38.74	-2.53	AA	AA	AA (1)
Company 2	20	20	30	16.35	2.02	--	AA	AA	-- (2)
Company 3	20	20	30	22.92	38.74	-2.53	BA*	BA	AA (1)
Company 4	--	20	20	--	--	--	--	--	-- (3)
Company 5	--	20	20	15.03	24.59	20.12	--	BA	A
Company 6	10	7	30	10.68	61.57	250.06	A	BA	BA (4)
Company 7	2	2	0	41.64	24.02	17.30	BA	BA	BA
Company 8	10	-5	20	-19.39	13.73	-16.81	AA	BA	AA
Company 9	--	25	-30	-19.39	13.73	-16.81	--	AA	BA
Company 10	10	10	10	16.17	28.73	61.76	BA	BA	BA
Company 11	10	20	30	10.68	61.57	250.06	A	BA	BA
Company 12	100	100	100	16.17	28.73	61.76	AA	AA	AA
Company 13	30	35	65	16.17	28.73	61.76	AA	AA	AA
Company 14	25	25	75	--	--	--	--	--	-- (3)
Company 15	45	45	100	35.78	31.60	28.95	AA	AA	AA
Company 16	--	100	120	16.17	28.73	61.76	--	AA	AA
Company 17	5	10	10	-2.63	8.47	-15.31	AA	AA	AA
Company 18	0	0	0	--	--	--	--	--	-- (3)
Company 19	8	8	8	31.21	58.37	35.61	BA	BA	BA

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Limitations of the comparison of company performance:

- (1) Although Company 1 and Company 3 were in the toy manufacturing industry, their performance was compared to the figures of plastic products manufacturing for two reasons. Firstly, no statistics could be found on the annual net income growth of toy manufacturing in China. Secondly, the chief raw material of the toys manufactured by these two firms was plastics. Hence, it was justified to use the figures of plastic products manufacturing as the industry norm for comparison for the two companies.
- (2) Company 2 specialized in the manufacturing of electronic audio products and computer accessories. It was compared to the statistics of consumer electronic apparatus rather than to those of electronic and telecommunication equipment, since the latter was a broad category which was comprised of large-scale computer and telecommunication products. No comparison could be made on the company performance for 1993, since the figure of consumer electronic apparatus could no longer be found in the China Statistical Yearbook 1994, due to a reformat of reporting lines.
- (3) Unfortunately, no statistics had been compiled by the State Statistical Bureau of China on the industry growth of the service sector. This was because the tertiary industry was not selected for priority development in the past decade; and thereby received less attention from the Chinese Government. Consequently, those respondents who were in the service sector would be treated as missing data if the analyses were related to company performance (except the case of Company 6).
- (4) Company 6 was a real estate construction and property management firm. Although it emphasized more on property management, its performance was compared to the figures of the construction industry for two reasons: (a) no statistics could be found on the annual net income growth of the property management sector in China; (b) construction industry figures encompassed profits derived from labor service, operation sales and construction. Property management was one of the components of the figures, as defined by the State Statistical Bureau of China.

- \* The performance of Company 3 was marginally below the industry norm by 2.9% in 1991. A benefit of doubt should be given to the company because the statistics quoted by Co. 3 representative during the interview were only approximate figures rather than actual values.

## **5.4 Control Variables and Coding Methods**

Meaningful relationships between independent and dependent variables in the research model may be confounded by some extraneous elements which should be controlled in hypothesis testing. Hence, five control variables were used to conduct the detailed analysis of research data. These five elements were suggested by respondents and the literature to be significant in affecting the *guanxi* pattern in China.

### **5.4.1 Ownership Type**

Respondents were categorized on the basis of ownership of their business operations in China. This is chosen as one of the testing dimensions because the behavior of companies operating in China is not only bound by Chinese laws and regulations, but is also governed by the jurisdiction of their home countries. Problems would arise when the regulations between the two locations are in direct conflict. For instance, American or Canadian firms are forbidden by the laws of their home countries to engage in any questionable payment which is a very common phenomenon in the Chinese business arena. Consequently, it would be interesting to see whether this dimension would have any impact on the *guanxi* development of non-Chinese firms versus Chinese companies.

The two basic types of ownership presented in the research are "Chinese" and "non-Chinese". The criterion for differentiating the two types of ownership is based on the nationality of parent company. For instance, a wholly owned subsidiary in China would be classified as having non-Chinese ownership if its parent company is foreign.

Conversely, if the parent company is based in Hong Kong, the subsidiary in China would be categorized as a Chinese firm.

In the case of a joint venture with parties of different nationalities, ownership is defined by the nationality of parent company and equity. Equity ownership is preferred to management control as a testing standard because of its objectivity. Although it seems to be a more appropriate defining criterion for the current research, which partner has greater management control is difficult to detect, unless the researcher has a thorough understanding of the organizational structure and of the internal decision making mechanism of the joint venture. Such detailed comprehension cannot be obtained within a two-hour interview. In contrast, equity ownership is not ambiguous in determining which partner has a greater share of the company. For the sake of parsimony, it is assumed that the partner who has a larger share of equity would assume more management control because of greater voting rights.

The threshold point for defining ownership into "Chinese" or "non-Chinese" is set at 51%. That is, if 51% or over of the company is owned by Hong Kong people, it would be classified as a "Chinese firm". Correspondingly, if the non-Chinese partner owns 51% or over of the company, it would be categorized as a "non-Chinese firm".

In the research sample, all participating companies were either wholly owned subsidiaries or had more than 51% of equity ownership.

Table 5.2: Nationality of Organizational Ownership

Coding Method: "1" Chinese ownership  
 "2" Non-Chinese ownership

<u>Respondent</u>	<u>Nationality of Parent Company</u>	<u>Coding</u>
Company 1	Chinese	1
Company 2	Chinese	1
Company 3	Chinese	1
Company 4	Chinese	1
Company 5	Chinese	1
Company 6	Chinese	1
Company 7	Chinese	1
Company 8	Chinese	1
Company 9	Chinese	1
Company 10	Chinese	1
Company 11	Chinese	1
Company 12	Swedish	2
Company 13	American	2
Company 14	American	2
Company 15	American	2
Company 16	American	2
Company 17	German	2
Company 18	American	2
Company 19	Canadian	2

#### 5.4.2 Experience Level in China Business

The tenure of respondents in China business was measured in terms of the years of experience. As suggested by the literature, tenure may be a significant element in *guanxi* development since *guanxi* operates on a longevity dimension. *Guanxi* relations cannot be achieved instantly. It is a long-term nurturing process which requires individuals to invest enormous time and patience. The experience in China trade is an indication of the level of social investment that investors have spent on *guanxi* building. With long tenure in China business, old-timers may have nourished good *guanxi* relations with the Chinese in past years; while newcomers are only at the starting point of *guanxi* building. Hence, old-timers may have great competitive advantage over newcomers in attaining business success because of established *guanxi* networks.

The personal experience of respondents rather than the duration of their companies in the China market was used for analysis, because *guanxi* was suggested by respondents and the literature to be person-oriented. Person-orientation is a unique feature that differentiates Chinese *guanxi* from the social relations of Euro-centric cultures. This follows the assertion that *guanxi* is embedded in dyadic relationships, since it is a particularistic tie between two specific individuals. It is postulated that *guanxi* evolves around a particular person. It exists when the person is there; it is lost when the person is gone. This proposition was fully supported by six respondents who claimed that *guanxi* in China was centered around particular persons, rather than being retained in corporations as in the business relations of Euro-centric cultures. Two respondents (Companies 7 and 9) had frustrating experiences in *guanxi* building because their efforts were lost overnight when their Chinese *guanxihu* were relocated by the Chinese Government to other regions. They had to start from scratch in building *guanxi* with the new government officers.

Similar frustration was found by four other respondents when they replaced their predecessors in heading the Chinese business operations. They complained that they did not benefit much from the good *guanxi* cultivated by their predecessors, except that it connected them with their current Chinese *guanxihu*. One interviewee (Company 3) who was named by the Managing Director (his uncle) to be the successor of the Chinese manufacturing plant, asserted that Chinese *guanxi* was not transferable. He had a hard time in utilizing the good *guanxi* nurtured by his uncle with the Chinese, simply because the Chinese did not equate him with his uncle. The rationale of the non-transferability of *guanxi* was that personal trust was the cornerstone of *guanxi*, and it was a unique element that was specific to individuals. In the perception of the Chinese, the new successors were separate individuals from the predecessors. The same level of trust cherished in the *guanxi* ties with predecessors might not be achieved in the relations with successors. Hence, successors had to convince the Chinese of their trustworthiness, so that the Chinese were willing to maintain the same *guanxi* relations with them.

Consequently, Chinese *guanxi* was person-oriented and would not be retained in corporations when the 'founders' of *guanxi* resigned from office. The good *guanxi* relations nourished by predecessors would only connect successors with their current *guanxihu*, but would not be transferred directly onto them. The development of *guanxi* ties was a function of the approaches employed by successors in *guanxi* building, rather than being a mere adoption of the inheritance built by their predecessors. Hence, the personal experience of respondents in China business takes precedence over the tenure of their companies in the China market. As a result, some respondents were classified as "newcomers" based on their minimal personal experience in China trade, even though their companies had been established in China for ten or more years.

Table 5.3: Experience Level in China Business of Respondents

Coding Method: "1" Old-timers with over 10 years of experience in China trade  
 "2" Mature investors with 6-10 years of experience in China trade  
 "3" Newcomers with five years of experience in China trade or less

<u>Respondents</u>	<u>Years of Experience</u>		<u>Coding</u>
	<u>Company</u>	<u>Respondent</u>	
Company 1	15	15	1
Company 2	15	15	1
Company 3	8	2	3
Company 4	4	10	2
Company 5	3	8	2
Company 6	4	1	3
Company 7	10	10	2
Company 8	10	11	1
Company 9	2.5	8	2
Company 10	13	14	1
Company 11	3	15	1
Company 12	15	8	2
Company 13	9	8	2
Company 14	20	2	3
Company 15	10	11	1
Company 16	2	2	3
Company 17	5	14	1
Company 18	15	1	3
Company 19	3	3	3

### 5.4.3 Firm Size

The size of the business operation in China was measured in terms of the number of local employees hired. Root (1987) has pointed out that company size is a critical factor in the formulation of foreign market entry strategy. It is an indicator of the company's resources for foreign investment. The constraint on resources may affect business performance in China, since it is revealed in the literature and in empirical research that long-term commitment is the key to doing business with China. In this research study, the size of the business operations in China was taken as the defining criterion of firm size instead of the size of parent corporations, because the latter does not always reflect the level of investment committed by respondents in the China market. Large multi-national enterprises may not invest in China as much as small companies may, since they have diversified their resources in markets in different countries. Hence, the size of the business operations in China was a better indicator for examining the investment and commitment of companies in the China market.

The number of local employees instead of the Hong Kong assignees or expatriates to China was taken as a consideration in data analysis, because it was suggested by respondents that creating employment in China was perceived by the Chinese Government as a contribution to the country, and it would reflect the business commitment of the firms in China.



Table 5.4: Size of Business Operations in China

Coding Method: "1" Large firm with over 1000 local employees  
 "2" Medium firm with 100 to 1000 local employees  
 "3" Small firm with less than 100 local employees

<u>Respondents</u>	<u>Number of Local Employees</u>	<u>Coding</u>
Company 1	700	2
Company 2	7000	1
Company 3	2000	1
Company 4	0	3
Company 5	20	3
Company 6	10	3
Company 7	0	3
Company 8	5	3
Company 9	0	3
Company 10	10000	1
Company 11	20	3
Company 12	400	2
Company 13	150	2
Company 14	25	3
Company 15	0	3
Company 16	0	3
Company 17	100	2
Company 18	200	2
Company 19	4	3

#### 5.4.4 Industry Type

The type of industry that the Chinese business operation is in is of primary importance in determining business success because different industry types require different success factors that fit their unique nature (Root 1987). Some industries are under the priority development of the Chinese Government, and thereby may have a higher chance of goal attainment in China, e.g., high technology industry.

There were four main types of industries in the research sample:

1. **Tertiary Industry** This included two consulting firms, one real estate company and one banking institute. The four companies tendered intangible services in business transactions without the involvement of any tangible commodities.

2. **Exporting Industry** Four companies were classified in this group and they specialized in exporting textile products, medical goods and furniture. The primary tasks of the four exporters were to import products from different regions of China and export them to world markets for sale.
3. **Manufacturing Industry** This group of companies erected manufacturing plants in China, either in the form of a wholly owned subsidiary or a joint venture, in order to extract the advantages of cheap labor and operation costs in China. The chief function of these Chinese business operations was to manufacture tangible commodities which would be exported to other countries for sale. There were two sub-categories in this classification, and the differentiating criterion was the establishment of domestic sales in China. The first sub-group was the exporting manufacturers who exported the total outputs of their manufacturing plants in China to world-wide markets without establishing any domestic sales in China. The second sub-group was the selling manufacturers who imposed multi-purposes on their Chinese business operations. In addition to the manufacturing function, these firms perceived China as a lucrative market for their products and they tried to establish domestic sales. Part of their manufactured products would be poured into the China market, while the remaining would be exported out to its counterparts in other countries.
- 4) **Importing Industry** These companies imported products from other countries into China which served mainly as a sales market for the in-coming products. The group included the importing of computers, power generation systems, chemical and telecommunication products.

Table 5.5: Industry Type of Business Operations in China

<u>Respondents</u>	<u>Industry Type</u>	<u>Coding</u>
Company 1	Toy manufacturing	3A
Company 2	Manufacturing of electronic audio	3A
Company 3	Toy manufacturing	3A
Company 4	Town-planning consultancy	1
Company 5	Importing of power generation system	4
Company 6	Real estate management	1
Company 7	Exporting of medical products	2
Company 8	Textile exporting	2
Company 9	Textile exporting	2
Company 10	Manufacturing of telecommunication products	3B
Company 11	Real estate construction	3B
Company 12	Manufacturing of telecommunication products	3B
Company 13	Importing of telecommunication products	4
Company 14	Banking	1
Company 15	Importing of beverage manufacturing system	4
Company 16	Importing of computer products	4
Company 17	Importing of chemical products	4
Company 18	Business consultancy	1
Company 19	Exporting of furniture products	2

#### 5.4.5 Type of Institutes Primarily Interacted With

The two major categories in this control variable are "government agents" and "private enterprises". It was suggested by respondents that *guanxi* patterns would be different between these two groups because of the divergence in operating styles and in the sphere of influence.

Since China is still largely under government control, government agents were perceived to have a greater sphere of influence, and would give much benefits to investors if they had good *guanxi* with them. However, respondents criticized that the interaction with government agents was marked with enormous red-tape due to bureaucratic constraints. A hierarchical approach in *guanxi* development might have to be enforced in

order to be compatible with the government structure. That is, *guanxi* ties had to be built with each level of the government hierarchy in order to have smooth functioning in business operations. Conversely, the private enterprises earned the reputation of maintaining high efficiency and flexibility in business transactions. Hence, *guanxi* building with private enterprises was subject to less bureaucratic rules and restrictions.

Table 5.6: Type of Institutes Primarily Interacted With by Respondents

Coding Method: "1" The respondent interacted primarily with government agents  
 "2" The respondent interacted primarily with private enterprises

<u>Respondents</u>	<u>Industry Type</u>	<u>Coding</u>
Company 1	Government agents	1
Company 2	Government agents	1
Company 3	Government agents	1
Company 4	Government agents	1
Company 5	Government agents	1
Company 6	Private enterprises	2
Company 7	Private enterprises	2
Company 8	Government agents	1
Company 9	Government agents	1
Company 10	Government agents	1
Company 11	Government agents	1
Company 12	Government agents	1
Company 13	Private enterprises	2
Company 14	Government agents	1
Company 15	Private enterprises	2
Company 16	Government agents	1
Company 17	Government agents	1
Company 18	Government agents	1
Company 19	Private enterprises	2

## 5.5 Quantitative Analysis

Since the research study was by nature a qualitative study, the research findings were mainly based on the qualitative analysis of research data. However, some statistical procedures were employed as auxiliary measures to substantiate the qualitative research findings. The binomial test of non-parametric analysis was used to evaluate the ranking

data of *guanxi*. Cross-tabulation was adopted as a test of independence between the predictor and criterion variables in various hypotheses, since the majority of data were non-metric. It was fully understood that some of the underlying assumptions of these statistical procedures were violated because of the small sample size due to time and resources constraints in this study. For instance, the assumptions of normal distribution and random sampling in cross-tabulation were unfulfilled by the limited sample. However, it would still be a valid attempt to evaluate the relationships between independent and dependent variables with accredited statistical procedures, so that the qualitative findings would be endorsed with greater validity. It was justified to make the attempt because the research was an exploratory study, and the quantitative tests would only be treated as supplementary analyses of the research data. The statistical results would be interpreted with great caution together with an understanding of their limitations.

Owing to the small sample size, the relationships that would have been statistically significant under large sample testing, might result in their not being significant at  $p < .05$  level. Since the current research was an exploratory study, a lower significance level was used to determine the level of independence among different variables. Statistical results at both  $p < .05$  and  $p < .1$  levels were reported to capture a better picture of the research findings.

Two levels of statistical analyses were performed with the use of the five control variables. The first level tested the relationships between independent and dependent variables which would be controlled for by the five testing factors. The second level assessed the correlation between independent and control variables. Its main purpose was to examine the impact of the five control factors on independent variables, and thereby unveil the special features of independent variables along the five dimensions.

## CHAPTER 6

### THE RELATIVE IMPORTANCE OF *GUANXI* IN DOING BUSINESS WITH CHINA

#### Hypothesis 1

*The business practitioners who have been doing business with China think that guanxi is the most important factor among the following 11 elements in attaining long-term business success in China.*

*Choosing the Right Business Location*

*Choosing the Right Entry Strategy*

*Competitive Prices*

*Complementarity of Goals*

*Familiarity with the Chinese Negotiation Style*

*Flexibility in Business Operations in China*

*Guanxi Relations with Chinese Business Associates*

*Long-term Business Commitments in China*

*Management Control in Business Operations in China*

*Product Differentiation / Quality*

*Understanding China's Policy and Legislation*

*Guanxi* has been cited in the literature as a key success factor in doing business with China. It would be essential to test the validity of the above assumption. Thus, hypothesis 1 was designed to evaluate the relative importance of *guanxi* in attaining long-term business success in China. Long-term business success was defined by the corporate financial performance of respondents over the years. It was tested by two different

measures: rating of *guanxi* on its own; and ranking of *guanxi* against other essential factors.

## **6.1 Rating of *Guanxi* for Its Importance in Attaining Long-term Business Success in China**

Respondents were asked to rate "*guanxi*" on a 10-point scale, as a factor of achieving long-term business success in China. They were instructed to give a rating of "10" if they perceived *guanxi* as essential; or "1" if perceived as nonessential. A total average was calculated to estimate its significance in this respect.

### **6.1.1 General Research Findings:**

The average rating of *guanxi* given by the nineteen respondents was 7.68, with a minimum of 5.5 and a maximum of 10.0 (standard deviation was 1.48). These figures indicate that *guanxi* assumes a high level of importance in gaining long-term business success in China.

### **6.1.2 Research Findings by Control Variables:**

No significant pattern emerged in the analyses by the five control variables, except that selling manufacturers had the highest average rating (9.33) with a standard deviation of 0.28. The prime importance allocated by selling manufacturers may be a result of their greater dependence on the China market which was both a manufacturing location and a sales market for their products. As for the other industry types, the China market served only one single purpose in their business operations. For instance, the China market was perceived by the exporting manufacturers as the manufacturing location for their products, or it was only a sales market for the tertiary industry; therefore the market risk was less substantial than the selling manufacturers. Hence, it was logical that selling manufacturers would assign a higher rating to *guanxi* if the hypothesis was valid.

Table 6.1: Rating of *Guanxi* for Its Importance in Attaining Long-term Business Success in China

<u>Control Variables</u>	<u>Sub-Categories</u>	<u>Number of Firms</u>	<u>Average Ratings</u>	<u>Standard Deviation</u>
Ownership Type	Chinese firms	11	7.63	1.81
	Non-Chinese firms	8	7.75	0.96
Experience Level in China Business	Old-timers	7	7.64	1.43
	Mature group	6	7.50	1.94
	Newcomers	6	7.91	1.24
Firm Size	Large firms	3	8.33	2.46
	Medium firms	5	8.00	1.11
	Small firms	11	7.36	1.39
Industry Type	Tertiary industry	4	7.25	1.04
	Exporting industry	4	7.00	1.47
	Exporting Manufacturers	3	7.33	2.36
	Selling Manufacturers	3	9.33	0.28
	Importing industry	5	7.80	1.35
Type of Institutes Primarily Interacted	Government agents	14	7.82	1.65
	Private Enterprises	5	7.30	0.83

## 6.2 Relative Ranking of *Guanxi* in Attaining Long-term Business Success in China

Respondents were required to choose five items from the list of eleven elements stated in hypothesis 1 as their perceived key success factors in doing business with China. The five selected elements were then ranked from "1" as the most important to "5" as the least important factor. This resulted in the gathering of non-metric data. Since the small research sample might not be normally distributed, the binomial test of non-parametric analysis was adopted to analyze the ordinal ranking data for three reasons (Siegel and Castellan 1988):

- i) The test was applicable to small samples of 35 or below;
- ii) The design was a one-sample test which fit to the requirement of analyzing ranking data;
- iii) The data was mainly in two discrete categories: selected and unselected.



In conducting the binomial test, all selected elements were recoded as "1" regardless of the ranking order given by respondents, and the unchosen items were classified as "0". The test would yield statistics on significance level and average mean based on frequency count.

(Note: There were only eighteen respondents covered in this section, as Co. 8 interviewee refused to do the ranking procedure since he found it too hard to select any five items from the list. Instead, he thought all of them were essential factors.)

### 6.2.1 General Research Findings:

Among the eleven items, *guanxi* was the only factor that was consistently chosen as a key success factor (mean=0.83,  $p < .01$ ). Fifteen respondents had selected *guanxi* as one of the five key success factors. In examining the ranking given by these fifteen respondents, 60% had assigned a ranking of "1" or "2" to *guanxi*, while the remaining 40% ranked it at "3" or "4". None of these respondents assigned a ranking of "5" to *guanxi*.

Table 6.2: Relative Ranking of *Guanxi* in Attaining Long-term Business Success in China

<u>Success Factors</u>	<u>Mean</u>	<u>Standard Deviation</u>	<u>Significance Level</u>
Choosing Right Business Location	0.33	0.48	0.23
Choosing Right Entry Strategy	0.44	0.51	0.81
Competitive Prices	0.38	0.50	0.48
Complementarity of Goals	0.44	0.51	0.81
Familiarity with Chinese Negotiation Style	0.44	0.51	0.81
Flexibility in Business Operations	0.50	0.51	1.00
<i>Guanxi</i> with Chinese Business Associates	0.83	0.38	0.00 *
Long-term Business Commitment	0.33	0.48	0.23
Management Control	0.27	0.46	0.09 #
Product Differentiation / Quality	0.38	0.50	0.48
Understanding China's Policy	0.55	0.51	0.81

\*  $p < .05$ , two-tailed test.

#  $p < .10$ , two-tailed test.

### 6.2.2 Discussion

As reflected in statistical analyses of the rating and ranking of *guanxi* by respondents, *guanxi* did assume a high level of significance in attaining long-term business success in China. Two of the respondents (Companies 3 and 9) even proposed that the supremacy of *guanxi* was exhibited at every single step of their business operations. They claimed that *guanxi* granted them abundant benefits which were critical to their business. Co. 3 representative recalled that the customs officers did a favor for him by working until 2:00 a.m. to process the necessary procedures so that his container could be delivered at the pier in time. He judged that this was a competitive advantage in terms of efficiency and timing which allowed him to win out over his competitors who did not have good *guanxi* with the customs.

The essentiality of *guanxi* was also felt by Co. 5 respondent who was grateful to his *guanxihu* for passing on important inside information which sharpened the competitive edge of his company. It was further confirmed by Co. 13 representative who asserted that building *guanxi* was the foremost step to be taken before anything could be sold in the China market. It was asserted by respondents that many *guanxi* transactions were on the border of corruption. In the extreme case, *guanxi* exchanges could involve illegal activities or twisted interpretations of Chinese legislation. The paramountcy of *guanxi* was best illustrated by a real life situation cited by one respondent. A drunken driver who had killed a pedestrian in a car accident was released after a few years of imprisonment, when he should be sentenced to death according to Chinese legislation. The light penalty for the drunken driver was a result of his good *guanxi* of high caliber in the local region.

All of the above incidents highlighted the fact that *guanxi* was prominent in China. But, why does it have such a high level of supremacy in the business arena?

In responding to the question, the interviewees unanimously agreed that it was the ambiguity of Chinese legislation. Cos. 3 and 9 representatives explained that the legislation of China was not as well established as that in the Euro-centric countries. There were many

blind spots in the business ordinance. These were the grey areas in which *guanxi* could function at its optimal, since institutional authority was overshadowed by the dominance of personal power in China. Cos. 14 and 18 interviewees rationalized that there was an absence of institutionalization in traditional China due to the Confucian emphasis on *li-zhi*. Personal power emerged to be the driving force in the Confucian society. Hence, decisions made on grey areas were based solely on the personal preference and interpretation of the government officers in charge. Since guidelines were not stated explicitly in the legislation, there was much room for government officers to grant "*fang bian*" (convenience 方便) to their close investors. Thus, having good *guanxi* with government officers was a means to influence the decision making process, so that the outcome would be in favor of investors.

With the foregoing research results, one would logically deduce that *guanxi* was paramount in bringing business success to investors in China. However, it was only a microscopic vision presented by the quantitative data. More enlightening insights were revealed in the qualitative information solicited in interviews. Respondents gave a slightly different picture of the importance of *guanxi* in attaining long-term business success in China, when they were asked to give elaboration on the role that *guanxi* actually played.

"*Guanxi* is prominent in gaining you business deals, but it is very unreliable in achieving long-term business success," commented by Co. 4 representative. His criticism on the impotence of *guanxi* was fully revealed by his differential ratings of *guanxi* in the two respects. He gave full marks (10 points) to *guanxi* in getting business deals, while he only allocated a rating of 6 on achieving business success. He explained that getting business deals and gaining business success were two different ball games. The former was a short-term goal, whereas the latter was put into a long-term perspective. *Guanxi* was competent in achieving the short-term objective, but was unreliable in the long-term attainment. This was echoed by Co. 8 interviewee who declared that *guanxi* had a higher priority as a factor in attaining short-term goals. But technical elements such as product

quality or right business strategy would take precedence over *guanxi* in achieving long-term business success.

The disparity of importance assumed by *guanxi* in the two endeavors was a good indication of the preliminary role of *guanxi* in business establishment. The ultimate function of *guanxi* was to open up business channels and to explore opportunities for investors, but it was not a definite route that guaranteed business success. The above proposition was supported by the remarks of Co. 12 representative.

"*Guanxi* is a basic requirement of business establishment in China. If you don't have it, you cannot even enter the China market." Because the Chinese were very conservative, they would not have business transactions with anyone whom they did not know nor trust. Investors would not even have a chance to do business with them if they did not have *guanxi*, since they were perceived by the Chinese as outsiders who were untrustworthy. Building *guanxi* with the Chinese would transform the identity of investors from outsiders to be insiders. This allowed investors to build a connection with the Chinese which would open business opportunities to them. However, "this connection is only a contact which will not elicit business success if you have wrong marketing strategies or undesirable products," asserted Co. 12 interviewee. He proposed that *guanxi* was an element of neutrality which did not embody business success in itself. The postulate was further elaborated by Co. 10 respondent who suggested that *guanxi* was only a pointer in the business expedition.

Co. 10 representative asserted that *guanxi* would give investors directions on which route to be taken in the business exploration. But, the chance of getting to the final destination (business success) depended largely on their efforts made in the expedition. He contended that business success was contingent on how investors utilized the *guanxi* they had in hand, rather than being inherited in the *guanxi* itself. He likened *guanxi* to a piece of wood given to a drowning swimmer. Whether he would be saved was subject to how he

made use of the timber in swimming back to the shore, rather than relying merely on the piece of "magic" wood which would bring him ashore.

As advanced by Co. 1 respondent, *guanxi* was only one of the three cardinal requisites for doing business in China. He stipulated that business success in China had to be built on three "Cs" or three "*ben*" (principles 本 ) which were capital, (*ben-qian* 本錢 ), capability (*ben-shi* 本事 ) and connection (*ben-xin* 本心 ). Capital was the financial resources that were required for business investments and for *guanxi* building. Capability denoted the competence of investors in business development. It entailed the possession of a business mind to develop competitive advantages in the business arena. Connection signified the *guanxi* relations with Chinese business associates.

Nevertheless, the vitality of *guanxi* decreased when investors were well established in the China market, and business channels had already been opened and stabilized. In the mature stage of business establishment, the primary task of investors was to strengthen their competitive advantages in the technical aspects, because keen competition was set in by their competitors who had built similar *guanxi* ties with the Chinese as investors had. At this stage of maturity, it was technical competitiveness that sustained investors in the long-term business battlefield. As proposed by respondents, technical competitiveness was exhibited in the form of good product quality/services (Companies 2, 4, 7, 9, 12, 13, 15 and 19), right business strategies (Companies 2, 3, 12, 13, 14, 15 and 17) and in-depth market knowledge (Company 17).

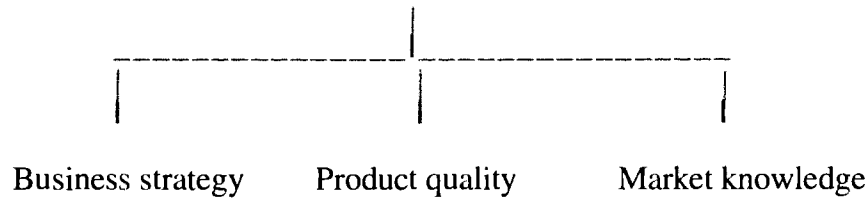
It was not the intention of this paper to evaluate the relative importance of the three above technical elements in achieving business performance. The more important message was that *guanxi* alone was insufficient for investors to attain long-term business success in China. As suggested by Co. 14 interviewee, *guanxi* would only help her get into the final round of a tender bid. But it would never get her the business if her proposal did not satisfy the requirement of the Chinese. She would lose to her competitors if they had better offers in their business proposals.

Consequently, *guanxi* should be perceived as a base upon which technical competitiveness was built. Investors were required to have *guanxi* for business establishment, because it opened business channels for them. They would not have business success if they did not establish *guanxi*, since they did not have a starting point to penetrate into the China market, and technical competitiveness had no base to anchor. However, investors would fail as well if they had only *guanxi* but did not possess any technical competitiveness, since they had nothing to sell and would not be able to survive in the severe business battle. Hence, it was concluded that *guanxi* was a necessary but insufficient factor for investors to attain long-term business success in China. Its role in the business expedition was best illustrated by the analogy depicted by Co. 3 representative.

The China market was likened to a treasure island full of underground fortunes. If investors desired to grab the riches, they had to pay an entry fee which was in the form of making a heavy investment in establishing and maintaining *guanxi*. Thus, *guanxi* could be perceived as a boarding pass that admitted investors onto the treasure island. However, they were not guaranteed wealth even if they were onboard. That depended on how they explored the mines. They might rely on *guanxi* for directions in the expedition, but the more effective device was their technical competitiveness which enabled them to track out the locations of the underground fortunes.

In conclusion, *guanxi* and technical competitiveness were two essential factors for attaining long-term business success in China. This research finding was also confirmed in the research studies by Tung (1982, 1989) in which the uniqueness of product and personal relationships were found to be the factors responsible for the success of business negotiations in China. The relationships among business success, *guanxi* and technical competitiveness were summarized in the following formula, as proposed by respondents.

*Guanxi* + Technical Competitiveness = Business Success in China  
 (Basic requirement) (Critical Factor for Success)



### 6.3 Research Findings by Control Variables:

#### 6.3.1 Ownership Type

It seemed that no specific pattern could be identified between the two ethnic groups on the ranking of *guanxi*. 80% of the Chinese firms and 87.5% of the non-Chinese companies selected *guanxi* as a significant factor for attaining business success in China. This was confirmed by cross-tabulation statistics which indicated that the relationship between ownership type and *guanxi* was not statistically significant ( $p=.67$ ). However, in examining the ranking assigned by the two ethnic groups, the Chinese firms allocated a higher order to *guanxi* than the non-Chinese companies. 60% of the Chinese firms ranked *guanxi* at "2" or above, while only 37.5% of non-Chinese companies gave a similar ranking.

The phenomenon was attributed to two reasons. The first reason was the divergence in organizational cultures between the two ethnic groups. Non-Chinese firms were embedded in the Euro-centric organizational cultures in which institutional authority was highly appraised. Although non-Chinese companies recognized the importance of *guanxi* in China, they tended to downplay the use of social connections in commanding resources and gave greater prominence to institutional authority. This was because institutionalization gave legitimacy to formalized constitutions that insulated organizational functioning from any personal influence. Hence, universalistic rationality was firmly established in non-Chinese firms. In contrast, the Chinese firms had inherited the enduring Chinese tradition of relying on *guanxi* to command resources. The tradition was founded

on the Confucian philosophy of relational construction of personhood which had an inclination for *li-zhi* and a distaste for *fa-zhi*. The consequence of the relational orientation was that *guanxi* functioned as a substitute for the missing institutional support (Xin & Pearce 1994). With the fundamental differences in organizational cultures, the two ethnic groups would definitely have discordant rankings for *guanxi*, even though both comprehended its importance in doing business with China.

The second reason was the importance of China market to the corporations. To the non-Chinese companies, China was only one of the markets in the Asia Pacific region. In the research sample, all the non-Chinese respondents were well established in other Asian markets such as Taiwan, Thailand or Singapore. Their sales revenue derived from the China market constituted only 5%-45% of total sales revenue from the Asia Pacific region. Hence, the importance of China market to non-Chinese corporations was comparatively lower than to the Chinese firms which generated 100% of their sales revenue from China. The Chinese firms had total dependence on the China market for survival and thus they would give higher priority to *guanxi* which was perceived as a key success factor in doing business in China.

### 6.3.2 Experience Level in China Business

The old-timers (with over 10 years of experience) gave much less emphasis on *guanxi* in attaining business success compared to other factors. While only one old-timer (16.7%) gave a high ranking ("2" or above) to *guanxi*, 50% of them did not even select it as a critical factor. Conversely, 83.3% of the mature group and 50% of the newcomers ranked *guanxi* highly. These research results were confirmed by the cross-tabulation statistical analysis ( $p=.02$ ). This indicated that the disparity in ranking between old-timers and mature group / newcomers was proved to be statistically significant at  $p<.05$  level. The relationship between experience level and *guanxi* was moderate, since the Spearman correlation coefficient was anchored at 0.54.



In investigating the priority that old-timers preferred, following was a list of their ranking orders:

Table 6.3: Important Factors in Attaining Long-term Business Success in China as Perceived by Old-timers

	<u>First Priority</u>	<u>Second Priority</u>	<u>Third Priority</u>
Company 1	Complementary Goals	Product Quality	<i>Guanxi</i>
Company 2	Choosing Right Locations	Understanding China's Policy	Management Control
Company 10	Choosing Right Locations	Choosing Right Strategies	Complementary Goals
Company 11	<i>Guanxi</i>	Choosing Right Locations	Familiarity with Chinese Negotiation
Company 15	Long-term Business Commitment	Competitive Price	Complementary Goals
Company 17	Understanding China's Policy	Choosing Right Locations	Complementary Goals

It appears that old-timers allocated a higher ranking to technical factors which embraced elements such as understanding China's policy, choosing right locations and having complementary goals with the Chinese. The lower priority of *guanxi* in attaining business success could be explained by two reasons.

The old-timers first went into China for trade in the late 1970's. The role of *guanxi* was only limited to connecting investors with the right Chinese business associates. Its significance dimmed as the business operations of investors were established. The old-timers asserted that it was their business minds that helped them to search for lucrative business opportunities in China. Hence, their personal experiences taught them that *guanxi* was secondary to the technical factors which had led them to their current success. On the contrary, the newcomers went to China for trade at a time when the practice of *guanxi* was predominant in every aspect of life. The significance of *guanxi* was no longer restricted to only building connections between investors and the Chinese as it had been in the past. It

was extended to every single step of business operations, and had the power of ruining the business if investors did not cultivate good *guanxi* with the Chinese. Thus, the newcomers were astonished by the paramountcy of *guanxi* in the business arena, and they gave top priority to this element in the attainment of business success in China.

As highlighted by some respondents, the importance of *guanxi* decreased as one moved along the learning curve. *Guanxi* assumed supremacy in the initial and developing stages of business establishment, because one had to rely on *guanxi* for guidance when one was inexperienced in China trade. *Guanxi* functioned as a gateway leading to the treasury of business. When one became more experienced, one realized that *guanxi* only opened up business channels, but it did not guarantee success. This proposition paralleled the findings of Tung's research study (1989). The study stipulated that experience in Chinese business negotiations did not enhance the probability of success when one was beyond the threshold level of the learning curve. Applying the same principle to the findings in the current study, what carried more weight in attaining business success when investors had in-depth experiences were technical factors. Right business strategies, in-depth market knowledge and good product quality were the weapons that would equip investors to compete with their competitors, after *guanxi* had led them to the China business battlefield. In the mature stage of business establishment, the technical factors took precedence over *guanxi*. It was suspected that the old-timers were in the stage of maturity, and hence had experienced a change in mentality. However, such a change had not yet been comprehended by the other two groups who were undergoing the initial and developing stages of the learning curve.

### 6.3.3 Firm Size

Only 33.3% of the large firms selected *guanxi* as a key success factor, while 100% of the medium companies and 90% of the small firms perceived *guanxi* as an element of great significance. The research results corresponded to the statistics generated by cross-

tabulation. The relationship between firm size and *guanxi* was statistically significant at the 0.05 level. It had a significance level of 0.03 with a Spearman correlation coefficient of 0.35. These statistics indicate that sizable companies tended to minimize the significance of *guanxi* in attaining business success in China. The de-emphasis of *guanxi* by large corporations might be due to two reasons.

The first reason was the focus of attention on sizable firms by the Chinese government. Some respondents commented that large enterprises were more attention seeking because of their large-scale and substantial economic impact on local regions. The higher ranking officers in the Chinese government tended to pay greater attention to large corporations and evaluate their operations more closely. The close supervision of top government officers required the large enterprises to take formal channels in doing business, unless they could have the opportunity to build good *guanxi* with top government officers. Conversely, the medium and small firms had a greater chance for *guanxi* functioning in their operations because the top government officers did not keep a watchful eye on them since their negative economic impact on local regions was less substantial in case of upheaval. Thus, these companies tended to utilize *guanxi* more in their business operations than large corporations, thereby they placed a heavier emphasis on *guanxi*.

The second reason was the tremendous economic contribution made to local regions by large corporations. Co. 1 representative boldly claimed that he did not initiate to build *guanxi* with Chinese officials who turned around and sought *guanxi* with him. The reversed situation was derived from the fact that he had invested over US \$50 million in the two local regions (*Pan-yu* and *Xin-hui* in *Guangdong* province) thereby greatly accelerating the economic development of these areas. He was perceived by the local government officials as the "savior" who contributed much to bringing the regions out of poverty.

The same situation occurred to other two respondents: Co. 2 interviewee was the largest employer in the private sector of *Dong-guan* in *Guangdong* province. He hired more than 7000 local Chinese to work in his manufacturing plant. At present, he was

financing the local government to build a power generation station to solve the power shortage problem. Co. 3 representative employed more than 2000 staff in his factory at *Pan-yu*. He improved the local transportation network by building railway, erecting bridges and paving roads. Both of these companies had made enormous contributions to bring the local regions economic prosperity.

As a result, the contribution of large corporations to the economic development of local regions was highly valued by the Chinese officials, and thus the investors did not have to do anything special for *guanxi* building. The Chinese would come to them for association instead. As Co. 2 interviewee remarked, "You will have business success easily in China if you can show them your contribution to the economic development of the region. In that case, the officials will treasure your presence and want you to stay with them. They will make everything smooth for you."

The gigantic investment of large corporations was hardly affordable for the medium and small firms which might have a hard time to seek *guanxi* with the Chinese officials. Hence, they perceived *guanxi* to be very important in doing business with China.

#### 6.3.4 Industry Type

Table 6.4: Relative Ranking of *Guanxi* by Industry Type

	Number of Firms	Ranking of <i>Guanxi</i>		Did not Select <i>Guanxi</i>
		"1" & "2"	"3" & "4"	
Tertiary Industry	4	50.0%	50.0%	0.0%
Exporting Industry	3	66.7%	33.3%	0.0%
Manufacturing Industry	6	50.0%	16.7%	33.3%
Importing Industry	5	40.0%	40.0%	20.0%

Both tertiary and exporting industries ranked *guanxi* higher than did the manufacturing and importing sectors. All members of the two former industry types

selected *guanxi* as a key success factor, whereas 33.3% and 20% of the manufacturing and importing groups (respectively) did not choose *guanxi* as a significant element. The disparity in ranking may be due to their unique industry nature.

One commonality between the exporting and tertiary sectors was that the *guanxi* networks they required were larger and more mobile in comparison with those of the manufacturing and importing industries. As commented by the respondents in the exporting industry (Companies 7, 8 and 9), their suppliers were everywhere in China and their business locations were distinct in different business transactions. Depending on the types of products their customers required and the prices that the Chinese suppliers offered, they would have transactions with anyone who offered them the cheapest price with the best quality. This resulted in their changing suppliers and having transactions in numerous business locations. This changeable pattern required that the exporting firms have broad *guanxi* networks in which they could source the types of products they desired. Yet, their *guanxi* ties were weak because the transient pattern of the exporting industry violated the principles of *guanxi* building which were loyalty and trust. The exporters expanded their *guanxi* networks at the expense of nurturing trustful and stable relations with the Chinese. In expanding their *guanxi* networks, the respondents had to rely on the referral of their Chinese business associates to source new suppliers, and hence they were always in the initial stage of *guanxi* building with new suppliers. Consequently, the importance of *guanxi* was often salient to their business operations.

By the same token, the tertiary industry requires an extensive *guanxi* network because a large customer base is needed to support business operations. As remarked by the respondent in town-planning consultancy (Company 4), he rarely had the same customer within a short period of time, because the consultation service on town-planning was mostly a one-time business deal. Seldom would the local government ask them to tender a second consultation service within a decade's time. Hence, he needed to have customers from different regions and he relied on the referral of his Chinese business

associates to source new customers. The same principle applied to real estate management service (Company 6) and business consultation (Company 18). As a result, these two firms relied on the referral of their *guanxihu* to sustain their business, and they also assigned a higher ranking to *guanxi* in attaining business success.

In contrast, the importing and manufacturing industries had more stable business locations for perpetual *guanxi* development. As they were more established in specific business locations, the importance of *guanxi* in gaining business success decreased because the channels for business had already been opened. What assumed greater importance in the mature stage were technical factors such as right business strategies and product quality. Consequently, the two industries assigned a lower priority to *guanxi* relative to the other success factors.

Surprisingly, the foregoing qualitative research results were not supported by the statistical analysis of the relationship between industry type and *guanxi* ( $p=.45$ ). The unreconciled quantitative statistics might be a reflection of the insignificant relationship between the two variables. Or, it might be a misconception induced by the small sample size which had imposed undesirable impact on the analysis. Consequently, this is an area requiring further investigation with a larger research sample.

#### 6.3.5 Type of Institutes Primarily Interacted With

There was no significant difference in the ranking of *guanxi* between the two groups of government agents versus private enterprises ( $p=.81$ ). 84.6% of government agents and 80.0% of private enterprises selected *guanxi* as one of the five important items in attaining business success in China. This implies that the relationship between the type of institutes primarily interacted with and *guanxi* was not statistically significant.

#### 6.4 Conclusions:

Based on these analyses of the rating and ranking of *guanxi*, it is concluded that hypothesis 1 is supported, that is, *guanxi* is a significant factor in attaining long-term business success in China. Yet, its role is confined to opening channels for investors to start playing the business game. Business success is actually a function of the technical competitiveness of investors which is manifested in the form of good product quality, right business strategies and/or in-depth market knowledge.

In the detailed analyses, significant relationships are established between *guanxi* and some of the five control variables.

**Ownership Type:** *Guanxi* is perceived as more important by the Chinese firms than by non-Chinese companies. This is attributed to the divergence in organizational cultures between the two ethnic groups. The relational construction of personhood in Chinese culture has shaped the Chinese firms to be inclined to *guanxi*, while the universalistic rationality of Euro-centric cultures induces non-Chinese companies to give a lower ranking to *guanxi*.

**Experience Level:** The prominence of *guanxi* in attaining business success in China decreases as one moves along the learning curve. *Guanxi* assumes prime importance in the initial and developing stages of establishment, because it gives guidance to inexperienced investors in their search for business opportunities. However, its significance dims when investors have gained in-depth knowledge of the idiosyncratic environment and have stabilized business channels. In the stage of maturity, technical factors will take precedence over *guanxi* in bringing investors to long-term business success in China.

**Firm Size:** *Guanxi* is more salient for medium and small companies than for sizable firms, since they are not under the same scrutiny of top government officers. Hence, the medium and small firms have more opportunities for *guanxi* functioning in their business operations. In addition, their economic contribution to local regions is much less than that of large corporations. Their presence is not as highly treasured by government

officials as that of large enterprises. Hence, they have to try every means to build *guanxi* for their business operations.

**Industry Type:** *Guanxi* assumes higher priority in industries which constantly press for expanding or building new *guanxi* networks. This is attributed to the industry requirement for mobile business locations or for a large customer base to sustain business. Both of which have to depend on the referral of current *guanxihu* to source new *guanxi* targets.

In summary, although the significance of *guanxi* is secondary to technical competitiveness in soliciting long-term business success in China, it is an indispensable factor that investors have to capture because it opens the channels for their business. As stipulated by Co. 1 representative, it is one of the 3 "Cs" that are cardinal for doing business with China.



## CHAPTER 7

### GUANXI ESTABLISHMENT

#### Hypothesis 2

*Other elements being equal, ascribed guanxi base is more effective than achieved guanxi base in establishing guanxi relations.*

With such a high level of importance assumed by *guanxi* in China business, the next logical question for investors to ponder is how to make the first move in *guanxi* establishment, especially for non-Chinese companies which are alien to China.

In the literature, it is postulated that *guanxi* can be established by either ascribed *guanxi* base founded on innate commonalities among individuals (group identification) or achieved *guanxi* base built by shared experiences (group identification) and altercasting. To evaluate the relative importance between the two base types of *guanxi* building, respondents were asked to describe how they originally established their *guanxi* ties in China. Surprisingly, none of the nineteen respondents used ascribed *guanxi* base to start any relations. All attributed the origins of their *guanxi* ties to achieved *guanxi* base. As a result, the hypothesis could not be tested in the current research study.

This unexpected research result was largely a consequence of the locality of respondents. Although all the respondents were ethnic Chinese, they were not local nationals in China. 78.9% were Hong Kong residents, while the remainder were Canadian immigrants. Most of the respondents were the second or even third generation in the Hong Kong Colony. Hence, their linkage in kinship with the local Chinese was remote, if there was any. The only alternative for them to establish *guanxi* relations was achieved *guanxi* base which could be cultivated between any unrelated individuals.

One might argue that the research should be launched in mainland China, so that the specificity of *guanxi* could be fully tested with the inclusion of local nationals in the research sample. However, such findings would not be relevant to the target audience of the research -- non-Chinese who intend to or are conducting business with China. These non-Chinese might not possess the same innate commonalities or personal characteristics for *guanxi* building and maintenance as the local Chinese do. Consequently, the research result, though seemingly disappointing, was meaningful because it gave new confidence to non-Chinese investors on *guanxi* establishment. Although it was stated in the literature that ascribed *guanxi* base was superior in *guanxi* building, because of the traditional emphasis on familism in China, the current study reveals that achieved *guanxi* base functions equally well in furnishing *guanxi* relations for investors in China.

In the next section, more detailed analyses by the five control variables are made on achieved *guanxi* base. Basically, there were two major types of achieved *guanxi* bases in the current research sample: formal working channels and informal referrals. Respondents were classified in the former group if they initiated their *guanxi* relations through formal business channels, such as making sales calls, soliciting relevant business associates in trade shows or exhibitions, or being introduced by colleagues because of position requirement. That is, they recruited their *guanxihu* without the referrals by any friends or relatives; nor did they have any past connections with the local Chinese.

Informal referrals encompassed cases in which respondents were referred by their friends or relatives to establish *guanxi* relations, or respondents had prior connections with the local Chinese such as classmates or colleagues. It should be highlighted that informal referrals was distinct from the use of intermediary firms. While both serve the function of connecting investors with the right Chinese business associates, the two differ in the extent of involvement and accountability. Informal referrals was largely performed by the personal friends or relatives of investors. They took the intermediary role because of their friendship or *renqing* with investors, therefore they had no accountability for the business

operations. Their involvement in the business development of investors was limited, and they would generally retreat from the picture after the introduction had taken place. In contrast, the intermediary firms were separate entities which had the obligation to source Chinese business associates for investors because of the fee received. They were accountable for helping investors enter the China market and would have extensive involvement in the business operations, even though they did not guarantee success in financial performance.

## **7.1 General Research Findings:**

There was no significant difference between the importance of formal working channels and informal referrals, as both groups received similar level of support from respondents. 57.9% of the respondents built *guanxi* relations based on formal working channels, while the remaining 42.1% relied on informal referrals. The binomial test of non-parametric analysis was utilized to test the significance of the two elements, because it was a one-sample test and the data were categorical. Statistical analysis showed that both formal working channels and informal referrals had equal importance in *guanxi* establishment ( $p=.64$ ).

## **7.2 Research Findings by Control Variables:**

### **7.2.1 Ownership Type**

There was a significant relationship between ownership type and the type of achieved base used for *guanxi* establishment. More Chinese firms (63.6%) tended to rely on informal referrals for *guanxi* development, while more non-Chinese firms (87.5%) resorted to formal working channels. Statistical analysis confirmed this relationship (Spearman  $r=-0.51$ ,  $p = .02$ ).

The difference in emphasis of achieved *guanxi* types could be explained by the divergent organizational cultures of the two ethnic groups. The non-Chinese firms that

participated in this research study were large multinational corporations that had institutionalized business mechanisms and channels. They had cultivated an organizational culture which focused on universalistic rationality and had a distaste for nepotism. The organizational functioning was highly regulated by their own business ethics and constitutions, rather than any personal influence. Hence, it was no surprise to see that non-Chinese companies put a greater emphasis on formal working channels than the Chinese firms did.

In contrast, the Chinese firms had a stronger preference for informal channels because of their prior personal connections with the local Chinese. Co. 8 representative had received education in China for a few years. Cos. 4 and 9 interviewees were assigned to work in China by their former companies before the current business occupation. Cos. 2 and 11 respondents were referred by their friends in building *guanxi* with the Chinese. Such prior connections and personal referrals were important in establishing *guanxi*, because the Chinese were very conservative in associating with outsiders. They would not build *guanxi* with anyone whom they did not know nor trust. The prior connections or personal referral served as a testimony of the trustworthiness of respondents (outsiders) who would seek the agreement of the Chinese to build *guanxi* with them.

### 7.2.2 Experience Level in China Business

A significant relationship was established between experience level and the type of achieved base for *guanxi* development. Formal working channels were more prominent to newcomers than to old-timers who relied more on informal referrals. The observation was supported by the cross-tabulation statistical results (Spearman  $r=-0.58$ ;  $p = .03$ ).

Table 7.1: Relative Importance of Achieved *Guanxi* Types by Experience Level in China Business

	No. of <u>Firms</u>	<u>Formal working channels</u>	<u>Informal referrals</u>
Old-timers	7	28.6%	71.4%
Mature group	6	50.0%	50.0%
Newcomers	6	100.0%	0.0%

In the late 1970's, when old-timers first went into China to trade, the trading mechanisms and business channels were not as well established as they are now. The China market, though portrayed as a fantasy garden for business success, was perceived by outside investors as an untouchable treasury, largely due to their ignorance of the market environment in China and its associated bureaucracy.

As commented by Co. 1 representative, investors were likened to an expedition team which probed their way out in a swift river. They would be lost in the flooding water if they could not hold onto the rock which guided them along the way. Informal referrals was the 'guiding rock' which connected old-timers with the right business channels and taught them the appropriate way of doing business in China. It would be very hard for respondents to establish business in China without the referral of insiders because of the distrust of outsiders by the local Chinese.

This conception was acknowledged by Co. 8 interviewee who expressed his agreement with the pond analogy as follows: "The China market is a pond full of hidden delicious food. Yet, you are starving because you are a new fish in the pond and are puzzling at where to get food. Your Chinese referral is an old fish who knows every single plant in the pond. He will show you the spots where you can have tons of food and will not be starved to death." The importance of referral was also echoed in the remarks of other respondents. They highlighted that the Chinese agreed to do business with them

because of the trust in their referrals rather than in themselves. Consequently, in the beginning era of the Open Door Policy, investors did not dare to step into the China market if they did not have any prior connection with the insiders of the Chinese local community. Hence, informal referrals were a necessity for old-timers in establishing business in China.

In contrast, newcomers had the good fortune of relying on formal working channels to establish business in China for two reasons. Firstly, one commonality of the newcomers in the research sample was that they were not entrepreneurs like the old-timers. All were employees of existing companies which were well established in China. They did not have to undergo the hardship of establishing a business operation in the country, since that had been accomplished by their predecessors. Hence, they had the advantage of relying on formal working channels for *guanxi* establishment, since their predecessors introduced them to their current *guanxi* due to position requirement. Secondly, with the advocacy of attracting more foreign investment by the Chinese Government, more formal channels and business agents had been set up to help investors to get established in China. The newcomers had a much easier life than the old-timers in finding the way for business. As a result, newcomers ranked formal working channels highly in establishing *guanxi* and business in China.

### 7.2.3 Firm Size

Table 7.2: Relative Importance of Achieved *Guanxi* Types by Firm Size

	No. of Firms	<u>Formal working channels</u>	<u>Informal referrals</u>
Large Firms	3	33.3%	66.7%
Medium Firms	5	100.0%	0.0%
Small Firms	11	45.5%	54.5%

Based on these figures, one might tend to conclude that there was a relationship between firm size and the type of achieved *guanxi* base, especially when one focused on the total reliance of medium firms on formal working channels. However, such a conclusion would likely be refuted by the statistics for large and small companies.

33.3% of the large companies voted for formal working channels while 66.7% chose informal referrals. Though the disparity appeared to be great, it could not lead to a conclusive comment because the difference was based on only one respondent in the small sample (3 respondents only). As for the small firms, there was no significant difference between the two groups since they received equivalent rankings from the respondents (45.5% versus 54.5%). Consequently, one cannot conclude that there is a significant relationship between firm size and the type of achieved *guanxi* base, given that two of the three sub-categories showed evidence to the contrary.

The heavy reliance on formal working channels by medium firms could be explained by the confounding effect of ownership type. Four of the five research subjects in this group were non-Chinese companies. They had a strong tendency to select formal working channels for *guanxi* establishment in China.

Surprisingly, the statistical result of cross-tabulation turned out to be significant ( $p=.07$ ) although very weak (Spearman  $r=0.17$ ). The significant correlation between firm size and the type of achieved *guanxi* base was largely influenced by the total reliance of medium firms on formal working channels which was in fact confounded by ownership type. The weak relationship could be easily rejected if one scrutinized the detailed statistics of both large and small firms outlined in the above qualitative analysis. Consequently, doubts should be cast on the significant relationship between the two variables, and one should be extremely careful in making any positive interpretation of these statistics.

#### 7.2.4 Industry Type

It was generally believed that industry type should have an impact on *guanxi* establishment, since the nature of an industry would shape the interaction pattern between investors and Chinese business associates. For instance, one would expect that the tertiary and exporting industries would depend more on formal working channels because they relied heavily on their Chinese business associates to source new customers/suppliers, thus leading to an industry requirement of having expanding *guanxi* networks. Nevertheless, such a significant relationship was not revealed by the research results, largely due to the type of data collected in this section.

The data are more reflections of how respondents originally established their first *guanxi* relation in China than how respondents recruited their current *guanxihu*. These were two different dilemmas which called forth different underlying factors. The former question was a historical account of the *guanxi* building of respondents when they first entered the China market. The latter issue was an examination on the on-going practice of recruiting current *guanxihu* in the developing and mature stages of business establishment. It is conceivable that the former situation was largely affected by the circumstances in which respondents entered the China market, e.g., political or business conditions at that time. However, the latter condition might be heavily influenced by the industry requirement which would induce an interaction effect between investors and Chinese business associates. Since the data solicited focused chiefly on the former issue, the effect of industry type on *guanxi* establishment as defined in this section might not be salient. This was fully reflected in the following research results.



Table 7.3: Relative Importance of Achieved *Guanxi* Types by Industry Type

	No. of Firms	Formal working channels	Informal referrals
Tertiary Industry	4	75%	25%
Exporting Industry	4	25%	75%
Manufacturing Industry	6	50%	50%
Importing Industry	5	80%	20%

Based on the above figures, one would likely conclude that both tertiary and importing industries relied on formal working channels for *guanxi* establishment, while the exporting industry depended on informal referrals, and the manufacturing sector relied on both. However, the seemingly direct relationships might be confounded by two factors: experience level in China business and ownership type.

For the service sector, three of the four research subjects were newcomers in China trade. Their experiences in China business ranged between one to two years. As discussed earlier, newcomers tended to favor formal working channels more than old-timers. Hence, it might be misleading to conclude that the tertiary industry had a strong preference for formal working channels.

By the same token, three of the four respondents in the exporting industry were old-timers who had an inclination for informal referrals. Hence, the direct relationship between the exporting industry and informal referrals was diluted by the experience level in China trade.

As for the manufacturing industry, one could conclude that there was no strong correlation between industry type and preference for a particular achieved *guanxi* type, since no confounding factor was found and the two types of achieved *guanxi* bases had received equal support from the respondents.

In the importing industry, the research result might be confounded by the factor of ownership type. Four of the five respondents were non-Chinese firms. As discussed

earlier, non-Chinese firms had a strong preference for formal working channels in *guanxi* establishment due to their organizational cultures.

There was no statistically significant relationship found between industry type and achieved *guanxi* types ( $p=.33$ ).

### 7.2.5 Type of Institutes Primarily Interacted With

Table 7.4: Relative Importance of Achieved Base by the Type of Institutes Primarily Interacted With

	No. of Firms	Formal working channels	Informal referrals
Government Agents	14	57.1%	42.9%
Private Enterprises	5	60.0%	40.0%

There was no statistically significant relationship between the type of institutes primarily interacted with and achieved *guanxi* types, since both groups had allocated similar levels of importance to both formal and informal channels for *guanxi* establishment ( $p=.91$ ). This indicates that there is no correlation between the type of institutes primarily interacted with and achieved *guanxi* types.

### 7.3 Conclusions:

Hypothesis 2 is not tested in the current research, because all the respondents had utilized achieved *guanxi* base to establish their business operations and to commence *guanxi* relations in China. The importance of particular achieved *guanxi* types has been tested to be significant for two control variables.

**Ownership Type:** Non-Chinese companies have a strong preference for using formal working channels to establish *guanxi* in China, because of the organizational culture in which universalistic rationality takes precedence over nepotism.

**Experience Level:** Old-timers who went to China for trade in the beginning era of the Open Door Policy had to rely on informal referrals for *guanxi* establishment. It was because of the distrust of outsiders by the local Chinese and their ignorance of the China market. Conversely, newcomers have the blessing of relying on formal working channels to establish *guanxi*, since more formal business channels have been set up to help outsiders to do business in China.

**Firm Size & Industry Type:** The relationships between achieved *guanxi* types and industry type / firm size are confounded by two factors: experience level in China business and ownership type.

This section delineates the different aspects of *guanxi* establishment. Yet, this is only step one in the *guanxi* management process. The transformation procedure only erects a bridge of connection between two individuals. The success and the utility of the relation have to depend on its consolidation in *guanxi* maintenance.

## CHAPTER 8

### HIDDEN DIMENSIONS OF *GUANXI* & WAYS OF *GUANXI* MAINTENANCE

#### Hypothesis 3

*Other elements being equal, the individual will have a higher chance of enhancing corporate financial performance, if he/she has employed a strategy of offering short-term gains to maintain guanxi relations.*

The greatest frustrations that investors have in *guanxi* development are their ignorance of the nature of *guanxi* and the ways of *guanxi* maintenance. What is *guanxi*? Which are the most effective strategies that enable investors to develop good *guanxi* relations in China? There is a conventional belief that *guanxi* relations have to be cherished by offering short-term gains to the Chinese. Hypothesis 3 was designed to evaluate the validity of this belief. In addition, this section explores the hidden dimensions of *guanxi* to detect the various methods of *guanxi* maintenance employed by respondents to cope with the requirements of corresponding dimensions.

#### 8.1 Methodology of Analysis

A correlation analysis was conducted between the essential ways (the methods that were coded as "1") of *guanxi* maintenance and company performance in order to assess their effectiveness in cultivating good *guanxi* which was assumed to solicit business success in China. The following coding protocol was utilized:

"1" : The respondent perceived the strategy as an essential method to maintain *guanxi*.

"2" : The respondent viewed the method as a supplementary way to maintain *guanxi*.

"3" : The respondent explicitly opposed the approach due to one of the following reasons:

- a) the method was ineffective in maintaining *guanxi*;
- b) the method was impossible to be accomplished;
- c) respondent was restrained to use the method because of legal or ethical constraints.

[Please refer to Appendix 4 for detailed coding on the ways of *guanxi* maintenance.]

The cross-tabulation statistical procedure was employed to test the statistical significance of the correlation between different approaches of *guanxi* maintenance and company performance. To do so, the company performance of respondents for the testing period (1991-1993) had to be recoded into a dichotomous variable with two categories: successful and unsuccessful. Those companies that consistently experienced financial results which were 'above average' in the three consecutive years were coded as "successful" (Companies 1, 2, 12, 13, 15, 16 and 17), and those that had either fluctuating or 'below average' company performance in the time span were coded as "unsuccessful" (Companies 3, 5, 6, 7, 8, 9, 10, 11 and 19). This classification method was based on the postulate that good *guanxi* relations cultivated by effective methods of *guanxi* maintenance would elicit long-term business success which was defined as superior corporate financial results over the years. This meant that company performance that was consistently above the industry norm in China would be maintained if the above assumption was valid. Thus, the conservative coding of business performance was justified for the testing procedure.

Owing to the missing data on industry statistics, the three companies in the service sector (Companies 4, 14 and 18) were excluded from the analyses relating to company performance. Hence, there were only sixteen firms to be examined in the first half of this section relating to the effectiveness of various *guanxi* building methods in soliciting business success. However, in the second half of the section, all the nineteen companies

were included for evaluating the impact of the five control variables on the adoption of *guanxi* maintenance strategies.

## **8.2 General Research Findings**

### **8.2.1 "What is *Guanxi*?"**

In responding to the question, different viewpoints were collected. "*Guanxi* is a contact," was suggested by Co. 1 representative. Yet, it was counter-proposed by Cos. 14 and 18 interviewees who said, "*Guanxi* is people; or it is a connection with people." It was a linkage of two unrelated individuals based on a person who was familiar to both sides. Co. 8 respondent elaborated that the connection was in essence a communication between two individuals by which both parties tried to seek common ground in each other's perspectives and areas of interests. Hence, *guanxi* was perceived by Cos. 2 and 15 representatives as the cooperative status between investors and their Chinese business associates.

Respondents revealed that the domain of *guanxi* was constituted by five cardinal dimensions: instrumentalism, trust, personal relationship, reciprocity and longevity. Various methods were proposed to cope with the requirements of each of the five dimensions.

### **8.2.2 Instrumentalism : Offering Short-term Gains**

#### **Nurturing Long-term Mutual Benefits**

#### **8.2.2.1 Instrumentalism**

All the respondents acknowledged in great unanimity that instrumentalism was the core element of *guanxi* relations. They advocated that *guanxi* was an exchange relationship of mutual pragmatic gains which involved giving "convenience" to one party and paying for the "convenience" by the receiving party. Hence, it was a relation of high commercial

value ("li-yi guanxi" 利益關係) that had to be sustained by utilitarian benefits. Co. 12 interviewee commented that no investors would develop a *guanxi* relation that had no value to their business. He contended that the commercialized relations were based on how much investors would give to the Chinese as personal or corporate gains; and how many benefits investors would receive in return. In the extreme case, *guanxi* was perceived as a game for building personal power, as was the case for Co. 10 representative: "I maneuver my way out of *guanxi*; I work and plan for it. The *guanxihu* are my chess in the business game. They are under my manipulation and help me to checkmate my opponents."

The high utilitarian value of *guanxi* was attributed to the fact that it was cultivated in a business environment, and instrumentalism was the rule of the game. To the investors, the main objective of developing *guanxi* was to search for business opportunities. But to the Chinese, it was a way of acquiring personal gains in the form of materialistic rewards or political advancement. *Guanxi* relations were meant to satisfy these pragmatic interests of both parties. Hence, Co. 4 interviewee claimed that *guanxi* was by nature instrumental.

However, this assertion was refuted by Cos. 7 and 8 respondents who witnessed that *guanxi* relations in the past were pure personal friendships based on *renqing* and *yi* without involving any pragmatic gains.<sup>14</sup> At the time when Co. 8 interviewee went back to China for study two decades ago, *guanxi* was sentimental and emotional relationship which meant knowing the person, developing emotional bond with and taking care of him/her.

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<sup>14</sup> According to Gold (1985) and Vogel (1965), social relations in China were characterized by friendship in the eve of Cultural Revolution. At that time, friendship was dominated by trust and personal commitment. In 1949, the Chinese Communist Party determined to establish comradeship in replacement of particularistic ties. This led to a transformation of social relations from trustful friendship to skeptical comradeship.

With the signing of Sino-U.S. Joint Communiqué in 1979, China opened herself to the outside world. The Open Door Policy marked a new era in the development of social relations in China. With the exposure to materialistic enjoyment, the rejuvenation of market mechanism, the increasing freedom from government control and the expansion on disposal income, social relations in China gradually became more benefit-oriented. The Chinese tended to relate to each other based on the utilitarian value of social transactions. This led to the dominance of instrumentalism in *guanxi* in today's China.

The Chinese would put the other party in the first place, and would sacrifice themselves for the sake of their *guanxihu* because they perceived him/her as their friend.

As rationalized by Co. 18 representative, the dramatic change in the nature of *guanxi* was the direct result of two factors. Firstly, the Chinese were very poor, but they were fascinated by the materialistic enjoyment experienced when China was opened to the capitalistic Western world. Hence, the Chinese wanted to grab money to satisfy their personal desires. Secondly, personal power was dominant in China, and there was no sense of security because of rampant political struggle. The government officials would never know when they would be dismissed from their current positions. Thus, they tried every means to seize the most gains during their reign.

Although they were sentimental in the old days, *guanxi* relations in today's China were heavily inflicted by instrumentalism which aimed at fulfilling the pragmatic interests of involved parties. As remarked by Co. 18 interviewee, "After all, that is why *guanxi* is built up for."

According to the opinions of respondents, the dimension of instrumentalism would be satisfied by two prominent means of *guanxi* maintenance: offering short-term gains and nurturing long-term mutual benefits.

#### 8.2.2.2 Offering Short-term Gains

Offering short-term benefits to the Chinese was one way to maintain *guanxi*. Gains were in the form of gift-giving, banqueting, questionable payment, out-country trips, or other benefits that were realized within a short duration and could easily be duplicated by anyone.

The strategy of offering short-term gains was appraised by some respondents as the fastest method to build *guanxi* relations in China. Co. 10 representative even proposed that banqueting and questionable payment were a must in *guanxi* development. He declared that no *guanxi* could be built without meat and wine, as most Chinese business deals were



concluded at dinner tables rather than in conference rooms. It was because the Chinese preferred taking a casual approach in developing business relations. After drinking, the two parties (investors and Chinese business associates) would take off their defending positions in business negotiations, and become "sworn brothers" (as cited by Co. 10 respondent) who could express themselves openly when they were drunk and the other party would not be offended.

However, the short-term approach was criticized by other interviewees as ineffective in cultivating *guanxi*. "The short-term gains are used to buy convenience, but not to build *guanxi*," Co. 5 interviewee disputed. The incompetence of offering short-term gains in developing perpetual *guanxi* relations was attributed to three factors.

Firstly, no stable long-term relations could be established by offering short-term gains, because the Chinese would switch to other competitors who duplicated similar short-term benefits.

Secondly, the use of questionable payment connoted a sense of cheating. "If your products are good, you don't have to bribe," was argued by Cos. 5 and 16 representatives. Hence, investors would eventually lose the trust of the Chinese in them and *guanxi* ties would deteriorate in the long run.

Thirdly, short-term gains were not motivating for top government officials who were millionaires in China. They were too scornful to accept "minute" short-term benefits. Yet, the amount of payment they demanded was unaffordable by some respondents.

Most of the respondents judged that the means of offering short-term gains was detrimental to company performance. This was because the enormous expenditure to sustain short-term offers would inflate the operation costs of the company, and thus greatly reduce the profit margin. A good illustration was offered by Co. 7 interviewee who admitted that a large portion of the profit was consumed by questionable payments and the costs of socializing with Chinese business associates.

In evaluating the effectiveness of this strategy in eliciting business success, it was found that the nine companies which took this approach had relatively inferior and more fluctuating financial results than those firms which nurtured long-term mutual benefits, with the exception of Company 12.

This observation was supported by the statistics of cross-tabulation. The relationship between the approach of offering short-term gains and company performance was statistically significant ( $p < .01$ ). The Spearman correlation coefficient was  $-0.80$ , indicating that the firms that did not utilize the short-term strategy had superior company performance, while those that employed the method suffered inferior financial results.

In controlling for the five testing variables, it was revealed that the negative relationship between company performance and the use of offering short-term gains was significant under four different conditions:

1. A negative significant relationship was established for both Chinese (Spearman  $r = -0.69$ ,  $p = .05$ ) and non-Chinese companies (Spearman  $r = -0.77$ ,  $p = .04$ ).
2. A negative significant relationship was also exhibited for old-timers (Spearman  $r = -1.0$ ,  $p < .01$ ), but not for the mature group ( $p = .23$ ) and newcomers ( $p = .13$ ).
3. A negative significant relationship was found in small companies only (Spearman  $r = -0.75$ ,  $p = .02$ ). No statistically significant relationship was found for large companies ( $p = .22$ ), while no statistical analysis was conducted for medium firms.
4. No statistical analyses were conducted for the tertiary, exporting and importing industries, given that there was only one column/row in the contingency tables. This was because all the respondents in respective groups were either coded as "1" or "3" in their adoption of the short-term strategy. As for the manufacturing industry, both sub-categories were weakly significant (Spearman  $r = -1.0$ ,  $p = .08$ ).
5. Statistically negative significant relationships were found for both sub-categories under the type of institutes primarily interacted with. For those companies which interacted primarily with government agents, the Spearman correlation coefficient was  $-0.71$

( $p=.05$ ). As for their counterparts which interacted with private enterprises more, the Spearman correlation coefficient was  $-1.0$  ( $p=.02$ ).

All the above statistics affirmed the conclusion that those companies which relied mainly on offering short-term gains in cultivating *guanxi* were comparatively less successful than their counterparts which did not employ the strategy. Nevertheless, it would be misleading to totally negate the importance of offering short-term gains in *guanxi* maintenance. As disclosed in interviews with the representatives of Companies 3, 8, 12 and 13, dramatic and immediate benefits were required in the initial stage of *guanxi* development, in order to gain a chance for *guanxi* building. But its importance decreased in the mature stage because both investors and Chinese business associates perceived a value in maintaining the relationship under the nurturing of long-term mutual interests.

In conclusion, the method of offering short-term gains might not be an effective approach in nourishing perpetual *guanxi* relations. However, it was a desirable strategy to commence the cycle of *guanxi* development.



### 8.2.2.3 Nurturing Long-term Mutual Benefits

There were two peculiarities of this strategy: long-term gains and mutual interests. Long-term gains denoted the type of benefits which had to be realized over a longer time horizon than the short-term offers. More importantly, they signified the enduring advantages that could not be easily duplicated by competitors.

Mutual interests were regarded by respondents as a significant element in *guanxi* relations. 84.2% of the respondents admitted that *guanxi* ties were relations in which both parties used their own resources to cultivate mutual pragmatic gains. At the superficial level, cultivating mutual interests was defined as a way to nourish similarities in the areas of interests and in the mentalities of involving parties, so that they could communicate well. However, some respondents provided a deeper understanding of the attribute.

"It is to generate a sense of inter-dependence between the two parties involved," defined by Cos. 2 and 10 representatives. The word "inter-dependence" connoted the meaning of a constant and regular need that both parties required to have in order to survive or operate properly. The inter-dependence originated from the fact that the gains derived from *guanxi* relations were benefits extracted from the cooperation of the two involving parties, by integrating their personal/corporate gains into one single goal. Breaking the cooperation would hurt either side because the mutual benefits were lost. Hence, perpetual *guanxi* relations had to be sustained by long-term mutual interests which generated two-way gains in the interaction. Any *guanxi* which could not fulfill this requirement would definitely collapse after a few unrewarding transactions, because the losing party perceived no value in maintaining the cooperation.

The long-term mutual benefits related by the research subjects included creating job employment, making great contribution to the economic development of local regions, and giving long-term profits to the Chinese in the form of high profit margin, great market share or steady sales order. These long-term gains were appraised as more effective benefits that would maintain *guanxi* relations in an enduring fashion.

In examining the effectiveness of this strategy, the ten companies that embraced this means for *guanxi* development had higher annual net income growth for the past three years, except three cases (Companies 3, 5 and 19). However, the observation was not tested statistically, since all the respondents who were tested in respective groupings were proponents of the long-term approach.

### **8.2.3 Trust : Cultivating Trust**

#### **8.2.3.1 Trust**

Trust was nominated by 84.2% of the respondents as the basic criterion for *guanxi* building. "You have to build trust with the Chinese before you can have any *guanxi* relations and business deals with them," said by Cos. 11 and 12 interviewees. Co. 6 representative even remarked that no corruption could be committed if the Chinese did not trust the investors who intended to bribe them. The prominence of trust was deep-rooted in the conservatism of the Chinese who did not want to take any risk. Hence, they did not trust outsiders whom were generally perceived as untrustworthy. They would only build *guanxi* and do business with the ones in whom they had confidence. If investors did not earn the trust of the Chinese, they did not even have the chance to build *guanxi*, much less cultivate mutual interests. Consequently, trust was, in fact, the backbone of *guanxi* relations.

It was apparent that investors had to seek the trust of the Chinese, but paradoxically very few respondents had trust in the Chinese. "Never trust the Chinese because they are too money-minded," advised by Co. 7 interviewee. Only 42.1% of the respondents rated trust highly (at 8 or above) in their most important *guanxihu*, while the remaining 57.9% show a low trust level in their Chinese business associates.

Some respondents criticized the Chinese for caring only about pragmatic gains. Hence, they did not trust the Chinese who would betray them when their competitors tendered better utilitarian benefits. An alternative reasoning for the untrustworthiness of the

Chinese was offered by Co. 5 representative who stressed self-protection. Since the Chinese were under the close supervision of the Communist government, they were under a lot of pressure to comply with the rules and requirements of the Party. The Chinese would betray anyone for self-protection when their own security was jeopardized.

#### 8.2.3.2 Cultivating Trust

Several strategies were advanced by respondents as competent methods for cultivating trust. They were applicable in different stages of business development.

**Use of Intermediary:** Intermediaries were defined as separate individuals/entities that were hired by investors to help them enter the China market. They had accountability to build *guanxi* relations for investors in China. Their presence was most significant in the initial stage of business establishment. When investors did not have any prior connections with the local Chinese, intermediaries would function as cable connections to link investors with their relevant Chinese business associates.

The use of intermediaries was highly recommended by respondents because it was an effective method to cultivate trust between the two unrelated parties (investors and the Chinese). "The Chinese don't trust outsiders. They only trust the third party who introduces you," some respondents highlighted. It was the trust of the Chinese in the intermediaries that transformed the identity of investors from outsiders to insiders of the Chinese society. Hence, the chief selection criterion of intermediaries was the possession of a strong *guanxi* network in China. It was stipulated by Co. 13 interviewee that his corporation would examine the scope and the strength of *guanxi* relations that an entity had before commissioning it to be the intermediary of his company in China. In fact, an intermediary could be as small as a single individual who was either a local Chinese or a Hong Kong resident who had strong *guanxi* ties in China; or as large as a multi-national company such as a business consulting firm or a banking institute.

In the research sample, there were four companies which relied heavily on intermediary firms for *guanxi* maintenance. Three were American firms and one was a Chinese company. The American firms had to choose this option because they were restricted by the U.S. anti-corruption act from engaging in any corruption activities. They resolved this constraint by dealing with other separate Chinese companies which acted as intermediaries between them and the targeted Chinese firms. The U.S. firms officially gave low prices to intermediary companies which would then earn great profits by selling the products. In return for the high profit margin, the intermediary firms helped the U.S. companies to source customers, distributors and many other important business associates. They would handle all the *guanxi* problems and associated payments. Hence, the three U.S. firms were detached from being engaged in any questionable payment<sup>15</sup>.

The Chinese firm (Company 6) which opted for the strategy understood that it was too difficult for them to handle *guanxi* relations as an "outsider" of the Chinese community. Thus, Co. 6 representative employed an intermediary firm to help him solve business problems by utilizing its *guanxi* network in China.

No statistical analysis between the use of intermediary and company performance was conducted because the method was perceived by respondents as a supplementary way of *guanxi* maintenance instead of an essential strategy.

**Building a Reputation of Trustworthiness:** When connections with the Chinese had been established, the primary task of investors in cultivating trust was to build a reputation of trustworthiness. Trust was conceived by respondents as essential in doing business with China. "Reliability is very important in China, because the Chinese live in a

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<sup>15</sup> The strategy of using intermediary firms by American firms to avoid getting involved in questionable payments may have an ethical concern, since it will indirectly fuel the growth of corruption in China. However, it is not the intention of this thesis to discuss the ethical aspect of the strategy. The objective of the thesis is to reflect the actual situation which occurs in China now.



relation-oriented society. Bad reputation will be spread around quickly and it will ruin your business," justified Cos. 4 and 15 interviewees.

There were two mottoes for cultivating the trustful image: "Deliver what you have promised" and "Don't cheat". Cos. 1 and 15 representatives attributed their success in China to the first principle. "I will definitely keep my promise, no matter how hard it is. Only in this way, can you win the trust and respect of the Chinese," they declared. The second motto was kept by most of the respondents, because they knew that the Chinese would never trust them again if they cheated only once. Their credibility in the Chinese business community would be gone, and so would be the *guanxi* relations.

In comparing the strategy with company performance, the seven firms that had built a reputation of trustworthiness in *guanxi* had higher annual net income growth, except in one case (Company 5). However, it was not reflected in the cross-tabulation analysis ( $p=.13$ ) which indicated that the relationship between building a trustful image and company performance was not statistically significant. Among the five control variables, only the exporting manufacturers achieved statistical significance (Spearman  $r=1.0$ ,  $p=.08$ ). There was no statistically significant relationship found for other control groupings. These statistical results might be true reflections of the insignificant relationship between the two variables; or they might be a consequence of the negative impact induced by small sample size; or an outcome of the confounding effects imposed by other extraneous variables. Further research is recommended to investigate the ambiguous relationship.

**Understanding Chinese Culture:** The last advice for cultivating trust was to learn the Chinese culture. This required investors to have a good understanding of Chinese history, language and thinking. The rationale was to show to the Chinese that the investors were part of them and they should not be treated as outsiders; thereby trust would be cultivated between the two parties.

In the research sample, there were two Chinese companies (Companies 1 and 8) and three non-Chinese firms (Companies 14, 18 and 19) which stressed the importance of understanding Chinese culture in *guanxi* building. No statistical analysis correlation between the strategy of understanding Chinese culture and company performance was conducted because the approach was perceived by respondents as a supplementary way of *guanxi* maintenance, but not an essential method.

## **8.2.4 Personal Dimension : Nourishing Personal Relationship**

### **8.2.4.1 Personal Dimension**

While different people might have contrasting interpretations of "personal", it was defined as the status in which one would relate one's deepest feelings and problems to a particular person when these were not generally disclosed to other individuals.

This dimension was most controversial, as it received the greatest arguments from respondents. 47.4% of the interviewees confirmed the importance of nourishing personal relationships, while the remaining 52.6% negated its relevance and the feasibility of achieving it. Opponents to this dimension argued that personal friendship was a past story which was faded away under the dominance of instrumentalism in *guanxi* relations. Cos. 14 and 18 representatives reasoned that the over-emphasis on utilitarian gains by the Chinese was the main obstacle that hindered the development of any personal relationship with them. Furthermore, cultural differences also widened the gap between investors and the Chinese, as they had discordant value systems and attitudes which were contributed by different social and education backgrounds. To the opponents, *guanxi* relations were restricted to business discussions without involving any disclosure of inner feelings or personal problems. They would not reveal their inner selves to the Chinese because they did not trust them.

The above propositions were refuted by the proponents of the approach, because of the essentiality of developing personal relationship in *guanxi* ties. They contended that

there was an intricate connection between personal friendship and business transactions. Business gains were generally perceived as the main nutrient of personal friendship which would die away soon if the refreshing substance was ignored. But in turn, personal friendship was required to facilitate the business transactions between investors and the Chinese. It would smoothen the interaction between the two parties and better the communication process. The strategy was conceived by the proponents as a means to hold the Chinese with them in a sustainable manner.

Some respondents even proposed that pure friendship with the Chinese would arise because *gan-ching* would be nourished in the course of interaction between the two parties. Both Cos. 1 and 2 interviewees declared that they regarded their most important *guanxihu* as part of their families. Cos. 13 and 15 representatives admitted that they would disclose their inner feelings and difficulties to those Chinese business associates who were their best friends in China. Proponents maintained that personal *guanxi* relations should not be confined only to the Chinese business associates themselves, but should be extended to their family members. Co. 12 respondent acknowledged that he knew the family members of his most important *guanxihu*, and was frequently invited for dinners prepared by the wife of the Chinese business associate.

#### 8.2.4.2 Nourishing Personal Relationship

In discussing how to build intimate personal friendship with the Chinese, the proponents suggested that sincerity and frankness were the two fundamental principles. One should try to build an in-depth knowledge of the Chinese business associates; as well as appeal to their personal needs, so that the Chinese felt that one was sincere in establishing personal relationships with them.

In evaluating the effectiveness of the personal strategy, an analysis was made of the relationship between the approach and company performance. Although there were only nine companies which took the strategy in *guanxi* building, they had superior company

performance in the testing period, with the exception of Companies 6 and 9. However, the representatives of both companies had a very different definition of "being personal". They interpreted it as only listening to the Chinese when they had problems. In rating how personal the *guanxi* relations were with their most important *guanxihu*, Co. 9 interviewee had a hard time in identifying the *guanxihu* because he did not have one who was particularly close to him. He declared that he would not have any personal relationship with any Chinese, because he thought that it was a waste of time and money. As for Co. 6 representative, he gave a rating of 4 on his *guanxi* relation with the most important *guanxihu*. He disclosed that he would never be too close to the Chinese because he did not trust them. Both companies were small Chinese firms. Company 6 was a real estate management firm, and Company 9 was an exporter of textile products. The former was classified as a newcomer since the representative had only one year of experience in China trade; while the respondent of the latter company was a mature investor who had been in China business for eight years.

Cross-tabulation statistical analysis revealed that the relationship was statistically significant (Spearman  $r=0.8$ ,  $p=.01$ ). This meant that those companies which adopted the strategy of nourishing personal relationships had a higher chance of attaining superior company performance. In controlling for the five testing variables, the following statistical results were obtained: [Please refer to Table 8.1 on page 144 for detailed statistical results.]

1. A significant positive relationship was established for both Chinese (Spearman  $r=0.57$ ,  $p=.10$ ) and non-Chinese (Spearman  $r=0.77$ ,  $p=.04$ ) firms.
2. It was found that the positive relationship was significant only for old-timers (Spearman  $r=0.74$ ,  $p=.08$ ), but not for mature group ( $p=.23$ ) or newcomers ( $p=.13$ ).
3. No statistics were computed for medium-sized companies, because all the respondents in the group had superior company performance, therefore they were all coded as "1" in

the contingency table. But the relationship was significant for both large corporations (Spearman  $r=1.0$ ,  $p=.08$ ) and small firms (Spearman  $r=0.83$ ,  $p=.03$ ).

4. Statistical analyses were conducted only for the manufacturing and importing industries. For both the exporting manufacturers (Spearman  $r=1.0$ ,  $p=.08$ ) and importers (Spearman  $r=.79$ ,  $p=.08$ ), there was a significant positive relationship between nourishing of personal relationships and company performance.
5. The companies that interacted primarily with government agents (Spearman  $r=0.82$ ,  $p=.04$ ) had a higher chance of attaining business success if they employed the personal approach, while it was not true for their counterparts who interacted with private enterprises more ( $p=.23$ ).

To conclude, the strategy of nourishing personal relationship was conceived as an essential way of *guanxi* maintenance. Those companies which had adopted the approach tended to experience superior company performance, while the enterprises which abandoned the strategy had inferior financial results.

## **8.2.5 Reciprocity : Tendering Favors**

### **8.2.5.1 Reciprocity**

Thirteen respondents alleged that *guanxi* relations operated on a dimension of reciprocity. They stated that the Chinese would remember what deeds investors had done for them, both positive and negative. They would, in future, return the favors to investors or request the payment of debts that investors had owed them. The accent on reciprocity by the Chinese was attributed to the Confucian philosophy of *shu* and *bao*. The notion of *shu* specified that one had to treat others as if one was treating oneself. The norm of *bao* demanded individuals to comply with the obligations to give, to receive and to repay. [Please refer to the section on the "Operating Concepts of *Guanxi*" for detailed discussion.] Both stipulations required the Chinese to reciprocate what they had received to the givers. These two Confucian ideas were deeply inculcated in the minds of the Chinese.

#### 8.2.5.2 Tendering Favors

In the domain of *guanxi* relations, reciprocity manifested itself mainly in the form of tendering favors. The Chinese would tender favors only to investors who had good *guanxi* ties with them. This was because the Chinese expected to gain a good rate of return in future for the favors they tendered. Hence, they would seldom perform favors for investors whom the Chinese had little inclination for *guanxi* development, since the chance of gaining back the returns was slim.

By the same token, the Chinese expected investors to tender favors to them when they were in need. Yet, the favors provided by investors would not be futile attempts because the Chinese would compensate them in future transactions for the loss or efforts incurred. Hence, it was conceived by respondents that tendering favors was a primary way of consolidating *guanxi* relations, because it was the most solid method to show the concern and care of investors towards the Chinese, especially when they were in difficulties. "As long as you can accommodate the needs of the Chinese, they like to be associated with you because they know that you are helping them in a constructive way," Co. 15 representative justified.

The favors tendered by respondents to the Chinese covered a wide range of activities. It could be as minor as supplying information which was readily accessible to investors; or as serious as committing illegal activities in helping the Chinese to reduce tax payment. It might be personal requests such as sponsoring the children of Chinese business associates to obtain overseas student visas; or business favors like helping the Chinese to discharge low quality products, so that the Chinese could gain credits in the eyes of their superiors. In return for all these efforts, investors would gain good *guanxi* relations with the Chinese. Consequently, it was fair for Co. 18 interviewee to conclude that *guanxi* was a two-way exchange relationship based on reciprocity.

While no conclusive comments could be made on the business results of the thirteen respondents who adopted the use of tendering favors, it was found that the three firms

(Companies 6, 10 and 19) which objected to the approach tended to have poorer financial performance. These three companies claimed that either it was an ineffective method of cultivating *guanxi*, or the Chinese would abuse the use of favors and take advantage of them. However, their company performance for the three years was consistently below the industry norm in China.

Unfortunately, this observation was not supported by the statistical analysis. The relationship between the strategy of tendering favors and company performance was not statistically significant ( $p=.12$ ). If controlled for the five testing variables, the relationship was significant under two circumstances: [Please refer to Table 8.1 on page 144 for detailed statistical results.]

1. A significant positive relationship was established only for non-Chinese firms (Spearman  $r=0.70$ ,  $p=.04$ ).
2. Contradictory evidence was provided by the mature group of investors for whom there was a negative relationship between the use of tendering favors and company performance (Spearman  $r=-1.0$ ,  $p=.08$ ). The firms that declared tendering favors as an essential way of *guanxi* maintenance had inferior company performance; while the two firms which took the strategy only as a supplementary approach in *guanxi* building had superior financial results. None objected to the use of tendering favors.

Both the statistical results and the qualitative analysis imply that the strategy of tendering favors might be a necessary but insufficient condition for attaining long-term business success in China.

## **8.2.6 Longevity : Maintaining Continuous Interaction**

### **8.2.6.1 Longevity**

Longevity was, in fact, the underlying assumption of the four foregoing dimensions: instrumentalism (nurturing long-term mutual benefits), trust, personal, and reciprocity. As discussed earlier, the strategy of nurturing long-term mutual benefits was

an effective approach to cultivate *guanxi* relations because pragmatic gains were realized over a long time horizon. Both trust and personal dimensions demanded relationships to be built over a lengthy period. The attribute of reciprocity advised investors to take a long-term perspective on tendering favors because the favors tendered today would be compensated by potential returns in the future. All these signified that *guanxi* was a long-term relationship which required a lot of time and resources for cultivation. The reason for the longevity requirement of *guanxi* building stemmed from the perception of the Chinese that time would reveal the sincerity of investors. "Over time, the Chinese will know the earnestness of outsiders (i.e. investors) in building *guanxi* with them," Co. 3 interviewee specified. "It would be the best if you build *guanxi* with the Chinese long before he/she gains power, because it purifies the relationship," recommended the representatives of Companies 3, 5, 8 15 and 17. In this way, the Chinese would conceive that the purpose of investors to build *guanxi* with them was their personalities, but not the associated benefits. This would convince the Chinese of the sincerity of investors in being associated with them.

Unfortunately, the long-term social investment might not be rewarding every time. According to five respondents, *guanxi* building was a gambling game. Since it would be impossible for investors to build *guanxi* with every Chinese, they had to select some particular individuals as the targets for *guanxi* building whom were perceived as prospective in giving them great future benefits. They named this strategy as "*da-ding*" (nailing the nail onto him/her 打釘) Yet, the nails nailed might be fatal efforts if the selected Chinese did not gain power and give them the desirable *guanxi* benefits in the end. Consequently, some respondents expressed great frustration in *guanxi* building. As they exclaimed, "*Guanxi* building is a risky venture that would make you a millionaire or a loser in the gambling investment overnight."



### 8.2.6.2 Maintaining Continuous Interaction

The longevity dimension requires investors to have continuous interaction with the Chinese. This was reflected in the research sample, as all the respondents maintained constant interaction with their *guanxihu*, except Co. 8 representative who claimed that he only called them when he needed their assistance. One of the respondents suggested that true *guanxi* did not require on-going interactions. He could talk to his *guanxihu* openly even after a long period of non-communication. Yet, such an idea was rejected by five other interviewees who explicitly commented that *guanxi* would be 'stolen' (i.e. captured) by others if they did not interact with them for some time. Respondents admitted that there was a keen competition for *guanxi* relations in the Chinese business arena. A long period of non-communication would weaken the particularistic ties between investors and their Chinese business associates. The positions of investors as givers of utilitarian gains would be easily replaced by their competitors who offered similar benefits to their *guanxihu*. Hence, maintaining continuous interaction was necessary in cultivating *guanxi* relations with the Chinese.

No correlation between the approach of maintaining continuous interaction and company performance was made because the method was perceived by respondents as a supplementary way of *guanxi* maintenance only.

Instrumentalism, trust, personal, reciprocity and longevity were the five fundamental dimensions of *guanxi* relations in China. It was noteworthy to specify that the five dimensions were by no means mutually exclusive. They were attributes that were complementary to each other in the domain of *guanxi* relations. Correspondingly, the various strategies of *guanxi* maintenance outlined above were approaches that were compatible with rather than competing against each other. As a matter of fact, it was revealed in the research that *guanxi* relations were best cultivated when investors employed

the use of four collaborative *guanxi* building techniques which would lead to long-term business success in China.

### **8.2.7 Four Collaborative Successful *Guanxi* Building Techniques**

As exhibited in both qualitative and quantitative research findings, nurturing long-term mutual benefits, nourishing personal relationship, cultivating trust and tendering favors were more successful strategies to develop good *guanxi* relations than the use of offering short-term gains. The impotence of the short-term approach was rooted in its incapability to cultivate perpetual instrumental relations and particularistic ties with the Chinese.

#### **8.2.7.1 Perpetual Instrumental Relations**

In essence, there was an important similarity between nurturing long-term mutual benefits and offering short-term gains. Both were giving pragmatic interests to the Chinese yet they differed in the form of gains, the duration of beneficial period and the extent of replaceability.

Short-term gains were direct, immediate materialistic rewards that were to be consumed or realized within a short period of time. The benefits were not long-lasting and could easily be duplicated by other competitors. The position as a giver of these short-term benefits could be easily replaced by anyone who presented similar terms to the Chinese. The Chinese would turn to the one who offered them the most materialistic rewards in business transactions. As a result, the Chinese were switching among different investors for pragmatic gains and therefore could not be secured for long. This would have great impact on the company performance of respondents, because the lucrative business opportunities that were associated with the Chinese would be lost as well when the Chinese turned to other investors. Consequently, for those respondents who relied mainly on offering short-term gains in *guanxi* building, their business results were largely dependent

on whether they could hold the Chinese on their side in that particular year. Thus, more fluctuating company performance often resulted.

In contrast, long-term mutual benefits were indirect, sustained gains that allowed the Chinese to enjoy the benefits on an on-going base. The superiority of nurturing long-term mutual benefits was derived from its potential to entangle the long-term gains of the Chinese with the business success of respondents.

The long-term gains exhibited in the research sample were of two major types. The first type was sustained profits derived from product sales. Its aim was to give the Chinese high profit margin, great market share, or large sales volume, so that the Chinese perceived a greater value in working with the investors than with other competitors. This was to tie the Chinese' gains with the business performance of investors. Hence, the higher the company sales of investors, the more profitable it would be for the Chinese.

The second type was to strengthen the political power of Chinese officials by helping them to fulfill their job responsibilities. At present, China aims at modernizing herself to attain the advanced standing of a world power. Any province which could outperform others in the economic advancement and bring prosperity to the regions would definitely gain high prestige and power in the Chinese government. Investors could give a helping hand to local government officials by making donations to build local transportation networks, setting up power generation stations or earning huge foreign reserves through the exporting of manufactured products from China.

The subtle benefits mentioned above were given to the Chinese on a prolonged time horizon. The benefits would be gone if investors failed in business and retreated from the China market. Hence, the Chinese officials would ensure that the business operations of these investors were smooth, so that the investors would continue to support them, and their own long-term gains would not be jeopardized. More importantly, the intricate relations of mutual benefit between the Chinese and investors could hardly be replaced by the competitors who offered short-term gains only. Consequently, nurturing long-term

mutual benefits fulfilled the basic requirement of *guanxi* for nourishing perpetual instrumental functions which would lead investors to have long-term business success.

#### 8.2.7.2 Particularistic Ties

Cultivating particularistic ties with the Chinese was a step further than nurturing perpetual instrumental relations. Its objective was to affix the Chinese to investors more firmly by building multiple points of association between the two parties in a *guanxi* relation.

*Guanxi* relations that were sustained only by instrumental functions (both short- and long-terms) were fragile connections. Investors who offered perpetual instrumental gains would still have the chance of losing the *guanxi* if their competitors could duplicate similar benefits one day. Hence, in capturing the *guanxi* in a more enduring fashion, investors should develop personal relationships with the Chinese which were irreplaceable by others. "Personal" connoted that it was something specific between the two parties involved such as sharing inner feelings or personal secrets between friends. Such specificity was highly distinctive and individualistic, and it could not be duplicated by others.

Going hand in hand with personal relationship was the element of trust. In fact, it was the preliminary requirement that had to be surmounted before any *guanxi* building could commence. The most effective way of building trust and cultivating personal relations with the Chinese was to tender favors. Tendering favors was to do favors for others at one's own expense. It was the primary way of building *guanxi* because it showed one's concern towards the Chinese and one's willingness to help them without requiring any immediate return. But, the Chinese would remember the favors, and would record all the pluses and minuses in the relation. They would reciprocate the favors with equal or even greater value to the investors in the future.

Nurturing long-term mutual benefits, nourishing personal relations, building trust and tendering favors seemed to be essential ways to furnish strong and reliable *guanxi* relations with the Chinese. However, it was inconclusive to put forward the above argument because some respondents still failed to have successful company performance even when they employed one of the above methods in *guanxi* building (Companies 3, 5 and 19 in nurturing long-term mutual benefits; Companies 6 and 9 in nourishing personal relations; Company 5 in cultivating trust; Companies 3, 5, 8 and 11 in tendering favors.)

The clue was that none of the above four methods was sufficient to cultivate strong *guanxi* ties on its own. They had to function in collaboration in order to achieve successful *guanxi* relations. Building personal and trustful relations without offering long-term mutual benefits would not sustain *guanxi* ties because the perpetual instrumental function which was the backbone of *guanxi* was unfulfilled. No *guanxi* connection could survive without the nourishment of utilitarian benefits. On the other hand, *guanxi* required the other three techniques to supplement the building of particularistic ties; otherwise, the *guanxi* relations could be easily "stolen" by other competitors who furnished similar instrumental functions.

The above proposition was supported by the magnificent company performance of six firms (Companies 1, 2, 12, 13, 15 and 17) which adopted the use of the four cardinal *guanxi* building techniques (nurturing long-term benefits, cultivating trust, building personal relations and tendering favors). It is notable that the company performance of these six respondents was consistently superior for the past three years. In line with the above postulate, the six respondents gave relatively high ratings to their most important *guanxihu* on the three dimensions of personal, trust and effectiveness in problem solving. Correspondingly, the nine companies that offered short-term gains in *guanxi* building gave very low ratings on the trust and personal dimensions, with the exception of Company 12. Company 12 was an exceptional case because its representative did not only offer short-term benefits, he nurtured long-term mutual interests, cultivated personal relationship and

built trust in *guanxi* relations. Hence, his company performance was brilliant in the past three years, and he had very different ratings on the personal and trust dimensions.

In testing the validity of the postulate on integrated *guanxi* building techniques, a dichotomous variable was created for conducting the cross-tabulation statistical procedure. The six respondents who embraced the use of the four cardinal *guanxi* building methods were coded as "1", while the remaining thirteen respondents were classified as "0". The statistical result was encouraging. The relationship between the four collaborative *guanxi* methods and company performance was statistically significant (Spearman  $r=0.87$ ,  $p<.01$ ). This signified that there was a strong relationship between the two elements, indicating that those enterprises which adopted the collaborative approach in *guanxi* building would have a higher chance to attain long-term business success in China than their counterparts who did not.

When controlled for the five testing factors, it was shown that the relationship was significant in all sub-categories, except for non-Chinese firms, small companies and importing industry. [Please refer to Table 8.1 on page 144 for detailed statistical results.]

In examining the attributes of the six companies which employed the collaborative strategy in *guanxi* maintenance, it was found that four were non-Chinese firms while the remaining two were Chinese companies. At the same time, four of the six respondents interacted primarily with government agents and the remaining two were with private enterprises. One might conclude that non-Chinese ownership and interaction with government agents would lead investors to embrace the collaborative approach in *guanxi* building, thereby enjoyed business success in China. The presumption was easily refuted when one examined the other attributes of the six firms.

The two most salient features of the six respondents were their in-depth experiences and the long-term business commitment. All of them were experienced investors in China trade with four old-timers and two mature investors. They were all engaged in industries which required long-term business commitment, since they were either in the

manufacturing or importing sector. Owing to the long-term business strategy, they made comparatively greater business investment in China. This was reflected in firm size, as five of them were either large or medium companies. The adoption of the integrated approach was an outcome of the above two factors. Their prolonged personal experiences guided them to adopt a means which was capable of maintaining *guanxi* in an enduring fashion. The long-term business commitment demanded they employ a method of *guanxi* maintenance which was compatible to their long-term business strategy. Both requirements were fittingly fulfilled by the collaborative *guanxi* building techniques.

More importantly, the foregoing reasoning highlighted the prominence of longevity in achieving business success in China, as the element was unveiled to be the common denominator of all the above evidence. In the attainment of business success in China, investors had to incorporate a long-term perspective which would definitely affect their choices on the type of industry they would be in and the ways of *guanxi* maintenance. With the current research sample, it was proved that those investors who had integrated longevity in the above two respects tended to have a greater chance of achieving long-term business success in China than the firms which had not.

To conclude, it was proposed that nurturing long-term mutual benefits, cultivating personal relationships, building trust and tendering favors were the four collaborative strategies in *guanxi* building that would solicit long-term business success in China.

### 8.3 Research Findings by Control Variables

Table 8.2: Relative Importance of the Ways of *Guanxi* Maintenance by the Five Control Variables

	No. of Firms	Short-term Gains	Long-term Benefits	Personal Relations	Trust	Tender Favors
<b>Ownership Type</b>						
Chinese Firms	11	63.6%	36.4%	36.4%	36.4%	63.6%
Non-Chinese Firms	8	25.0%	87.5%	62.5%	50.0%	87.5%
<b>Experience Level in China Business</b>						
Old-timers	7	42.9%	57.1%	57.1%	57.1%	85.7%
Mature Group	6	50.0%	50.0%	50.0%	66.7%	66.7%
Newcomers	6	50.0%	66.7%	33.3%	0.0%	66.7%
<b>Firm Size</b>						
Large Firms	3	66.7%	66.7%	33.3%	33.3%	66.7%
Medium Firms	5	20.0%	80.0%	80.0%	80.0%	100.0%
Small Firms	11	54.6%	45.5%	36.4%	27.3%	63.6%
<b>Industry Type</b>						
Tertiary	4	25.0%	25.0%	25.0%	25.0%	75.0%
Exporting	4	100.0%	25.0%	25.0%	0.0%	25.0%
Manufacturing	6	66.7%	66.7%	50.0%	50.0%	83.3%
Importing	5	0.0%	100.0%	80.0%	80.0%	100.0%
<b>Type of Institutes Primarily Interacted</b>						
Govt. Agents	14	42.9%	57.1%	42.9%	42.9%	85.7%
Private Firms	5	60.0%	60.0%	60.0%	40.0%	40.0%

#### 8.3.1 Ownership Type

Needing to comply with the U.S. anti-corruption act, the American firms objected to the approach of offering short-term gains as a primary means to maintain *guanxi*. This stood in great contrast to the preference of Chinese firms. [Please refer to Table 8.2 for the figures.] 63.6% of the Chinese firms opted for offering short-term gains as a way of *guanxi* maintenance, as opposed to 25.0% of the non-Chinese companies.



In light of the legal and ethical constraints by parent companies, non-Chinese firms resorted to two other alternatives:

1. Use of Intermediaries

It was found that more non-Chinese firms (37.5%) employed intermediary companies than Chinese firms did (9.1%). The non-Chinese companies relied on intermediaries to handle all the *guanxi* problems and associated questionable payments.

2. Adoption of Collaborative Successful *Guanxi* Building Techniques

87.5% of non-Chinese firms engaged in cultivating long-term mutual interests while only 36.4% of Chinese companies did. Non-Chinese firms also gave greater emphasis on nurturing personal relationship, building trust and tendering favors than did Chinese firms.

The above observations were partially supported by cross-tabulation statistical analyses. The importance of ownership type was tested to be statistically significant only in its relationships with cultivating personal relationship (Spearman  $r=-0.34$ ,  $p=.05$ ) and building trust (Spearman  $r=-0.45$ ,  $p=.09$ ). These results confirmed the qualitative analysis by specifying that non-Chinese companies tended to assign a greater level of importance to the two *guanxi* building techniques than Chinese firms did. It was surprising that no statistically significant result was generated for the other three essential methods and the collaborative approach of *guanxi* building.

Table 8.3: Statistical Results on the Relationships between Ways of *Guanxi* Maintenance and the Five Control Factors

	Offering Short-term Gains	Nurturing Long-term Benefits	Cultivating Personal Relations	Building Trust	Tendering Favors	Collaborative Approach						
	r	Sig.	r	Sig.	r	Sig.						
Ownership Type	--	0.16	--	0.42	-0.34	0.05 *	-0.45	0.09 #	--	0.75	--	0.14
Experience Level in China Business	--	0.85	--	0.38	--	0.60	0.67	0.03 *	--	0.15	0.50	0.08 #
Firm Size	--	0.14	--	0.51	--	0.64	--	0.57	--	0.27	0.46	0.01 *
Industry Type	0.35	0.01 *	-0.53	0.01 *	--	0.45	--	0.57	--	0.21	-0.54	0.08 #
Type of Insitutes Primarily Interacted With	--	0.38	--	0.52	--	0.87	--	0.65	--	0.15	--	0.63

r Spearman correlation coefficient

\* p<.05, two-tailed test.

# p<.10, two-tailed test.

-- Statistics could not be computed because there was only one column/row in the contingency tables.

### 8.3.2 Experience Level in China Business

The emphasis on cultivating personal relationship was in direct proportion to the experience level in China business. [Please refer to Table 8.2 on page 164 for the figures.] The experienced investors in China trade had a stronger inclination for cultivating personal relationship, since 57.1% of the old-timers and 50.0% of the mature group perceived its importance in *guanxi* building, contrasting with only 33.3% of the newcomers who accepted the option. Correspondingly, the newcomers rejected the importance of cultivating trust in *guanxi*. None voted for the notion, as opposed to 66.7% of the mature group and 57.1% of the old-timers who supported the means.

The unbalanced emphases on nourishing personal relationship and cultivating trust between old-timers and newcomers were good indications of the fact that *guanxi* operated on a longevity dimension. It took a long time to cultivate personal and trustful relationships with the Chinese. The emphases on the two aspects by old-timers were reflections of their prolonged personal experiences with the Chinese. It indicated that the newcomers did not have enough time to experience the essence of cultivating personal and trustful relations, and their importance in *guanxi* building.

Unfortunately, the qualitative analysis was not fully confirmed by the statistical results. [Please refer to Table 8.3 on page 166 for detailed statistical results.] The relationship between cultivating personal relationship and experience level was not significant ( $p=.60$ ). On the contrary, the importance of experience level was exhibited in its relationships with building trust (Spearman  $r=0.67$ ,  $r=.03$ ) and collaborative successful *guanxi* building techniques (Spearman  $r=0.5$ ,  $p=.08$ ). The statistics signified that the more experience the investors had, the greater tendency they would adopt the strategy of building trust and the collaborative successful *guanxi* building techniques.

### 8.3.3 Firm Size

A misconception would be easily conveyed by the statistics. [Please refer to Table 8.2 on page 164 for the figures.] It is that medium firms advocated the approach of the four collaborative *guanxi* building techniques, and had a great distaste for the use of offering short-term gains; while the large and small companies adhered to the short-term method. However, such an observation is confounded by two control factors: ownership type and experience level. Four of the five medium firms were non-Chinese companies which were restricted by the legal and ethical requirements of their parent countries to offer short-term gains to the Chinese. At the same time, four of the five respondents were classified as either old-timers or mature investors who had a strong preference for the four long-term *guanxi* building methods due to their extensive personal experiences. Both attributes of ownership and experience level would govern the respondents of medium sized firms to be more inclined to use the collaborative method of *guanxi* building and to disapprove the short-term strategy.

As for the large and small companies, they had similar levels of emphasis on the various methods, and no specific pattern was found.

It was surprising to see that there was a significant correlation between the collaborative approach and firm size, indicating that large and medium companies had greater tendencies to employ the integrated strategy in *guanxi* maintenance. [Please refer to Table 8.3 on page 166 for detailed statistical results.] Two different rationales were offered to explain this relationship.

#### 1. Direct impact of firm size

Company size was an indication of the business commitment of investors in the China market. As investors made greater investment by increasing the company size through recruiting more local employees, they assumed a higher level of risk and a longer time span for the return of their investment. In light of the prolonged business

commitment in China, the large and medium firms had to adopt the collaborative *guanxi* building techniques which were compatible to their long-term business strategy.

Nevertheless, if the above argument is valid, individual significant relationships should also be established between firm size and any of the four long-term *guanxi* building methods (nurturing long-term benefits, cultivating personal relationship, building trust and tendering favors). The four *guanxi* building approaches did not reach statistical significance thus indicating that the chance of formulating significant relationships was slim with the current research sample. Hence, it is suspected that the significant correlation between firm size and the collaborative strategy was largely an outcome of the confounding effect of experience level.

## 2. Confounding effect of experience level

One of the most salient features of the six respondents who embraced the collaborative approach was their in-depth China business experience (4 old-timers and 2 mature investors) By coincidence, five of the six respondents were in large and medium companies and they constituted to 62.5% of the total group when the two groups were combined. The heavy weight carried by these five experienced respondents in cross-tabulation analysis would induce a positive correlation between firm size and the collaborative strategy, and thereby a significant relationship between the two variables.

### 8.3.4 Industry Type

[Please refer to Table 8.2 on page 164 for the figures.]

#### 1. Tertiary Industry: Tendering favors

The four research subjects showed that the method of tendering favors was important in the tertiary industry to build *guanxi*, as 75% of the group asserted its significance versus only 25% for the other means.

One major characteristic of the tertiary industry was that the 'products' transacted in business deals were intangible services tendered by companies. In furnishing services, the firms had to rely on the assistance of many Chinese entities, especially the supply of information. As confirmed in the research findings on "*Guanxi* Networking", the Chinese entities which served as information agents to tertiary companies held a significant position in constituting the ideal *guanxi* network of the industry group. The supply of information was a favor tendered by the Chinese entities to investors. In maintaining the long-term relations with these information suppliers, investors had to reciprocate similar favors in return. Hence, tendering favors was considered by the tertiary industry as an important means to consolidate *guanxi*.

## 2. Exporting Industry: Offering short-term gains

The way of offering short-term gains won the total support of all exporting firms in the research sample. 100% of the sample affirmed its importance in *guanxi* building, and relatively ignored the essentiality of the other means (25% for nurturing long-term mutual interests, cultivating personal relationships and tendering favors; 0% for nourishing trust).

The emphasis on offering short-term gains by the exporting industry was attributed to the "grab-and-go" nature of the industry. The exporting firms exported products from China and sold them in world markets. It did not require investors to make any heavy initial investment in China so they had a relatively short-term business commitment in the oriental country. Their primary task was to source products from areas throughout China. As they had different transactions at different locations, it was hard for these companies to build perpetual *guanxi* with any Chinese business associates in each individual region, especially when it required a lot of time and monetary resources to sustain *guanxi* relations. Hence, offering short-term gains to the Chinese served as a short-cut for exporting firms to 'buy' *guanxi* for each business

transaction. This was to remedy their inability to build long-term *guanxi* relations due to the high inability of business locations.

### 3. Manufacturing Industry: Comprehensive approach of *guanxi* maintenance

No specific pattern could be traced in the ways of *guanxi* maintenance. The different methods received equal support from the respondents in manufacturing industry: 66.7% for offering short-term gains, 66.7% for nurturing long-term mutual interests, 50% for cultivating personal and trustful relationships, and 83.3% for tendering favors.

The non-existence of a consistent pattern in *guanxi* maintenance indicated that the manufacturing sector experienced greater complexities in *guanxi* building than the other three industries, and could not be served by any single method. These complications were due to the fact that the manufacturing industry demanded more extensive and intensive interactions with the Chinese in order to have smooth business operations.

"Extensiveness" was put in terms of the scope of *guanxihu*. This was reflected in the research findings on the section of "*Guanxi* Networking". More Chinese entities were required to constitute the ideal *guanxi* network of manufacturing industry, such as the Industry Bureau and the Tax Bureau. The manufacturing industry had more complex operations than the other three sectors in that it encompassed importing, manufacturing, exporting and/or marketing. With its increased scope of operations, there was a demand for greater co-operation from the Chinese entities which could only be secured through intensive interactions and good *guanxi* with them. Consequently, no single means had the potency to cater to these complicated needs. A combination of all the methods outlined above had to be employed to handle the *guanxi* complexities.

4. Importing industry: Long-term mutual benefits, cultivating personal and trustful relationships, and tendering favors

This group voted for the options of nurturing long-term mutual interests, cultivating personal and trustful relations, and tendering favors in *guanxi* building. Each of the four approaches gained the advocacy of 80-100% of the importing firms.

Their choices were a consequence of their industry nature in China. Building a sales market in China required investors to be stationed at some particular business locations more permanently than the exporting industry. The stability in business locations enabled investors to have perpetual relations with the Chinese business associates. In addition, the industry demanded investors to make a large initial investment (in terms of time, monetary resources and efforts) up-front before a rewarding rate of return could be achieved. Generally, the return would only be realized after a long period of establishment. In light of the long-term commitment, the importing firms had to resort to means which were mutually beneficial to both parties on a continuous base. Giving short-term gains was definitely out of consideration since it would inflate the cost greatly, and was detrimental to the business operations in the long-run. Conversely, nurturing long-term mutual benefits, being personal, building trust and tendering favors were better alternatives to consolidate *guanxi* relations. This was so because importers could satisfy the instrumental requirement of *guanxi* on a long-term base, as well as nourish particularistic ties with the Chinese whom were engaged with investors more firmly.

It was surprising to see that the distinct patterns exhibited in the qualitative analysis were not supported by the quantitative statistical analysis. [Please refer to Table 8.3 on page 166 for detailed statistical results.] The impact of industry type was only significant in three ways of *guanxi* maintenance: offering short-term gains; nurturing long-term mutual benefits; and the collaborative *guanxi* building techniques.



There was a significant relationship between the strategy of offering short-term gains and industry type (Spearman  $r=0.35$ ,  $p=.01$ ). The statistics signified that the tertiary and exporting industries had a greater preference for this strategy, whereas the manufacturing and importing sectors objected to its use. The contradiction between qualitative and quantitative findings in the tertiary industry was primarily due to the large proportion of the opponents to *guanxi* in the manufacturing and importing industries compared to those in the tertiary and importing industries. The manufacturing and importing companies constituted 70.0% of the total opponents, and thereby induced a negative effect on the overall relationship.

As for the long-term approach, the manufacturing and importing industries had a greater inclination for this strategy than the tertiary and exporting sectors (Spearman  $r=-0.53$ ,  $p=.01$ ). This was consistent with the results of the qualitative analysis.

A significant relationship was also revealed in the adoption of the collaborative *guanxi* building techniques. Manufacturing and importing industries favored the integrated approach more than the tertiary and exporting sectors (Spearman  $r=-0.54$ ,  $p=.08$ ). This was mainly due to the compatibility of the integrated approach to the long-term business requirement embodied in the manufacturing and importing industries.

### 8.3.5 Type of Institutes Primarily Interacted With

Companies that interacted primarily with government agents seemed to have a greater emphasis on tendering favors than the companies that interacted more with private enterprises. [Please refer to Table 8.2 on page 164 for the figures.] 85.7% of the former group asserted that tendering favors was an important means for *guanxi* development, while only 40% in the latter group made the same assertion.

One reason for this finding is that government agents were in authoritative positions to command resources. Their reciprocated actions would be in the form of government approval for business permits, access to restricted resources or acceleration of the

processing of requests. These actions were salient and crucial to the business operations of investors. Consequently, respondents were willing to do favors for government agents in order to accumulate the wealth of *renqing* which would be at their disposal when they experienced hard times.

In contrast, the reciprocated actions of private enterprises might only have accelerated processing time, information supply or connecting investors to relevant others. These *guanxi* benefits were less detrimental to business operations. Hence, tendering favors to private enterprises were not perceived as important as to government agents whom were expected to reciprocate the favors with more handsome return.

Nevertheless, the relationship between tendering favors and the type of institutes primarily interacted with was not found to be statistically significant ( $p=.15$ ). [Please refer to Table 8.3 on page 166 for detailed statistical results.]

#### **8.4 Conclusions:**

The conventional belief that the offering of short-term gains is essential in cultivating strong *guanxi* relations has been shown to be misleading. According to these research findings, the strategy of offering short-term gains is incapable of nurturing perpetual *guanxi* ties, because it cannot fulfill the utilitarian and particularistic requirements of *guanxi* in the long-run. The enterprises which employ the short-term approach in *guanxi* maintenance tend to have either fluctuating or inferior company performance. Hence, it is concluded that hypothesis 3 is not supported.

These research findings suggest that there are five cardinal dimensions in the domain of *guanxi* relations. They are instrumentalism, trust, personal relationship, reciprocity, and longevity. In light of the five dimensions, it is proposed that nourishing long-term mutual benefits, cultivating personal relationship, nurturing trust, and tendering favors are the "collaborative successful *guanxi* building techniques" which will lead to long-term business success in China. The strength of the integrated approach lies in its

capacity to nurture perpetual instrumental functions and to cultivate strong particularistic ties between investors and Chinese business associates on a long-term base. The integrated approach is mainly embraced by investors who have long-term business commitment in China, due to its compatibility to the long-term business strategy; or by investors who have in-depth experiences in *guanxi* building, since they know that it can maintain *guanxi* in an enduring manner.

In the detailed analyses, significant relationships are established for the following control variables.

**Ownership Type:** Non-Chinese firms have a greater distaste for offering short-term gains because of compliance with the legal and ethical constraints of their parent companies. They are inclined to employ intermediary firms to handle *guanxi* problems, and/or to use the collaborative successful *guanxi* building methods.

**Experience Level:** Experienced investors in China trade have a stronger preference for cultivating personal relations, building trust and tendering favors in *guanxi* than newcomers do.

**Firm Size:** There is a significant relationship between company size and the adoption of the collaborative approach in *guanxi* building. However, it may be an outcome of the confounding effect of experience level.

**Industry Type:** The exporting industry relies heavily on offering short-term gains for *guanxi* building; whereas the importing firms are inclined to use the four collaborative successful *guanxi* building techniques. The tertiary sector emphasizes tendering favors while the manufacturing industry has to employ various *guanxi* techniques to cater to the complex needs of its business operations.

**Type of Institutes Primarily Interacted With:** The companies that primarily interact with government agents should consider tendering favors as their primary way of *guanxi* building due to the valuable return of favors by government agents.

Some inconsistent research results were obtained for the qualitative and quantitative analyses. The contradictions between the two types of analyses may be reflections of the insignificant relationships among various variables; or they may be a consequence of the negative impact induced by small sample size; or they may be the outcome of the confounding effects imposed by other extraneous variables. In light of the limitations on the statistical procedures induced by small sample size, more weight should be given to the qualitative analysis. In addition, further research with greater sample size is recommended to clarify the ambiguous relationships among the different variables in *guanxi* maintenance.

## CHAPTER 9

### RELATIVE IMPORTANCE OF THE FIVE FACTORS IN THE DILEMMA OF *RENQING*

#### Hypothesis 4a

*The cost to the individual in performing the request is the most important factor in the decision-making process when considering a request.*

#### Hypothesis 4b

*The anticipation of reciprocation is the most important factor in the decision-making process when considering a request.*

#### Hypothesis 4c

*The evaluation of an individual's behavior by significant others in the same social network is the most important factor in the decision-making process when considering a request.*

#### Hypothesis 4d

*The guanxi with the requester is the most important factor in the decision-making process when considering a request.*

#### Hypothesis 4e

*The face of the requester is the most important factor in the decision-making process when considering a request.*

As previously identified, tendering favors is one of the successful *guanxi* building techniques. However, investors are often tortured by the dilemma of *renqing* in tendering favors for their Chinese business associates. It is vital to examine the relative importance of the above five factors in the decision making processes of respondents in considering business requests in China.

Respondents were asked to select the factors that were relevant considerations in their decision-making processes in China business, and to rank them in a descending order of importance. That is, the most important factor would receive a ranking of '1', while the least significant factor was ranked '5'. The binomial test of non-parametric analysis was utilized to analyze the ordinal data for the same reasons stipulated in the section on the "Relative Importance of *Guanxi* in Attaining Long-term Business Success in China" (Siegel and Castellan 1988). [Please refer to page 108 for details.] In conducting the binomial test, the selected elements were recoded as "1", and the unchosen items were classified as "0".

### 9.1 General Research Findings:

Table 9.1: Statistics on the Relative Importance of the Five Factors in the Dilemma of *Renqing*

	<u>Mean</u>	<u>Standard Deviation</u>	<u>Significance Level</u>
Cost Consideration	0.84	0.37	0.00 *
Anticipation of Reciprocation	0.47	0.51	1.00
Social Evaluation	0.15	0.37	0.00 *
<i>Guanxi</i> with Requesters	0.42	0.50	0.64
Face of Requesters	0.15	0.37	0.00 *

\*  $p < 0.05$ , two-tailed test.

Based on the binomial test results, three factors were revealed to be statistically significant at  $p < .01$ . They were the cost of individuals to perform requests, the social evaluation of individuals' behavior by significant others and the face of requesters.

However, great disparity was exhibited in the level of importance as the cost consideration was considered much more important than the two latter factors.

The cost element received great support from respondents given that 84.2% confirmed its essentiality in considering China business requests (mean=0.84; standard deviation=0.37). In examining the order given by respondents, twelve of the sixteen respondents (75.0%) who voted for the cost consideration assigned it a ranking of "1". In great contrast, the other two factors had a mean of 0.15 (standard deviation=0.37), with only 15.8% of the respondents selecting them as critical factors for consideration. These statistics fully reflect the weight of cost consideration in the decision-making processes of investors in revealing China business requests. They also indicate that the social evaluation of individuals' behavior and the face of requesters were statistically insignificant in the dilemma of *renqing*. Their impact on the respect was much less than economic cost.

As for the remaining two factors (the anticipation of reciprocation and the *guanxi* relations with requesters), 47.4% and 42.1% of the respondents selected them respectively. The equal support between the proponents and opponents of the two factors yielded non-significant results ( $p=1.0$  and  $p=.64$  respectively).

### 9.1.1 Discussion

The supremacy of economic cost in considering China business requests is deep-rooted in the utilitarian nature of commerce. "Business is business. Economic cost is the rule of the game," asserted most respondents. They reasoned that profit making was the primary objective of doing business. The profit-oriented motive was paramount in any commercial operations across different countries, different cultures and different time horizons. They insisted that economic cost was the prime factor and should take precedence over all other elements, even if it was in China. They alleged that there was no significant difference between the business considerations in China and in other countries. The only deviation was the long-term perspective imposed on cost consideration. Of the

sixteen respondents who cited cost as an important factor, eleven affirmed that it had to be put in a long-term perspective if one desired to have business success in China. This stood in great contrast to the business ideology of Euro-centric cultures.

In Euro-centric business schools, it is taught that each business deal should be perceived as an independent transaction and profit should be made in every business transaction. As Co. 16 representative commented, incurring a loss in any individual transaction is unacceptable, especially in the publicly held companies which are accountable to their share-holders. However, in doing business with China, investors should incorporate a long-term perspective and re-orient themselves to have a different mentality on business deals. Co. 17 interviewee specified that: "There should be no clear-cut transactions in China business, because each business proceeding is a continuation of the *guanxi* relations between investors and their Chinese business associates. A balance in business exchanges implies a termination of *guanxi* relations between the two parties."

In maintaining the *guanxi* relations, investors generally have to suffer immediate losses because tremendous monetary resources need to be spent on *guanxi* building to open up business channels. These initial expenses are sunk costs that are incurred before any profitable business transactions can be secured, since the Chinese do not trust outsiders. Fortunately, these immediate losses in business proceedings would be later rewarded because the Chinese would reciprocate the favors investors had done for them. The business favors tendered to the Chinese today entail handsome rewards in the future, once good *guanxi* ties are established. It is this element of reciprocity that validated the decisions of investors to incur losses in business transactions. As reflected in the remarks of Co. 18 representative: "Immediate losses would generate much more benefits in the end, because they would lead to good *guanxi* which is an essential element in doing business with China." Hence, respondents advised investors to take a long-term perspective such that profit making would only be realized in the long-term balance sheet rather than for each individual business deal.



In conclusion, cost consideration in Euro-centric perspective was not found to be applicable in the Chinese business environment. The short-term evaluation of profit/loss would collapse in the face of the long-term requirement in China business, since it would demand investors to retreat from the China market in the initial stage of development. This would eliminate the chance of investors to enjoy the long-term profit which would be realized after good *guanxi* relations had been established with the Chinese.

## 9.2 Research Findings by Control Variables:

Table 9.2 : The Significance of the Five Factors in the Dilemma of *Renqing* by the Five Control Variables

	Ownership <u>Type</u>	Experience <u>Level</u>	Firm <u>Size</u>	Industry <u>Type</u>	Type of <u>Institute</u>
Economic Cost	0.34	0.28	0.56	0.78	0.25
Social Evaluation	0.10 #	0.99	0.27	0.78	0.76
Reciprocity	0.46	0.95	0.52	0.12	0.70
<i>Guanxi</i> Relations	0.55	0.14	0.63	0.93	0.91
Face of Requesters	0.73	0.25	0.56	0.39	0.25

#  $p < .10$ , two-tailed test.

Among the five control variables, it was revealed that only ownership type had a significant relationship with the factor of social evaluation of individuals' behavior by others (Spearman  $r = -0.36$ ,  $p = .10$ ). This indicates that the Chinese companies had allocated a higher priority to the factor in considering China business requests than non-Chinese firms had. The different emphasis on the factor is mainly derived from the divergence of the two cultures.

In the Confucian world, the relational construction of personhood required individuals to be closely related with one another. Their behavior was constantly under the social evaluation of others in the community. Hence, they would comply with the social

expectations of behavior. A deviation from the social norm would be condemned, and shame would be brought onto the individuals who had committed the deviated behavior as well as onto their significant others. In contrast to the relational orientation in China, the Euro-centric cultures put great emphasis on individuality which treats every individual as a discrete and complete entity that is independent. It follows that individuals should have more autonomy and little interference from others. With the great disparity in the perception of social relations in the two cultures, it is logical that the respondents from non-Chinese firms paid negligible attention to the factor of social evaluation, while those from the Chinese companies regarded it as having greater importance.

However, one might argue that the respondents from both cultural groups were ethnic Chinese, and hence they should have similar perceptions. One explanation may be found in the differentiated exposure of respondents to each culture. It was found that the respondents of Chinese companies were older than the "youngsters" in non-Chinese firms, -- 45.5% of the respondents from Chinese firms were 40-65 years old while 36.4% were 31-40 years of age. In contrast, all respondents in non-Chinese companies were 31-40 years old. The great disparity in age would lead the respondents of the two cultural groups to have different perspectives on business requests. It is suspected that the older respondents are more receptive to the traditional Chinese culture given their Chinese educational background resulting in less exposure to Euro-centric ideologies. However, the "youngsters" in non-Chinese companies had more modern education in Euro-centric cognitive thinking, therefore they were more familiar with Euro-centric organizational philosophy. Since the respondents of Chinese companies were more responsive to the Chinese culture, the factor of social evaluation would constitute a significant element in their decision making processes, while this was not the case for the respondents in non-Chinese firms.

### **9.3 Conclusions:**

According to these research findings, the cost of performing requests is the foremost factor in the decision-making processes of investors when they are in the dilemma of *renqing*. Its supremacy is derived from the utilitarian nature of business. However, the cost consideration should be put in a long-term perspective because profit will only be realized in the long-term balance sheet, rather than for individual business transactions. Hence, it is concluded that hypothesis 4a is supported, while hypotheses 4b, 4c, 4d and 4e are not supported.

## CHAPTER 10

### GUANXI NETWORKING

#### Hypothesis 5

*Other elements being equal, the firms that have right guanxi with Chinese business associates are more successful in enhancing corporate financial performance than firms that do not.*

#### Hypothesis 6

*Other elements being equal, the firms that have strong guanxi with Chinese business associates are more successful in enhancing corporate financial performance than firms that do not.*

The last two hypotheses to be tested concern the relevance and the effectiveness of *guanxi* networks. It is proposed in the literature that building strong *guanxi* relations with the right persons is crucial in the attainment of long-term business success in China. Hypotheses 5 and 6 were designed to evaluate the validity of this proposition.

Owing to the missing data on industry statistics and the non-participation of three interviewees, only thirteen respondents were evaluated in this section.

#### 10.1 The Relevance of *Guanxi* Network (Right *Guanxi* Network)

The relevance of *guanxi* network was defined as the appropriateness of *guanxi* network in enabling respondents to establish successful business operations in China. In detecting the relevance, a comparison base had to be constructed for measurement. The comparison base should be industry-specific, because it was suggested by respondents that

each industry would have very different components of *guanxi* network. In addition, it should be readily accepted by the business practitioners of respective industries. Since no such reference point has been established in the empirical literature, the panel judgment of respondents in the current research was adopted to be the measuring standard. Hence, the testing procedure involved two major steps.

Step 1: Compiling the panel judgment of respondents on ideal *guanxi* network

Respondents were invited to rate a list of Chinese entities on a 10-point scale, in terms of their relative importance in constituting the ideal *guanxi* networks of respective industries. They were instructed to give a rating of "10" if they perceived the entity was significant, or a rating of "1" if perceived as not significant at all. The basic components of ideal *guanxi* networks in respective industries were compiled by incorporating the entities that were consistently rated as important by over 50% of the respondents in the same industry. An "important" entity was defined as an institute which received a rating of 8 or above for its importance in constituting to the ideal *guanxi* network.

As determined by the panel judgment of respondents, the basic components of the ideal *guanxi* network in each specific industry were suggested as follows:

Tertiary Industry:

Information agents and government departments for granting approval

Exporting Industry:

Import/Export Companies and Suppliers

Importing Industry:

Customs Department, Dealers, Import/Export Companies and License Department.

Manufacturing Industry:

Customs Department, Industry Bureau and Import/Export Department, Finance Ministry, License Department, Tax Bureau, Telecommunication Department and Transportation Department

## Step 2: Determining the relevance of *guanxi* network

Respondents were asked to indicate whether they had built *guanxi* relations with the important entities of their perceived ideal *guanxi* network. They were also asked to give reasons on what hindered the *guanxi* development if they had not. All respondents affirmed that they had cultivated *guanxi* relations with the important entities since they were crucial to their business operations.

The next step was to compare the perceived ideal *guanxi* network of each respondent to the panel judgment on the basic components of ideal *guanxi* network in respective industries as listed above. Respondents were then classified as follows:

"**Right *Guanxi* Network**" meant that the *guanxi* network of the respondent covered a large portion of the appropriate authorities in the industry. This was determined when the respondent rated high (a rating of 8 or above) in terms of importance for 67% or more of the suggested ideal *guanxi* network components.

"**Partially Right *Guanxi* Network**" meant that the *guanxi* network of the respondent covered a fair portion of the appropriate authorities in the industry. This was determined when the respondent rated high (a rating of 8 or above) in terms of importance for 33%-66% of the suggested ideal *guanxi* network components.

"**Wrong *Guanxi* Network**" meant that the *guanxi* network of the respondent covered a small portion of the appropriate authorities in the industry. This was determined when the respondent rated high (a rating of 8 or above) in terms of importance for less than 33% of the suggested ideal *guanxi* network components.

### **10.1.1 General Research Findings:**

Among the thirteen respondents, seven managed to have right *guanxi* networks. Three interviewees had cultivated partially right *guanxi* relations and the remaining three were evaluated to have wrong *guanxi* networks.

A correlation was conducted between the company performance of the thirteen respondents and the relevance of their *guanxi* networks. It was shown that there was a significant correlation between the two variables (Spearman  $r=0.59$ ,  $p=.10$ ). This indicates that the companies which had developed right *guanxi* networks tended to have superior company performance to those firms which had not. However, the relationship was not very distinct because counter evidence was found in all three sub-categories of *guanxi* network.

#### 1. Right *Guanxi* Network

Of the seven respondents who claimed to have right *guanxi* networks, only five had company performance that was above the average industry norm for the past three years. The remaining two companies (Companies 3 & 9) suffered unsatisfactory business results.

#### 2. Partially Right *Guanxi* Network

Of the three respondents who were evaluated to have partially right *guanxi* networks, only Company 15 had stable and superior company performance. The other two firms (Companies 7 and 19) had consistently poor financial results.

#### 3. Wrong *Guanxi* Network

The three companies (Companies 5, 6 and 11) which had developed wrong *guanxi* networks had comparatively inferior financial performance for the testing period.

### **10.2 The Effectiveness of *Guanxi* Network (Strong *Guanxi* Network)**

The effectiveness of *guanxi* network was measured in terms of the competency of respondents' *guanxihu* in helping them to solve daily business problems. The measurement was accomplished by conducting a similar rating procedure for the important Chinese entities of respondents. The evaluation was confined to important entities only because they were assessed by respondents as having the greatest impact on their business operations; hence, having good *guanxi* with them was critical to their business success. As

specified in the previous section, an "important" entity was an institute that was rated 8 or above for its importance in constituting to an ideal *guanxi* network. With the rating on the effectiveness of *guanxi* network, respondents were then coded as follows:

"Strong *Guanxi* Network" implied that the relations between respondents and important Chinese entities were strong. This was determined when respondents rated high (a rating of 8 or above) in terms of effectiveness for 67% or more of the important entities.

"Moderate *Guanxi* Network" implied that the relations between respondents and important Chinese entities were moderate. This was determined when respondents rated high (a rating of 8 or above) in terms of effectiveness for 33%-66% of the important entities.

"Weak *Guanxi* Network" implied that the relations between respondents and important Chinese entities were weak. This was determined when the respondents rated high (a rating of 8 or above) in terms of effectiveness for less than 33% of the important entities.

### **10.2.1 General Research Findings:**

There were eight respondents who had achieved strong *guanxi* networks, while four interviewees had moderate *guanxi* ties, and the remaining one was evaluated to have weak *guanxi* relations.

Correlations between the effectiveness of *guanxi* network and company performance revealed that the relationship between the two variables was not significant.

#### **1. Strong *Guanxi* Network**

Of the eight companies with strong *guanxi* networks, only four had attained stable and superior business performance. Three of the remaining respondents had fluctuating company results, with two (Companies 3 and 5) having an upward trend on performance, while the third (Company 9) was sliding downwards. The last company (Company 19) suffered poor performance in the testing period.



## 2. Moderate *Guanxi* Network

Of the four respondents with moderate *guanxi* relations, two (Companies 12 and 13) enjoyed satisfactory performance, while the other two (Companies 7 and 11) had consistently discouraging company results for the past three years.

## 3. Weak *Guanxi* Network

Company 6 was revealed as having a weak *guanxi* network and its performance was below the average industry norm.

The nonsignificant relationship was further confirmed by cross-tabulation statistical analysis ( $p=.62$ ).

### **10.3 Right and Strong *Guanxi* Network**

These analyses on the relevance and the effectiveness of *guanxi* network revealed that no strong and distinct relationships could be established between company performance and the two elements since predictions could not be made regarding company performance by examining the *guanxi* networks of respondents. Such an inconclusive result not only negates the proposition in the literature, it also nullifies the overall importance of *guanxi* in the Chinese business arena.

Yet, this is a misconception based on adopting a simple approach in scrutinizing the complex nature of *guanxi* network. The dilemma would be solved when the two elements (relevance and effectiveness) were combined into one category for examination. That is, the company had to maintain a right and strong *guanxi* network if it desired to have business success in China. With the integration of the two elements, a significant pattern emerged.

Table 10.1: The Relationship between *Guanxi* network and Company Performance

<u>Respondents</u>	<u>Guanxi Network</u>		<u>Company Performance</u>		
	<u>Relevance</u>	<u>Effectiveness</u>	<u>91</u>	<u>92</u>	<u>93</u>
Company 2	Right	Strong	AA	AA	--
Company 3	Right	Strong	BA*	BA	AA
Company 9	Right	Strong	--	AA	BA
Company 16	Right	Strong	--	AA	AA
Company 17	Right	Strong	AA	AA	AA
Company 12	Right	Moderate	AA	AA	AA
Company 13	Right	Moderate	AA	AA	AA
Company 19	Partial	Strong	BA	BA	BA
Company 15	Partial	Strong	AA	AA	AA
Company 7	Partial	Moderate	BA	BA	BA
Company 5	Wrong	Strong	--	BA	A
Company 11	Wrong	Moderate	A	BA	BA
Company 6	Wrong	Weak	A	BA	BA

### 10.3.1 General Research Findings:

#### 1. Right and Strong / Moderate *Guanxi* Network

With the exclusion of Company 9, there were six respondents who had achieved right and strong/moderate *guanxi* networks. Five of them had consistently brilliant company results for the past three years (Companies 2, 12, 13, 16 and 17), and the remaining one had fluctuating performance with an upward trend in 1993 (Company 3).

Company 9 was excluded from the analysis because of the qualitative data given in the interview. During the interview, Co. 9 representative had a hard time in identifying the important *guanxihu* because he had none. In addition, he stressed that it was a waste of time and effort in cultivating *guanxi*. His current strategy was to expand the pool of manufacturers and import/export companies (his two major categories of *guanxihu*) so that he did not have to rely on any particular Chinese business associates. He intentionally created a competition among different manufacturers and import/export

companies, so that he could cut off any one of them when he was not satisfied with their offers, or switch different Chinese business associates in his favor. He perceived that this would give him high flexibility and great bargaining power. However, according to the literature and the research findings on the "Hidden Dimensions of *Guanxi*" deduced earlier, he committed actions that were detrimental to *guanxi* building.

*Guanxi* is a particularistic tie which requires a high level of trust with long-term cultivation. Co. 9 respondent's current strategy would not enable him to have trustful relationships with any particular Chinese business associates, as he was switching around for the cheapest price. Furthermore, he gave very low ratings on the effectiveness of problem solving and trust level of his most important *guanxihu* (he rated both at 5 on a 10-point scale). Hence, it was surprising that he rated so high (a rating of 10) on the general effectiveness of his *guanxi* relations which was contradictory to his ratings on the most important *guanxihu*. On the basis of the qualitative data solicited in the interview, the effectiveness of his *guanxi* was expected to be low with his disagreeable *guanxi* building strategies. Consequently, his exclusion from the analysis is justified based on the questionable validity of his ratings.

## 2. Other status of *guanxi* network

For the respondents who had attained *guanxi* networks other than the status of right and strong/moderate, their performance levels were generally low and fluctuating, with only one exception (Company 15). Company 15 was a small non-Chinese firm which imported beverage manufacturing system into China. The representative of the company was an old-timer who had 11 years of experience in China trade.

The above qualitative analysis was supported by the results of the cross-tabulation statistical analysis. In conducting the statistical procedure, a new dichotomous variable was created. The six companies which had right and strong/moderate *guanxi* networks were coded as "1", while the remaining respondents were classified as "0". The research

findings were encouraging. The correlation between company performance and the integration of the two elements was highly significant (Spearman  $r=0.66$ ,  $p=.02$ ). This implies that companies which had nurtured both right and strong/moderate *guanxi* networks would have a higher probability of attaining superior company performance in China.

This finding provides a valuable message for investors: both the elements of relevance and effectiveness were equally important in building *guanxi* network. Capturing only one of the two factors would not facilitate investors to have brilliant company performance in China. Building weak *guanxi* relations with appropriate authorities was of no use because the government officers would reserve the lucrative business opportunities for their close *guanxihu* who had strong ties with them. Correspondingly, cultivating strong *guanxi* relations with irrelevant authorities was equally ineffective, since Chinese parties could not provide investors with the desirable *guanxi* benefits which were essential for attaining business success in China. Consequently, investors had to satisfy the dual requirement of *guanxi* network and ensure that their *guanxi* relations were both relevant and effective.

In controlling for the five testing factors, significant relationship between company performance and the integration of the two elements was established in three different conditions.

1. There was a positive significant relationship for the mature group of respondents (Spearman  $r=1.0$ ,  $p=.04$ ). As for the old-timers and newcomers, both had nonsignificant relationships ( $p=.24$ ).
2. Statistical analysis was conducted only for small companies. The positive relationship between *guanxi* network and company performance was found to be significant (Spearman  $r=0.64$ ,  $p=.08$ ).
3. The positive relationship between *guanxi* network and company performance was significant for those companies which interacted primarily with government agents

(Spearman  $r=0.73$ ,  $p=.05$ ), but not for their counterparts which interacted with private companies more..

[Please refer to Appendix 5 for detailed statistical results.]

## 10.4 Research Findings by Control Variables:

### 10.4.1 Ownership Type

It seemed that non-Chinese firms were more successful in developing strong/moderate and right *guanxi* networks than the Chinese firms. Support for the proposition could be found in two respects. Firstly, 50% of the Chinese firms had either weak or wrong *guanxi* networks, whereas none of the non-Chinese firms had made any of the two errors in *guanxi* building. Secondly, only 33.3% of the Chinese firms had achieved both right and strong/moderate *guanxi* networks, while 66.7% of the non-Chinese firms had similar achievement in *guanxi* building.

This surprising phenomenon was attributed to two reasons:

1. The attainment of right and strong *guanxi* networks was a direct result of the appropriate methods used in *guanxi* building which was a consequence of industry type. 83.3% of non-Chinese firms were in the manufacturing or importing industry. Both types required investors to have long-term business commitment in China. Hence, the non-Chinese firms tended to acquire the collaborative approach in *guanxi* building which was compatible to the long-term business strategy. The objective of offering long-term mutual benefits was to entangle the long-term gains of Chinese business associates with the business success of respondents. Hence, the two parties were in the same boat in exploiting lucrative business opportunities. Their *guanxihu* would give them unlimited assistance, such as important inside information on who the right decision maker was for *guanxi* development. With the right *guanxi* targets in hand, strong ties could be easily developed under the nourishment of personal and trustful relationships which were sustained by tendering favors.

2. The non-Chinese companies which were expected to be at a more disadvantageous position to develop strong and right *guanxi* networks had employed ethnic Chinese to handle the China market. The four non-Chinese companies with good *guanxi* networks had Chinese representatives who had been in China trade for at least five years. Their in-depth experiences and knowledge would compensate for the possible ignorance of China market on the part of non-Chinese.

Nevertheless, the qualitative analysis was refuted by the statistical analysis which failed to reach significance ( $p=.78$ ). This indicates that the chance for establishing a significant correlation between ownership type and the integration of the two elements was remote.

#### 10.4.2 Experience Level in China Business

It was surprising to find that no specific pattern of *guanxi* networking was found among the three different experience groups which had similar achievement in *guanxi* development. This relationship was confirmed by the cross-tabulation statistical analysis ( $p=.66$ ).

One would expect that newcomers might have problems in developing strong and right *guanxi* networks due to their inexperience. However, the weakness of newcomers was compensated for by the in-depth experience of company executives who were the "founders" of the *guanxi* relations with the Chinese. These executives were still holding authoritative positions in the companies, and continued to maintain good *guanxi* ties with the Chinese in spite of the inexperience of newcomers.

#### 10.4.3 Firm Size

There was a significant relationship between firm size and the development of good *guanxi* network. All of the large and medium firms had cultivated strong/moderate and right *guanxi* networks, whereas only 14.3% of the small firms had a similar achievement in

*guanxi* development. The reason for this discrepancy lay in the business commitment of companies as reflected by firm size.

The large and medium companies had greater financial resources for long-term business and *guanxi* development. They could enhance their value to the Chinese by creating many job opportunities for the locals or making donations to the economic development of the regions. From the perspective of the Chinese, the large and medium firms made a greater commitment to China since they had invested more in local regions. Consequently, the Chinese were more willing to have good *guanxi* relations with them than with small firms which might be perceived by the Chinese as "grab-and-go" companies that intended to take advantage of them rather than contribute to the country.

This finding was confirmed by the cross-tabulation statistical analysis (Spearman  $r=0.61$ ,  $p=.05$ ). This indicates that the large and medium companies had a greater chance of cultivating right and strong/moderate *guanxi* networks than small companies.

#### 10.4.4 Industry Type

There seemed to be a correlation between industry type and the attainment of good *guanxi* network. More companies in the manufacturing industry (75%) and importing industry (60%) were able to develop strong/moderate and right *guanxi* networks than firms in the tertiary and exporting industries (0% for both groups). This might due to the stability of business locations. As discussed earlier, the targets of *guanxi* development for the manufacturing and importing groups were anchored at a few investment locations. However, the exporting industry had to source products from many different areas in China. It was more difficult for them to develop perpetual and strong *guanxi* ties with the Chinese business associates in each investment location than their counterparts in the manufacturing and importing industries. However, this was not supported by the statistical analysis ( $p=.24$ ).

#### 10.4.4 Type of Institutes Primarily Interacted With

Those firms that primarily interacted with government agents had developed better *guanxi* networks than companies which interacted more with private enterprises. 71.4% of the former group had attained right and strong/moderate *guanxi* networks, whereas only 20.0% of the latter group had a similar achievement in *guanxi* development. To account for this disparity, one has to focus on the *guanxi* networks of government agents versus those of private enterprises.

Since China is largely under government control, it is conceivable that the *guanxi* networks of government agents were generally greater than those of private enterprises, in terms of scale and importance. This was because people were willing to be on good terms with government agents, in order to avoid any trouble in their business operations. These people would also welcome having *guanxi* with respondents who were referred by government officials, either because of their trust in the officials or having to give face to the government referrals. Hence, the large *guanxi* networks of government agents formed a readily accessible *guanxi* base for respondents. Furthermore, the government agents had connections with other government officials who were the *guanxi* targets of respondents. This would make it easier for respondents to extend their *guanxi* networks. Consequently, having *guanxi* with government officers would greatly expand the *guanxi* pool of respondents and shorten the distance between respondents and their *guanxi* targets. These two advantages might not be offered to respondents who were associated with private enterprises. Unfortunately, this pattern was not confirmed by the statistical analysis ( $p=.14$ ).

### 10.5 **Pattern of *Guanxi* Network**

#### *Guanxi* with the government agents are primary

All respondents agreed that it was of utmost importance to have good *guanxi* relations with government agents because China was still largely controlled by the



Communist government. Having problems with government agents would be detrimental to business operations because they could create problems if there were minor disagreements. The worst outcome would be a suspension of one's operating license. Hence, government agents were perceived by respondents as the paramount group of *guanxi* targets.

#### Guanxi targets are industry-specific

In regards to which level of government hierarchy one should build *guanxi*, 40% of the respondents suggested that it was industry-specific and depended on the scale of operations and industry type. Large scale of operations or products of high significance such as telecommunication should have *guanxi* with both central and local governments. This was because they were under the priority development of the National government, and would have substantial economic impact on the country. Hence, they attracted much attention from both levels of government. Conversely, the business of small scale or of insignificance should concentrate on building *guanxi* with local government.

#### Small *guanxi* network is preferred

In general, respondents preferred a small network but strong *guanxi* ties to a dispersed network with weak *guanxi* relations. The preference was influenced by the importance of strong *guanxi* relations and resource constraints for *guanxi* development. Building weak *guanxi* was of no use because government officials would reserve the precious business opportunities for those who had strong *guanxi* ties with them. In addition, building strong *guanxi* ties required a lot of time, effort and monetary resources which would be unaffordable, if companies targeted to cultivate strong *guanxi* relations with both local and central governments. In making the choice, local government was preferred. With the small sample in the research, only one respondent (Company 14)

claimed that the *guanxi* with central government was important to the business operations of her banking institute.

#### Assign higher priority to local government

The preference for local government stemmed from its proximity to the business operations of investors. It was the local government that gave operation permits, processed daily requests and executed the laws in local regions. Having good *guanxi* with the central government did not help much because of the decentralization of power from central to provinces and the dominant regionalism in China.

#### Guanxi with the right decision maker is the key

In considering who the right *guanxi* target was in local government, 75% of the respondents asserted that one must have *guanxi* with the final decision maker. Generally, it would be the person holding the highest position in an entity. However, 35% of the respondents pointed out that the right decision maker might not be the top person given that they did not have time to review all cases in the region. They suggested that the personal assistant of the top person would be a more feasible *guanxi* target since it would be too difficult for them to be associated with the top decision maker. Respondents explained that the personal assistant was influential to their business operations because the top person often relied on the opinion of the personal assistant for decision making. If they could win the personal assistant to their side, they would have similar benefits as if they had *guanxi* with the top decision maker.

Unexpectedly, 15% of the respondents suggested it was equally important to have *guanxi* with the staff at lower levels for two reasons:

1. They were the ones who actually processed requests. Having good *guanxi* with them would definitely shorten the processing time.

2. The political struggle and personnel changes were severe in China. Nobody could predict who would be in power in the future. Hence, the staff at a lower level today might gain authority in the future and it would be too late to build *guanxi* with them at that time. Hence, cultivating good relations with staff at lower level (such as janitors) was perceived by respondents as a type of social investment which might be of great use in the future.

## **10.6 Conclusions:**

According to the research findings, Hypothesis 5 and 6 are partially supported. The relationship between the status of *guanxi* network and company performance is more significant when the relevance and the effectiveness of *guanxi* network are combined into one element. This means that:

Other elements being equal, the firms which have right and strong *guanxi* with the Chinese local parties are more successful in enhancing corporate financial performance than firms which do not.

**Ownership Type:** In line with the research findings on the "Ways of *Guanxi* Maintenance", non-Chinese firms which have employed Chinese representatives who use collaborative successful *guanxi* building techniques have a higher chance of developing strong and right *guanxi* networks. The adoption of the integrated approach is also consistent with the long-term business requirement embodied in the manufacturing and importing industries in which non-Chinese firms are invested.

**Firm Size:** Large and medium firms have a better chance of developing strong and right *guanxi* networks because of their greater investment in local regions. The contribution can be in the form of creating many job opportunities or upgrading the economic development of the regions.

**Industry Type:** Industries that anchored at stable business locations have a better chance of developing strong and right *guanxi* networks, such as the importing and manufacturing sectors, since the stability allows companies to have perpetual *guanxi* building.

**Type of Institutes Primarily Interacted With:** The firms that primarily interact with government agents have the advantage of developing strong and right *guanxi* networks, because the large *guanxi* networks of government agents form an accessible base for the *guanxi* development of investors .

***Guanxi* Networking:** Government agents are the primary group for *guanxi* development by investors. Owing to resource constraints and the benefits of strong *guanxi* ties, a small network with strong *guanxi* ties is preferred to a dispersed network of weak *guanxi* relations. The right decision maker of the entity or his/her personal assistant is the most desirable *guanxihu* who may bring tremendous *guanxi* benefits to the business operations of investors.

## CHAPTER 11

### CONCLUSIONS AND MANAGERIAL IMPLICATIONS

#### 11.1 Summary and Managerial Implications

*Guanxi* has been cited in the literature as the foremost success factor in doing business with China. It is also highly regarded by the business practitioners of China trade as being important for attaining long-term business success. In light of its supremacy in the China business arena, this research study sought to assess the impact of *guanxi* on company performance, and to formulate a strategy which would enhance business success through the practice of *guanxi*. Surprisingly, the omnipotence of *guanxi* was not supported by the research findings, and new insights on the specificity of the *guanxi* construct were unveiled.

Contradicting conventional belief in the prominence of *guanxi*, the element is revealed only to be a necessary condition for entering the China market, but insufficient for ensuring long-term business success for investors. This is reflected by the assessment of its relative importance in long-term goal attainment. When compared to other success factors, *guanxi* is considered to have greater importance in the preliminary stage of business establishment to explore new business opportunities and to open up channels for investors. However, its significance diminishes when investors are well established in the market. At the mature stage of business establishment, technical competitiveness assumes a greater significance in helping investors succeed in the business battlefield, as keen competition is set forth by competitors who have similar achievements in *guanxi* building.

This above research finding has an important message for non-Chinese investors who may either neglect the importance of *guanxi*, or put undue emphasis on the element. They are advised to give equal attention to *guanxi* and technical competence, since both are

indispensable factors in the China business exploration. The former element enables non-Chinese investors to gain a foothold in the market, while the latter factor allows them to compete on the business platform. Ignoring either one will obstruct their long-term business goal attainment.

In formulating a strategy of *guanxi* management, one starts with the process of *guanxi* establishment. Although the relative importance between ascribed and achieved *guanxi* bases was not tested in the current research study, it was revealed that the latter approach functions equally well in establishing *guanxi* relations for non-Chinese investors, since all the respondents originated their *guanxi* ties in achieved *guanxi* base.

Achieved *guanxi* base can be constructed by group identification and altercasting. Since non-Chinese investors are newcomers to the Chinese society, they do not have any commonality for shared identification with the locals. Hence, altercasting through intermediaries can be conceived of as the initial step in establishing *guanxi* connections. There are two means of altercasting: formal working channels and informal referrals. Both aim at transforming the out-group identity of non-Chinese investors to in-group status. Non-Chinese investors are advised to take both means in establishing *guanxi* relations. They can participate in the annual trade shows and business exhibitions of China; or they can hire business consulting firms which will help them build *guanxi* networks. Non-Chinese investors also have opportunities to utilize informal referrals if they have friends/partners who are insiders of the Chinese business community. These individuals serve the intermediary role by connecting non-Chinese investors with the right Chinese business associates.

Nevertheless, it is not the end of the building process. It is suggested that altercasting has to be followed by group identification, in order to consolidate the *guanxi* relations between non-Chinese investors and the Chinese. Non-Chinese investors should aim at entangling themselves into the *guanxi* networks of the Chinese if they desire business success. This would require them to have personal presence in China so that

more common attributes for shared identification can be cultivated through continuous interaction.

There is a conventional belief that *guanxi* relations have to be cherished by offering short-term gains to the Chinese. Yet, this notion is rejected by the research findings for hypothesis 3. It was found that offering short-term gains is a strategy which is essential in the initial stage of *guanxi* building in order to gain a chance for *guanxi* establishment. However, it is inadequate in nurturing stable and strong *guanxi* ties, due to its incapability to fulfill the perpetual instrumental function of *guanxi* relations and to nourish particularistic ties with the Chinese. Alternatively, it is proposed that nurturing long-term mutual benefits, cultivating personal relationship, building trust and tendering favors are the four collaborative successful *guanxi* building techniques which can cultivate strong *guanxi* relations. The integrated approach is underlined by the five fundamental dimensions of *guanxi*. They are instrumentalism, personal relations, trust, reciprocity and longevity. The complementarity of these five dimensions is fully reflected in the four recommended strategies which have to function in collaboration in order to satisfy the dual requirement of *guanxi* relations. On one hand, they entangle the long-term utilitarian gains of the Chinese with the business performance of investors; on the other hand, they cultivate personal relationships with the Chinese which are irreplaceable by competitors. It was discovered that the collaborative approach is mostly embraced by investors who have in-depth experiences and long-term business commitment in the China market. The integrated approach was found to be effective in building good *guanxi* ties which are highly correlated with superior company performance.

Nevertheless, the above presumption is valid only when the *guanxi* ties built are both relevant and effective. The essentiality of the two qualifiers is reflected in the testing of hypotheses 5 and 6. Building weak *guanxi* relations with appropriate authorities or cultivating strong *guanxi* ties with irrelevant parties are equally deficient, since they cannot

elicit the desirable *guanxi* benefits embodied in good *guanxi* relations which should be both relevant and strong.

Consequently, non-Chinese investors are advised to take two steps in building *guanxi* networks. Step one is the identification of relevant *guanxi* targets. Relevant targets can be found at two different levels. The first level is the type of Chinese entities which are required for the business operations of non-Chinese investors. The selection is industry-specific, since each industry will have different components of its ideal *guanxi* network. It is proposed that local government agents are the primary group for *guanxi* building because of their detrimental and immediate impact on the business operations of non-Chinese investors.

The second level is with whom non-Chinese investors should build *guanxi* in the identified Chinese entities. This relates to the question of who the right decision makers are in selected institutes. This is of primary importance in *guanxi* building because they are the ones who command resources. It is suggested that the top persons and their personal assistants can give similar *guanxi* benefits, and thus both can be the *guanxi* targets of non-Chinese investors. After identification, the second step is the approach of *guanxi* maintenance. Non-Chinese investors are recommended to adopt the four collaborative *guanxi* building techniques so that perpetual and strong *guanxi* ties can be cultivated.

In *guanxi* maintenance, non-Chinese investors are often in the dilemma of *renqing* when confronted with the requests of Chinese business associates. Owing to the utilitarian nature of business, the cost consideration will take a paramount position in the decision-making process. However, non-Chinese investors are advised to incorporate a long-term perspective in their mindscape when considering China business requests. The short-term evaluation of profit/loss in the business philosophy of Euro-centric cultures will collapse in the face of the long-term requirement of China business. Profit-making will only be realized in the long-term balance sheet, rather than for individual business transactions. This is because the favors tendered today will incur immediate loss to non-Chinese



investors, but they will provide handsome rewards in future since the Chinese have a great tendency to reciprocate. The reciprocation entails an accumulation of *renqing* which will be at the disposal of non-Chinese investors when they are in hard times in future.

In conclusion, *guanxi* is an essential factor that non-Chinese investors need to attain in doing business with China, but its significance is secondary to technical competence in achieving long-term business success. The best illustration is found in the incident of Venturetech, which is a state enterprise in China and is staffed by the 'princelings' (siblings of China's statesmen). Though it is backed by powerful *guanxi* relations, it came to its downfall in November 1994, caused by the low product quality of the state enterprise. (Sender 1995) However, this is not to totally negate the importance of *guanxi* in the China business arena, but to specify that the element is not as omnipotent as rumors have indicated. Its importance lies in the preliminary role of establishing investors in the market. Non-Chinese investors will definitely fail if they have not captured the cardinal element in their business expedition.

## 11.2 Control Factors

Five different control factors were used to dissect the domain of *guanxi*. It was revealed that each control factor has a unique effect on the management of *guanxi*.

**Ownership Type:** It was found that ownership type has induced two major effects on *guanxi* management. Firstly, non-Chinese investors have been prevented by the legislation and ethical constraints of their parent countries from engaging in particular *guanxi* building methods, such as questionable payment. Secondly, the behavior of non-Chinese companies is governed by the Euro-centric organizational cultures in which universality is firmly established. Hence, non-Chinese companies were found to assign a lower ranking order to the importance of *guanxi* in business goal attainment. They tend to adhere to formal working channels for *guanxi* establishment, and express a distaste for the strategy of offering short-term gains in *guanxi* building. The evidence indicates that non-Chinese

companies are inclined to employ the collaborative approach and thereby have a greater chance of cultivating right and strong/moderate *guanxi* networks. However, the relationship may be diluted by another control variable: industry type.

**Industry Type:** Industry type emerges as the most influential variable on *guanxi* management. Its significance lies in its capability to shape *guanxi* patterns required for specific industries. For industries which are constantly pressed for expanding *guanxi* networks, such as tertiary and exporting sectors, there is a tendency to allocate a higher priority to *guanxi* in business establishment. With the high mobility of business locations, the two industries find it difficult to employ the four collaborative *guanxi* building techniques which are long-term strategies. Thus, they resort to other methodologies for *guanxi* building. The tertiary industry takes tendering favors and the exporting industry uses short-term gains to 'buy' *guanxi*. As a result, the two industries have a lower chance of building right and strong/moderate *guanxi* networks.

In contrast, the manufacturing and importing industries have superior achievement in *guanxi* management, owing to their long-term business commitment. The stability of business locations bestows dual advantages. On one hand, it enables the investors of the two sectors to develop stabilized business channels so that they perceive a lower priority in *guanxi*. On the other hand, it allows them to employ the integrated approach in *guanxi* maintenance, thus giving them a higher chance of attaining right and strong/moderate *guanxi* networks.

It is noteworthy to specify that the majority of non-Chinese companies in the research sample are in the manufacturing and importing industries. This may give a misconception that non-Chinese companies are more successful in cultivating good *guanxi* ties whereas it is more of a consequence of the industry they are in.

**Experience Level in China Business:** According to the research findings, the experience level of investors in China business has significant impact on *guanxi* management. It was found that the importance of *guanxi* decreases as one moves along the

learning curve. The old-timers have undergone a change in mentality after their prolonged experiences in China trade. Hence, they perceive technical competence as more important than *guanxi* in attaining long-term business success, and they tend to adopt the collaborative approach in *guanxi* building. However, such a change has not been experienced by the mature investors and newcomers who are in the initial and developing stages of the learning curve. Thus, they have assigned a higher priority to *guanxi* and have not captured the essence of cultivating personal and trustful relationships in *guanxi* ties.

The lower priority to *guanxi* given by old-timers is also influenced by the market conditions in late 1970's. The old-timers relied on informal referrals for *guanxi* establishment because of their ignorance of the China market. This stood in great contrast to the newcomers who have the advantage of using formal working channels for *guanxi* building, since more business mechanisms have been set up in China to help them in business establishment.

**Firm Size:** Firm size is an indication of the amount of resources allocated by investors for *guanxi* building. There was a significant correlation between firm size and the attainment of right and strong/moderate *guanxi* networks. The success of *guanxi* building by large and medium companies is a direct result of their contributions to local regions. It is most salient for large corporations. Their contributions are in the form of creating tremendous job opportunities for the locals, or making donations to the economic development of the regions. Both will greatly enhance the value of investors to the Chinese, who are more willing to seek *guanxi* with them. Hence, large enterprises do not have to make any special efforts for *guanxi* building, and thus they perceive a lower priority in *guanxi*.

In contrast, the small companies allocated a higher priority to *guanxi* in business establishment because of their desperate desire for the element. Their negligible economic impact on local regions protects them from the close supervision of top government officials, and they have more space for *guanxi* functioning in their business operations.

Yet, their achievement in *guanxi* building is lower than their counterparts in large-scale enterprises in large part due to their little economic contribution to the country. Hence, they have a hard time in *guanxi* building.

**Type of Institutes Primarily Interacted With:** It was found that the investors who have primarily interacted with government agents preferred the method of tendering favors in *guanxi* building. They also have a greater chance of cultivating right and strong/moderate *guanxi* networks. This result may be attributed to the great *guanxi* networks of government agents, both in terms of scale and importance. Since China is still largely under the control of the government, people like to build *guanxi* with government agents for the associated *guanxi* benefits. Hence, the large *guanxi* networks of government agents form an accessible base for the *guanxi* development of investors. In addition, the inclusion of other government officers in the *guanxi* networks of government agents shorten the proximity between investors and their targeted *guanxihu*. Hence, the investors who primarily interact with government agents have greater achievement in *guanxi* building.

### 11.3 Limitations and Recommendations

The research study is a preliminary attempt to understand the complications of *guanxi* management. Due to its exploratory nature, the study also sought to identify directions for future research on the complex *guanxi* construct.

It should be acknowledged that the current research study has many of the limitations commonly found in exploratory studies. The greatest limitation is small sample size which limits the external validity and generalizability of the research findings. Due to time and resources constraints, only nineteen respondents were recruited for personal interviews. Further research with a larger sample is highly recommended to confirm these research findings.

As stated earlier, all respondents were ethnic Chinese who had been hired by both Chinese and non-Chinese companies to handle the China market. This may have introduced a sampling bias in that only reflects the mentality of ethnic Chinese (Hong Kong) on the *guanxi* construct. Further research which includes Caucasians is needed to examine possible contrasts between these two ethnic groups on *guanxi* management.

Subjectivity may be another limitation in an exploratory qualitative research study of this kind. Throughout the research process, personal bias may have been present during the interviews, data analysis and interpretation. Hence, further studies employing quantitative methodologies are recommended to substantiate the qualitative findings of this study.

In the current research study, it is suspected that multicollinearity may exist among three control variables: ownership type, industry type and experience level in China business. Due to the small sample size, no conclusive comments can be made on the confounding relationships since they cannot be tested with the current research sample. However, it does suggest some enlightening insights on the significance of the three variables in the *guanxi* construct. Further research along this line is advised to confirm their impact on *guanxi* management.

This study is an initial attempt to explore the specificity of *guanxi*. Although the research is small and preliminary, it is hoped that this study will enhance the understanding of *guanxi*, and provoke new directions for future exploration of the *guanxi* construct.

**APPENDIX 1: COMPARATIVE FINDINGS ON *RENQING* OBLIGATIONS  
BETWEEN KINSHIP AND FRIENDS**

(Adapted from G.C. Chu and Y. Ju. The Great Wall in Ruins. Albany: State University of New York Press, 1993.)

<b>Nature of Favors Requested</b>	<b>To Relative</b>	<b>To Friend</b>
<b>If asked to lend money</b>		
would lend	61.8%	43.9%
would not lend	2.5%	4.6%
would depend	35.7%	51.8%
<b>If asked to help</b>		
would help	70.9%	64.3%
would not help	8.0%	11.4%
would depend	21.1%	24.3%

## APPENDIX 2: INTERVIEW PROTOCOL

### Background Information

1. What is your position title in the China business operation?
2. What kind of ownership does your company have in China?
3. What type of management personnel does your company have in China?

### General Information

1. What type of industry has your company invested in China?
2. Where does your company invest in China?
3. How long has your company been doing business with China?  
Has your company ever invested in other Asian countries before entering into China?
4. What were the percentages of China revenue compared to worldwide revenue for 1991, 1992 & 1993  
*(Refer to appendix for the scale line.)*
5. How many employees did your China operations have for 1991, 1992 & 1993?
6. With what type of institute do you primarily interact in China?

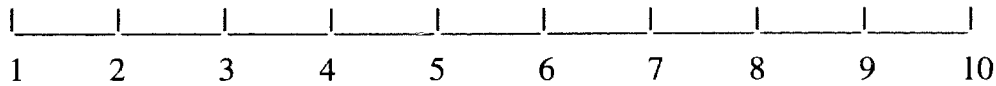
### Company Performance

1. How would you rate your company performance as compared to the industry norm in China?
2. Are you satisfied with the company performance in China? If not, why?
3. Do you agree that business success is more easily obtained in China than in other Asian countries?  
*(Please refer to appendix for the scale line for growth rate.)*
4. How would you rate your corporate company performance as compared to the industry norm worldwide?

### Macro Level of *Guanxi*

1. What do you consider to be the most important factors in achieving business success in China?  
*(Please refer to appendix for the checklist.)*
2. Do you agree that *guanxi* in business is defined as relations cultivated with Chinese business associates based on mutual interests, together with a heavy emphasis on obligations and instrumentalism?
3. How is *guanxi* in China different from business relations in your home country?

4. How would you rate *guanxi* as an important factor for attaining business success in China on a 10-point scale?



Never Important

Always Important

5. Do you feel that it is important to enlarge one's *guanxi* network in order to have business success in China? Why?

### **Micro Level of *Guanxi***

#### **Group Identification and Altercasting**

1. How did you/your company first establish business relations in China?  
*(The following three questions will presented in questionnaire format.)*
2. What percentage of your business associates are:
  - \_\_\_% Relatives
  - \_\_\_% Clan
  - \_\_\_% Friends
  - \_\_\_% Unrelated persons introduced to you through others
3. Please rank the following groups in terms of the priority of seeking help from them when you encounter business problems in China, with "1" as the first one to seek help from and "4" as the last one.
  - \_\_\_ Relatives
  - \_\_\_ Clan
  - \_\_\_ Friends
  - \_\_\_ Unrelated persons introduced to you through others
4. Please rank the following groups in terms of the effectiveness in solving your business problems in China, with "1" as the most effective and "4" as the least effective.
  - \_\_\_ Relatives
  - \_\_\_ Clan
  - \_\_\_ Friends
  - \_\_\_ Unrelated persons introduced to you through others

(Business associates are defined as someone who has business relations with you, or someone who does not have direct business relations with you, but has great influence on those who do.)

(Unrelated persons are defined as individuals who have no kinship nor share any personal relations with you, such as friends and clan.)



### Right and Strong Guanxi

5. For which Chinese business entities is building *guanxi* relations of utmost importance in achieving business success in China? (Ideal *guanxi* network)

(Please refer to appendix for the checklist.)

- What kind of benefits would you gain from having good *guanxi* with them?
- Have you already built good *guanxi* with them? (Refer to appendix for ideal *guanxi* checklist.)
- If not, what hinders you to build *guanxi* with them?
- How effective are the Chinese entities with which you have already built *guanxi* in helping you to solve business problems? (Actual *guanxi* network)

(Please refer to appendix for the checklist.)

6. Please identify the most important entity that has helped you to gain business success in China.

- How did you start building *guanxi* with the right targeted person (the one who is most helpful to you) in the entity?

7. What kind of interactions do you have with the targeted person in the entity?

- Is it mostly in business or social settings? If it is mostly in social setting, then why?
- How frequently do you interact with the targeted person in each setting?

\_\_\_ Business setting

\_\_\_ Social setting

- Will you continue the close relationship with him/her when he/she resigns from the entity?

8. Please evaluate your *guanxi* relation with the targeted person of the selected entity on the following aspects.

- How personal is the *guanxi* relation between you and the targeted person?

Always Personal      10 9 8 7 6 5 4 3 2 1      Never Personal

- To what extent do you trust the targeted person?

Always trust him/her    10 9 8 7 6 5 4 3 2 1    Never trust him/her

- How effective is the targeted person in helping you to solve business problems?

Always Effective      10 9 8 7 6 5 4 3 2 1      Never Effective

### ***Guanxi Maintenance***

#### Social Interaction

1. How do you maintain the *guanxi* relation with the targeted person of selected entity?
2. What kind of considerations do you take in proposing requests to Chinese business associates?

3. How much money would you advise someone to spend on socializing with Chinese business associates, in order to have good *guanxi* relations?

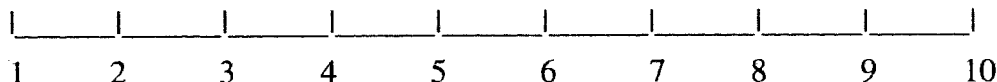
\_\_ % of annual sales volume in China

- Will the expenses on *guanxi* building be increased over years?

#### Dependability

4. How important is it to be reliable in doing business in China?

(Reliable relations is one that the two individuals have trust with each other. They can always count on the other party for help in case of seeking assistance for problem solving.)



Never Important

Always Important

5. How did you establish reliability in doing business with China?

#### Dilemma of *Renqing*

6. Which of the following factors will you regard as most important in considering a China business request?

- a) evaluation of your actions by significant others in the same social network
- b) cost of granting the request
- c) anticipation of reciprocity
- d) *guanxi* relations with the Chinese business associate who makes the request
- e) face

#### Reciprocity

7. Is it important to reciprocate the gifts/favors/banquets of Chinese business associates?

#### Face

8. Is "face" an important consideration in doing business with local nationals of China?

9. What are the situations for losing or saving face in China?

#### **Summary**

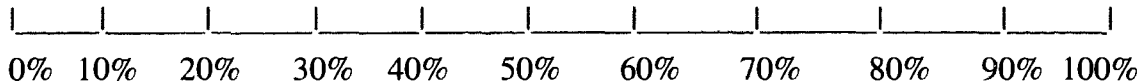
1. What advice would you give to someone who has just entered into the China market and would like to build *guanxi* for business operations?

## Appendix of Interview Protocol

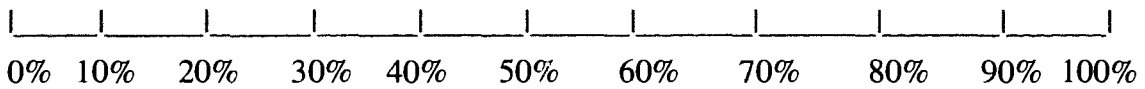
### Company Performance

Please indicate on the scale below the approximate percentage of revenue from your Chinese operation as compared to the revenue of your company worldwide for the past three years.

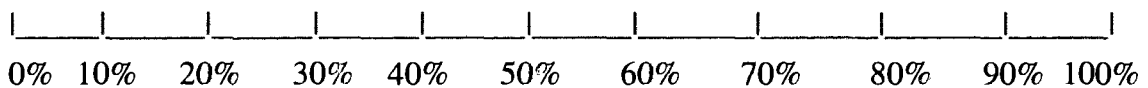
**1991 :**



**1992 :**

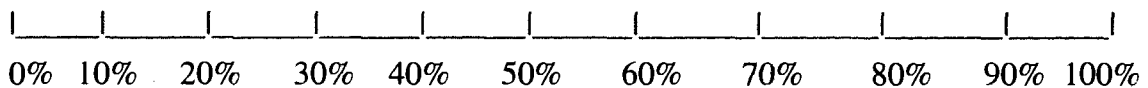


**1993 :**

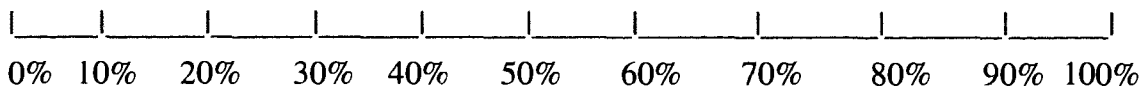


Please indicate on the scale below the approximate growth rate of your company in China in terms of **annual sales** for the past three years.

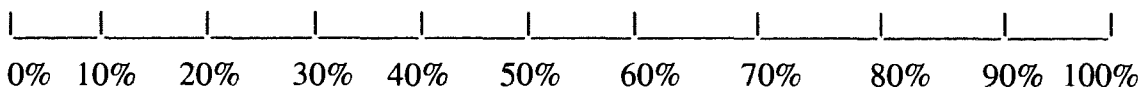
**1991 :**



**1992 :**

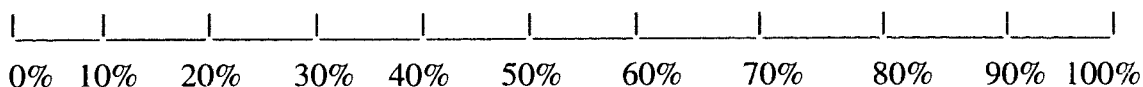


**1993 :**

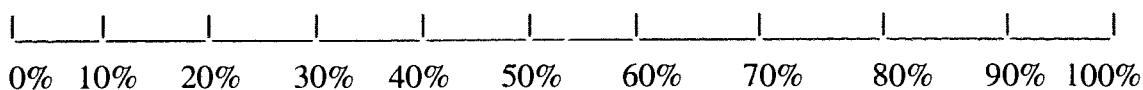


Please indicate on the scale below the approximate growth rate of your company in China in terms of **net income before tax** for the past three years.

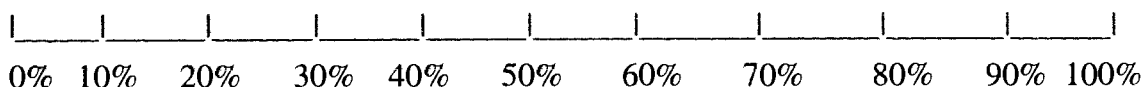
**1991 :**



**1992 :**



**1993 :**



Relative Importance of *Guanxi* in Attaining Business Success in China

Please select **five** items from the following list as the most important factors in achieving business success in China, and rank them in descending order of importance with "1" as the most important and "5" as less important.

- \_\_\_ Choosing right business location
- \_\_\_ Choosing right entry strategy
- \_\_\_ Complementarity of goals between you and Chinese parties
- \_\_\_ Competitive price
- \_\_\_ Familiarity with Chinese business negotiating style
- \_\_\_ Flexibility in business operations in China
- \_\_\_ *Guanxi* (Connections) relations with Chinese local parties
- \_\_\_ Long-term business commitment in China
- \_\_\_ Management control in business operations in China
- \_\_\_ Product differentiation / quality
- \_\_\_ Understanding China's policy and legislation

Guanxi Network

Ideal guanxi network: Please indicate the importance of the following entities in achieving business success in China.

Entities	Is the Relation Important?										Not Applicable
	Never Important										
Banks	1	2	3	4	5	6	7	8	9	10	N/A
Customs Department	1	2	3	4	5	6	7	8	9	10	N/A
Dealers	1	2	3	4	5	6	7	8	9	10	N/A
Finance Ministry	1	2	3	4	5	6	7	8	9	10	N/A
Gas Supplier	1	2	3	4	5	6	7	8	9	10	N/A
Hydro/Electricity Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Imports & Exports Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Industry Bureau	1	2	3	4	5	6	7	8	9	10	N/A
License Department	1	2	3	4	5	6	7	8	9	10	N/A
Manufacturers	1	2	3	4	5	6	7	8	9	10	N/A
Personnel Department	1	2	3	4	5	6	7	8	9	10	N/A
Police Department	1	2	3	4	5	6	7	8	9	10	N/A
Price Department	1	2	3	4	5	6	7	8	9	10	N/A
Suppliers	1	2	3	4	5	6	7	8	9	10	N/A
Tax Bureau	1	2	3	4	5	6	7	8	9	10	N/A
Telecommunication Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Transportation Department	1	2	3	4	5	6	7	8	9	10	N/A
Others : (please specify)											
_____	1	2	3	4	5	6	7	8	9	10	N/A
_____	1	2	3	4	5	6	7	8	9	10	N/A

Actual guanxi network: Please evaluate only the entities that you have already built guanxi with. How effective have *guanxi* relations with the following entities been in helping you to solve business problems in China?

Entities	How effective are your relations?										Not Applicable
	Never Effective										
Banks	1	2	3	4	5	6	7	8	9	10	N/A
Customs Department	1	2	3	4	5	6	7	8	9	10	N/A
Dealers	1	2	3	4	5	6	7	8	9	10	N/A
Finance Ministry	1	2	3	4	5	6	7	8	9	10	N/A
Gas Supplier	1	2	3	4	5	6	7	8	9	10	N/A
Hydro/Electricity Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Imports & Exports Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Industry Bureau	1	2	3	4	5	6	7	8	9	10	N/A
License Department	1	2	3	4	5	6	7	8	9	10	N/A
Manufacturers	1	2	3	4	5	6	7	8	9	10	N/A
Personnel Department	1	2	3	4	5	6	7	8	9	10	N/A
Police Department	1	2	3	4	5	6	7	8	9	10	N/A
Price Department	1	2	3	4	5	6	7	8	9	10	N/A
Suppliers	1	2	3	4	5	6	7	8	9	10	N/A
Tax Bureau	1	2	3	4	5	6	7	8	9	10	N/A
Telecommunication Depart.	1	2	3	4	5	6	7	8	9	10	N/A
Transportation Department	1	2	3	4	5	6	7	8	9	10	N/A
Others : (please specify)											
_____	1	2	3	4	5	6	7	8	9	10	N/A
_____	1	2	3	4	5	6	7	8	9	10	N/A

Personal Information of Respondents

1. Please indicate below the age group you are in now.

- \_\_\_ 21 - 30
- \_\_\_ 31 - 40
- \_\_\_ 41 - 50
- \_\_\_ 51 - 60
- \_\_\_ Over 60

2. Please indicate below the highest education level you have attained.

- \_\_\_ Below High School
- \_\_\_ High School
- \_\_\_ University / College Graduate
- \_\_\_ Post Graduate

3. What is your current nationality?

- a. Local national of China \_\_\_\_\_
- b. Chinese from Hong Kong \_\_\_\_\_
- Taiwan \_\_\_\_\_
- Singapore \_\_\_\_\_
- North America \_\_\_\_\_
- Others: \_\_\_\_\_
- c. Caucasian \_\_\_\_\_
- d. Others: \_\_\_\_\_

If you have chosen (a), please go on to question 4. If you have chosen (b), (c) or (d), please go on to questions 5 and 6.

4. Have you ever studied abroad? Yes / No

If yes, please specify the number of years you have spent abroad for the respective education level.

- High school \_\_\_\_\_ years
- University/College \_\_\_\_\_ years
- Post Graduate \_\_\_\_\_ years

5. How long have you personally been conducting business with China?

\_\_\_ years

6. How much time in total did you spend in China in 1993?

- 1 - 3 months
- 4 - 6 months
- 7 - 9 months
- 10 - 12 months

If you spent less than 6 months in China last year, please answer the following question.

Have you hired a Chinese person to take charge of the daily business operations in China?

Yes

No

If yes, is he/she a local national of China

Chinese from Hong Kong

Chinese from Taiwan

Chinese from Singapore

Chinese from North America

Chinese from another country



### **APPENDIX 3: QUALITATIVE DATA OF RESPONDENTS ON THE ROLE OF *GUANXI***

#### Company 1

- *Guanxi* is one of the three essential elements in doing business with China. The other two criteria are capability and capital.
- Your contribution to the Chinese and making the Chinese perceive your value to them are more important.

#### Company 2

- *Guanxi* is used to open the channel for business. Success still counts on your business strategy and product quality.

#### Company 3

- *Guanxi* is the gate leading to the treasure island. You have to pay an entrance fee in getting into the treasury. *Guanxi* is used to open the channel for you. But it does not mean business success.
- Formula for Business Success :  
Success = *Guanxi* + Financial resources + Business mind

#### Company 4

- *Guanxi* is unreliable. I believe more in product quality.
- *Guanxi* is definitely desirable for getting the business, I will give a '10' on the 10-point scale for its importance. But in terms of attaining long-term business success, I will rate it 6 only.

#### Company 5

- One cannot do business without *guanxi*, because it gives you the business opportunities. But it does not give you the success.

#### Company 6

- *Guanxi* is not omnipotent. If your products are bad, you are giving troubles to your intermediary and will lose trust of the Chinese in you.

#### Company 7

- *Guanxi* cannot give us the product quality and competitive prices which are more important in our business.

#### Company 8

- Higher priority should be given to *guanxi* for short-term goals; but lower priority should be given to *guanxi* for long-term goals.
- *Guanxi* teaches you the way of doing business in China.

#### Company 9

- Product quality is more important now.

#### Company 10

- *Guanxi* is only a starting point or a base upon which other key success factors are built. Business success has to depend on how you use the *guanxi*.

Company 11

- (no comment on this subject.)

Company 12

- *Guanxi* is the basic requirement. But it does not guarantee you business success, if you don't have the right business strategies and products.

Company 13

- If your product is very good and the Chinese want it, there is no need to acquire *guanxi*. They will come to you.

Company 14

- *Guanxi* gets you to the final round of a tender bid, but it cannot give you the business if your proposal is not good.

Company 15

- Uniqueness of the product is inversely related to the importance of *guanxi*.

- Formula for Business Success in China:

$$\text{Guanxi} + \text{Product Quality} + \text{Business Strategy} = \text{Success}$$

Company 16

- *Guanxi* is not important for us because it is totally handled by the distributor.

Company 17

- Formula for Business Success in China:

$$\text{Guanxi} + \text{Market Knowledge} + \text{Business Strategy} = \text{Success}$$

Company 18

- *Guanxi* is required to sell products in China. The Chinese cannot differentiate product quality which is less important than *guanxi*.

Company 19

- *Guanxi* is less important than product quality and management control.

**APPENDIX 4: DIFFERENTIATED IMPORTANCE ON THE WAYS OF  
GUANXI MAINTENANCE BY RESPONDENTS**

<u>Respondents</u>	Offering	Nurturing	Nourishing		
	Short-Term	Long-Term	Personal	Cultivating	Tendering
	<u>Gains</u>	<u>Mutual Interest</u>	<u>Relations</u>	<u>Trust</u>	<u>Favors</u>
Company 1	3	1	2	2	2
Company 2	3	1	2	2	1
Company 3	2	1	3	3	2
Company 4	3			2	2
Company 5	3	1	3	2	1
Company 6	1		2		3
Company 7	1		3		
Company 8	1				1
Company 9	1		2		
Company 10	1		3		3
Company 11	1				1
Company 12	2	1	1	1	2
Company 13	3	1	2	2	2
Company 14	3	2	3	3	2
Company 15	3	1	1	1	1
Company 16	3	1	1		1
Company 17	3	1	1	1	1
Company 18	3		3		2
Company 19	1	1	3		3

**APPENDIX 5: STATISTICS ON THE RELATIONSHIP BETWEEN RIGHT AND STRONG/MODERATE *GUANXI* NETWORK AND COMPANY PERFORMANCE, CONTROLLED FOR THE FIVE TESTING FACTORS**

<u>Control Variables</u>	<u>Categories</u>	<u>Spearman r</u>	<u>Significance Level</u>
Ownership Type:	Chinese firms	--	0.12
	Non-Chinese firms	--	0.12
Experience Level: in China Business	Old-timers	--	0.24
	Mature group	1.0	0.04 *
	Newcomers	--	0.24
Firm Size:	Large firms	--	--
	Medium firms	--	--
	Small firms	0.64	0.08 #
Industry Type:	Tertiary Industry	--	--
	Exporting Industry	--	--
	Exporting Manufacturing	--	--
	Selling Manufacturing	--	0.15
	Importing Industry	--	0.17
Type of Institute: Primarily Interacted	Government agents	0.73	0.05 *
	Private Enterprises	--	0.17

\* p<0.05, two-tailed test.

# p<0.10, two-tailed test.

-- Statistics could not be computed because there was only one column/row in the contingency tables.

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