

*GUANXI IN THE PEOPLE'S REPUBLIC OF CHINA (PRC):
AN AUSTRALIAN BUSINESS PERSPECTIVE*

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LIST OF ABBREVIATIONS

A\$	Australian Dollar
AMCHAM	American Chamber of Commerce
ANZSIC	Australian and New Zealand Industrial Classification
ASX	Australian Stock Exchange
AT	Agency Theory
CCP	Chinese Communist Party
CJV	Contractual Joint Venture
CPCC	Chinese People's Consultative Committee
EAAU	East Asia Analytical Unit
FDI	Foreign Direct Investment
FIE	Foreign Invested Enterprises
GDP	Gross Domestic Product
GNP	Gross National Product
HK	Hong Kong
IPR	Intellectual Property Rights
IT	Information Technology
JV	Joint Venture
NPC	National People's Congress
NIE	New Institutional Economics
Non-FDI	Non-Foreign Direct Investment
PBOC	People's Bank of China
PRC	People's Republic of China
ROA	Rest Of Australia
SEZ	Special Economic Zone
S-fEJV	Sino-foreign Equity Joint Venture
SOC	State Owned Company
SOE	State Owned Enterprise
SPSS	Statistical Package for the Social Sciences
SWJV	Sino-Western Joint Venture
TCE	Transaction Cost Economics
UCL	Unified Contract Law
UK	United Kingdom
US	United States
US\$	United States Dollars
VAT	Value Added Tax
WFOE	Wholly Foreign Owned Enterprise
WIPO	World Intellectual Property Organisation
WTO	World Trade Organisation

SUMMARY

Despite China remaining a mystery to many Western investors, it has become the largest recipient of Foreign Direct Investment in the world. It is this latter point, which makes the study of considerable importance. With China's continuing rapid growth in both its domestic economy and in its place in international trade, an understanding of the ways in which business is conducted in the PRC has become increasingly important. This study hopes to contribute to the growth of knowledge in this area by examining the role and importance of *guanxi* for Australian businesses operating with or within the PRC.

The investigation comprises a methodological approach combining a mail questionnaire, semi-structured personal interviews, and content analysis. The qualitative information obtained from the mail questionnaires and semi-structured personal interviews are analysed using content analysis.

While the PRC has attracted much attention from both academics and managers, studies in the area of *guanxi* are dominated by evidence from Overseas Chinese, North American, and European companies, to the exclusion of Australian businesses. This study contributes a comprehensive analysis of the legal problems faced by Australian businesses in the PRC, and the advantages and disadvantages of *guanxi*, which are assessed according to the theoretical framework of transaction cost economics and the first mover theory of competitive advantage respectively.

The study found that despite the decline in the salience of *guanxi* in the formal decision making process, Australian businesses may obtain competitive advantages through the employment of *guanxi* possibly enhancing their business success in the PRC. However, competitive advantages derived from *guanxi* or other sources may be threatened by discretionary policies, such as human resource policies and practices and policies and practices pertaining to the terms and conditions governing a sale in the PRC. In short, *guanxi* alone is no guarantee for business success in the PRC.

DECLARATION

I certify that this thesis does not incorporate without acknowledgement any material previously submitted for a degree or diploma in any university; and that to the best of my knowledge and belief it does not contain any material previously published or written by another person except where the reference is made in the text.

Andrew Scott Whitehead

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CHAPTER ONE:

INTRODUCTION

Since Deng Xiaoping announced the policy of economic reform in the People's Republic of China (PRC) over two decades ago, the Chinese economy has been moving from a centrally planned economy to an economy based more on market principles. During this period, the Chinese economy has averaged nearly 10 percent economic growth per annum, attracting investment from major multinational corporations and much attention from both academics and managers (Ahlstrom et al 2000, p. 5; Fock & Woo, 1998). In this time, the PRC has also become one of the largest recipients of Foreign Direct Investment (FDI) in the world (Chen, 1997, no. 97/14, p.1), with foreign investors acknowledging the importance of *guanxi* for conducting business in the PRC (i.e. Bjorkman & Schaap, 1994; Bjorkman & Kock, 1995; Leung et al 1996; Yeung & Tung, 1996; Ahmed & Li, 1996; Luo, 1997; Ewing et al 1998). *Guanxi* can be defined as an establishment of a connection between individuals to enable bilateral flows of social or economic transactions (Yeung & Tung, 1996, p. 3). Based on a random sample of 150 Hong Kong (HK) chief executives who were responsible for China trade within selected companies, Leung et al (1996) concluded that maintaining good 'connections or relationships' was beneficial to conducting trade with the PRC. Luo's study (1997) examined the relationship between *guanxi*-based business factors (sales force marketing and credit liberalisation) and enterprise performance, where it was concluded that *guanxi*-based factors have had a significant and positive impact on the enterprises' accounting and market performance. In addition, Luo (1997, p. 51) found that a Foreign Invested Enterprise's (FIE's) mode of entry, the place of origin of its investment and the duration of its operation influenced the association between *guanxi* and performance. Furthermore, he concluded that if transnational investors build up and maintain their *guanxi* in a country where *guanxi* connections constitute the most effective and efficient marketing tool, they may gain a competitive edge over their rivals (1997, p. 51). The data set for

Luo's (1997, p. 61) study, which consisted of firm-specific performance data of 156 randomly selected FIEs operating in Jiangsu province during the 1990-1991 period, was obtained from the Provincial Commission of Foreign Economic Relations and Trade. Specifically, the data concerning performance and business strategy variables was obtained from the sample FIE's external financial statements, which included the balance sheet, income statements and the detailed sheet of expenses and expenditures (Luo, 1997, p. 61). Bjorkman & Kock (1995) noted that virtually all respondents in their study found *guanxi* to be important in the PRC, especially for gaining access to information and influencing Chinese decision makers. Bjorkman & Kock's (1995) study on the role played by social relationships when penetrating a foreign business network consisted of more than 50 interviews with Chinese and foreign employees in a convenience sample of 24 Scandinavian companies. These companies were involved in the marketing of projects and industrial goods of different kinds to the PRC. Similarly, a majority of Yeung & Tung's (1996) research participants indicated the importance of *guanxi* for expediting the Chinese bureaucracy and overcoming business problems. Yeung & Tung's (1996, p. 59) research was based on 19 companies, which were all ethnic Chinese: HK (11), United States (US) (5), Canada (1), Germany (1), and Sweden (1). The individuals interviewed for their study were all ethnic Chinese and headed up the China operations for the company. These companies were engaged in a diverse range of industries, including real estate, finance, import/exports, and the manufacture of toys, electronic products, and telecommunication equipment. Ahmed & Li (1996, p. 284) also noted that *guanxi* is important for the success of foreign operations in the PRC because it can serve as an information gathering device on market trends and business opportunities, act as a means of securing access to important resources in the form of raw materials, land, labour, as well as smoothing the way in gaining privileged rights, such as import licences and government approval, which may build and enhance a competitive advantage. According to Bjorkman & Schaap (1994, p. 148), the importance of *guanxi* for Sino-Western joint

ventures (SWJV) in the PRC can be found in its ability to obtain different kinds of permits, raw materials, assist in the access to prospective buyers, and it may even enable the SWJV to win a business deal. Within the SWJV itself, *guanxi* will, among other things, enable the expatriate managers to influence the Chinese decision makers (Bjorkman & Schaap, 1994, p. 148). Bjorkman & Schaap's research was based on 36 interviews with Chinese and foreign employees in SWJV. These interviews represented 14 joint ventures with North American owners, 10 with Scandinavian parents, and 12 with parent organisations from other parts of Europe. Ewing, Caruana and Wong's (1998, p. 1) findings suggest that *guanxi* has a positive impact on business performance for those firms who successfully cultivate social and business networks in the PRC. Ewing, Caruana and Wong's (1998, p. 4) research was based on a self-completion mail survey of the top 300 Singaporean exporters to China.

Despite the importance of *guanxi* for conducting business in the PRC, Guthrie claims that the salience of *guanxi* is declining due to the construction and implementation of a rational-legal system at the state level and formal rational organisations at the firm level (Guthrie 1998, p. 259). His argument is based on 155 in-depth interviews conducted in 1995 with Chinese officials and industrial managers in the PRC's urban industrial economy, which is still dominated by State Owned Enterprises (SOE) (Smart & Smart, 2000, p. 259). Guthrie suggests that *guanxi* is still an important part of business in the market economy, but *guanxi* practices (*guanxi xue*-literally the study of *guanxi*) have diminished in importance (1998, p. 255). The distinction between the two for Guthrie is that 'guanxi is the set of relationships', while *guanxi xue* is the practice and technique of using and manipulating these relationships for specific ends (Guthrie, 1998, p. 262). Guthrie asserts that in the PRC today, powerful economic actors often pay more and more attention to the laws, rules and regulations that are part of the emerging rational-legal system because *guanxi xue* is viewed as unnecessary and dangerous in the face of the new laws and regulations against such approaches (Guthrie, 1998, p. 255). Smart and

Smart (2000, p. 260) suggest the changes that Guthrie puts forth as a decline in the importance of *guanxi xue* may be more representative of the effective controls on manipulative forms of *guanxi xue* related to cadre power than an emerging rational legal system in the PRC. Smart and Smart also point out that even if *guanxi xue* is more likely to meet with reprobation and failure *guanxi* is not certain to fade away as the PRC's economy converges with the West. For example, *guanxi* is far from insignificant in HK and Taiwan, where *guanxi* has been domesticated in such a way as to be more or less limited by the rule of law and concern for economic efficiency (Smart & Smart, 2000, p. 260).

Guthrie also argues that one of the main reasons for the declining significance of *guanxi xue* revolves around the competitiveness of the PRC's emerging market economy (1998). He suggests that as the PRC is moving away from a redistributive system, where all the costs for firms in the command economy were covered by the state, to a system where efficiency and competitiveness on the open market are important, and where tight fiscal constraints exist and SOEs are forced to take responsibility for their own economic positions, bureaucrats are increasingly likely to consider Western economic principles of product quality, price competitiveness and service instead of *guanxi xue* for economic decision making in the reform era (1998, p. 274). Even though Guthrie's (1998) argument that the salience of *guanxi xue* is in decline because of the implementation of a rational legal system and the increasing importance of Western economic principles in the decision making process may be appropriate for the Chinese urban industrial economy, its appropriateness for the foreign business environment of the PRC is unclear.

The applicability of Guthrie's (1998) proposition that the salience of *guanxi xue* is in decline because of the implementation of a rational legal system and the increasing emphasis placed on Western economic principles by Chinese decision makers for the foreign business environment in the PRC, is made even more unclear by the indeterminability of whether the above research scholar's reference to *guanxi* is either

‘*guanxi* as a relationship’ or *guanxi xue*. The separation of the terms within the context of ‘*guanxi*’ by Guthrie (1998) may not be as clear or appropriate for the foreign business environment in the PRC. This is because the advantages of *guanxi* for foreign investors in the PRC, as noted by Leung et al (1996), Luo (1997), Bjorkman & Kock (1995), Ahmed & Li (1996), Bjorkman & Schaap (1994), and Ewing, Caruana, and Wong (1998), can not be obtained without first developing ‘*guanxi* as a relationship’. More important than pinning down differences between ‘*guanxi* as a relationship’ and *guanxi xue*, is acknowledging that both terms are embodied in the Chinese concept of *guanxi*.

Therefore, to determine the applicability of Guthrie’s argument for Australian firms conducting business with or within the PRC, this study aims to answer the following broad research questions:

- (1) Where and when is *guanxi* important for Australian businesses conducting business in the PRC?
- (2) Is the salience of *guanxi* in decline in the foreign business environment of the PRC?
- (3) If so, what affect does this have on the First Mover Competitive Advantages and Transaction Cost Advantages of *guanxi* for Australian businesses operating in the PRC?

In light of these broad research questions, this study has four related research aims:

- (1) To examine the possibility of success for Australian businesses conducting business with the PRC through a greater understanding of *guanxi*.
- (2) To explore the role and importance of *guanxi* for Australian businesses in the PRC.
- (3) To link the theory of Transaction Cost Economics with *guanxi* through empirical research.

- (4) To clearly link the First Mover Theory of Competitive Advantage to the advantages of *guanxi* through empirical research.

Unless otherwise stated in this thesis, reference to either Australian businesses conducting business ‘in’ or ‘with’ the PRC incorporates Australian businesses that employ both FDI market entry strategies, such as Joint Ventures (JVs), and Non-FDI market entry strategies, such as export and representative offices.

1.1 BACKGROUND TO THE STUDY

Studies of *guanxi* include theoretical papers that debate the ways in which *guanxi* is an alternative to the market, hierarchy, and hybrid forms of governance that reduces transaction costs (Boisot & Child, 1988; Blackman, 1997; Davies, 1995; Standifird & Marshall, 2000; Lee, 1996), and papers that enhance the understanding of the ‘art of *guanxi*’ (Smart, 1993; Smart, 1999; Smart & Smart, 2000). Research in the area of *guanxi* also includes empirical studies on the role and importance of *guanxi* for Chinese officials and industry managers in the Chinese urban industrial economy (Guthrie, 1998), and the role and importance of *guanxi* for foreign businesses in the PRC (Leung et al 1996; Yeung & Tung, 1996; Luo, 1997; Bjorkman & Kock, 1995; Ahmed & Li, 1996; Bjorkman & Schaap, 1994; Ewing et al 1998; Fock & Woo, 1998). Moreover, a number of empirical studies have affirmed that the advantages of *guanxi* may be a source of competitive advantage for foreign investors in the PRC (Smart & Smart, 1991; Tracy, 1995; Hsing, 1998). Other research however, has argued that the salience of *guanxi* in the PRC is in decline in the face of the implementation of a rational legal system and increasing competition where a greater emphasis is placed on Western economic principles of price, product quality and service (Guthrie, 1998).

In much of this literature on *guanxi*, two main themes become identifiable. First, there is the importance and role that *guanxi* has played in facilitating economic transactions for Chinese and foreign businesses in the PRC’s uncertain commercial

environment since the late 1970s. The second theme to emerge in the literature is the suggestion of the declining significance of *guanxi* for facilitating economic transactions for Chinese businesses as the PRC moves to reduce the uncertainties surrounding its commercial environment. This study is concerned with the role and importance of *guanxi* for facilitating the economic transactions of Australian businesses operating in the PRC. It is also concerned with whether the significance of *guanxi* is in decline and how this may affect the competitive advantages of *guanxi* for Australian businesses. The motivation for the study was to determine the applicability of Guthrie's (1998) argument to Australian businesses operating in the PRC, and because of the dearth of research on the importance and role of *guanxi* for Australian businesses conducting business with or operating in the PRC.

1.2 THEORETICAL FRAMEWORK

This study employs the theoretical frameworks of the First Mover Theory of Competitive Advantage and Transaction Cost Economics to ascertain the role and importance of *guanxi* for Australian businesses conducting business with the PRC. The First Mover Theory of Competitive advantage asserts that businesses are able to achieve competitive advantages through a pioneering discovery or an innovative competitive action (Schumpeter, 1936; Porter, 1985, Porter, 1990). In analysing the advantages of *guanxi*, which in a number of ways can be likened to innovative competitive actions, this study determines whether Australian firms are able to obtain first mover competitive advantages through the employment of *guanxi* in the course of conducting business in the PRC.

Transaction Cost Economics contends that the criterion for organising commercial transactions is assumed to be the strictly instrumental one of cost economising (Williamson, 1979, p. 245). Essentially, this consists of two parts: economising on production costs and economising on transaction costs. Due to

Transaction Cost Economics' focus on the transaction as the unit of analysis, this study only considers economisation of transaction costs. The economisation of transaction costs may occur when commercial transactions shift from one governance structure to another (e.g. market based exchange, hybrid, or bringing the commercial transaction within the firm. In other words, internalisation through hierarchy (Williamson, 1991, p. 269). However, it is argued that the market and hierarchies' frameworks of Transaction Cost Economics provide a too limited set of transactional options to account adequately for many of the organisational problems encountered in the PRC (Boisot & Child, 1988; Standifird & Marshall, 2000). In analysing the problems encountered by the Australian businesses operating in the PRC, this study ascertains whether *guanxi* may be a viable alternative to formal institutional support in the PRC (Davies, 1995; Xin & Pearce, 1996; Blackman, 1997). In other words, does relying on *guanxi* rather than formal institutional support economise on transaction costs and lead to competitive advantages for the Australian businesses?

In short, the First Mover Theory of Competitive Advantage is employed to ascertain whether the advantages of *guanxi* can lead to competitive advantages for Australian businesses operating in the PRC. The theoretical framework of Transaction Cost Economics is employed to determine whether *guanxi* is a viable alternative to formal institutional support in the PRC for Australian businesses in the PRC.

This research indicated that despite the move to a rational legal system in the PRC where greater emphasis is placed on Western economic principles than *guanxi* by decision makers *guanxi* is a viable alternative to formal institutional support that reduces transaction costs. It also showed that despite the greater emphasis on Western economic principles, the advantages of *guanxi* can lead to first mover competitive advantages for Australian businesses operating in the PRC. Moreover, the findings revealed that the importance of *guanxi* has increased rather than decreased as competition has intensified in the PRC. Furthermore, this research disclosed that competitive advantages derived

from *guanxi* or any other source can be undermined by a businesses' discretionary policies, such as human resource policies and practices, and terms and conditions governing a sale in the PRC.

1.3 JUSTIFICATION FOR THE RESEARCH

This study was undertaken for a number of reasons. First, no research has examined *guanxi* in the context of Australian business. Most studies on the role and importance of *guanxi* have been dominated by evidence from North American, and European companies. This study aims to reduce this gap in the literature. Secondly, as Western businesses search the globe for business opportunities, they are faced with an increasing need to adapt and operate in environments where Western business practices may be less pronounced. This increases the attention that Western businesses need to pay to non-western business systems if they are to take full advantage of the global business opportunities that present themselves. Thirdly, the economic importance of the PRC is increasing, and as noted above the PRC's market is becoming increasingly competitive. Therefore, Western businesses that better understand and use the complexities of *guanxi* than their rivals may be in a more advantageous position to enjoy competitive advantages. Fourth, the area of *guanxi*, while previously considered by a large number of studies, has been researched mainly by either mail questionnaires or personal interviews. This study breaks new ground by employing the combination of a mail questionnaire, semi-structured personal interviews, and content analysis. These measures are jointly employed to strengthen the legitimacy of the findings. The final justification for this study is that it considers the empirical findings in the light of theoretical developments.

1.4 RESEARCH METHOD

The methods employed in the study comprise a mail questionnaire, semi-structured personal interviews, and content analysis. The mail questionnaire is used to answer the first, second, and third research questions. The qualitative information yielded from both the mail questionnaire and the semi-structured personal interviews are also employed to answer the first, second, and third research questions. Qualitative data obtained from the semi-structured personal interviews and questionnaires are analysed using content analysis.

The employment of both a mail survey and semi-structured personal interviews is based on the premise that each method has inherent weaknesses and strengths unmatched by other methods, with the weaknesses in each method being counter balanced by the strengths of another method (Brewer & Hunter, 1989; Jick, 1979; Sieber, 1973), and that multiple methods increase research robustness, by identifying and analysing the findings that agree, disagree or, at least, do not contradict one another (Miles & Huberman, 1994).

This study targets Australian businesses dealing with the PRC. To maximise the variation in the site selection, this study conducted semi-structured personal interviews in Adelaide, South Australia, the Chinese cities of Beijing and Shanghai, and administered a mail questionnaire throughout Australia, excluding South Australia. Increasing the variation in site selection enabled the researcher to have more confidence in those patterns that emerge as common among sites, while at the same time being able to describe some of the variation that has emerged to make programs unique as they adapt to different settings.

The data analysis is comprised of descriptive statistics, which are presented in tables. Full details of the methods employed, including justification, pre-testing and limitations are contained in Chapter Four.

1.5 SCOPE AND LIMITATIONS

As previously mentioned, Australian businesses that conduct business in the PRC are the focus of the study. This limits the extent to which inferences could be made from the findings about other foreign businesses operating in the PRC.

A number of studies in the area of *guanxi* have either framed their sample around business size (i.e. value of total assets, sales, or employee numbers), industry classification, market entry strategy or length of experience of the executives in conducting business with the PRC (Xin & Pearce, 1996; Yeung & Tung, 1996; Bjorkman & Kock, 1995; Luo, 1997). Although a variety of sampling frames have been employed in the area of *guanxi*, this study, for comparative purposes of the questionnaire and semi-structured interview data and replication purposes, employs the following characteristics to classify the Australian businesses: market entry strategy, industry classification, number of years conducting business in the PRC, and business size (employee numbers). This study, for comparative and replication purposes, also obtained the research participants individual characteristics, which include nationality, position held, length in current position, length with current employer, and length of PRC business experience.

Large Australian businesses were over-represented in the study, as were the following: Australian businesses classified as tertiary, Australian business that entered the PRC through non-direct investment strategies, and Australian businesses that entered the PRC during the 1991-2000 period.

Part of the samples' geographic location introduced difficulties for the researcher that may not have been experienced if the researcher were a resident of Beijing or Shanghai. As the researcher was based in Australia except when conducting fieldwork, time delays and communication difficulties in negotiating access to the sample, clarifying procedures, and following up research participants, were expected and experienced. These difficulties are consistent with Adler's (1983) description of the problems of doing research in overseas locations.

1.6 THESIS STRUCTURE

This Chapter has laid the foundations for the following study. The research problem was introduced, *guanxi* was defined, theoretical frameworks were discussed, the research was justified, methods were briefly outlined, and limitations were provided.

Chapter Two and Chapter Three discuss the theoretical frameworks within which this study is located. Chapter Two begins with a discussion on the complexities of *guanxi*, and then focuses on the First Mover Theory of Competitive Advantage. The Chapter develops a model that depicts interaction between the advantages of *guanxi* and the innovative competitive actions that may lead to First Mover competitive advantages. This model is referred to again in Chapter Seven, when the empirical results of the study are assessed in terms of the model.

Chapter Three begins with a broad analysis of New Institutional Economics and then focuses on the specific theory of Transaction Cost Economics applicable to this study. The Chapter then develops a framework for *guanxi* as a viable alternative to the lack of formal institutional support in the PRC. This framework is referred to again in Chapter Eight, when the empirical results of the study are assessed in terms of this framework.

Chapter Four describes the methods employed to conduct the study, including design, data collection and analysis techniques used. Limitations of the methods are also discussed. Chapter Five reports the results of the data collection and analysis, summarising the findings and briefly discussing the outcomes. Chapter Six, in order to further enhance the understanding of *guanxi* examines in-depth the methods employed by the research participants to develop and maintain *guanxi* which include banquets, gift giving, and regular contact, and whether *guanxi* is a form of corruption. Finally, Chapters Seven and Eight discuss the results, consider the theoretical implications, and present the conclusions drawn. Chapter Nine highlights the point that competitive advantages, whether derived from *guanxi* or other competitive actions, are no guarantee for business

success in the PRC. Practical implications and recommendations for further research are included in the final Chapter, Chapter Ten, with a summary of the contributions that this research has made to the literature.

CHAPTER TWO:
THE COMPLEXITIES OF *GUANXI* IN THE PEOPLE'S REPUBLIC OF CHINA
(PRC) AND THE COMPETITIVE ADVANTAGES OF *GUANXI*: A FIRST
MOVER THEORY PERSPECTIVE

2.1 Introduction

This Chapter analyses the complexities of the Chinese concept ‘*guanxi*’. It includes the following: a definition of *guanxi*, the recent history of *guanxi*, and its workings, its development and maintenance, *guanxi* exchange, the obligations of *guanxi*, *mianzi* (face), the reciprocal nature of *guanxi*, and the ‘gift economy’ in the PRC. In addition, this Chapter analyses the salience of *guanxi* for facilitating investment in the PRC by examining HK investment in Guangdong, Taiwanese investment in Fujian and Singaporean investment in Hainan. Furthermore, it examines the advantages obtained by Singaporean, Taiwanese, and HK investors who facilitate their investment through *guanxi*, which may enable them to obtain first mover competitive advantages. Moreover, this chapter examines the requirements needed to sustain a competitive advantage, and the disadvantages of being a first mover.

2.2 The Complexities of *Guanxi*

The term *guanxi* is a word of recent origin. Although used in speech since the beginning of the century, it does not appear in either of the classic Chinese dictionaries published in the early twentieth century: *Ci Yuan* (*Source of Words*, 1915 edition) (Ambler, 1995, p. 27) or *Ci Hai* (*Word Sea*, 1938 edition) (*Ci Hai*, 1938, p. XU 110). The first part of the term *guanxi*, ‘*guan*’, traditionally meant pass. Later, its meaning was extended to ‘to close’ or ‘to shut’. The second part ‘*xi*’ means to tie up, and its meaning was extended to relationships (Ambler, 1995, p. 27). The two Chinese characters, when placed together to form the term *guanxi*, literally mean a gate/pass or ‘to connect’. Thus, *guanxi* can be

translated as the establishment of a connection between individuals to enable bilateral flows of social or economic transactions (Yeung & Tung, 1996, p. 3). Correspondingly, Davies loosely defines *guanxi* as “the set of ‘personal connections’ that an individual can draw upon to secure resources or advantage when [conducting] business or in the course of social [interaction]” (1995, p. 155). Even though the Chinese term *guanxi* is a relatively modern expression, its meaning can be found in the Confucian classics under the word *lun*. *Lun* means order, or more specifically, ‘differentiated order’ among individuals. In other words, how one acts within differing relationships (King, 1991, p. 65). This is not drawing a direct relationship between *lun* and *guanxi* but merely highlighting the point that the idea of *guanxi* has been in existence in Chinese society for over 2000 years (Luo, 1997, p. 52). Although the contemporary expression of *guanxi* has its origins in the Confucian classics, a historical account of the evolution of human relationships in Chinese society is beyond the scope of this thesis. Nevertheless, a historical overview of *guanxi* since the establishment of the People’s Republic of China (PRC) in 1949 is given in the following section.

2.3 Recent History of *Guanxi*

The great upheaval of the Communist Revolution produced a transformation which was acutely felt in social relationships. Friendship, as a relationship of confidence, not only declined but situations where one gave economic assistance or used one’s influence to help a friend also became rare (Yang, 1994, p. 153; Vogel, 1965, p. 53). ‘Comradeship’ came to displace the personalistic values of friendship and kinship, decreeing that all persons should treat relationships as equal (Vogel, 1965, p. 59; Yang, 1994, p. 153). This was the direct result of the Communist régime’s concerted attacks on nepotism and the application of personal influence. Although during the late fifties the desire to employ *guanxi* was discernible, people were apprehensive to do so. They did not dare approach a person for favours due to fear that that person might turn them over to the authorities and

complain that one's 'collective spirit' was lacking and that one deserved punishment (Vogel, 1965, p. 53; Yang, 1994, p. 153; Whyte & Parish, 1984, pp. 343-349; Walder, 1996, p. 49). According to Yang (1994, p. 154) and Walder (1996, p. 49), the aftermath of the Great Leap Forward (1959-1961), where food and goods were scarce, saw the beginnings of a resurgence of *guanxi*. The subsequent Cultural Revolution (1966-1976) is believed to have provided a major catalyst for further developing *guanxi* ties. During the Cultural Revolution (1966-1976) production was again disrupted, resulting in numerous people not having access to the basic necessities of life - food, clothing and shelter (Brunner et al 1989, p. 12). Many people, therefore, in their daily struggle for life, began to rely on *guanxi* as a means of survival (Yang, 1994, p. 158). An informant in Whyte & Parish's 1970s (1984, pp. 97-98) research noted the importance of *guanxi*:

One should maintain relations with 'three valuables' (*sanbao*) a doctor, a truck driver, and a sales clerk. The doctor would help one beat the lines and medical shortages at hospitals. The truck driver could get cheap goods from markets outside the city. The sales clerk could notify one when scarce goods like electric fans, televisions, and better clothing were about to appear on the market and might 'forget' to check purchases off on one's ration book.

In addition, those in high positions, such as cadres and military officers, began to employ their personal connections to save their children from being persecuted and sent down to remote rural areas. This behaviour was resented by ordinary folk and encouraged the practice of gift giving and asking for favours to prevent their children from leaving urban areas (Yang, 1994, p. 156). Thus, it could be argued that the re-emergence of *guanxi* during the Cultural Revolution was a social response to the collapse of regular state structures (Yang, 1989, pp. 35-36).

Prior to the 1980s, a majority of urban Chinese worked in socialist work units (*danwei*) (Kipnis, 1997, p. 150). These work units were no ordinary work units. Many distributed housing, foodstuffs, furniture, and/or other goods, and moreover operated schools and health clinics. This system of political and economic organisation, which created scarcity, encouraged *guanxi* (Walder, 1986, pp. 6-7; Henderson & Cohen, 1984).

As Kipnis (1997, p. 150) argues, since workplace officials rather than the market place allocated goods, developing *guanxi* with officials was a necessary means in circumventing formal regulations to obtain what one required.

The significance of *guanxi* continued during the economic reforms of the 1980s, where the development of relationships followed the introduction of market elements, linkages to the global capitalist economy, changes in production, distribution, and consumption and changes in how people viewed employment and money (Yang, 1994, p. 159). Yang (1994, pp. 166-167) noted that during the mid 1980s the language of friendship, mutual obligation and assistance, and sharing, which constituted the practice of *guanxi*, had been transformed by the infiltration of money as an alternative medium of *guanxi* exchange. The development of money relationships, however, has not impinged on the growing importance of *guanxi* in the PRC's economic transition (Yang, 1994, p. 166).

2.4 *Guanxi* and its Workings

A base for *guanxi* exists when individuals have a commonality of shared attributes, such as identity, language, or origin. Some of these *guanxi* characteristics are inherited at birth (e.g., kinship, locality, and father-son relationship), acquired later in life (e.g., husband-wife, classmates, co-workers, and military experience), or by achieved status (Tsui & Farh, 1997, p. 59; Greenblatt et al 1982, pp. 211-212; Fried, 1974). The nature of some shared attributes is quite elastic, in that they can be expanded or contracted depending on the situation. For example:

Locality can mean a small village, a county, a city, a province, or even a regional grouping of provinces. Even kinship (family) can stretch to the furthest horizons, ranging from nuclear family (primary familism) to the more distant family (generalised familism) where people who are remotely connected to someone in the family (e.g., distant relatives) may be embraced. The elasticity of these bases of 'guanxi' allows individuals to use their social ingenuity to build a web of personal relationships (Tsui & Farh, 1997, p. 60).

Family in the Chinese context is quite unlike the typical Western family. It embraces people who are not family but who are connected to someone in one's family, to friends of the family, and to all their families. The Chinese 'family' is really a system of contacts rather than an emotional unit as in the modern West (Montagu-Pollock, 1991). However, the existence of a *guanxi* base does not imply an alliance or the absence of 'emotional unit'. For example, an individual may have many relatives, many of whom he or she has never met or is not personally close to. In the event that this kin's assistance is needed, the individual could use the existing *guanxi* base to establish an alliance. The existence of *guanxi* bases only provide an opportunity to establish *guanxi*. Without a pre-existing *guanxi* base, it is more difficult to establish an alliance (Kiong & Kee, 1998, p. 83). Nevertheless, *guanxi* can be established with an 'outsider' through the employment of an intermediary or a go-between (Tsui & Farh, 1997, p. 60). The intermediary or go-between is usually a friend (business associate) who is familiar with the person with whom one wishes to make contact with and who implicitly vouches for one's virtue, trustworthiness and reliability (Yang, 1994, pp. 124-125; Pearce & Robinson, 2000, p. 33). For example, in her field work, Yang wanted to interview a certain factory deputy Party secretary. That secretary's response to the request to be interviewed stated: 'Old Liao and I have been close friends for a long time. Since it was old Liao who introduced you to me, it must mean that he trusts you, so I trust you too' (Yang, 1994, p. 125). Similarly, one of the research participants in Pearce & Robinson's (2000) study wanted to schedule an appointment with the person in charge of a construction project in Kunming. That research participant noted:

The person in charge of the construction project would not schedule an appointment with us because we did not have *guanxi* with him. It did not matter to him that we had the best lumber, the best engineers, and the lowest bid. He refused to meet us. We had to employ an intermediary who had *guanxi* with him to get an appointment (Pearce & Robinson, 2000, pp. 33-34).

These examples demonstrate the importance Chinese place upon a letter of introduction. If an individual were to simply walk off the street, without first establishing a basis of familiarity and request an appointment with a factory deputy Party secretary or the person in charge of the construction project in Kunming, more often than not an appointment would not be granted. Victor Fung, chairman of a HK investment bank, stated in relation to letters of introduction:

If you are being considered for a new partnership, a personal reference from a respected member of the Chinese business community is worth more than any amount of money you could throw on the table (Yeung & Tung, 1996, p. 62).

Not only does this comment indicate the importance of letters of introduction in the course of business in the PRC, it also demonstrates that the Chinese have a deep distrust of persons who are 'outsiders' and not-members of one's *guanxi* network. Thus, *guanxi* exchange can only be carried out between two parties who, in one way or another, have established a basis of familiarity. The larger one's *guanxi* network, and the more diverse one's *guanxi* members with differing occupations and positions of authority and power, the better one's manoeuvrability in society becomes and the greater one's power to obtain resources and opportunities (Yang, 1994, p. 123; Brunner et al 1989, p. 12). In short, one who does not possess *guanxi* is almost invisible in the PRC (Ambler, 1995, p. 28).

2.5 Developing and Maintaining *Guanxi*

Developing and maintaining *guanxi* consists of the personal exchange and circulation of gifts (*liwu*), banquets (*yanhui*), and favours (*bangmang*) (Xin & Pearce, 1996; Yeung & Tung, 1996, p. 61; Kipnis, 1997, p. 46, p. 64, p. 28). These are described by Yang (1994) as both the 'art of *guanxi*' and the 'Chinese gift economy'. The credence placed on developing and maintaining *guanxi* through the personal exchange and circulation of gifts, banquets, and favours leads this study to examine the manner in which the participants develop and maintain their *guanxi*. A gift may be either in material form or a

piece of information possibly concerning whom one should talk to regarding certain business activities or opportunities (Smart & Smart, 1991, pp. 227-228; Tsang, 1998). In developing *guanxi*, according to Brunner et al (1989, p. 10), there is a need for *ganqing*, which is a measure of its relative ‘usefulness’, or its emotional commitment and psychological dependency. *Ganqing* also alludes to the willingness and depth of feeling to sacrifice one’s personal interests to assist a *guanxi* member (Brunner et al, 1989, p. 10). In other words, *ganqing* is a measure of the emotional commitment between the parties involved (Tsang, 1998, p. 3; Jacobs, 1979, pp. 252-253). *Ganqing* varies in warmth and intensity and may be improved over time (Brunner et al 1989, p. 10). The intensity and warmth of *ganqing* is built up through shared experience such as living, working or studying together, but a base for *guanxi* between two individuals can exist without *ganqing*. For example, a *guanxi* base may have risen purely because both are alumni of the same university, though if one had already graduated before the other entered university, the *guanxi* between the two would be distant (Tsang, 1998, p. 3). Kipnis (1997, p. 23) points out, the terms of *guanxi* and *ganqing* are often interchangeable. For example, *guanxi* can refer to the more material aspects of reciprocity, and *ganqing* can refer to the human feelings involved between individuals. Conversely, *guanxi* involves human feelings and *ganqing* involves material obligation, such that the more *ganqing* there is, the closer the *guanxi*. The closer the *guanxi*, the more it can be relied upon for economic, political, and social benefits. In turn, such benefits produce stronger *ganqing*.

Brunner et al (1989, p. 10) also points out that the term *renqing*, connoting human sentiments, is essential for the understanding of *guanxi*. *Renqing* is associated with the Confucian canons. It signifies a bond of reciprocity between individuals based either on emotional attachment, a sense of obligation, or indebtedness. *Renqing* can be in part equated with the content of the Confucian principle *li* (propriety), which refers to the proper way of conducting social relationships, or treating others according to their status

and relationship to oneself (Wright, 1964, p. 21; Brugger & Reglar, 1994, pp. 177-178; King, 1991, p. 74; Brunner et al, 1989, p. 10; Fried, 1974). In other words, *renqing* means conducting relationships with one another on certain prescribed rules of behaviour. King (1991, p. 74) points out that *renqing*, which is merely sentiment, or an affective component of all human relations, is different to *ganqing*. *Renqing* is social, while *ganqing* is personal. More important than pinning down translations and differences between *guanxi*, *ganqing* and *renqing* is to acknowledge that all three terms cross the boundaries between social relationship, material obligation, and sentimental attachment. As Kipnis (1997, p. 189) points out, it invokes a world in which these domains overlap. Therefore, the term *guanxi* to be employed in this thesis embodies the meanings of both *ganqing* and *renqing*, while acknowledging the overlap.

2.6 Social and Economic *Guanxi*

As previously discussed, *guanxi* refers to the establishment of a relationship between individuals in the course of economic or social exchange. In other words, there are two levels of *guanxi*. The following discussion refines the understanding of the two levels. What Jacobs (1979, p. 252) describes as economically based *guanxi*, Hwang (1987) refers to as the instrumental tie of *guanxi*. Parties to this type of relationship consider it as a means to achieve their own purposes (Hwang, 1987, p. 951; Jacobs, 1979). In contrast, social *guanxi*, according to Yang (1994, p. 117), is characterised by friendship (Yang, 1994, p. 117). According to Yang (1994, p. 111), friendships serve ‘as bases for or potential sites for the art of *guanxi*’. Notions of friendship are expressed in the different categories of “heart-to-heart friends” (*zhixin pengyou*) and friends who use each other (*huxiang liyong*), a contrast that follows the distinction between expressive or emotional friendship and instrumental friendship (Yang, 1994, p. 117). “Heart-to-heart friends” are ‘real friends’. They can not be used ‘as an instrument to acquire resources’, because in real friendship, one gives without thinking of a return. This means that the allocation of

limited resources is determined by individual need rather than individual contribution (Wong & Chan, 1999, p. 108). According to Kipnis (1997, p. 148), this type of friendship is based on a deep mutual *ganqing*. Such friends are rare and most people tend to have more 'ordinary friends' (*yiban pengyou*). Ordinary friends are people with whom one can share a good time, but are not always reliable during hard times (Yang, 1994, p. 117).

Although economic *guanxi* may consist of an affected *ganqing*, the main purpose of establishing this relationship is for mutually beneficial material exchanges (Kipnis, 1997, p. 148). This means that the allocation of resources to outsiders or strangers depends on individual contributions (Wong & Chan, 1999, p. 108). Once a relationship of instrumental *guanxi* is no longer advantageous it can be neglected or dropped (Guo, 2001, p. 73). Smart (1999, p. 129) argues that *guanxi* straddles the economic and social level because *guanxi* without the affective dimension of solidarity and trust would not be as effective in providing the instrumental advantages that it does. Although *guanxi* may be cultivated for the primary purpose of attaining instrumental goals, the forms must be followed if the goals are to be achieved. The relationship must be presented as primary and the exchanges, useful though they may be, treated as secondary (Smart, 1999, p. 129). Accordingly, economic *guanxi* does not necessarily involve friendship, although friendship is preferred (Park & Luo, 2001, p. 457). In other words, friendships often form the basis for economic exchange. According to Yang (1989, p. 48), if instead it becomes apparent that the relationship involves only material interest and is characterised by direct and immediate payment, the exchange may be classified as bribery.

In short, social *guanxi* refers to personal friendship and economic *guanxi*, as the name suggests refers to the use of a relationship to achieve one's goals in the course of business. Although *guanxi* straddles the economic and social levels, unless otherwise stated, the term *guanxi* employed in this thesis refers to economic *guanxi*.

2.7 *Guanxi Exchange*

Many people in the People's Republic of China see the pursuit of *guanxi* as eminently practical. Playing by the bureaucratic rules and regulations or going through official channels to get things done is something only the 'naive and inept would do' (Gold, 1985, p. 662). Similarly, Leung et al (1996, p. 750) contend that relying on *guanxi* is more practical than placing one's reliance on a primitive communication system and a bureaucratic maze. According to Yang (1994) the first step in the successful initiation of *guanxi* exchange is to identify a suitable target person. The individual must then ascertain whether the target person is able to help. Once a target person for *guanxi* overtures has been selected and the basis for familiarity has been presented, one must then find the most diplomatic way of signalling to the target the intention of engaging in exchange.

Finally, one must ascertain whether the target person is amenable to giving help in exchange for gifts, banquets and favours. These questions must be presented in such a manner that one receives answers without appearing to have asked questions. Diplomacy is important in the initiation of *guanxi* exchange as blatant requests usually meet with blatant refusals and jeopardise the entire relationship (Yang, 1994, pp. 130-131). Thus, *guanxi* gives people the power to access goods or services during economic interaction that individuals by themselves do not have the capacity to acquire (Davies, 1995, p. 155).

2.8 The Obligations of *Guanxi*

Greenberg (1980, p. 4) maintains that once rewards (gifts, banquets, or favours) are received, the recipient acquires a cost in terms of obligation. According to Greenberg (1980, p. 4), this obligation leads to increased alertness and sensitivity to opportunities for its reduction. Participants in a *guanxi* relationship, however, do not necessarily see obligations as having negative overtones. This is perhaps because one shares an identity with the donor in terms of shared attributes, or identifies with the donor's labour and hardship embodied in the gift (Yang, 1989, p. 41). Since 'gift' exchange is difficult to

quantify, the ‘debt’ rarely is cleared in one transaction. As a result, favours are accumulated, with interpersonal relationships thickening as the exchange of gifts and favours continue (Hsing, 1997, p. 154). One is expected to return the favour given, and those who give others a favour see it as a form of investment to be reclaimed in time of need (Hsing, 1997, p. 154). This is not suggesting that all economic relationships are infinite, as relationships that are no longer profitable are easily severed (Alston, 1989, p. 58), in the sense that when the relationship with another does not have the ability to achieve one’s desired goals then the relationship becomes superfluous. Thus, the art of *guanxi* exchange lies in the mobilisation of moral and cultural resources, and forging obligations and reciprocity in pursuit of economic ends, while acknowledging that *guanxi* exchange straddles the economic and social levels (Yang, 1989, p. 35; Yeung & Tung, 1996, p. 62).

2.9 *Mianzi* (Face)

In his study of the natives of the Trobriand Islands in the Archipelago of Melanesian New Guinea, Malinowski maintained that an individual within that society did not act to safeguard his or her individual interest in the possession of material goods; the primary motivation was to maintain social standing, social claims and social assets (Malinowski, 1926, pp. 24-26). Malinowski’s findings are consistent with the Chinese concept of ‘face’ (*mianzi*).

Mianzi can be defined as one’s reputation, which is achieved through success, ostentation and the fulfilment of obligations regardless of the hardships involved. It also represents the confidence of society in the integrity of one’s moral character (Hu, 1944, p. 45). The fairness of each other’s conduct in an economic exchange is not only monitored by the parties to the exchange, but is also monitored by individuals connected directly or indirectly to the parties concerned (Ho, 1976, p. 875; Malinowski, 1926, p. 26; Polanyi, 1944, p. 46). Actions of an individual that result in a loss of *mianzi* make it

impossible for the individual to function properly within their *guanxi* network (Hu, 1944, p. 45; Luo, 2000a, p. 45). In other words, by disregarding the accepted code of honour or generosity, the individual is defined as untrustworthy and is ostracised by his or her *guanxi* network (Alston, 1989, p. 58). Because the confidence of society in the integrity of one's moral character plays an important part in determining the willingness of parties to enter economic exchanges with one another (Fama, 1980), *guanxi* based exchange offers the advantage of reduced opportunistic behaviour.

Despite the strong effects of *mianzi*, which Standifird and Marshall (2000, p. 29) and Luo (2000a, pp. 40-45) contend are indicative of an institutional constraint, there is an argument that reputation is limited in its efficacy to attenuate opportunism. Hill (1990, p. 509) argues that reputation may be difficult to establish due to the dispersion problems or lack of communication among the population of potential participants to an exchange. More generally, Hill (1990) argues that there is a cost involved in establishing the reputation of a trading partner. However, information passed through a *guanxi* network in a market characterised by information imperfection is far more trustworthy, richer, and more useful in establishing another member's reputation than gained by other means (Luo, 2000a, p. 45). Thus it saves on research costs and allows *guanxi* network members to make more informed decisions (Luo, 2000a, pp. 45-46). It may be argued that if a member of a *guanxi* network traded with an individual outside such a network, then the cost of establishing the reputation of that individual may be high. But this fails to consider that in the PRC the Chinese mainly trade with individuals where a basis of familiarity already exists or where someone else, as discussed previously, vouches for the other person's reputation (Yang, 1994, p. 124). Therefore, *mianzi* may act as an institutional constraint deterring opportunism.

2.10 Gift Economy

Westerners often perceive the ‘Chinese gift economy’ in the PRC negatively as ‘corruption’ (Tracy & Ip, 1995, p. 278). In doing so the social context may be disregarded. Taking into account political and cultural aspects of Chinese society, Theobald (1990, p. 110) argues to the contrary that the gift economy is not only useful to the individuals concerned but in certain respects is also beneficial to society as a whole. Through the gift economy people are able to ‘oil the wheels of the administration’ and streamline bureaucratic red tape. In addition, the gift economy opens up channels for the masses to acquire scarce and valued resources in the Chinese state redistributive economy (Theobald, 1990, p. 123; Henderson & Cohen, 1984, p. 21). That is not to deny that palpable corruption, detrimental to the citizens of China, exists. For example, in some farming districts, officials in charge of education misappropriated several million yuan. The money, originally intended for the construction of schools, was used to buy cars, build apartment blocks, carry out trade negotiations and even construct hotels (Rocca, 1992, p. 410). The point is simply that all *guanxi* should not be labelled ‘corruption’ without considering specific political and cultural circumstances. Ethnocentricity is undesirable when evaluating the patterns of social and economic exchange in different cultures.

In making such an evaluation, it is important to examine just how concepts are used. Consider the word ‘resources’. Yuchtman and Seashore broadly define resources:

as a more or less generalised means, or facilities, that are potentially controllable by social organisations [or members of a society] that are potentially usable - however indirectly - in relationships between the organisation [or members of a society] and their environment (Yuchtman & Seashore, 1967, p. 900).

This definition does not restrict the concept of resources to physical or economic objects (Yuchtman & Seashore, 1967, p. 900). As Gamson (1966, p. 122) argues, reputation is a resource; it refers to potential influence rather than just influence in use. Gamson (1966) insists that an individual who holds great potential influence in an elaborate network,

such as in a *guanxi* network, possesses a powerful set of inducements. It is certain that there will be some present or future situation in which he or she can influence decision-makers concerning the allocation of valuable and scarce resources in order to benefit a member of their *guanxi* network (Gamson, 1966, p. 123). This behaviour is not particularly Chinese and can be found in societies such as Indian, Lebanese, Japanese (*Wa*) and Korean (*Inhwa*) (Alston, 1989, pp. 56-59). However, according to Davies *guanxi* is much more important in the context of China business than elsewhere (1995, p. 155). Therefore, to enhance the understanding of *guanxi* this study examines whether the research participants consider *guanxi* to be a form of corruption.

2.11 The Facilitation of Investment in the PRC Through *Guanxi*

The above discussion pointed out that utilising *guanxi* in the PRC may enable individuals to obtain certain advantages, which may include expedition of the PRC's bureaucratic process, and access to scarce resources and opportunities. This indicates that *guanxi* may play an integral part in facilitating investment in the PRC. To highlight this possibility, this thesis analyses HK, Taiwanese and Singaporean investment in the PRC. These countries and territories were chosen on the basis of the overseas Chinese connection and that HK has been the single largest investor in the PRC for the past two decades, and Taiwan, Singapore and HK as a group have on average accounted for approximately 61 percent of FDI in the PRC between 1995-1999 and even more during the 1987-1994 period (China Statistical Yearbooks, 1988-2000).

2.11.1 Hong Kong's Investment in the PRC

During the 1970s and 1980s, HK achieved spectacular economic growth, doubling its Gross National Product (GNP) per capita in each decade. After the mid-1980s, rising wages, overhead costs, land shortage and a shortage of cheap labour forced HK to relocate its labour intensive industries outside its borders (EAAU, 1992, p. 11). The

Chinese province of Guangdong, after it was opened to FDI, with its close proximity to Hong Kong, and lower production costs (wages plus overhead costs) was an obvious choice (Smart & Smart, 1991, p. 225; EAAU, 1992, p. 11). Guangdong and its Special Economic Zones (SEZs) became an integral part of HK's structural change (Overholt, 1993). Hong Kong's actual realised FDI in Guangdong amounted to US\$5.5 billion for the 1986-1991 period, making HK by far the largest investor in Guangdong. Japan came second with realised FDI of US\$534 million for the same period (EAAU, 1992, p. 73). This trend continued through the mid 1990s. In 1996 Guangdong accounted for around 40 percent of HK investment in the PRC (Sung, 1997, p. 711).

Although economic theory concentrates on tariffs, controls on migration and exchange rate integration, among other things economic the effect of cultural and geographical distances may be even more important for economic integration (Sung, 1997, p. 707). Hong Kong and the Pearl River Delta share a cultural identity through the common Cantonese dialect, and many HK people have their ancestral roots in Guangdong, the primary site of HK investment. On the geographical front, the SEZ of Shenzhen is only a 30 minute train ride from HK (EAAU, 1992, p. 14; Smart & Smart, 1991, p. 225; Sung, 1997). Notwithstanding the geographical explanation for economic integration, HK FDI in Guangdong has been heavily influenced by shared attributes, such as cultural and linguistic affiliation (Eng & Lin, 1996, p. 1113; Sung, 1991, p. 11). This is confirmed by Tracy's (1995, p. 20) research of 400 foreign invested companies in the Chinese province of Guangdong. He established that the local connections of the majority of investors from HK in Guangdong were based on local dialect, local origin and local kin. This cultural and linguistic affinity of HK investors in Guangdong provided a base for establishing *guanxi* through gift exchange (Weidenbaum & Hughes, 1996). This is not to suggest that HK investment in the PRC has only been concentrated in Guangdong, or that HK investment in other areas of the PRC has not been facilitated by *guanxi*. It merely highlights the importance of *guanxi* for facilitating HK investment in the PRC.

2.11.2 Taiwanese Investment in the PRC

Despite the political stand-off between the mainland and Taiwan, by 1991 Taiwan had surpassed the USA and Japan to become the second largest investor in the PRC after HK. Realised FDI from Taiwan reached US\$10 billion between 1978 and 1994, accounting for 10 percent of the PRC's FDI (Hsing, 1998, p. 3). The level of investment by Taiwan in the PRC is quite interesting because it was not until 1987 that the Taiwanese government lifted a long standing ban on Taiwanese visiting the PRC (Hsing, 1998, p. 3). During this period, the majority of Taiwanese investment was concentrated in a few geographical areas of Guangdong and Fujian province. These areas included Guangzhou, Shenzhen and Dongguan in Guangdong, and Xiamen and Fuzhou in Fujian (Chen, 1996, p. 451).

According to Chen (1996, pp. 460-461), it was not only product cycles and external state policies that were key determinants of Taiwanese investment in the PRC, but also the favourable socio-cultural environment of traditional and ethnic ties among the peoples of the region. For example, 17 million of the 21 million inhabitants of Taiwan speak the same Chinese dialect (Hokkien) as the inhabitants of southern Fujian, to which many Taiwanese trace their ancestry (EAAU, 1992, p. 14; Sung, 1991, p. 11). This cultural and linguistic affinity between the Taiwanese investors and local mainland Chinese officials provided the base for establishing *guanxi* through the principle of gift exchange (Hsing, 1998, p. 143).

Although Taiwanese investment continued to cluster in Guangdong and Fujian, during the 1990s it began to move north and west in the PRC. Shanghai, Zhejiang, and Jiangsu began to feel the impact of that move with these areas taking a substantial portion of Taiwanese FDI (Chen, 1996, pp. 450-451; *Xinhua* News Agency, July 16, 2001, p. 100). Many of the families of Taiwan's *Guomindang* have ancestral ties with the people of Southern Jiangsu and Zhejiang, providing a cultural link (EAAU, 1992, p. 14; Hsing, 1998; Weidenbaum & Hughes, 1996, p. 72). It must be noted that this is new investment

and does not include re-invested profits or investment routed through HK and not notified to the authorities in Taiwan. Statistics released by Taiwan authorities show that 52.27 percent of the island's investment in the PRC, in the first four months of 2001, was concentrated in Jiangsu province in the Yangtze delta (*Xinhua* News Agency, July 16, 2001, p. 100). This is quite a shift from the early 1990s where 70 percent of Taiwanese FDI was channelled into Guangdong and Fujian (EAAU, 1992, p. 5). Today, more and more Taiwanese are settling in the Yangtze River Delta area. It is estimated that approximately 30,000 Taiwanese are now living in the area, and Taiwanese communities have been formed in Shanghai (*Xinhua* News Agency, July 16, 2001, p. 100). There are also quite a number of Taiwanese in Dongguan, which has become a centre for Information Technology (IT) investment by Taiwanese companies (Tracy, 2000, pp. 175-177). These settlements provide Taiwanese investors a cultural and linguistic affinity with the Yangtze River Delta area and Dongguan. This cultural and linguistic affinity may provide Taiwanese investors, in such areas, a base for the establishment of *guanxi*.

2.11.3 Singaporean Investment in the PRC

During the nineteenth and early twentieth centuries, Chinese immigrants arrived at Singapore from traditional immigrant source areas in the southern coastal provinces of the PRC, such as Guangdong, Fujian, and Hainan (Tan & Yeung, 2000a, p. 440). Historically, Singaporean Chinese have maintained strong linkages with their immediate family members or close relatives in the PRC.

Prior to the 1980s, Singaporean investment in the PRC was minimal, like that of many other countries, because of the fear of Communist China. Since 1980, the level, variety, and extent of investment in the PRC has increased as a result of political and economic changes in the region (i.e., the PRC's economic reforms and the normalisation of diplomatic relations between the PRC and Singapore's neighbouring countries), which provided an environment where investors (non-Chinese and overseas Chinese) were

comfortable conducting business in the PRC (Tan & Yeung, 2000a). During the 1983-1996 period, Singapore invested approximately US\$6 billion in the PRC (Tan & Yeung, 2000a). Singapore's investment in the PRC has steadily increased with approximately US\$8.6 billion invested in the PRC between 1997-1999 (China Statistical Yearbook, 1995-2000).

Early investment in the PRC from Singapore was spatially concentrated in the SEZs of the southern coastal city and provincial areas of Guangdong and Fujian (Tan & Yeung, 2000a; Tan & Yeung, 2000b). These SEZs included Shenzhen, Zhuhai, Xiamen, Shantou, and Hainan. According to Tan & Yeung (2000b, p. 221), the high concentration of Singaporean firms in Guangdong and Fujian reflects in part the close family and *guanxi* ties Singaporean business people have in these two provinces. The significance of *guanxi* for facilitating Singaporean investment in the PRC is highlighted by Tan and Yeung (2000a, p. 444) in their study of 22 Singaporean firms in Hainan. They argued that *guanxi* arising from family ties and from individuals with shared experience, such as classmates, is a crucial business advantage. In addition, other characteristics of this ethnic advantage, such as commonality of language, enabled commercial barriers for Singaporean firms in Hainan to be reduced. In short, economic *guanxi* emanating from this ethnicity linkage ensured preferential treatment for Singaporean firms in Hainan province (Tan & Yeung, 2000a; Tan & Yeung, 2000b, p. 448).

This suggests that HK, Taiwan and Singapore's FDI relationship with the PRC, in relation to the Chinese provinces of Guangdong, Fujian, and Hainan respectively, in part, has been facilitated by a cultural affinity, which enabled the establishment of *guanxi*.

Although the cultural affinity of HK, Taiwanese, and Singaporean investors with the mainland may provide an initial advantage in the development of *guanxi* over non-Chinese investors, it does not suggest that non-Chinese investors are unable to develop *guanxi* and obtain its benefits. This thesis now examines the importance of *guanxi* by

demonstrating that HK, Taiwanese, and Singaporean investors in the PRC may be able to obtain competitive advantages by utilising *guanxi*.

2.12 The Competitive Advantages of *Guanxi*

Hong Kong and Taiwanese investment practices in the PRC often differ in character from the practices of non-Chinese investors. Like others, many HK and Taiwanese investments are large and have been negotiated with central government officials in Beijing; nevertheless many of them implemented a strategy different from that of other foreign multinationals (Smart & Smart, 1991, p. 216; Hsing, 1998, p. 130). Hong Kong and Taiwanese investments are usually directed at small scale enterprises up to US \$10 million, (Tracy, 1995, p. 8; Hsing, 1998, p. 130) and on occasions up to US \$30 million, the establishment of which are negotiated with local authorities through pre-existing *guanxi* networks (Smart, 1993, p. 398; Hsing, 1996; Hsing 1998, p. 130). The strategic decision to establish small scale enterprises through pre-existing *guanxi* networks enables the HK and Taiwanese investors to avoid the delays and conflicts that may arise in dealing with the central and provincial bureaucrats (Beamish & Wang, 1989, p. 59; Tracy, 1995, p. 7; Hsing, 1996; Hsing, 1998, p. 130). Some medium to large-sized Taiwanese investors would even split their investment into a number of smaller projects to avoid the involvement of higher level governments (Hsing, 1998, p. 130). In other words, they circumvented the Chinese bureaucracy by implementing such a strategy. The pre-existing *guanxi* networks, utilised by HK and Taiwanese investors in a particular locale, furnish them with initial advantages, which may include introductions to local officials who have the power and authority to expedite the Chinese bureaucratic inefficiencies and overcome resource shortages (Weidenbaum & Hughes, 1996, p. 16; Tracy, 1995, p. 8; Hsing, 1998, p. 130). Thus, by utilising *guanxi* many HK investors may establish their enterprises in as little as three months, compared with the many years of negotiations commonly involved in ventures concluded by non-Chinese investors

(Smart, 1993, p. 398). In addition, through the utilisation of *guanxi*, many Taiwanese and Singaporean investors are able to implement and establish their ventures more quickly than investors without the necessary *guanxi* (Hsing, 1998, p. 130; Tan & Yeung, 2000a).

Although overseas Chinese may initially be at an advantage when developing *guanxi* because of cultural and ancestral ties, it does not suggest that non-Chinese investors are unable to obtain the benefits of *guanxi* (Tsang, 1998; Bjorkman & Kock, 1995). For example, the Coca Cola Company in its pursuit of entering the beverage market in the PRC chose Robert Kuok's Kerry Group as a joint venture partner. The extensive *guanxi* network of Robert Kuok was the main reason why the Coca Cola Company chose the Kerry Group as a joint venture partner. As John Farrell, president of Coca Cola China Ltd put it:

What could take us 18 to 24 months in China, Robert Kuok's Kerry Group could do in 2 months. Robert Kuok's whole life has been built around building networks. The Kerry Group's ability to do things quickly is incredible (Tanzer, 1997).

Thus, through *guanxi*, non-Chinese and overseas Chinese investors in the PRC may be able to expedite the Chinese bureaucracy, gain access to scarce resources and opportunities, and establish businesses in less time than ordinarily would be the case, possibly resulting in a competitive advantage.

The term competitive advantage is used to describe a position where a business achieves and maintains a unique and valuable competitive position (Ball et al 2002, p. 483). Businesses create competitive advantage by perceiving or discovering new and better ways to compete in an industry and bringing them to the market, which is ultimately an act of innovation. *Innovation* here is defined broadly, to include both improvements in technology and better ways or methods of doing things (Porter, 1990, p. 45; Ball et al 2002, p. 483), which can include:

- (1) The introduction of a new good that is one which consumers are not yet familiar-or of a new quality good (Schumpeter, 1936, p. 66; Porter, 1990, p. 45).

(2) The introduction of a new method of production, that is one not yet tested by experience in the branch of manufacture concerned, which need by no means be founded upon a discovery scientifically new, and can also exist in a new way of handling a commodity commercially (Schumpeter, 1936, p. 66; Porter, 1990, p. 45).

(3) The opening of a new market, that is a market into which the particular branch of manufacture of the country in question has not previously entered, whether or not this market has existed before (Schumpeter, 1936, p. 66; Porter, 1990, p. 46).

(4) The conquest of a new source of supply of raw materials or half manufactured goods, again irrespective of whether this source already exists or whether it has first to be created (Schumpeter, 1936, p. 66; Porter, 1990, p. 46).

(5) The carrying out of the new organisation of any industry, like the creation of a monopoly position or the breaking up of a monopoly position (Schumpeter, 1936, p. 66; Porter, 1990, p. 47).

There are a number of ways that these innovative competitive actions can be adapted to encompass the advantages of *guanxi*. For example, through the employment of *guanxi* access to opportunities may be forthcoming. In other words, *guanxi* may enable an existing market to be opened that ordinarily would be denied. In addition, *guanxi* enables business access to scarce resources, which equates to the conquest of a new source of supply. Furthermore, the expedition of the Chinese bureaucracy through *guanxi* may enable businesses to complete processes or establish a business in less time than otherwise would be possible, which may result in the creation of a monopoly position. As a result of *guanxi*, these businesses may become first movers. A first mover is a firm that initiates a competitive action (Porter, 1985, pp. 79-80; Porter, 1990, pp. 47-48; Hitt et al 1996, p. 151). There are a number of competitive advantages that can be obtained by a business that initiates a competitive action. The following is a list of the possible advantages of a first mover:

(1) Successful completion of a competitive action enables businesses to earn above average returns until other competitors are able to duplicate or respond effectively to the competitive action (Porter, 1985, p. 188; Porter, 1990, pp. 47-48).

- (2) First movers have the ability to obtain customer loyalty. Thereby increasing the difficulty responding businesses will encounter in capturing customers (Porter, 1985, pp. 186-187; Porter, 1990, pp. 47-48; Hitt et al 1996, p. 151).
- (3) A first mover may pre-empt an attractive market position, forcing competitors to adopt less desirable ones (Porter, 1985, p. 186-187; Porter, 1990, pp. 47-48).
- (4) First movers may be able to lock in later sales if switching costs are present (Porter, 1985, pp. 186-187; Porter, 1990, pp. 47-48).
- (5) A first mover may gain unique channel access for a new product or product generation (Porter, 1985, pp. 186-187; Porter, 1990, pp. 47-48).
- (6) First movers may be able to gain a cost or differentiation advantage if there is a proprietary learning curve in value activities that are affected by the early move (Porter, 1985, pp. 186-187; Porter, 1990, pp. 47-48).
- (7) A first mover may be able to define the standards for technology or other activities, forcing later movers to adopt them (Porter, 1985, pp. 187-188; Porter, 1990, pp. 47-48).
- (8) First movers may enjoy institutional barriers against imitation (Porter, 1985, pp. 187-188; Porter, 1990, pp. 47-48).

However, a business's ability to obtain and sustain these competitive advantages through the employment of *guanxi* depends on how costly or difficult it is for competing businesses to duplicate (Porter, 1985, p. 20; Porter, 1990, pp. 49-53). The more difficult and costly it is to duplicate first mover competitive actions, the longer the business may receive the competitive advantages of being a first mover (Porter, 1985, p. 20; Porter, 1990, pp. 49-53; Hitt et al 1996, p. 152). The possibility of the advantages derived from *guanxi* leading to a competitive advantage warrants analysis, and it would not be complete without an examination of the disadvantages of *guanxi* perceived by the research participants.

2.13 The Sustainability of the Competitive Advantages Obtained From *Guanxi*

Tsang (1998, p. 68) contends that *guanxi* must be rare and difficult to imitate for a competitive advantage to be sustained. It is rare in the sense that this *guanxi* is not only developed with one individual but with a number of individuals in areas which may

include the central ministries in Beijing, government bodies at the provincial and local levels, and the customer. Thus, it is important to exert influence at different levels and in different organisations (Tsang, 1998, pp. 68-69). This does not imply that a scatter gun approach is employed, as the individuals selected for the development of *guanxi* must possess the power to influence decisions that will have an impact on the business. An alternative to developing *guanxi* with a number of individuals in differing organisations is to develop *guanxi* with a handful of top officials in Beijing. In this case, the *guanxi* is also likely to be rare because not many businesses are able to approach these top cadres (Tsang, 1998, p. 68). Not only does developing *guanxi* with a number of individuals in differing organisations cause *guanxi* to be rare, it also makes it difficult for a competitor to imitate.

Tsang (1998, p. 69) argues that when competitors try to imitate the *guanxi* developed, the time compression diseconomies factor needs to be taken into consideration. The time compression diseconomies factor expresses the law of diminishing returns when time, as an input, is held constant. Thus, over a particular time interval, the quality of *guanxi* that can be developed is unlikely to be proportional to the efforts invested in cultivating it. Establishing a *guanxi* base may be simple, but it takes time to develop *ganqing*, which according to Tsang (1998) is a key determinant of the quality of *guanxi*. A one year relationship is hardly comparable to a ten year one. Therefore, competitors may find it difficult to imitate long-standing *guanxi*.

Even if *guanxi* may be rare and difficult to imitate, a businesses' competitive advantage obtained through *guanxi* may not be sustainable. The reason, as Tsang (1998, p. 70) argues is that individuals within a business are mobile. He contends that one way to reduce the mobility of *guanxi* is to convert interpersonal *guanxi* into interorganisational *guanxi*. For example, if the knowledge of an employee is not recorded by the business, the business will lose that knowledge once the employee leaves. Similarly, it is not uncommon for a sales person to bring some of their clients with them

to a new employer. This suggests that the sales person's former employer failed to transform some of the customer *guanxi* from an individual to the business level. An acid test of the strength of a businesses organisational *guanxi* is determined by how far the businesses' operations are affected by the departure of an employee who has strong individual *guanxi* (Tsang, 1998, p. 71).

On the issue of transferring interpersonal *guanxi* into organisational *guanxi*, one of the research participants in Tsang's study, who is a Chinese general manager of a wholly foreign owned company in the PRC, stated:

Whenever we employed a local staff member that possessed some valuable *guanxi* with say a senior manager of a state enterprise. I and other senior staff would try to become involved in the *guanxi*, not only with that senior manager but also with other key decision makers in that state enterprise. This was achieved through organising regular meetings and social activities for the staff of the two companies (Tsang, 1998, p. 71).

This comment not only suggests ways at transforming interpersonal *guanxi* into organisational *guanxi* but also highlights the importance of developing *guanxi* with a number of individuals in one organisation.

The competitive advantages obtained through *guanxi* may not only be sustainable because of the mobility of employees within a business but because individuals outside the business, such as Chinese officials, are also mobile. For example, an individual of business A has developed *guanxi* with individual C in a Chinese government department. If C leaves his or her position for one reason or another, where he or she is no longer able to be of assistance to business A, then the competitive advantage of that *guanxi* may not be sustained. Thus, it is proposed that to sustain the competitive advantages of *guanxi*, individual *guanxi* should be transformed into interorganisational *guanxi* and *guanxi* should be developed with a number of individuals of differing authority in the same government department or business. It must also be pointed out that to rest on one's laurels and not maintain and improve the *guanxi* developed may make it easier for competitors to replicate (Porter, 1990, p. 51).

2.14 The Disadvantages of Being a First Mover

Although the advantages of *guanxi* may enable a business to be a first mover and gain a competitive advantage over their rivals, being a first mover, according to Porter (1985, pp. 189), is not without its disadvantages. These disadvantages stem from two broad sources, the costs of pioneering and the risk that market conditions will change, which include the following:

- (1) A first mover often bears substantial pioneering costs, which include educating buyers, investing in the development of complementary products, developing infrastructure in areas such as service facilities and training.
- (2) A first mover bears the risk of uncertainty over future demand. It must put capacity in place first, while later movers can base their decisions on more current information.
- (3) First movers are vulnerable if buyer needs change and its technology is no longer valued. A first mover's reputation advantage may also be eliminated if buyer's need change.
- (4) A first mover may be at a disadvantage if early investments are specific to the current technology and can not be easily modified for later generations.
- (5) Technological discontinuities work against the first mover by making obsolete its investments in the established technology. Technological discontinuities are major shifts in technology that a first mover may be ill-prepared to respond to given its investment in the old technology.
- (6) A first mover exposes itself to followers who may be able to imitate the innovation at lower costs than the cost of innovating (Porter, 1985, pp. 189-191).

Although the disadvantages of a first mover may stem from pioneering costs or market factors, this thesis is only concerned with those costs that relate to *guanxi*, such as the costs of developing *guanxi* and maintaining that *guanxi*. These costs can be likened to Porter's (1985) pioneering costs of initiating the competitive advantage. The development of *guanxi* is the initial step in the process that may see the advantages of *guanxi* becoming competitive advantages for Australian businesses operating in the PRC.

2.15 Cost Benefit Analysis of *Guanxi*

Tsang (1998, p. 68) argues that before developing *guanxi* one should conduct a cost benefit analysis because time, effort and money are required to develop and maintain *guanxi*. Tsang's (1998) argument embodies Yang's (1994) notion of the 'art of *guanxi*', which entails the exchange of gifts (*liwu*), banquets (*yanhui*), and favours (*bangmang*). However, it is difficult to reduce the elements of the 'art of *guanxi*' to a cost benefit analysis. Even though it may be simple to place a dollar value on the cost of a tangible object such as a gift or banquet, how does one place a dollar value on a favour and relate it to the benefits of facilitating access to the bureaucratic process, safeguarding a business from bureaucratic interference and gaining access to invaluable information or to scarce resources and opportunities in an economy encompassed by uncertainty? A dollar value may be given to the time saved in expediting the Chinese bureaucracy to obtain certain benefits by valuing an hour saved at average hourly earnings of the business operation (Becker, 1976, p. 510). But that crude method can not calculate a dollar value for the social benefits an individual receives from cultivating and reinforcing relationships through the 'art of *guanxi*'.

A dollar-based cost benefit analysis of the 'art of *guanxi*' will not give a true indication of the value of all the benefits received through *guanxi*. Engaging in cost benefit analysis of the usual kind, moreover, may itself unduly increase the costs of the business operation. This is not arguing that developing and maintaining *guanxi* through the 'art of *guanxi*' is not a cost, but it is merely pointing out that developing and maintaining *guanxi* may not be reduced to a cost benefit analysis.

2.16 Summary

This chapter examined the Chinese concept of *guanxi* and the complexities of *guanxi*, which include the history of *guanxi* post-1949, *guanxi* and its workings, the development and maintenance of *guanxi*, the difference between social and economic *guanxi*, *guanxi*

exchange, the obligations and reciprocal nature of *guanxi*, *mianzi*, the gift economy in the PRC, and existing empirical research on the importance of *guanxi* in conducting business with the PRC.

It also highlighted the significance of *guanxi* in facilitating Singaporean investment in Hainan, Taiwanese investment in Fujian, and HK investment in Guangdong. In addition, it pointed out that through the employment of *guanxi* foreign businesses may be able to obtain certain advantages, which include expedition of the Chinese bureaucracy, and access to scarce resources and opportunities. These advantages may enable foreign investors to obtain first mover competitive advantages in the PRC. Furthermore, this Chapter indicated that the sustainability of the competitive advantages obtained through *guanxi* not only depended on *guanxi* being rare and difficult to duplicate but also depend on an employee's *guanxi* being transformed into organisational *guanxi* and making certain the business is not dependent on any one individual's *guanxi* in areas, such as the Chinese bureaucracy. Moreover, it analysed the disadvantages of being a first mover, which stem from either pioneering costs or market factors. This analysis focused on the pioneering costs in relation to the development and maintenance of *guanxi*, which demonstrated that applying a cost benefit analysis to the 'art of *guanxi*' may not be the most appropriate method to ascertain the costs of developing and maintaining *guanxi*.

Observing that *guanxi* plays a significant role in rewarding non-Chinese and overseas Chinese investors in the PRC with competitive advantages, this thesis is led into the theoretical field of New Institutional Economics, which is employed to determine the applicability of Guthrie's (1998) argument, that the salience of *guanxi* is in decline because of a move to a rational legal system in the PRC and the increasing level of competition where Western economic principles have come to the fore, to Australian businesses and to examine the role and importance of *guanxi*. The following chapter

considers Agency Theory and Transaction Cost Economics that come under the rubric of New Institutional Economics.

CHAPTER THREE: THE COMPETITIVE ADVANTAGES OF *GUANXI*: A TRANSACTION COST THEORY PERSPECTIVE

3.1 Introduction

This Chapter examines the commonalities and differences among elements of the New Institutional Economic theories of Transaction Cost Economics and Agency Theory. It develops the justification for employing Transaction Cost Economics in the analysis of *guanxi* based economic exchange. In addition, given the assumption that all economic transactions are governed by efficacious rules of law (Williamson, 1985, p. 20), the legal framework of the PRC and the foreign investment legal framework of the PRC is briefly reviewed. Furthermore, in identifying how a legal system of a country is a cost driver for a business, this Chapter discusses the notion that *guanxi*, with its built in institutional constraint *mianzi*, may be an alternative to the market, hybrid, and hierarchies typology of transaction governance.

3.2 The New Institutional Economics

Since the 1950s a new class of theories about economic organisation have emerged, these theories are collectively referred to as the New Institutional Economics (NIE) (Coase, 1984, pp. 229-231; Nilikant & Rao, 1994, p. 649). New Institutional Economic theories frame the study of organisations in terms of contracting, whereas traditional microeconomics views all economic transactions either as market exchanges or departures from them. New Institutional Economic theories claim that non-market modes of economic organisation exist not necessarily as 'market failures' but as potentially more efficient modes of organisation under similar circumstances (Nilakant & Rao, 1994, p. 649). Two streams of the literature - Agency theory and Transaction Cost Economics exist within NIE. Nilakant and Rao argue that:

both of the streams adopt a contractual framework, but differ in their study of contracts. One stream referred to as agency theory, proposes that problems of organisation arise when principals delegate tasks to agents since they neither have the time nor the resources to complete the task themselves. As a result, agents have opportunities to misrepresent information and divert resources to their private use. Thus, principals have a need to monitor agents or induce them to co-operate by designing incentive schemes (Nilakant & Rao, 1994, p. 649).

The main branch of Agency theory, Principal-agent, focuses on the design of *ex-ante* employment contracts and information systems (Jensen & Meckling 1976; Brickley et al 1997, p. 154). The other stream of NIE, transaction cost economics, focuses on the computing, writing and enforcement of contracts. According to Williamson (1988, p. 567), the agency theory of principal-agent (hereafter, often abbreviated as AT) and transaction cost economics (hereafter, often abbreviated as TCE) are mainly complementary. However, before accepting Williamson's formulation, the commonalties and differences between AT and TCE are discussed.

3.3 Commonalties of Agency Theory and Transaction Cost Economics

Transaction Cost Economics and AT are very similar in that they adopt an efficient-contracting orientation to economic organisation, and both regard the firm as a production function geared to profit maximisation (Williamson, 1988, p. 569). Transaction Cost Economics assumes that human beings are subject to 'bounded rationality' and are given to opportunism (Williamson, 1988, p. 569). Bounded rationality is defined as behaviour that is 'intendedly rational, but only limitedly so' (Simon, 1976, p. xxviii). Opportunism can be defined as:

self-interest seeking with guile. This includes but is scarcely limited to more blatant forms, such as lying, stealing, and cheating.... More generally, opportunism refers to the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse (Williamson, 1985, p. 47).

Agency theory similarly assumes that if both parties to a relationship are utility-maximisers, there is good reason to believe that the agent or the principal may deviate from the contract and take self-interested actions or 'moral hazard' (Jensen & Meckling,

1976, p. 308; Brickley et al 1996, p. 140). Thus, opportunism and ‘moral hazard’ are similar (Williamson, 1988, p. 570). In addition, AT and TCE normally assume risk-neutrality rather than impute differential risk aversion to the contracting parties. Both AT and TCE maintain that the board of directors of a firm arises endogenously as a control instrument (Williamson, 1988, p. 569). The board, as prescribed by Fama (1980, p. 293), is an instrument by which managers control other managers. Despite the commonalities between AT and TCE, however, differences are evident. These are highlighted in the following section.

3.4 Differences of Agency Theory and Transaction Cost Economics

Transaction Cost Economics regards the transaction as the basic unit of analysis (Commons, 1931, pp. 651-653). Agency theory, on the other hand, focuses on the individual as the unit of analysis by recognising that most firms are simply legal fictions that serve as a nexus for a set of contracting relationships among individuals (Jensen & Meckling, 1976, p. 310). Transaction Cost Economics’ focus on the transaction as the basic unit of analysis has led to examination of the dimensions according to which transactions differ (e.g., asset specificity) and different governance structures (e.g., market or hierarchy) (Bergen et al 1992, p. 8). In contrast, AT’s focus on the agent has led to a concentration on individual differences between agents (Bergen et al 1992, p. 8). Transaction Cost Economics also adopts an incomplete-contracting view of transactions between principal and agent; thus it emphasises transaction costs, which include the direct costs of:

- (a) obtaining the information that the various parties to the contract need to assess the relevant quantities and qualities of what is transacted and more generally the benefits and the costs of the contract,
- (b) negotiating among parties to reach an agreement on the provisions of the agreement, and

(c) communicating all such provisions to all the relevant agents (Nabli & Nugent, 1989, p. 36).

Nabli and Nugent (1989, p. 36) distinguish between *ex ante* and *ex post* transaction costs. Among the former are the indirect costs arising from the contract selection process, including those of generating the relevant information and of drafting, negotiating, and safeguarding the agreement. According to Nabli and Nugent (1989, p. 36), *ex post* transaction costs arise because contracts in the ‘faceless’ market are typically grossly incomplete. *Ex post* transaction costs include the following:

- (a) formal legal action with respect to disputes and the establishment and operation of governance procedures,
- (b) dealing with the maladaptation of the actual provisions of the contract, including the renegotiation of contracts,
- (c) monitoring the contracts, and
- (d) bonding the parties to continue to work together (Nabli & Nugent, 1989, p. 36).

The distinct orientation of TCE is to reduce *ex post* transaction costs by aligning transactions with the appropriate governance structures (Williamson, 1988, p. 572). By way of contrast, AT adopts an *ex ante* view of the principal and agent relationship. The emphasis of the agency theory of principal-agent is on minimising *ex post* costs through the *ex ante* alignment of incentives (Bergen et al 1992, p. 8). *Ex ante* agency costs include:

- (a) the monitoring expenditures by the principal,
- (b) the bonding expenditures by the agent, and
- (c) the residual loss (focal point of AT) (Jensen & Meckling, 1976, p. 308).

The residual loss is defined as the dollar equivalent of the loss from trade that results from the divergence of interest in the agency relationship (Brickley et al 1996, p. 139).

The above discussion indicates support for Williamson’s proposition that AT and TCE are complementary despite their differences. Yet notwithstanding the

commonalities, the focus of this thesis on determining whether Australian businesses are able to economise on transaction costs through *guanxi* based economic exchange lends itself to the employment of the New Institutional Economic theory of TCE, with its concentration on the transaction as the unit of analysis.

3.5 Transaction Cost Economics

Williamson (1979, p. 245) argues that the criterion for organising commercial transactions is assumed to be the strictly instrumental one of cost economising. Essentially this consists of two parts: economising on production costs and economising on transaction costs. Due to TCE's focus on the transaction as the unit of analysis, this thesis only considers economisation of transaction costs. Williamson (1979, p. 246) points out that a shift from one governance structure to another may permit a simultaneous reduction in the expense of both writing a complex contract and executing it effectively in an adaptive, sequential way by attenuating opportunism; in other words, by economising on transaction costs. Williamson identifies two transaction governance structures:

(1) Market Governance: Classical Contracting. Market governance is the main governance structure for standardised transactions of both occasional and recurrent contracting.

(2) Transaction-specific Governance: Relational Contracting. The two types of transactions for which specialised governance structures are commonly employed are recurring transactions of the mixed and highly idiosyncratic kinds. The non-standardised nature of these transactions makes primary reliance on market governance hazardous, while their recurrent nature permits the cost of the specialised governance structure to be recovered. Two types of transaction specific governance structures for intermediate-production transactions can be distinguished: bilateral structures, where the autonomy of the parties is maintained, and unified structures, where the transaction is removed from the market and organised within the firm (Hierarchical Governance Structure) (Williamson, 1979, pp. 248-250).

According to Williamson (1979), shifting from a market governance structure to a hierarchical governance structure may economise on transaction costs. This is based on

the assumption that individuals within a hierarchy are not self-seeking actors, though, Williamson (1979, p. 234) also acknowledges that individuals within a hierarchy sometimes are. Goshal and Moran (1996) argue that the organisation will only be able to ascertain whether individuals behave opportunistically after the transaction is brought within the hierarchy. This is assuming that opportunism can be detected. If individuals are opportunistic then this behaviour poses a cost to the firm, a transaction cost. The firm acknowledging the opportunistic behaviour implements a monitoring and incentive system to increase the costs of opportunistic behaviour. Even though the system may be effective in curtailing some opportunistic behaviour, it will not deter all. Goshal and Moran (1996, p. 23) contend that individuals who are not deterred by the increased cost of opportunism may continue to be opportunistic in a manner that may make it more difficult and costly for the firm to detect and control. As the transaction costs for the hierarchical form of governance increase the firm may become progressively uncompetitive (Goshal & Moran, 1996, p. 26). In addition, if the managers of the firm become preoccupied with attenuating opportunism they may become distracted from the main task of running the business (Goshal & Moran, 1996, p. 34). Consequently, Williamson's (1979, p. 234) assumption that a shift from a market governed transaction to a hierarchically governed transaction may permit a reduction in both transaction costs and opportunism proves to be fallible.

Transaction Cost Economics has been criticised for assuming only two structural alternatives: market-based exchange or internalisation through hierarchy (Standiford & Marshall, 2000, p. 28). In response, Williamson (1991, p. 269) suggests a third alternative in which relational contracts are used to fill the gap between markets and hierarchies. This alternative hybrid mode, includes various forms of long term contracting, such as reciprocal trading, regulation, and franchising (Williamson, 1991, p. 280). Williamson (1991, p. 280) points out that the neo-classical contract law of hybrid governance differs from both the classical contract law of markets and the forbearance contract law of

hierarchies. Neo-classical contract law is more elastic than classical contract law and more legalistic than forbearance contract law. Classical contract law, according to MacNeil (1974, p. 738), applies to the ideal transaction in law and economics' "sharp in by clear agreement; sharp out by clear performance". According to Williamson (1991, p. 271), neo-classical contract law relieves parties from strict enforcement, as the contract is mediated by an elastic contracting mechanism. In other words, the hybrid form relies on contractual safeguards and increased information disclosure to reduce opportunistic behaviour (Standifird & Marshall, 2000, p. 28; Williamson, 1991, p. 280).

Notwithstanding the differing forms of transactional governance, it is the level of asset specificity involved in the transaction that determines which governance structure is to be employed to reduce opportunistic behaviour and economise on transaction costs. Asset specificity refers to the degree to which an asset can be re-deployed to alternative uses and by alternative users without sacrifice of product value (Williamson; 1991, p. 281). Six kinds of asset specificity have been made:

- (1) Site specificity, as where successive stations are located in a cheek-by-jowl relation to each other so as to economise on inventory and transportation expenses;
- (2) Physical asset specificity, such as specialised dies that are required to produce a component;
- (3) Human asset specificity that arises in learning by doing;
- (4) Brand name capital;
- (5) Dedicated assets, which are discrete investments in general purpose plant that are made at the behest of a particular customer; and
- (6) Temporal specificity, which is akin to technological non-seperability and can be thought of as a type of site specificity in which timely responsiveness by on-site human assets is vital (Masten et al 1991, pp. 8-11).

At moderate levels of asset specificity, the hybrid form incurs fewer transaction costs than market-based exchange by reducing incentives to act opportunistically (Williamson, 1991, pp. 280-281; Luo, 2000a, p. 44; Standifird & Marshall, 2000, p. 28). As a result,

the hybrid form of governance transpires as the cost economising transaction at moderate levels of asset specificity (Williamson, 1991; Luo, 2000a; Standifird & Marshall, 2000). Conversely, at high levels of asset specificity hierarchies are superior to the hybrid form in their ability to reduce threat of opportunism by allowing for incomplete contracts. Incomplete contracts reduce transaction costs while increasing access and allowing for internal dispute resolution and alternative incentive options. Consequently, hierarchies emerge as the most cost economising form over both market exchange and the hybrid form at higher levels of asset specificity (Williamson, 1991; Luo, 2000a, Standifird & Marshall, 2000). Thus, as asset specificity increases, the costs of opportunism increases, thus heightening the need for increased structural protection.

Despite Williamson (1991) addressing the criticism levelled at TCE, through the introduction of a hybrid form amongst market and hierarchies, Boisot and Child (1988, p. 507), and Standifird and Marshall (2000, p. 28) argue that the market and hierarchies framework of TCE provide a too limited set of transactional options to account adequately for many of the organisational problems encountered in a developing country, such as the People's Republic of China (PRC).

Despite the PRC's spectacular economic development for much of the last two decades, uncertainty continues to plague the business environment of the PRC (Ahlstrom, Bruton & Lui, 2000, p. 5). According to Ahlstrom, Bruton and Lui (2000, p. 5), this uncertainty stems from the lack of institutions that support and legitimise private businesses, such as property rights, contract laws, contract enforcement, and numerous commercial conventions, which are reviewed in the next section.

3.6 The Legal Framework of the PRC

Most studies of exchange assume that efficacious rules of law governing contractual and legal disputes are applied by the courts in an informed, sophisticated and low cost way (Williamson, 1985, p. 20). However, as noted in the preceding discussion, not all

countries are at a point where economic transactions are governed by formal institutions of support. The PRC is one such country, where it is not always clear to whom disputing parties might turn in the event of legal disputes. This reflects the turbulent history of the Chinese legal system, where the Communist Party in the late 1950s attacked the laws enacted to replace the pre-liberation law because of its perceived failure. The perceived failure of the law also resulted in the Communist Party attacking the law during the Cultural Revolution. Those attacks on the PRC's socialist legal system produced a legal situation that by the mid-1970s was characterised by both bureaucratism and unpredictability (Brugger & Reglar, 1994, p. 205). Effectively, the socialist legal system of the 1950s was unable to function because the attacks brought about a system that served legal and political needs, and not necessarily in that order. Even though this system survived the economic reforms of the 1980s (Lubman, 2000, p. 253), the past twenty years has witnessed a number of developments in the PRC's legal system (Wong, 1997, p. 65; Rosen, 1999, p. 200). One of those developments was the establishment of formal training programs by the Supreme People's Court at Beijing University, where judges attend from one to three years (Lubman, 2000, p. 255). Previously, judges were not required to possess legal qualifications but rather a certain political ideology and class background (Lubman, 2000, p. 253). Although this example is not suggesting that such a practice has been eliminated, it is nevertheless highlighting the development taking place to raise standards in the PRC's legal system.

Having briefly indicated the turbulent past of the PRC's legal system, this Chapter now focuses its attention on the legal framework pertaining to foreign businesses in the PRC.

3.7 The Foreign Investment Legal Framework of the PRC

Since Deng Xiaoping initiated economic reform in 1979, officially opening the doors of the PRC to foreign investment through the promulgation of its Joint Venture Law, the

PRC has gradually established a legal framework regulating foreign investment and trade (Luo, 1996, p. 535; Tay & Leung, 1995, p. 156). This legal framework consists of national administrative laws and regulations on various facets of foreign investment and trade, and local regulations and rules concerning, largely, investment incentives and economic preferential treatment in the PRC's provinces and SEZs (Tay & Leung, 1995, p. 156). Together with local rules, several hundred laws and regulations governing foreign investment and trade have been issued. The legal framework has been, and still is, in a state of continual change (Blackman, 1997, p.11). Many of the laws and regulations have been amended or supplanted by other regulations at national and local levels. The fact that economic concessions and preferential treatments for foreign investment are not only provided by national laws and measures but also by local regulations and laws, arouses the possibility of conflict between central and local bureaucrats (Tay & Leung, 1995, p. 158). This possibility arises because the Chinese Constitution does not expressly give any exclusive powers to the central government. It allows local governments at the provincial level to forge regulations and rules, on the proviso that these regulations and rules do not contravene the Constitution or administrative rules and regulations issued by the central government (Tay & Leung, 1995, p. 158). Thus, it is unclear for the parties involved whether locally granted preferential treatments and concessions are legally valid when the central government changes its policies. More importantly, in an environment where officials are granted substantial discretion to interpret regulations, policy uncertainty promotes tendencies among officials to interpret and enforce laws and regulations based on parochial concerns rather than regulatory intent (Potter, 1995, p.175). This obscures the meaning of laws and regulations from the business operators who are required to comply with them (Potter, 1995, p. 176). In addition, the adjudicators that enforce these regulations and laws are not only subjected to the Communist Party leadership, they are also subjected to local government which controls their financial sources (Tay & Leung, 1995, p. 182). This further exacerbates the flexibility in the

interpretation of the laws and regulations that foreign business operators, as well as local Chinese business operators, have to contend with in the PRC.

In a study by Daniels et al (1985, p. 47) data was obtained from interviews with management personnel from eleven United States (US) firms that entered into a joint venture (JV) with Chinese firms during 1979-1983. Several aspects of the PRC's political environment was revealed as having a potentially significant impact on their Chinese joint venture. One concern was the PRC's underdeveloped commercial code and uncertainty surrounding future laws and regulations affecting joint ventures (Daniels et al 1985, p. 53). With numerous amendments and supplements to laws and regulations governing Sino-foreign Equity Joint Ventures (S-fEJV), Contractual (Co-operative) Joint Ventures (CJV), Wholly Foreign Owned Enterprises (WFOEs) and the Foreign Economic Contract Law (1985), it may have been argued that the concerns of foreign investors might have been reduced or eliminated. However, a 1992 survey of American business executives with operations in the PRC revealed that problems with the regulatory environment were still considered to be obstacles to an improved investment climate. Specifically cited were problems with "lack of uniformity and consistency in interpreting and implementing rules and regulations" (China Business Review, 1992, pp. 6-11). Chao et al's (1998, p. 75) research also confirmed that Western executives still perceived that the Chinese laws, government red tape and bureaucracy posed an unfavourable environment for foreign investment. The target sample of Chao et al's (1998, p. 75) study consisted of a number of executives from Chinese corporations, joint ventures, wholly foreign owned ventures, Chinese central and provincial governments and ministries, and Western multinational corporations.

Consistent with Daniels et al (1985) and Chao et al (1998), Zhuang et al concluded that the unreliable legal system is an area where problems are likely to occur, with varying degrees of impact on foreign investment activities in the PRC (1998, p. 611). Zhuang et al based their research on Chief Executives of 22 foreign companies in

the PRC. These foreign companies were involved in a variety of business activities including labour intensive manufacturing, food, drink and restaurant chains, hi-technological manufacturing, investment and properties, services and servicing (Zhuang, 1998, pp. 608-609). The sample companies represented overseas partners from HK (40 percent), United States (US) (20 percent), Japan (10 percent), Taiwan (10 percent), Germany (5 percent), Macau (5 percent), Singapore (5 percent), and the United Kingdom (UK) (5 percent) (Zhuang et al 1998, p. 609). Thus, foreign businesses continue to face an uncertain and unpredictable legal system in the PRC, despite the developments and changes pertaining to foreign businesses.

3.8 The Determinants of the Cost Behaviour of a Business

According to Porter (1985), the legal framework and system of a country is one of the institutional factors that determine the cost behaviour of a business. These institutional factors are known as cost drivers. Porter (1985, p. 70) defines a cost driver as the structural factors that influence a businesses' cost in performing a given activity, such as producing, marketing, delivering and supporting a product or service. These activities are known as value activities. Ten major cost drivers determine the cost behaviour of the value activities of a business:

- (1) Economies of scale. Economies of scale arise from the ability to perform activities differently and more efficiently at larger volume, or from the ability to amortise the cost of intangibles such as advertising and research and development over a greater sales volume.
- (2) Learning. The cost of a value activity can decline over time due to learning that increases its efficiency, which may include such factors as labour efficiency improvement or layout changes.
- (3) The pattern of capacity utilisation. Where a value activity has substantial fixed cost associated with it, the cost of an activity will be affected by capacity utilisation. Fixed costs create a penalty for under-utilisation, and the ratio of fixed to variable cost indicates the sensitivity of a value activity to utilisation.
- (4) Linkages. The cost of a value activity is frequently affected by how other activities are performed. Thus, linkages mean that the cost behaviour of a value

activity cannot be understood by examining that activity alone. Changing the way in which one of the value activities is performed can reduce the total cost of both.

(5) Interrelationships. Interrelationships with other business units within a firm affect cost. The most important for interrelationships is when a value activity can be shared with a sister unit. Sharing a value activity raises throughput in the activity. It reduces unit costs if cost in the activity is sensitive to economies of scale or learning, or if sharing improves the pattern of capacity utilisation because different business units place demands on the value activity at different times.

(6) Integration. The level of vertical integration in a value activity may influence its cost. The cost of an order processing system can be lower if the firm owns its computer and software instead of contracting with a computer service company. However, integration may also raise costs by creating inflexibility.

(7) Timing. The cost of a value activity often reflects timing. Sometimes a business may gain first mover advantages from being among the first to take a particular action.

(8) Discretionary policies. The cost of a value activity is always affected by policy choices a firm makes, quite independently of other cost drivers. Some of the policy choices that tend to have the greatest impact on cost include: product configuration, delivery time, buyers served, wages paid, and human resource policies. Though policy choices always play an independent role in determining the cost of value activities, they also frequently affect or are affected by other cost drivers.

(9) Location. The geographic location of a value activity can affect its cost, as can its location relative to other activities. Locations differ in the prevailing costs of labour, management, scientific personnel, raw materials, and tax levels.

(10) Institutional factors. Institutional factors, including government laws and regulations, tax and other financial incentives, tariffs, and local content rules (Porter, 1985, pp. 70-83).

Cost drivers often interact to determine the cost behaviour of a particular activity, and the relative impact of cost drivers will differ widely among value activities (Porter, 1985, p. 70). Reducing cost drivers may enable a business to obtain a competitive advantage. However, sustaining this competitive advantage depends on how difficult and costly it is for competitors to imitate the actions that reduce the cost drivers (Schumpeter, 1936; Porter, 1985; Porter, 1990, Hitt et al 1996).

As discussed above, the legal system of the PRC is characterised by uncertainty and unpredictability. To rely on such a system would undoubtedly increase a businesses

transaction costs. Higher transaction costs may increase the cost of performing the value activities of a business, possibly resulting in a competitive disadvantage for the business. Alternative measures of support and governance that reduce transaction costs, and possibly provide a competitive advantage, need to be considered. One such alternative to the market, hybrid and hierarchy frameworks of TCE is *guanxi* based exchange (Boisot & Child, 1988; Davies, 1995; Standifird & Marshall, 2000). *Guanxi* based exchange may be thought of as corresponding to a set of ‘obligational contracting relationships’. The interaction of parties to *guanxi* based exchange place the individuals in the equivalent of an infinitely repeated game with a set of people they know and trust (Davies, 1995, p. 161). Transactions are allowed to take place among individuals in the presence of legal and regulatory uncertainty, and asset specificity that would otherwise force the creation of more expensive governance structures (Davies, 1995, p. 161).

3.9 The Trust Inherent in *Guanxi* May Not Attenuate Opportunism

Even though trust is a central tenet of *guanxi*, Granovetter (1985, p. 491) argues that trust is not a sufficient guarantee against opportunism and may even provide occasion and means for opportunistic behaviour on a larger scale than its absence. Moreover, trust engendered by personal relations presents, by its very existence, enhanced opportunity for opportunistic behaviour. In personal relations, it is often the closest individuals that end up being hurt; that person’s trust results in a position far more vulnerable than that of an outsider (Granovetter, 1985, p. 491). For example, certain crimes, such as embezzlement and fraud, are simply impossible for those who do not have relationships of trust that permit the opportunity to act or conspire in an opportunistic manner. This indicates that the higher the level of trust between individuals with *guanxi*, the greater the potential gain from opportunistic behaviour (Granovetter, 1985, p. 491). Although *guanxi* based exchanges have clearly defined standards of behaviour easily policed by the efficient dissemination of information about opportunistic individuals, the temptations

posed by the considerable levels of trust between individuals with *guanxi* is considerable (Hill, 1990, p. 509). Therefore, as there exists a level of trust between individuals with *guanxi* the greater is the potential for opportunistic behaviour (Granovetter, 1985, p. 493).

Even though the reputational effects of *mianzi* may act as an institutional constraint on opportunism that leads to a reduction in transaction costs, the very existence of trust between individuals with *guanxi* may counteract the advantages of *mianzi*. But as Nichols (1991) argues, the existence of trust enables implicit contracts or non-specific contracts to substitute for formal contracts that are expensive to write with detailed performance and monitoring costs. This is evident in the PRC where the preferred way of conducting business is through a verbal agreement between individuals with *guanxi*. If a contract is necessary, more often than not, it will be shorter than Western equivalents because the Chinese prefer to rely on the trust between parties to solve any contractual disputes (Tai, 1988, p. 8). Even though *mianzi* and trust may counteract each other in attenuating opportunism, the trust between individuals with *guanxi* may still enable the economisation of transaction costs. As a result, Australian businesses may be able to obtain a competitive advantage by using *guanxi* and its inherent governance mechanism, *mianzi*, as an alternative to the uncertain and unpredictable institutions of support in the PRC, such as the legal system.

3.10 The Importance of *Guanxi* as an Alternative for Formal Institutional Support

Many scholars support the importance of *guanxi* as an alternative for formal institutional support. Blackman (1997, p. 11) argues that in the PRC *guanxi* rather than the commercial law provides security in conducting business. Blackman is not alone in these findings. Xin and Pearce concluded that private company executives compensated for the lack of continuity and vagueness in the commercial legal framework by cultivating *guanxi* (1996, p. 1658). Xin & Pearce's (1996, p. 1645) research findings were based on a sample, which included departmental heads and directors of key functional areas from 15

SOEs, 8 collective hybrid companies, and 9 private companies. These companies were in the following areas: industrial and textile manufacturing, finance, transport, retail, and wholesale trade (Xin & Pearce 1996, p. 1645).

Yeung and Tung (1996, p. 59) in their research on the importance of *guanxi* concluded that as a relationship it was an important factor for long term business success because of the ambiguity of the PRC's legislation (Yeung & Tung, 1996, p. 59). Nineteen companies surveyed, as follows: HK 11, US 5, Canada 1, Germany 1, and Sweden 1. These companies were engaged in a wide range of industries and services, which included: the manufacture of toys, electronic products and telecommunication equipment; real estate; finance; importing; and exporting (Yeung & Tung, 1996, p. 59). Pearce & Robinson (2000, p. 36) also proposed that foreign businesses must both study the Chinese legal system and develop and maintain relationships with its law enforcers to gain support. This is because Chinese laws and regulations are often vague, change quickly without warning, and are rarely enforced in a consistent or comprehensive manner.

In short, *guanxi* as a relationship oils the wheels of a transaction in the absence of a well developed legal system (Wong, 1997, p. 65; Luo, 1997, p. 54; Coleman, 1993; Nee, 1992, p. 10). This is not to suggest that business dealings, governed by law, are not a common and necessary part of daily life for the Chinese people (Lever-Tracy, et al 1991, p. 78). It is merely to stress the salience of *guanxi*, where its dynamics assist businesses in economising on transaction costs in the uncertain and unpredictable legal environment of the PRC (Lee, 1996, p. 68; Luo, 2000a, p. 44; Standifird & Marshall, 2000, p. 40).

As discussed above, *guanxi* is an alternative to the uncertain and unpredictable legal environment of the PRC. But to what extent is this argument applicable to Australian businesses operating in the PRC, when it is claimed that the salience of *guanxi* is in decline because of the move to a rational-legal system in the PRC (Guthrie, 1998)? To ascertain whether *guanxi* continues to be an alternative to formal institutional support,

which may provide Australian businesses a competitive advantage, Chapter Seven examines the main problem encountered by the research participants whilst conducting business in the PRC and whether the significance of *guanxi* is actually in decline.

3.11 Summary

This Chapter discussed the theories of Transaction Cost Economics and Agency Theory, which form part of the New Institutional Economics. It also gave a brief overview of the commercial legal framework and the foreign investment legal framework of the PRC. In addition, it justified the employment of Transaction Cost Economics in the analysis of *guanxi* based economic exchange. Furthermore, it argued that *guanxi* with its inherent governance mechanism, *mianzi*, is an alternative to market, hybrid and hierarchical forms of governance. In other words, relying on *guanxi* rather than the uncertain and unpredictable legal system of the PRC enables transaction costs to be economised, which may result in a competitive advantage for foreign businesses in the PRC. Moreover, it raised the question whether the salience of *guanxi* is in decline in the face of the implementation of a rational legal system, and a greater emphasis placed on Western economic principles in the foreign business environment. Does this necessarily translate into a reduction or elimination of the first mover and transaction cost competitive advantages an Australian business may receive by utilising *guanxi* in the course of business in the PRC?

The following Chapter outlines the methods employed to undertake an investigation into where and when *guanxi* is important for Australian firms conducting business with the PRC, and whether a decline in the importance of *guanxi* translates into a reduction or elimination of the transaction cost or first mover competitive advantages.

CHAPTER FOUR:

RESEARCH METHODS

4.1 Introduction

This Chapter discusses research design, data collection and analysis techniques used in this study. Specific research procedures are described, with reference to sampling criteria, processes, response rates, and data coding and analysis. Detailed discussion of findings is left until Chapters Five-Nine.

This thesis is a study of the importance and role of *guanxi* for Australian businesses conducting business in the PRC. A number of previous studies on the importance of *guanxi* consist of either mail questionnaires, interviews or a combination of both. Most of these studies are dominated by Overseas Chinese, North American, and European companies and their business executives (Leung et al 1996; Luo, 1997; Bjorkman & Kock, 1995; Bjorkman & Schaap, 1994; Ewing et al 1998). This thesis combines a mail questionnaire administered to Australian business executives based in Australia, excluding South Australia, with semi-structured personal interviews of Australian business executives based in Adelaide, South Australia, and the Chinese cities of Beijing and Shanghai. It tries to reduce the gap in the literature on Australian businesses operating in the PRC. It also tries to discover whether the findings of the semi-structured personal interviews and the mail questionnaire agree, disagree or, at least, do not contradict one another (Miles & Huberman, 1994, p. 266). In addition, it attempts to enhance understanding of *guanxi*.

4.2 Qualitative and Quantitative Data

Qualitative data consist of detailed descriptions of events, people, interactions and observed behaviours; people's experiences, attitudes, beliefs and thoughts. It is collected as open-ended narrative or observation without attempting to place activities or people's

experiences into predetermined, standardised categories (Patton, 1980; Neuman, 1997). Quantitative measurements, on the other hand, rely upon the use of techniques that provide a standardised framework to limit data collection to certain predetermined response categories (Patton, 1980; Neuman, 1997).

Personal interviews fall into both categories depending on whether they are open ended or structured. Document analysis also falls into both categories. It depends on whether the researcher adopts a case study approach, which allows for the selection of examples that illustrate the points the researcher wishes to make, or a content analysis approach which involves systematically coding messages or information from a qualitative source into categories, thus allowing quantitative analysis (Bailey, 1987, pp. 298-300; Chadwick et al 1984, p. 239). Thus quantitative data collection conceptualises reality in terms of variables, and relationships between them. It rests on measurement, and therefore prestructures data, conceptual frameworks and design. It is more standardisable than qualitative approaches, making them easier to replicate. The procedures for the analysis of quantitative data, being well developed and codified, bring some objectivity to the research, in the sense that the results may be less directly affected by the researcher conducting the analysis (Punch, 1998, p. 243). Quantitative data, in other words, enable standardised objective comparisons to be made. Quantitative approaches also do not see context as central, often stripping data from its context (Punch, 1998, pp. 241-242).

Qualitative approaches, on the other hand, are sensitive to context and lived experience where the researcher tries to get closer to what is being studied. The qualitative approach aims at in-depth and holistic understanding of the complexity of the social phenomena being studied, to bring justice to it. Samples in qualitative approaches are often small compared with quantitative approaches. Sampling is guided by theoretical rather than probabilistic considerations, and design pre-structuring is less common. Methods are less formalised than in a quantitative approach, making qualitative

approaches more diverse and more difficult to replicate (Punch, 1998, p. 243). Therefore, qualitative approaches can be employed in a greater range of situations and purposes than quantitative approaches, and can also be easily modified as the study progresses (Punch, 1998, p. 243).

More often than not, quantitative research is concerned with verifying, or identifying causal relationships among concepts that derive from *a priori* theoretical frame. Qualitative research, while being aware of existing theoretical frames for the phenomena under study, prefers the “theory” to emerge from the data (Salasin & Perloff, 1979, pp. 37-38; Miles & Huberman, 1994, p. 27). In short, the quantitative approach employs a logico-deductive reasoning from theory to propositions, concept formation, operational definition, measurement of the operational definition, data collection, hypothesis testing, and analysis. The qualitative approach is an interchange between theory, concepts, and data, with constant feedback and modifications of theory and concepts based on the data collected (Salasin & Perloff, 1979; Miles & Huberman, 1994; Punch, 1998).

It must be taken into consideration when employing a qualitative or quantitative approach that they both lend themselves to bias. The influence of a researcher in the qualitative approach may be a bias. Any bias, however, can be reduced as long as the researcher makes his/her values explicit in the report and builds in a coding verification technique. Quantitative approaches also lend themselves to bias, the bias of the mechanical techniques that they employ (Neuman, 1997, p. 333). This Chapter now discusses the survey research approaches available to gather data and outlines the approaches used in this study.

4.3 Survey Research

To survey is to question people and record their responses for analysis. Manipulation of the situation or condition is not undertaken; people simply answer questions. The answers

are usually summarised in percentages, tables, or graphs. Surveys give the researcher a picture of what many people feel, think, or report doing (Neuman, 1997, p. 31). There are two main types of survey methods: the interview and the questionnaire. Each survey method includes a number of subtypes. For example, interviews may be conducted face to face, by telephone or in group settings. Similarly, questionnaires may be administered by return mail. They may be hand delivered to respondents who are instructed to treat the questionnaire as if it were a self administered interview, or they may be administered to large groups in institutional settings (Chadwick et al 1984, p. 100). The subtypes of each survey method have inherent advantages and disadvantages. (For an in-depth discussion on the advantages and disadvantages of each subtype refer to Chadwick et al 1984; Dooley, 1984; Oppenheim, 1992; Denzin & Lincoln, 1994; Cooper & Emory, 1995). Nevertheless, this thesis employs the following two data collection methods to answer the research questions: (1) semi-structured personal interviews, and (2) mail questionnaires. The employment of two methods in a single study is referred to as triangulation.

4.4 Triangulation

Triangulation of research strategies include method (observation, personal interviews, questionnaire), data source (which can include persons, times, places), researcher (interviewer A, B, C), theory and data type (qualitative or quantitative) (Fielding & Fielding, 1986, pp. 23-24; Rossman & Wilson, 1985, p. 632; Denzin & Lincoln, 1994; Punch, 1998, p. 246; Miles & Huberman, 1994). There is also a distinction between combining methods, combining data and combining findings. Punch (1998, p. 246) points out that there is a continuum of complexity here. At the simpler end, combining findings means that quantitative and qualitative data and methods are not combined, only the results from the two types of inquiry. At the more complex end of the continuum, combining data means that the two types of data from the respective methods are brought together during analysis, and contribute to the findings (Punch, 1998, p. 246). This thesis

brings the results from the semi-structured personal interviews and mail questionnaires together for analysis. Triangulation stripped to its basics should support a conclusion by showing that independent measures agree with, or at least do not contradict, it (Miles & Huberman, 1994, p. 266). However, caution is needed to ensure that research reliability, validity and generalisability are not compromised by inappropriate triangulation.

The effectiveness of triangulation relies on the premise that each method employed has inherent weaknesses and strengths unmatched by other methods, and that the weaknesses in each method are counter balanced by the strengths of another (Brewer & Hunter, 1989, pp. 48-52; Jick, 1979, p. 604; Sieber, 1973, p. 1337; Miles & Huberman, 1994, pp. 266-268; Fielding & Fielding, 1986, pp. 23-26). In essence, triangulation purports to exploit the assets and neutralise, rather than compound, the liabilities. The employment of triangulation in this thesis is based on the propositions of Neuman (1997, p. 337) and Sieber (1973, p. 1345) which advocate that personal interviews contribute to questionnaires in the following manner:

- (1) provide familiarity with issues so that the researcher is able to develop new hypotheses and theories;
- (2) provide verification of questionnaire findings that are out of the ordinary or unexpected, or at least provide persuasive plausibility, by recourse to observations and personal interviews;
- (3) allow statistical relationships to be interpreted by reference to personal interviews;
- (4) permits the validation of a scale or index that has been developed; and
- (5) allows provocative and ambiguous but significant responses to be clarified by revealing the subjective meanings of respondents.

Conversely, Neuman (1997, p. 337) and Sieber (1973, p. 1352-1356) also advocate that questionnaires contribute to personal interviews in the following manner:

- (1) provide verification of personal interviews;

- (2) enlighten personal interviews, or more precisely, the unexpected nature of some questionnaires findings may illuminate personal interviews that may have been inexplicable or misinterpreted;
- (3) demonstrate that a single observation may be generalisable. When the single observation plays an important role in the theoretical structure of the personal interviews, questionnaire data become essential in discrediting the argument;
- (4) questionnaires correct for bias in the interpretation of events;
- (5) assist researchers control for alternative explanations by measuring additional variables; and
- (6) correct for the tendency of researchers to perceive all aspects of the social phenomena as congruent.

In sum, triangulation allows the researcher to be more confident about their results by enhancing the validity of the findings. This is the overall strength of the multi-method design. Despite the advantages of triangulating the findings of semi-structured personal interviews and a mail questionnaire, triangulation also has its limitations. First, triangulation is exceedingly difficult to replicate. Second, triangulation is of no use with the wrong question. Third, if the research is not clearly focused theoretically or conceptually, then triangulation with all its strengths would not produce a satisfactory outcome (Jick, 1979, p. 610). Fourth, according to Fielding & Fielding (1986, p. 31), employing several different methods may increase the chance of error. Finally, triangulation may lead to selective interpretation of data from incompatible procedures (Fielding & Fielding, 1986, pp. 30-32). Triangulation is not an end in itself but rather a better way of defining and analysing problems of social phenomena (Jick, 1979, p. 610). Despite these limitations, this study uses multiple methods to increase research robustness, by identifying and analysing the findings which agree, disagree or, at least, do not contradict one another (Miles & Huberman, 1994, p. 266).

4.5 Research Design

As previously noted, this thesis employs semi-structured personal interviews and a mail questionnaire to gather data.

4.5.1 Interviews

Semi-structured personal interviews are one of a number of sub-types of personal interviews. Personal interview types include: (1) Informal interviewing, characterised by a total lack of structure or control. It is used throughout fieldwork to build rapport and to uncover new topics that may have been overlooked; (2) Unstructured interviewing, is quite different from formal interviewing. Unstructured interviews are based on a clear plan, but are also characterised by a minimum of control over the interviewee's responses. The method allows the interviewee to open up and express their feelings and thoughts about a particular social phenomenon. Unstructured interviews are often employed when there is limited time to carry out field research and when the informants can be interviewed on more than one occasion (Bernard, 1995, p. 209); (3) Structured interviews. In structured interviews all interviewees are asked to respond to nearly as identical a set of stimuli as possible; and (4) Semi-structured interviews. This interviewing technique is most appropriate when time is limited and there is only one chance to interview each respondent. Semi-structured interviews contain much of the unconstrained approach of unstructured interviews, but semi-structured interviews are based on the use of an interview guide. The interview guide is a list of questions that need to be covered in a particular order. There are opportunities to follow leads and probe, but the interview guide is a set of clear instructions. The interview guide allows the researcher to obtain reliable, comparable qualitative data. Semi-structured interviews are most suited when the fieldwork involves interviewing managers, bureaucrats, and elite members of the community in question, as they are accustomed to efficient use of their time (Bernard, 1995, p. 210). Semi-structured personal interviews are most appropriate for this study because it is limited by time, it allows reliable and comparable qualitative

data to be gathered, and it is most suited for interviewing managers. The following section discusses the advantages of personal interviews.

4.5.2 Personal Interviews-Advantages

Personal interviews have inherent advantages over other data collection methods. Personal interviews can be employed to acquire information from people such as non-literate, blind, bedridden or the very old who may not be contacted through other approaches. If the interviewee does not understand a question in the personal interview, the researcher can probe for more information. Personal interviews may also be longer than telephone interviews or questionnaires. For example, it would be very difficult to obtain interviewees who would complete a questionnaire that would take a few hours to complete. However, it is not unusual for personal interviews to last between two and three hours (Bernard, 1995, p. 258). Their greatest value lies in the depth and detail of the information that can be secured. It far exceeds the information secured from telephone and mail surveys. Personal interviews allow the interviewer to gather information on the attitude of the interviewee, the nature of their surroundings, the presence of other people, their body language, their appearance, which would not be obtained through a mail or telephone survey (Bernard, 1995, p. 259; Cooper & Emory, 1995, p. 271). The interviewers also have more control than with mail or telephone surveys (Cooper & Emory, 1995, p. 271). As with all research methods, however, personal interviews are not without some disadvantages.

4.5.3 Personal Interviews-Disadvantages

Personal interviews are subject to the interviewer's emotional state and lack of awareness. Interview data is also subject to recall error, which may be overcome with a tape recorder, and the reactivity of the interviewee to the interviewer (Patton, 1980, p. 157). Personal interviews are costly in both monetary and time terms. These costs are not

only incurred by the interviewer, but also by the interviewee. The costs of personal interviews increase dramatically when interviews are conducted in distant locations. The number of people that can be interviewed is limited as opposed to mail questionnaires and telephone interviews where a large number of respondents may be surveyed. Personal interviews conducted by an individual may run the risk of being taken over by events, such as natural disasters or wars, and the data collected before and after these events may differ greatly (Bernard, 1995, p. 259). Despite these disadvantages, the semi-structured interview method of data collection is employed on the basis of its advantages and because its weaknesses are overcome by the strengths inherent in a mail questionnaire.

4.5.4 Questionnaires

The mail questionnaire is one of several questionnaire techniques that can be adopted for data collection, which include self-administered questionnaires and group administered questionnaires (Bernard, 1995; Cooper & Emory, 1995; Oppenheim, 1992; Dillmam, 1978). Although each technique has its advantages and disadvantages (see Bernard, 1995; Cooper & Emory, 1995; Oppenheim, 1992; Dillman, 1978), the mail questionnaire is most suited for collecting data because this study is constrained by time and resources to effectively self-administer questionnaires throughout Australia, excluding South Australia, and the inability to gather business executives dispersed across Australia into a number of locations to administer a group questionnaire efficiently and effectively. The following section discusses the advantages and disadvantages of a mail questionnaire.

4.5.5 Mail Questionnaire-Advantages

Mail surveys are questionnaires that are sent out by and returned by mail. They allow data to be gathered from a large sample of respondents at a relatively low cost. The respondents of a mail questionnaire all receive the same questions, eliminating

interviewer bias. With a mail questionnaire the researcher is able to ask more complex questions than may be asked in a personal interview. Questions that involve a large list of response categories, or that require much background data, or are hard to follow orally, are often used in a mail questionnaire. Respondents to mail questionnaires report socially undesirable behaviour more freely than they do in face to face interviews. This is due to the respondent not having to impress the interviewer, and the respondent having anonymity and a sense of security (Bernard, 1995, p. 260; Cooper & Emory, 1995, p. 282). Employing a mail questionnaire as a data collection method expands the geographic area of the study at a fraction of the cost and time of personal interviews. It also allows contact with respondents that may be otherwise inaccessible. In a mail questionnaire, the respondent can take more time to gather information, converse with others, or consider their response at length than is typically possible with other forms of interrogation such as telephone interviews (Cooper & Emory, 1995, p. 282). Although the mail questionnaire has numerous advantages, it also has its disadvantages, as discussed below.

4.5.6 Mail Questionnaire-Disadvantages

Mail questionnaires are limited in the type and amount of information that can be secured. They can not generally secure large amounts of information, and the researcher is unable to probe deeply into questions (Cooper & Emory, 1995, p. 283). There is no control over how the respondents will interpret the questions and there is always the danger that respondents will be forced into making culturally inappropriate choices in closed-ended questionnaires. In such a frame of reference, the respondent may be answering a question different from the one being asked (Bernard, 1995, p. 261; Cooper & Emory, 1995, p. 269). Mail questionnaires are also prone to sampling problems. Sampling frames are often flawed. For example, the respondent in question may have changed address without giving notification of a forwarding address. The listed address may not have a telephone number listed to enable confirmation of the correct address,

and if the phone number is listed it may be an incorrect number (Bernard, 1995, p. 261). As a result, response rates are generally low for mail questionnaires, which is the single greatest criticism of questionnaires that must be addressed (Oppenheim, 1992, p. 102).

The quality of information secured depends on the willingness and ability of the respondents to co-operate. Often, people will fail to return a mail questionnaire. There are many reasons why people are unwilling to co-operate. Some people fail to see the significance of the mail questionnaire and they may view the topic in question as too sensitive (Dillman, 1978, p. 63). Even if respondents do participate and return the mail survey, they may not have the knowledge or an opinion on the topic of concern. Often respondents feel compelled to express an opinion even though they may not have one. Even when the respondent returns the completed mail questionnaire, there is no measure of assurance that the respondent who received it is the person who actually filled it out (Dillman, 1978, p. 64). Finally, a respondent may intentionally give false information, and it is difficult to ascertain and identify when these situations have arisen. Therefore as Cooper and Emory state, survey responses should be accepted for what they are: statements by others that reflect varying degrees of truth (1995, p. 263). Although a mail questionnaire has inherent weaknesses, it is employed in conjunction with semi-structured personal interviews to expand the geographic coverage of the study and to increase the sample size at a low cost.

4.5.7 Questionnaire Details

The questionnaire comprises two sections. In the first section, two questions were asked to determine whether the Australian firms conducted business in the PRC, and whether they were majority Australian owned or listed on the Australian Stock Exchange (ASX). This section was used to identify and disregard those that did not conduct business with the PRC and were not majority Australian owned or listed on the ASX. Section two contains specific questions about the Australian businesses' characteristics,

the individual respondents' characteristics, the problems encountered while conducting business in the PRC, and the role and importance of *guanxi* for conducting business with the PRC. Most of the questions in section one are closed-ended questions that produce nominal or categorical data, as they are 'yes' or 'no' questions. One problem with closed-ended questions is that they may suggest ideas that the respondent may not have otherwise held, or force research participants to give simplistic responses to otherwise complex issues and concepts (Cooper & Emory, 1995). Closed-ended questions, nevertheless, are used because they are easier and quicker for respondents to answer and the answers given are easier to code, compare and statistically analyse. In addition, the respondents are more likely to provide answers about sensitive topics and the less articulate or less literate respondents are not at a disadvantage (Neuman, 1997, p. 241). Furthermore, replication of the study with closed-ended questions is easier than a study that mainly comprises open-ended questions.

Section two does include one open-ended question. This type of question has no answer choices that respondents select from. Respondents have to provide answers in their words. Although open-ended questions are difficult to analyse statistically, they are used to obtain precise information that respondents can recall easily, and to allow respondents freedom of expression (Dillman, 1978, pp. 86-87). In addition, open-ended questions permit richness of detail and also reveal a respondent's logic, thought process, and frame of reference (Neuman, 1997, p. 241). A majority of the questions in section two comprise partially closed questions. This is a compromise between closed-ended and open-ended questions. This question type allows for the building of variables and the testing of hypotheses, but does not force respondents into categories that they clearly do not fit. It takes the format of closed-ended questions with unordered answer choices with another category called "other", which allows the respondents to freely express themselves and state the category that is most applicable (Dillman, 1978, p. 88). Although the "other" category may make it difficult for statistical analysis, it may also

provide some useful information. For example, a high number of responses in the “other” category may suggest that something is amiss and that further evaluation must be made before attempting to reach conclusions (Dillman, 1978, p. 92). A number of questions in section two are closed questions with ordered choices. In this type of question structure, answer choices are provided; each is a gradation of a single dimension of some attitude or belief (Dillman, 1978, pp. 86-89). This question type uses a 5-point Likert scale.

As Neuman (1997, p. 241) states, mixing the questions in a mail questionnaire offers a change of pace, ensuring that the respondent does not become bored and there is an opportunity in some questions for the respondents to express themselves freely. A total reliance on closed-ended questions in a mail questionnaire with ordered responses can distort results and a total reliance on open-ended questions may result in a higher non-response rate (Neuman, 1997, p. 241).

The mail questionnaire, more than any other type of questionnaire, requires careful construction, because poor construction may result in a lower response rate (Dillman, 1978, p. 119). Following Dillman (1978, p. 121) and Bernard (1995, p. 278), the questionnaire in this study is produced in booklet form with no questions on the front or back pages. The responses are spaced for easily circling, and lines are used for written responses for any open-ended questions. Where Likert scales are used, they are spaced for easily circling. Dillman (1978, pp. 120-122) and Bernard (1995, pp. 277-280) suggest that a self administered mail survey should be between 10-12 A4 pages long, with no more than 125 questions, otherwise response rates may be lower. The questionnaire in this study is limited to 10 pages and 20 questions. Bernard (1995, p. 277) also suggests that green paper produces a higher response rate than mailed questionnaires using white paper. Therefore, this study used green paper. A white copy of the mail questionnaire is reproduced in Appendix (A).

4.5.8 Mail Questionnaire Pilot Test

It is also particularly important to ensure validity and reliability of the questionnaire employed (Holsti, 1969; Weber, 1990; Carney, 1972). Initially a pilot test was undertaken to determine the *prima facie* validity and reliability of the instrument. In September 1999, the survey was given to an independent group of people consisting of business executives, academics and university students to determine the overall understandability and flow of questions, and to identify any typographical errors. Multiple human coders, as Weber (1990, p. 15) and Holsti (1969, p. 18) contend ensure an acceptable degree of consistency and uniformity in the results, thus, enabling quantitative assessment of achieved reliability (Weber, 1990, p. 15). The responses and comments received were employed to remove any errors in the questionnaire design as well as to check for validity and reliability as outlined below.

According to Cooper & Schindler (2001, p. 210), validity “refers to the extent to which a test measures what we actually wish to measure”. Cooper and Schindler (2001, p. 211) point out that it is difficult to meet the test of validity. However, this may be overcome through: (1) content validity, (2) construct validity, and (3) criterion-related validity (Hoslti, 1969).

Content validity measures the “degree to which the content of the items adequately represents the universe of all relevant items under study” (Cooper & Schindler, 2001, p. 211). Are the results plausible? Are they consistent with other data about the same topic? (Holsti, 1969, p. 143). Determination of content validity is judgmental. In this study, content validity of the questionnaire was tested during the pilot testing stage to ensure that it was measuring what it intended to measure. The errors in design identified in the pilot test were acknowledged and the questions were amended accordingly.

Construct validity answers the question, “What accounts for the variance in the measure?” In other words, it attempts to identify the underlying constructs being

measured and determine how well the test represents them (Cooper & Schindler, 2001, p. 213). This study is not concerned with concurrent validity, as it is not trying to validate the theory underlying the measure.

Finally, criterion-related validity reflects the success of measures employed for prediction or estimation. These are predictive and concurrent validity, respectively (Cooper & Schindler, 2001, p. 213). Predictive validity is concerned with the ability of the instrument to predict events for which evidence is not presently available to the researcher. Concurrent validity is the ability of the instrument to distinguish sources with known differences (Holsti, 1969). This study is not concerned with predictive and concurrent validity, because it is not forecasting its predictive ability, or distinguishing sources with known differences.

Reliability refers to a measure that supplies consistent results. Reliability is also a necessary contributor to validity but is not a sufficient condition for validity (Cooper & Schindler, 2001, p. 215). Thus, to ensure reliability, any questionnaires that contained responses for questions that should not have been answered based on the previous question, were discounted. The pilot test also assessed the elements of reliability outlined by Cooper and Schindler (2001, p. 215-218) - stability, internal consistency, and equivalency.

Stability refers to “the consistency of the results with repeated measurements of the same person with the same instrument or if the same result is obtained on a particular person when repeated one or more times” (Cooper & Schindler, 2001, pp. 215-216). In order to ensure stability in this study, a pilot test was undertaken.

Internal consistency can be assessed using a reliability coefficient which is generally calculated either by using two equivalent forms of the test administered at the same time (split-half technique), or a single form of the test administered twice (Freeman, 1960). These techniques were not used in this study due to the need to keep the questionnaire short to ensure a higher response rate.

Finally, equivalency is the correlation between two parallel forms of a test (Freeman, 1960). Although this type of check question (a question that asks the same thing as a previous question) was not included in the questionnaire, some questions relied on a previous question to be answered in the affirmative before the next question should be answered.

Pre-testing of the qualitative data gathered from the mail questionnaires and semi-structured personal interviews is discussed later in the Chapter under the heading Data Coding and Analysis Procedures.

4.6 Research Procedures

4.6.1 Sampling

Samples can be divided into two groups: those that are based on principles of randomness that come from probability theory and those that are not (Neuman, 1997, p. 204). Probability sampling is based on the concept of random selection- “a controlled procedure that assures each population element is given a known non-zero chance of selection” (Cooper & Schindler, 2001, p. 166). In other words, each population element has an equal chance of being selected (Cooper & Emory, 1995, p. 202; Bernard, 1995, p. 74; Bailey, 1987, p. 87). Probability sampling allows the researcher to generalise from the sample studied to some larger population. The reason for using random sampling is to increase the likelihood that the data collected is representative of the entire population (Patton, 1980, p. 100). In contrast, samples that are not based on probability theory (non-probability sampling) are non-random and subjective. In other words, each element of a population does not have a known chance of being included (Cooper & Emory, 1995, p. 202; Bailey, 1987, p. 92). Although non-probability sampling is more limited, in the sense that the findings can not be generalised beyond the sample (Bailey, 1987, p. 92), non-probability sampling is employed in this study for the following reason: the number

of Australian firms conducting business in the PRC is not known, as it is deemed classified information by the Australian Government.

The problem of representativeness in employing non-probability sampling in this study is overcome by maximising the variation in site selection (Patton, 1980, pp. 101-102). This study maximises the variation in the site selection by conducting semi-structured personal interviews in Adelaide, South Australia, the Chinese cities Beijing and Shanghai, and administering a mail questionnaire throughout Australia, excluding South Australia. Increasing the variation in site selection enables the researcher to have more confidence in those patterns that emerge as common among sites, while at the same time being able to describe some of the variation that has emerged to make programs unique as they adapt to different settings (Patton, 1980, pp. 101-102).

The non-probability sampling techniques employed in this study are judgement and snowball (Neuman, 1997; Bernard, 1995; Cooper & Emory, 1995). In judgement sampling, a decision is made on the purpose a participant is to serve and then they are located. In this study, the research participants are selected on the basis that they conduct business with the PRC. As Bernard (1995, p. 95) contends, it would be pointless to select a handful of research participants randomly from a population and turn them into key informants. In other words, it would be unproductive to randomly select Australian businesses and elicit information on the salience of *guanxi* in the PRC's business environment. In snowball sampling, research participants are asked to name others who would be likely candidates for the study. Snowball sampling is useful in studies of small, bounded, or difficult to find populations, like members of elite groups, or urban migrants from a particular tribal group (Bernard, 1995, p. 97). This technique can generate 'up to 90 percent of all cases of phenomenon of interest', particularly where a formal or informal network operates between people in the sample (Lin, 1976, p. 163).

4.6.2 Mail Questionnaire

The mail questionnaire was designed to elicit research participants' perceptions of the role and importance of *guanxi* for conducting business with PRC, and the problems encountered. The mail questionnaires were sent to businesses located within Australia that advertised in the 1998 Australia-China Business Directory. Not all the businesses that advertised received a questionnaire because they clearly did not conduct business either with or within the PRC. This was determined on the information provided in the companies' advertisement. In addition, any businesses in the Directory that were located in Adelaide, South Australia, did not receive a questionnaire as semi-structured personal interviews were to be arranged with those businesses. Questionnaires were also not sent to executives of Australian businesses who were based in the PRC because there was no guarantee that the survey would reach its intended destination, and if it did, the delivery time can range from a few weeks to months. Nevertheless, those businesses with an address in Beijing and Shanghai were contacted to arrange a personal interview. At the time data was collected for this study, the Australia-China Business Directory 1998 was not a comprehensive data set of all Australian businesses that conduct business with the PRC. As noted previously, a data set of this nature does exist in the realms of the Australian Government, but it is not available to the general public because it is deemed classified information. Therefore, the Australia-China Business Directory 1998 is the only accessible data set of Australian businesses that conduct business in the PRC. In addition, questionnaires were also sent to Australian businesses that conducted business with the PRC, which were selected through industry contacts (Snowball Sampling). In total 76 questionnaires were posted.

The first mailing took place on the 24 October 1999. An introductory letter from the head of the School of Political and International Studies, Flinders University accompanied the questionnaire. Each questionnaire was coded so that after approximately 8 weeks a second and final copy of the questionnaire and letter were sent to all businesses

identified as not responding. The first mailing resulted in 28 responses of which 18 were useable. The second and final mailing received 22 responses of which 14 were useable. Copies of all correspondence relating to the questionnaire can be found in Appendix (B).

Of the 76 questionnaires originally posted, 50 were returned and 32 were useable. The survey was conducted on a final sample of 32, which represented a response rate of 50.8 percent. The response rate was determined by using the following formula from de Vaus (1991):

$$\text{Response Rate} = \frac{\text{Number Returned (50)} - \text{Number Unusable (18)}}{\text{Number in sample (76)} - \text{Ineligible (13)}} \times 100$$

Out of the 18 questionnaires returned and not useable: 1 was returned undeliverable, 8 were removed because they did not conduct business with or within the PRC, 4 were removed because they were wholly foreign owned businesses, and the remaining 5 were removed because it was not their policy to complete questionnaires.

According to Babbie (1983, pp. 226-227) and Bailey (1987, p. 149, p. 162, p. 169), a response rate of 50 percent is adequate for analysis and reporting. A response rate of at least 60 percent is good. And a response rate of 70 percent or more is very good. However, these are only rough guides, and they have no statistical basis. Although the overall response rate was adequate for analysis and reporting, it compares reasonably with previous mail questionnaires on *guanxi*. For example, Park & Luo's (2001) mail questionnaire on *guanxi* and its organisational dynamics for Chinese businesses in the PRC yielded a 32 percent response rate. Fock & Woo's (1998) study on the strategic implications of *guanxi* from a Hong Kong business executive perspective produced a 12.8 percent response rate. Ewing et al's (1998) study on the consequences of *guanxi* from a Sino-Singaporean perspective returned a response rate of 52.7 percent.

4.6.3 Semi-Structured Personal Interviews

The mail questionnaire formed the interview guide for the semi-structured personal interviews, thus allowing for comparability between questionnaire data and semi-structured personal interview data. The businesses that were interviewed in Adelaide, South Australia, and the Chinese cities of Beijing and Shanghai were selected on the basis that they conducted business with the PRC and were at least majority Australian owned or listed on the ASX. The businesses based in Adelaide were selected from the 1998 Australia-China Business Directory. Australian businesses that had representation in Beijing, and Shanghai were selected from the Australian Commercial Interests in China 1999 Directory; the Australian Businesses in Hong Kong 1998 Directory; and the 1998 Australia-China Business Directory. In addition, 'snowball' sampling procedures were used, in which a number of business executives were asked to nominate at least one other business that fitted the requirements of the study (i.e. majority Australian owned business conducting business with or within the PRC) (Lin, 1976; Kidder & Judd, 1986; Cooper & Emory, 1995, p. 230; Neuman, 1997, p. 207; Bailey, 1997, p. 95).

During November 1999-February 2000, 18 semi-structured personal interviews were conducted in Adelaide, South Australia. Throughout March 2000-May 2000, 17 and 16 semi-structured personal interviews were conducted in the Chinese cities Beijing and Shanghai respectively. In total, 51 semi-structured interviews were conducted for this study.

Permission was sought to audiotape interviews with participants. Details of procedures for safeguarding confidentiality and conditions for retaining the audiotapes were included in the letter to participants and interview consent form (see Appendix B). All reasonable attempts were made to avoid leading questions or statements during interviews. Overall this study is based on 83 research participants, which consist of 32 mail questionnaires and 51 semi-structured personal interviews.

4.6.4 Sample Limitations: Mail Questionnaire and Semi-structured Personal Interviews

Other than the general limitations of survey research, as discussed earlier, there are other limitations to consider. The limited scope of the questionnaire should be examined. Whilst 32 Australian businesses conducting business in the PRC were surveyed, the results can not be generalised beyond this sample.

The limitation of using directories and guides that are dated 1998 and 1999 is that they are not a current representation of the Australian businesses that may advertise in the directory or conduct business with the PRC. In the case of the Australia-China Business Directory 1998, some members may not have advertised in this issue but may advertise in the next issue. In addition, the businesses that have advertised in the 1998 issue may no longer be operating or be members of the Australia China Business Council which publishes the directory. These limitations not only apply to the Australia-China Business Council Directory 1998 but to all directories and guides used in this thesis that predate the present, such as the Australian Commercial Interests in China 1999 and the Australian Businesses in Hong Kong 1998 Directory.

4.7 The Characteristics of the Research Participants

Xin and Pearce argue that small Chinese private companies place greater importance on *guanxi* than larger companies (1996, p. 1643). Similarly, Yeung & Tung (1996) contend that small and medium sized foreign firms tend to place greater emphasis on *guanxi* than large ones in the PRC. Research also noted that the importance of *guanxi* differed among industry classifications, the length of PRC business experience of foreign business executives (Yeung & Tung, 1996; Bjorkman & Kock, 1995), and the market entry strategy used by foreign businesses (Luo, 1997). As previous research indicates, a number of variables have been employed in determining the importance of *guanxi* for Chinese private companies and foreign businesses. This study also employs a number of

business and individual characteristics in its analysis, however, these characteristics of the research participants are used solely for duplication purposes of this study, and for comparative purposes of the semi-structured personal interview and questionnaire data.

The business characteristics obtained include the following: market entry strategy; industry classification; number of years conducting business with or within the PRC; and business size. And the individual characteristics acquired include the following: nationality; position held; length in current position; length with current employer; and length of business experience with the PRC. To distinguish between the interview participants based in South Australia and the mail questionnaire respondents, the mail questionnaire respondents are identified as the 'Rest of Australia' (ROA). These research participants represent the 'Australian based' research participants. The research participants based in Beijing and Shanghai represent the 'PRC based' research participants.

4.7.1 Business Characteristics

4.7.1a PRC Market Entry Strategies

Table 4.1 outlines the market entry strategy used by the Australian based participants to enter the PRC.

Table 4.1: The Most Recent Market Entry Strategy Employed by the Australian Based Research Participants into the PRC (n=50)

Market Entry Strategy	Research Participants			
	Foreign Direct Investment	South Australia (n=18)	ROA (n=32)	Total (n=50)
Joint Venture	3 (16.67%)	6 (18.75%)	9 (18%)	
Wholly Foreign Owned	2 (11.11%)	5 (15.6%)	7 (14%)	
Non-Foreign Direct Investment				
Export	13 (72.22%)	12 (37.5%)	25 (50%)	
Representative Office	-	2 (6.25%)	2 (4%)	
Other	-	7 (21.9%)	7 (14%)	
Total	18 (100%)	32 (100%)	50 (100%)	

Table 4.1 shows that the percentage of the Foreign Direct Investment (FDI) market entry strategies employed by the South Australian and ROA participants are similar. It also reveals that the participants in South Australia employ the Non-FDI market entry strategy of export more than those in the ROA. Overall, the majority of participants in Australia use the Non-FDI market entry strategy of export to enter the PRC.

Table 4.2 summarises the PRC based participants according to market entry strategy.

Table 4.2: The Most Recent Market Entry Strategy Employed by the PRC Based Research Participants into the PRC (n=33)

Market Entry Strategy	Research Participant		
Foreign Direct Investment	Beijing (n=17)	Shanghai (n=16)	Total (n=33)
Joint Venture	1 (6%)	8 (50%)	9 (27%)
Wholly Foreign Owned	-	-	-
Non-Foreign Direct Investment			
Export	-	-	-
Representative Office	16 (94%)	8 (50%)	24 (73%)
Other	-	-	-
Total	17 (100%)	16 (100%)	33 (100%)

The Beijing participants overwhelmingly used the Non-FDI market entry strategy of a representative office for entry into the PRC, whereas those in Shanghai equally employed Non-FDI and FDI market entry strategies. The main market entry strategy employed by the PRC participants was the Non-FDI market entry strategy of a representative office. Representative offices are limited to the provision of services that do not give rise to earnings, such as investigating and collecting market information, providing introductory services to potential buyers and sellers, assisting in making arrangements for trade visits to the PRC, and co-ordinating with the parent organisation and other associated companies and affiliates (PricewaterhouseCoopers, 1999, p. 83).

Table 4.3 reviews the market entry strategies used by the Australian and PRC based participants to enter the PRC.

Table 4.3: The Number of FDI and Non-FDI Market Entry Strategies Employed by the Australian and PRC Based Research Participants (n=83)

Research Participants	Market Entry Strategy		
	FDI	Non-FDI	Total
Australia (n=50)	16 (32%)	34 (68%)	50 (100%)
PRC (n=33)	9 (27%)	24 (73%)	33 (100%)
Total (n=83)	25 (30%)	58 (70%)	83 (100%)

Table 4.3 reveals that the percentage of Australian and PRC based participants that employed a FDI or a Non-FDI market entry strategy is similar. However, on the whole Non-FDI market entry strategies are more widely employed by the participants in this study than FDI market entry strategies. It is evident from Table 4.3 that there is a significant market entry strategy response bias in the data. That is, FDI market entry strategies are under-represented in the sample. For this reason, the results of this study must be treated with caution.

4.7.1b Industry Classification Categories

Previous research on *guanxi* has not generally used industry categories to classify data, except for Yeung & Tung's (1996) study. Nevertheless, for duplication purposes, and for comparing the questionnaire and semi-structured interview data, this study employs industry categories to classify Australian businesses. The Australian and New Zealand Standard Industrial Classification (ANZSIC) categories, of which there are 17 (see Appendix C), were used to classify the Australian businesses.

Once the data from the mail questionnaires and semi-structured personal interviews were collected, the ANZSIC categories were re-classified to increase the sample size within the categories and to ensure participant confidentiality. The ANZSIC categories were re-classified using the following industry types:

1. Primary Industry: agriculture, forestry, & fishing; and mining.
2. Secondary Industry: manufacturing; and construction.
3. Tertiary Industry: electricity, gas & water supply; retail trade; wholesale trade; accommodation, cafes, & restaurants; transport & storage; communication services; finance & insurance; property & business services; government administration & defence; education; health and community services; cultural and recreational services; and personal & other services.

Table 4.4 summarises the industry classifications of the Australian participants.

Table 4.4: The Industry Classification of the Australian Participants (n=50)

Research Participants	Industry Classification			
	Primary	Secondary	Tertiary	Total
South Australia (n=18)	4 (22%)	7 (39%)	7 (39%)	18 (100%)
ROA (n=32)	7 (22%)	6 (19%)	19 (59%)	32 (100%)
Total (n=50)	11 (22%)	13 (26%)	26 (52%)	50 (100%)

According to Table 4.4, there is a significant difference between the participants in South Australia and the ROA for the following industry classifications: secondary and tertiary. There also appears to be a significant tertiary industry response bias in the data. In other words, the primary and secondary industry classifications are under-represented in the Australian based data.

Table 4.5 shows the industry classifications of the PRC participants.

Table 4.5: The Industry Classification of the PRC Participants (n=33)

Research Participants	Industry Classification			
	Primary	Secondary	Tertiary	Total
Beijing (n=17)	4 (23%)	1 (6%)	12 (71%)	17 (100%)
Shanghai (n=16)	1 (6%)	8 (50%)	7 (44%)	16 (100%)
Total (n=33)	5 (15%)	9 (27%)	19 (58%)	33 (100%)

It can be seen from Table 4.5 that across all the industry classifications, primary, secondary, and tertiary there are significant differences between Beijing and Shanghai. On the whole, tertiary industries are over represented in the PRC based data.

Table 4.6 reviews the industry classifications of the Australian and PRC participants.

Table 4.6: The Industry Classification of the Australian and PRC Participants (n=83)

Research Participants	Industry Classification			
	Primary	Secondary	Tertiary	Total
Australia (n=50)	11 (22%)	13 (26%)	26 (52%)	50 (100%)
PRC (n=33)	5 (15%)	9 (27%)	19 (58%)	33 (100%)
Total (n=83)	16 (19%)	22 (27%)	45 (54%)	83 (100%)

In this study, there is a significant tertiary industry classification response bias. That is, the primary and secondary industry classifications are under-represented in the sample. For this reason, the results in this study must be interpreted with caution.

4.7.1c Number of Years Conducting Business with the PRC

To provide an indication of a businesses' experience in dealing with the PRC, participants were asked to identify when the business first entered the PRC. The following Table 4.7 summarises the Australian participants according to the decade in which they first entered the PRC.

Table 4.7: The Australian Participants Date of First Entry into the PRC (n=50)

Range in Decades	Research Participants		
	South Australia (n=18)	ROA (n=32)	Total (n=50)
1940-1950	-	1 (3%)	1 (2%)
1951-1960	-	-	-
1961-1970	-	1 (3%)	1 (2%)
1971-1980	-	4 (13%)	4 (8%)
1981-1990	7 (39%)	9 (28%)	16 (32%)
1991-2000	11 (61%)	17 (53%)	28 (56%)
Total	18 (100%)	32 (100%)	50 (100%)

Between 1940-1980, only 12 percent of the Australian based participants had begun conducting business with the PRC, whereas 88 percent entered the PRC during 1981-2000. These findings are consistent with the opening up of the PRC to foreign investment during the late 1970s.

Table 4.8 outlines the PRC participants according to the decade in which they first entered the PRC.

Table 4.8: The PRC Participants Date of First Entry into the PRC (n=33)

Range in Decades	Research Participants		
	Beijing (n=17)	Shanghai (n=16)	Total (n=33)
1940-1950	-	-	-
1951-1960	-	-	-
1961-1970	-	-	-
1971-1980	2 (12%)	-	2 (6%)
1981-1990	5 (29%)	1 (6%)	6 (18%)
1991-2000	9 (53%)	14 (88%)	23 (70%)
Total	16 (94%)	15 (94%)	31 (94%) *

* Totals do not equal 33 because of missing data (i.e. Some research participants chose not to answer).

The majority of the PRC based research participants entered the PRC during 1991-2000, which is consistent with the increased liberalisation and continual improvement of the foreign investment environment in the PRC.

Table 4.9 points out the decade in which the Australian and PRC participants first entered the PRC.

Table 4.9: The Australian and PRC Participants Date of First Entry into the PRC (n=81)*

Range in Decades	Research Participants		
	Australia (n=50)	PRC (n=31)	Total (n=81)*
1940-1950	1 (2%)	-	1 (1.2%)
1951-1960	-	-	-
1961-1970	1 (2%)	-	1 (1.2%)
1971-1980	4 (8%)	2 (7%)	6 (7.4%)
1981-1990	16 (32%)	6 (19%)	22 (27.2%)
1991-2000	28 (56%)	23 (74%)	51 (63%)
Total (n=81)*	50 (100%)	31 (100%)	81 (100%)

* Total number of research participants in this study equals 83. However, totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer).

Between 1981-2000, seventy-three percent of the Australian and PRC participants began conducting business within the PRC. This finding corresponds to economic initiatives of the late 1970s designed to open up the PRC to foreign investment, and the liberalisation and continued improvement of the PRC's foreign investment environment during the 1980s and 1990s. It must be noted that all participants in this study have operated continuously in the PRC since their first date of entry.

4.7.1d Measure of Business Size: Employee Numbers

Previous studies on *guanxi* have commonly used number of employees (Ewing et al 1998; Xin & Pearce, 1996; Yeung & Tung, 1996; Leung et al 1996; Fock & Woo, 1998), and to a lesser extent value of total assets and sales (Luo, 1997; Abramson & Ai, 1996), as determinant of business size. This study chose to stratify the sample according to one measure of business size: the 'number of employees', as most previous studies on *guanxi* have commonly used such a measure. Although the results of this measure may be

comparable to other studies on *guanxi*, this measure is ultimately employed for the purpose of comparing mail questionnaire and semi-structured personal interview data, and for replication of the study. The specific categories of employee numbers that determine the size of the businesses in this study include: small (less than 20 employees), medium (between 20 and 199 employees), and large (200 employees and above) (McLennan, 1999, p. 2).

Table 4.10 outlines the size of the businesses in Australia according to employee numbers.

Table 4.10: The Size of the Businesses in Australia: Employee Numbers (n=50)

Research Participants	Size of Business Depicted By Employee Numbers			
	Small < 20	Medium 20-199	Large 200 >	Total
South Australia (n=18)	1 (6%)	6 (33%)	11 (61%)	18 (100%)
ROA (n=32)	10 (31%)	6 (19%)	16 (50%)	32 (100%)
Total (n=50)	11 (22%)	12 (24%)	27 (54%)	50 (100%)

Significant differences are visible between the participants in South Australia and the ROA for small and medium sized businesses. Data for the Australian based participants indicates plainly that small and medium businesses are under represented. There is, in other words, a significant response bias towards large businesses in the Australian based data.

Table 4.11 summarises the size of the businesses in the PRC according to employee numbers.

Table 4.11: The Size of the Businesses in the PRC: Employee Numbers (n=33)

Research Participants	Business Size Depicted by Employee Numbers			
	Small < 20	Medium 20-199	Large 200 >	Total
Beijing (n=17)	6 (35%)	1 (6%)	10 (59%)	17 (100%)
Shanghai (n=16)	1 (6%)	4 (25%)	11 (69%)	16 (100%)
Total (n=33)	7 (21%)	5 (15%)	21 (64%)	33 (100%)

It is evident from Table 4.11 that significant differences are apparent between the Beijing and Shanghai participants for small and medium sized businesses. As with the Australian

based participants, there is a significant response bias in the PRC based data towards large businesses.

Table 4.12 points out the size of the businesses in Australian and the PRC according to employee numbers.

Table 4.12 The Size of Businesses in Australia and the PRC: Employee Numbers (n=83)

Research Participants	Business Size Depicted by Employee Numbers			
	Small < 20	Medium 20-199	Large 200 >	Total
Australia (n=50)	11 (22%)	12 (24%)	27 (54%)	50 (100%)
PRC (n=33)	7 (21%)	5 (15%)	21 (64%)	33 (100%)
Total (n=83)	18 (22%)	17 (20%)	48 (58%)	83 (100%)

No significant differences exist between the Australian and PRC businesses across all the size categories. In this study, however, there is a significant response bias towards large businesses. As a result, the findings must be interpreted with caution.

4.7.2 The Individual Characteristics of the Research Participants

This section summarises the individual characteristics of the research participants in this study, which include nationality, position held, length in current position, length with current employer, and length of PRC business experience.

4.2.2a Nationality

Table 4.13 summarises the nationality of the Australian participants.

Table 4.13: The Nationality of the Australian Participants (n=50)

Nationality	Research Participants		
	South Australia (n=18)	ROA (n=32)	Total (n=50)
Australian	14 (78%)	30 (94%)	44 (88%)
British	1 (5.5%)	-	1 (2%)
Australian Chinese	-	2 (6%)	2 (4%)
Hong Kong Chinese	1 (5.5%)	-	1 (2%)
Mainland Chinese	1 (5.5%)	-	1 (2%)
Singaporean Chinese	1 (5.5%)	-	1 (2%)
Total	18 (100%)	32 (100%)	50 (100%)

The majority of the Australian based participants identify themselves as Australian, with only a small proportion being of Chinese extraction.

Table 4.14 outlines the nationality of PRC participants.

Table 4.14: The Nationality of the PRC Participants (n=33)

Nationality	Research Participants		
	Beijing (n=17)	Shanghai (n=16)	Total (n=33)
Australian	14 (82%)	6 (38%)	20 (61%)
British	-	1 (6%)	1 (3%)
Hong Kong Chinese	2 (12%)	1 (6%)	3 (9%)
Mainland Chinese	1 (6%)	6 (38%)	7 (21%)
Singaporean Chinese	-	1 (6%)	1 (3%)
Malaysian Chinese	-	1 (6%)	1 (3%)
Total	17 (100%)	16 (100%)	33 (100%)

A greater proportion of Beijing than Shanghai participants identify themselves as Australian, whereas those in Shanghai are predominately of Chinese extraction. Although 56 percent of Shanghai participants are of Chinese extraction, the PRC participants are primarily Australian.

Table 4.15 reviews the nationality of the Australian and PRC participants.

Table 4.15: The Nationality of the Australian and PRC Participants (n=83)

Nationality	Research Participants		
	Australia (n=50)	PRC (n=33)	Total (n=83)
Australian	44 (88%)	20 (61%)	64 (77%)
British	1 (2%)	1 (3%)	2 (2.4%)
Australian Chinese	2 (4%)	-	2 (2.4%)
Hong Kong Chinese	1 (2%)	3 (9%)	4 (5%)
Mainland Chinese	1 (2%)	7 (21%)	8 (9.6%)
Singaporean Chinese	1 (2%)	1 (3%)	2 (2.4%)
Malaysian Chinese	-	1 (3%)	1 (1.2%)
Total	50 (100%)	33 (100%)	83 (100%)

More participants in this study identify themselves as Australian than any other nationality. Table 4.15 also points out that only about 20 percent of participants are of Chinese extraction. This is interesting because one would assume that individuals of Chinese extraction may be more suited for roles responsible for the PRC than individuals identifying themselves as Australian, unless the Australian individuals are in their position because of their business experience with the PRC.

4.7.2b Positions Held

To ascertain the seniority of the research participants, they were asked to reveal their position within their business. Table 4.16 summarises the positions held by the Australian participants.

Table 4.16: The Positions Held by the Australian Participants (n=50)

Position Held	Research Participants		
	South Australia (n=18)	ROA (n=32)	Total (n=50)
Owner/Manager	1 (5%)	-	1 (2%)
Executive	3 (17%)	14 (44%)	17 (34%)
Senior Management	6 (33%)	6 (18.75%)	12 (24%)
Middle Management	3 (17%)	6 (18.75%)	9 (18%)
Lower Management	3 (17%)	4 (12.5%)	7 (14%)
Other	2 (11%)	2 (6%)	4 (8%)
Total	18 (100%)	32 (100%)	50 (100%)

Significant differences are noticeable between ROA and South Australian participants who hold executive and senior management positions. Executive and senior management positions account for approximately 60 percent of the positions held by the Australian based participants.

Table 4.17 indicates the positions held by the PRC participants.

Table 4.17: The Positions of the PRC Participants (n=33)*

Positions Held	Research Participants		
	Beijing (n=17)	Shanghai (n=16)	Total (n=33)*
Owner/Manager	3 (18%)	-	3 (9.1%)
Executive	-	3 (19%)	3 (9.1%)
Senior Management	6 (35%)	7 (44%)	13 (39.4%)
Middle Management	7 (41%)	4 (25%)	11 (33.3%)
Lower Management	-	1 (6%)	1 (3%)
Other	1 (6%)	1 (6%)	2 (6.1%)
Total	17 (100%)	16 (100%)	33 (100%)

* Total number of research participants based in the PRC (n=33).

A larger number of participants in Beijing hold middle management positions than those in Shanghai. Another significant difference is that owner-manager positions are only represented in Beijing and executive management positions are only represented in Shanghai. Overall, more PRC based participants hold either senior management or middle management positions than any other position.

Table 4.18 reveals the positions held by the Australian and PRC participants.

Table 4.18: The Positions of the Australian and PRC Participants (n=83)

Position Held	Research Participants		
	Australia (n=50)	PRC (n=33)	Total (n=83)
Owner/Manager	1 (2%)	3 (9.1%)	4 (5%)
Executive	17 (34%)	3 (9.1%)	20 (24%)
Senior Management	12 (24%)	13 (39.4%)	25 (30%)
Middle Management	9 (18%)	11 (33.3%)	20 (24%)
Lower Management	7 (14%)	1 (3%)	8 (10%)
Other	4 (8%)	2 (6.1%)	6 (7%)
Total	50 (100%)	33 (100%)	83 (100%)

The Australian based participants hold more executive and lower management positions than those in the PRC. Table 4.18 also shows that the PRC participants who hold either senior management or middle management positions exceed that of the Australian

participants by approximately 15 percent. Participants in this study hold senior management positions more than any other position, though executive management and middle management positions follow closely.

4.7.2c Number of Years in Current Position and with Current Employer

To provide an indication of managerial and organisational experience, participants were asked to indicate how long they have held their current position, and the length of employment with their current employer. Table 4.19 summarises the number of years the Australian participants have held their current position.

Table 4.19: The Number of Years the Australian Participants have held their Current Position (n=50)

Research Participants	Number of Years in Current Position				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
South Australia (n=18)	9 (50%)	6 (33%)	1 (5.5%)	1 (5.5%)	17 (94.4%)
ROA (n=32)	16 (50%)	9 (28%)	2 (6%)	5 (16%)	32 (100%)
Total (n=50)*	25 (50%)	15 (30%)	3 (6%)	6 (12%)	49 (98%)*

* Totals do not equal 50 because of missing data (i.e. Some chose not to answer).

There is little difference between the percentage of participants based in the ROA and South Australia among the four ranges. A large proportion of the Australian based research participants have held their current position for five years or less.

Table 4.20 reviews the number of years the PRC participants have held their current position.

Table 4.20: The Number of Years the PRC Participants have held their Current Position (n=33)

Research Participants	Number of Years in Current Position				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Beijing (n=17)	11 (65%)	5 (29%)	1 (6%)	-	17 (100%)
Shanghai (n=16)	13 (81%)	2 (13%)	-	-	15 (94%)
Total (n=33)	24 (73%)	7 (21%)	1 (3%)	-	32 (97%)*

* Totals do not equal 33 because of missing data (i.e. Some chose not to answer).

The difference in percentage between the Shanghai and Beijing participants who have held their current position for five years or less and 6-10 years is a significant 16 percent. Most participants in the PRC have held their current position for five years or less.

Table 4.21 outlines the number of years the Australian and PRC participants have held their current position.

Table 4.21: The Number of Years the Australian and PRC Participants have held their Current Position (n=81)*

Research Participant	Number of Years in Current Position				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Australia (n=49)	25 (51%)	15 (31%)	3 (6%)	6 (12%)	49 (100%)
PRC (n=32)	24 (75%)	7 (22%)	1 (3%)	-	32 (100%)
Total (n=81)*	49 (61%)	22 (27%)	4 (5%)	6 (7%)	81 (100%)

* Total number of research participants in this study (n=83). However, totals do not add up to 83 because of missing data (i.e. Some chose not to answer).

Table 4.21 indicates that 75 percent of the PRC participants have held their current position for five years or less, compared to 51 percent of the Australian based participants. Table 4.21 also shows that no participant in the PRC has held their current position for 16 years or more, compared to 12 percent in Australia. There are no considerable differences among the Australian and PRC participants for the ranges 6-10 and 11-15 years. In this study, a high number of participants have held their current position for five years or less. This suggests that the research participants may have been placed in or hired for their position because of their business experience with the PRC.

Table 4.22 summarises the number of years the Australian participants have been with their current employer.

Table 4.22: The Number of Years the Australian Participants have been with their Current Employer (n=50)

Research Participant	Number of Years with Current Employer				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
South Australia (n=18)	3 (17%)	5 (28%)	4 (22%)	5 (28%)	17 (95%)
ROA (n=32)	8 (25%)	9 (28.1%)	2 (6.25%)	10 (31.25%)	29 (91%)
Total (n=50)	11 (22%)	14 (28%)	6 (12%)	15 (30%)	46 (92%)*

* Total does not equal 50 because of missing data (i.e. Some chose not to answer)

The percentage of participants in the ROA and South Australia is similar among the following ranges: 0-5 years, 6-10 years, and 16 years or more. Table 4.22 also shows that 22 percent of South Australian participants have been with their current employer between 11-15 years, compared to 6 percent of the ROA participants. The majority of Australian based participants have been with their current employer for 16 years or more. This is closely followed by the range 6-10 years.

Table 4.23 indicates the number of years the PRC participants have been with their current employer.

Table 4.23: The Number of Years the PRC Participants have been with their Current Employer (n=33)

Research Participant	Number of Years With Current Employer				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Beijing (n=17)	5 (29%)	6 (35%)	1 (6%)	4 (24%)	16 (94%)
Shanghai (n=16)	4 (25%)	3 (19%)	4 (25%)	2 (12.5%)	13 (81%)
Total (n=33)	9 (27%)	9 (27%)	5 (15%)	6 (18%)	29 (87%)*

* Total number of PRC based research participants do not equal 33 because of missing data (i.e. Some chose not to answer)

Significant differences between the percentage of Beijing and Shanghai participants are evident among the following ranges: 6-10 years, 11-15 years, and 16 years or greater. Overall, the ranges 5 years or less and 6-10 years have a greater percentage of PRC participants than any other range. Thus, 54 percent of participants in the PRC have been with their current employer for 10 years or less, whereas only 33 percent have been with their current employer for 11 years or more.

Table 4.24 outlines the number of years the Australian and PRC participants have been with their current employer.

Table 4.24: The Number of Years the Australian and PRC Participants have been with their Current Employer (n=75)*

Research Participant	Number of Years with Current Employer				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Australia (n=46)	11 (24%)	14 (30%)	6 (13%)	15 (33%)	46 (100%)
PRC (n=29)	9 (31%)	9 (31%)	5 (17%)	6 (21%)	29 (100%)
Total (n=75)*	20 (27%)	23 (30%)	11 (15%)	21 (28%)	75 (100%)

* Total number of research participants in this study (n=83). However, total number of research participants does not equal 83 because of missing data (i.e. Some chose not to respond)

Table 4.24 shows that there is quite an amount of variability among the number of years the participants have been with their current employer.

4.7.2d PRC Business Experience

To provide an indication of the extent of the participant's PRC business experience, participants were asked to indicate the number of years they have been conducting business with the PRC. Table 4.25 indicates the Australian participant's PRC business experience.

Table 4.25: The Australian Participant's Length of Business Experience with the PRC (n=50)

Research Participant	Number of Years of Business Experience with the PRC				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
South Australia (n=18)	10 (56%)	6 (33%)	2 (11%)	-	18 (100%)
ROA (n=32)	13 (40.5%)	6 (19%)	7 (22%)	4 (12.5%)	30 (94%)
Total (n=50)	23 (46%)	12 (24%)	9 (18%)	4 (8%)	48 (96%)

* Total number of Australian based research participants does not equal 50 because of missing data (i.e. Some chose not to answer).

A number of participants in the ROA have 16 years or more of business experience with the PRC, compared to none in South Australia. There are also significant differences between the South Australian and ROA participants for the ranges 6-10 and 11-15 years. The Australian based participants overwhelmingly have 5 years or less of business experience with the PRC. This suggests that a large part of the Australian participants have been hired or placed into their position with little regard for their degree of PRC business experience.

Table 4.26 reviews the PRC participant's length of business experience with the PRC.

Table 4.26: The PRC Participant's Length of Business Experience with the PRC (n=33)

Research Participant	Number of Years of Business Experience with the PRC				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Beijing (n=17)	4 (23.5%)	10 (59%)	2 (12%)	1 (5.5%)	17 (100%)
Shanghai (n=16)	11 (69%)	2 (12.5%)	3 (18.5%)	-	16 (100%)
Total (n=33)	15 (45.5%)	12 (36.5%)	5 (15%)	1 (3%)	33 (100%)

Table 4.26 reveals that there are significant differences between the Beijing and Shanghai participants for the ranges 0-5 and 6-10 years. It also shows that a high proportion of the participants in the PRC have 5 years or less of PRC business experience. This suggests that the PRC based participant's business experience may not impact upon their employers decision to place or hire them for positions responsible for China .

Table 4.27 points out the Australian and PRC participant's business experience with the PRC.

Table 4.27: The Australian and PRC Participant's Length of Business Experience with the PRC (n=81)*

Research Participant	Number of Years of Business Experience with the PRC				
	0-5 yrs	6-10 yrs	11-15 yrs	16 yrs >	Total
Australia (n=48)	23 (48%)	12 (25%)	9 (19%)	4 (8%)	48 (100%)
PRC (n=33)	15 (45.5%)	12 (36.4%)	5 (15%)	1 (3%)	33 (100%)
Total (n=81)*	38 (47%)	24 (30%)	14 (17%)	5 (6%)	81 (100%)

* Total number of research participants in this study (n=83). However, total number of research participants does not equal 83 because of missing data (i.e. Some Chose not to answer).

There are no considerable differences between the participants in Australia and the PRC across all the ranges: 0-5 years, 6-10 years, 11-15 years, and 16 years or higher. Approximately half of the participants in this study have five years or less of business experience with the PRC. This indicates that the majority of participant's employers may be hiring or placing individuals into positions responsible for the PRC who are inexperienced in dealing with or within the PRC on a business level.

4.8 Data Coding and Analysis Procedures

The responses to the questionnaire that yielded nominal or categorical data were entered into a Statistical Package for Social Sciences (SPSS) Windows worksheet where frequencies were produced. Trends and general emphases of the nominal or categorical data are shown using frequency tables. The results of questions that were answered using Likert Scales in the questionnaire are presented in tables of frequency where the mean, standard deviation and the percentage in each category are shown. All tables are

presented in Chapter Five. The questionnaire also yielded qualitative data. This data along with the qualitative data gathered from the semi-structured personal interviews were analysed using content analysis.

4.8.1 Content Analysis

Berelson (1952, p. 18) states that “content analysis is a research technique for the objective, systematic, and quantitative description of the manifest content of communication”. In other words, it is a process of identifying, coding, and categorising the primary patterns in the data (Patton, 1980, p. 381). Content analysis has been widely employed in social science research where text is important (Weber, 1990, p. 13); for example, international relations and in the assessment of cultural and social trends. This technique, however, has not been widely employed in research concerning the Chinese concept of *guanxi* (i.e. Luo, 1997; Leung et al 1996; Bjorckman & Kock, 1995; Bjorckman and Schaap, 1994; Ewing et al 1998). But this does not discount the significance of content analysis employed in this study.

Although there are a variety of definitions of content analysis, there is however, agreement on the objectivity and generality of content analysis (Carney, 1972, pp. 25-26; Holsti, 1969, pp. 3-5). Objectivity, according to Holsti (1969, p.3) signifies “that each step in the research process must be carried out on the basis of explicitly formulated rules and procedures”. A test of objectivity is to determine whether one or more analyst is able to reach similar conclusions, following identical procedures with the same data. That is, the rules and procedures for selecting and interpreting the relevant data are clearly defined in a manner that allows for duplication with similar results. Systematic analysis, according to Holsti (1969, p. 4), indicates “that the inclusion and exclusion of content or categories is done according to consistently applied rules”. In other words, they must conform to certain general canons of category construction. This requirement eliminates analyses where only text supporting the propositions and/or hypotheses are admitted as

evidence. Generality, according to Holsti (1969, p. 5), betokens “that the findings must have theoretical relevance because purely descriptive information about content is of little value”.

As discussed earlier regarding survey research, the same two methodological issues must be addressed when employing content analysis: reliability and validity (Holsti, 1969; Weber, 1990; Carney, 1972).

Krippendorff (1980, pp, 140-150) states that there are three types of reliability pertinent to content analysis: stability, reproducibility, and accuracy. Weber (1990, p. 17) points out that stability refers to the extent to which the results are invariant over time. Weber (1990, p. 17) also states that stability can be determined when the same content is coded more than once by the same coder. To check for stability in this study, an interview and a questionnaire were randomly selected, analysed, and coded. The interview and questionnaire were again analysed and coded after four weeks. Reliability using stability, however, is the weakest form of reliability because only one person is coding (Weber, 1990, p. 16). A stronger test of reliability is that of reproducibility. Reproducibility refers to the extent to which content classification produces the same results when the same text is coded by more than one coder (Weber, 1990, p. 17). This is referred to by Holsti (1969, p. 135) as “individual reliability”. To meet the requirements of reproducibility in this study, a pilot test was conducted that used two independent coders and the researcher to refine the categories used for coding.

Accuracy, refers to the extent to which the classification of text corresponds to a standard or norm (Weber, 1990, p. 17). Norms or standards are not evident for research on the Chinese concept of *guanxi*. Nevertheless, the results of this study are compared to previous studies on the Chinese concept of *guanxi* and foreign businesses operating in the PRC.

Validity, as noted previously, refers to the extent to which an instrument is measuring what it is intended to measure, and can be overcome through content validity,

construct validity, and criterion-related validity (Holsti, 1969, p. 142). This study acknowledges the importance of predictive and concurrent validity in inferring future trends from the data concerning the Chinese concept of *guanxi* and its complexities. However, this study is mainly concerned with content validity. Reliability and validity of the instrument employed for the content analysis was accomplished during the pre-testing stage.

This study created and applied a coding scheme, which consisted of the following necessary steps (Weber, 1990, pp. 21-24):

1. Define the recording units,
2. Define the categories,
3. Test coding on sample of text,
4. Assess accuracy or reliability,
5. Revise the coding rules,
6. Return to step 3,
7. Code all the text, and
8. Assess achieved reliability or accuracy.

All eight steps were conducted during pre-testing and coding was conducted manually.

The final coding of the data was conducted by the researcher.

4.8.2 Unit of Analysis

By definition, content analysis calls for the quantification of content elements. The quantification of the content may range from small to large (Berelson, 1952, p. 135). One of the most fundamental and important decisions concerns the definition of the basic unit of text to be classified. The aim in content analysis is to do the minimum amount of counting possible while still reaching valid conclusions. For example, the smaller the units used for counting, the greater the amount of counting that needs to be done (Carney, 1972, p. 144). Holsti (1969, p. 116) and Bailey (1987, p. 280) state that the use of a word

as the unit of analysis has generally been avoided in research involving large volumes of data. Units, such as sentences and paragraphs in content analysis have also generally been avoided because they do not usually lend themselves to classification into a single category. Holsti (1969, p.116) and Berelson (1952, p. 139) assert that the theme is the most useful unit of content analysis, particularly where research is undertaken on values and attitudes.

Themes are an assertion about subject-matter. It may take only a few words or part of a sentence, or it may require many paragraphs to elucidate a theme (Holsti, 1969, p. 116; Berelson, 1952, p. 138; Bailey, 1987, p. 281). Themes can often reach into aspects of communication that cannot be dealt with by frequency counts or even contingency analysis; where two or more passages contain almost identical words but mean different things (Carney, 1972, p. 159). Nevertheless, employing themes does have its drawbacks: the boundaries for themes are not as easily identified as those of the word, paragraph or sentence, and is among the most difficult unit of analysis, from the standpoint of reliability. However, it has also been found that themes can give quite as reliable results as can smaller units of analysis (Carney, 1972, p. 144). Notwithstanding the disadvantages, themes are employed as the unit of analysis in this study because any unit, such as a sentence or paragraph, would not capture the essence of the participant's views and attitudes towards the Chinese concept of *guanxi* and the PRC's business environment. Any smaller unit of analysis, such as a word, would prove to be futile because 51 semi-structured personal interviews were conducted each averaging 45 minutes in duration and overall yielding approximately 636 A4 pages of double spaced text. This does not include the qualitative text gathered from 32 questionnaires. Refer to Appendix (D) for the coding scheme and a sample of the coding scheme in use.

4.8.3 Categorisation

A pertinent element of research design in content analysis is the selection and development of categories to suit both the research questions and subject matter (Carney, 1972, p. 167). Berelson (1952, p. 147) states that “content analysis stands or falls by its categories”. According to Holsti (1969, p. 95), “categories should reflect the purpose of the research, be exhaustive, be mutually exclusive, independent, and derived from a single classification principle”. This, in other words, refers to the development of clearly defined variables (“conceptual definitions”) and the specification of indicators that determine whether the data falls within the category (“the operational definition”). A succinct operational definition allows for the valid representation of the analysts’ concepts, and guides the coder/s to reliable judgements (Holsti, 1969, p. 95). Exhaustiveness means that all relevant items in the sample data must be capable of being placed into a category. Mutual exclusiveness means that the sample data cannot be placed into more than one category. Mutual exclusiveness and exhaustiveness can generally be met by letting the categories emerge from the sample data to be analysed (Bailey, 1987, p. 279). Independent refers to any data that is classified into a category, which does not affect the classification of other data (Holsti, 1969, p. 100). To meet the requirements of mutual exclusiveness and exhaustiveness, categories were developed through analysis of empirical and theoretical research in the area of study and by letting categories emerge from the qualitative data in the pilot test and final data.

4.8.4 Pre-Testing of Qualitative Data

The instrument to be employed in this study was tested for validity and reliability through pre-testing. The researcher and two independent coders were employed to test the instrument. One of the coders was a research postgraduate commerce student, and the other was a business executive. The independent coders were only used for pre-testing, which was limited to simple data coding. These coders were not involved in making

inferences, however, they were involved in discussions regarding the classifications to ensure content validity; but the researcher made all the final decisions regarding classification. Pre-testing is conducted to test the reliability and validity of the coding instrument, but it is not tested to draw inferences about the qualitative data to be analysed (Bailey, 1987; Holsti 1969). To undertake pre-testing, each coder was provided with an exact copy of an interview transcript. This interview transcript was randomly selected from the South Australian based interview transcripts because there was a large lapse of time between the commencement of interviews in South Australia and those in Beijing and Shanghai. Qualitative data from the questionnaires were not included for pre-testing because of the limited number of qualitative response questions. It would not have exposed the coders to the rigour of coding an interview transcript and the many themes developed. Results of coding were compared and discrepancies discussed.

During pre-test coding, there was no consultation between coders until the coding was complete. The coders were provided with basic instructions and a copy of the categories to be used to code the qualitative interview data. The coders highlighted the themes outlined by the categories given to them. Any themes that did not fall into a category listed on the coding sheet were highlighted in a different colour, thus allowing for the development of new categories or sub-categories. The themes were then totalled and the percentage of agreement between the coders was identified using Holsti's (1969, p. 140) coefficient of reliability test:

$$3(M)/(A+B+C) \quad 3(10)/14+14+14 = 0.7143$$

Where M is the number of coding decisions on which the three coders are in agreement, and A, B, and C refer to the number of themes coded by the two independent coders and the researcher respectively. When the coefficient reliability test was calculated for the two independent coders and the researcher respectively, a coefficient reliability of 0.7143

was achieved before discrepancies were discussed. As noted by Holsti (1969), defining an acceptable level of reliability is one of the many problems in content analysis, which there is no single solution. A review of some 30 studies and experiments reveals correlation coefficients between 0.78 and 0.99 (Berelson, 1952, p. 172). The reliability coefficient calculated in this study falls below the correlation coefficients Berelson reviewed, indicating a lower magnitude of reliability. A higher magnitude of reliability, however, does not guarantee the reliability of content analysis. A simpler unit of analysis, such as a word or sentence may have increased the reliability coefficient, but reduced the richness and the insights gained from the data using themes (Berelson, 1952, pp. 172-174). Even though the reliability coefficient may be just below the commonly accepted level, the richness of the data and the insights into the data gained through content analysis supersede the low magnitude of reliability.

It is noted by Weber (1990) that coding over a length of time may cause discrepancies to appear in the coding of the text. Thus, to ensure the continuity of the coding instrument an interview randomly selected from the sample was re-coded once the final coding of the entire sample was complete. This was considered pertinent, as the researcher was required to code 51 semi-structured interviews and qualitative data from 32 questionnaires that were gathered over an eight-month period. Such copious amounts of coding may result in subtle changes to the coding being undertaken and thus reliability coefficients were undertaken to ensure that any changes, if any, were insignificant. The research postgraduate commerce student used in pre-testing for inter coder reliability was unavailable. Therefore, the reliability coefficient test was calculated between the researcher and the business executive. The calculation of the coefficient reliability test resulted in:

$$\text{Coefficient Reliability } 2(10)/14+14 = 0.7143$$

As the coefficient was equal to the previous reliability coefficient test undertaken, no re-coding was undertaken.

Once the coding of the qualitative data was complete, the data was analysed using descriptive statistics. The coding sheets were transcribed into an SPSS for Windows data sheet and frequencies produced. These frequencies, where applicable, allowed for comparative analysis of the nominal and categorical questionnaire data. The frequencies produced are presented in tabular format in Chapter Five. In order to improve the depth of analysis of the frequency counts, Chapters Six, Seven, Eight, and Chapter Nine analyse and discuss the qualitative data obtained from the semi-structured personal interviews according to themes. In these Chapters when direct quotes are used, the research participant's identity is hidden for confidentiality purposes. The identity of the research participant is hidden using codes, which are as follows: 'A' refers to Adelaide participants, 'B' refers to Beijing participants, and 'S' refers to Shanghai participants. A number will be used in conjunction with either 'A', 'B', or 'S', which depicts the number of the interview. For example, A1 refers to research participant one based in Adelaide, and B5 refers to research participant five based in Beijing. The details of each individual personally interviewed are located in Appendix (E), which include the following individual characteristics: nationality, position held, length of business experience, and their employers business characteristics: industry classification, market entry date, market entry strategy, and business size.

4.8.5 Content Analysis Limitations

As with all methods of analysis, content analysis has inherent limitations. Although a large number of conclusions may be drawn from a small amount of data, the number of ways open for substantiating them will be proportionally small (Carney, 1972). However, this limitation is overcome with copious amounts of qualitative data from 51 semi-structured interviews and 32 useable questionnaire responses.

4.9 Summary

This Chapter outlined and justified the two data collection methods: (1) semi-structured personal interviews, and (2) a mail questionnaire. This study uses these two methods to strengthen the findings and conclusions drawn from the results.

The results of the mail questionnaire and content analysis are presented in Chapter Five. An in-depth analysis and discussion of the qualitative interview data in relation to the complexities of *guanxi*, the applicability of *guanxi* as a substitute for formal institutional support in the PRC, the first mover competitive advantages of *guanxi*, and that competitive advantages may be undermined by a businesses' discretionary policies follow in Chapters Six-Nine respectively. Chapter Ten discusses the significance of the study, the study's contribution to knowledge, implications of the findings for Australian businesses conducting business with the PRC, the limitations of the study, and suggestions for further research.

CHAPTER FIVE:

QUANTITATIVE RESEARCH RESULTS

5.1 Introduction

This Chapter reports the quantitative results of the content analysis of the qualitative data obtained from the questionnaire and semi-structured personal interviews, and the quantitative findings from the questionnaire. These results relate to the role and importance of *guanxi* for Australian businesses in the PRC. As indicated in Chapter Four, the questionnaire results from the Rest of Australia (ROA) and the semi-structured personal interviews undertaken in South Australia comprise the Australian based participants. The results of the semi-structured interviews in Beijing and Shanghai form the PRC based participants. Together, they form the population of this study. Findings are discussed in this Chapter in general terms only, with detailed consideration left until Chapters Six, Chapter Seven, Chapter Eight, and Chapter Nine.

5.2 Quantitative Research Results

The quantitative results are presented in frequency tables, which include the following areas: how to develop and maintain *guanxi*; whether *guanxi* is a form of corruption; problems encountered while conducting business in the PRC; the methods employed to initiate contact in the PRC; whether *guanxi* was used after the initial contact stages; whether *guanxi* is important for conducting business in the PRC; whether the importance of *guanxi* is in decline; the problems overcome through *guanxi*; the advantages of *guanxi*; and the disadvantages of *guanxi*. The following tables and the subsequent analysis lay the foundation for enhancing the understanding of *guanxi*, determining the perceived role and importance of *guanxi* for Australian businesses operating in the PRC, and whether *guanxi* may lead to competitive advantages for the Australian businesses.

To further enhance our understanding of *guanxi*, information was solicited from the semi-structured personal interview participants regarding its complexities, including how to develop and maintain *guanxi*, and whether *guanxi* is a form of corruption. Similar information was not solicited from the questionnaire respondents because these issues became evident as the study progressed. Although data is absent from the questionnaire respondents, the richness of detail obtained from the semi-structured personal interviews compensates for the absent data.

5.2.1 Methods Employed to Develop and Maintain *Guanxi*

Table 5.1 reviews the manner in which the participants in South Australia, Beijing and Shanghai develop and maintained *guanxi*.

Table 5.1: The Methods Employed to Develop and Maintain *Guanxi* by the South Australian, Beijing and Shanghai Participants (n=51)

Research Participant [^]	Banquets+	Gifts+	Regular Contact+
South Australia (n=18)	6 (33%)	8 (44%)	11 (61%)
Beijing (n=17)	12 (70.5%)	2 (12%)	3 (18%)
Shanghai (n=16)	11 (69%)	8 (50%)	3 (19%)
Total (n=51)	29 (57%)	18 (35%)	17 (33%)

⁺ Multiple answers permitted.

* Data may be missing (i.e. Some research participants were unable to answer the question).

Although regular contact has not been quantified, the South Australian participants appear to place more emphasis on regular contact than those in Beijing and Shanghai. It may be argued that this significant difference is the result of the geographical distance between the South Australian participants and their operations or customers in the PRC. This is not to suggest that the Beijing and Shanghai participants do not keep in regular contact with their customers. Rather it merely indicates that the South Australian participants may be more aware of the importance of regular contact because of the geographical distance. Table 5.1 also indicates that the Shanghai participants are more likely to use gifts to develop and maintain *guanxi* than those in Beijing. It may be argued that because of the large concentration of Chinese officials and bureaucrats in the PRC's

capital, Beijing, that recent measures to curb blatant forms of *guanxi xue* is having a more profound effect in the Chinese capital than Shanghai. However, this issue is beyond the scope of the thesis and is an area that needs further research. Overall, the main method employed to develop and maintain *guanxi* is banquets, followed by gifts, and regular contact respectively. This finding supports Hwang (1987) who argued that banquets and gifts were the most favoured measures to develop and maintain *guanxi* in the PRC. Although differences exist, the participants employ a variety of measures.

5.2.2 Whether *Guanxi* is a Form of Corruption

The responses of the South Australian, Beijing and Shanghai participants in relation to whether *guanxi* is a form of corruption are outlined in Table 5.2.

Table 5.2: The Responses of the South Australian, Beijing and Shanghai Participants Regarding Whether *Guanxi* is a Form of Corruption (n=51)

Research Participants	Is Guanxi a Form of Corruption?		
	No	Yes	Total
South Australia (n=18)	15	-	15 (83%)
Beijing (n=17)	12	2	14 (82%)
Shanghai (n=16)	14	-	14 (87.5%)
Total (n=51)	41 (80%)	2 (4%)	43 (84%)**

** Totals do not equal 51 because of missing data (i.e. some participants were unable to answer the question).

Table 5.2 indicates that all the participants believe overwhelmingly that *guanxi* is not a form of corruption.

5.2.3 Problems Encountered while Conducting Business in the PRC

To establish whether the PRC's legal system continues to be marred by uncertainty, a question was asked about the problems encountered whilst conducting business with the PRC. The problems are summarised in Table 5.3

Table 5.3: The Problems Encountered by the Australian Participants while Conducting Business in the PRC (n=50)

Problems Encountered	Research Participant [^]		
	South Australia (n=18)+	ROA (n=32)+	Total (n=50)
Legal	16 (89%)	12 (37.5%)	28 (56%)
Bureaucratic	2 (11%)	11 (34%)	13 (26%)
Human Resource	5 (28%)	11 (34%)	16 (32%)
Distribution	2 (11%)	10 (31%)	12 (24%)
Taxation	-	7 (22%)	7 (14%)
Product Quality	-	8 (25%)	8 (16%)
Tariffs	-	2	2 (4%)
Financial	5 (28%)	11 (34%)	16 (32%)
Language	8 (44%)	-	8 (16%)
Cultural	3	-	3 (6%)
Corruption	4	-	4 (8%)
Competition	3	-	3 (6%)

+ Multiple answers permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question).

It appears that the South Australian participants are more likely to experience legal, language, cultural, corruption, and competition problems than those in the ROA. In contrast, participants in the ROA are more likely to encounter bureaucratic, distribution, taxation, product quality, and tariff problems than those in South Australia. Language and cultural problems experienced by Australian businesses are consistent with the previous literature on foreign businesses (i.e. Rich, 1996; Wong, 1995). The principal problems encountered by the Australian participants were clearly legal (56%): human resource (32%), financial (32%), and bureaucratic (26%). The percentage of Australian participants who encountered legal problems is significantly lower than those in South Australia.

Table 5.4 outlines the problems encountered by participants in the PRC.

Table 5.4: The Problems Encountered by the PRC Participants while Conducting Business in the PRC (n=33)

Problems Encountered	Research Participant [^]		
	Beijing (n=17)+	Shanghai (n=16)+	Total (n=33)
Legal	10 (59%)	9 (56%)	19 (58%)
Bureaucratic	6 (35%)	5 (31%)	11 (33%)
Human Resource	5 (29%)	8 (50%)	13 (39%)
Distribution	2	-	2 (6%)
Financial	4 (23.5%)	6 (37.5%)	10 (30%)
Product and Technology Theft	-	5 (31%)	5 (15%)
Partner	-	3	3 (9%)
Corruption	-	3	3 (9%)
Competition	1	-	1 (3%)

+ Multiple answers permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question)

The percentage of Beijing and Shanghai participants who faced legal and bureaucratic problems is similar. Notwithstanding the similarities, 50 percent of participants in Shanghai experienced human resource problems, compared with only 29 percent of those in Beijing, a significant difference of 21 percent. In addition, Table 5.4 indicates that those in Shanghai may be more likely to experience financial problems, product and technology theft, partner and corruption problems than the participants in Beijing. This implies that Shanghai may be a more difficult location for Australian businesses to operate in than Beijing. Overall, the central problem encountered by the PRC participants were legal in nature, followed by human resource problems, with 39 percent of PRC participants noting such problems. This was closely followed by bureaucratic problems.

Table 5.5 reviews the problems faced by the Australian and PRC participants while conducting business in the PRC.

Table 5.5: The Problems Encountered by the PRC and Australian Participants while Conducting Business in the PRC (n=83)

Problems Encountered	Research Participant		
	Australia (n=50)+	PRC (n=33)+	Total (n=83)
Legal	28 (56%)	19 (58%)	47 (57%)
Bureaucratic	13 (26%)	11 (33%)	24 (29%)
Human Resource	16 (32%)	13 (39%)	29 (35%)
Distribution	12 (24%)	2	14 (17%)
Taxation	7	-	7 (8%)
Product Quality	8	-	8 (10%)
Tariffs	2	-	2 (2.4%)
Financial	16 (32%)	10 (30%)	26 (31%)
Product and Technology Theft	-	5	5 (6%)
Partner	-	3	3 (4%)
Language	8	-	8 (10%)
Cultural	3	-	3 (4%)
Corruption	4	3	7 (8%)
Competition	3	1	4 (5%)

+ Multiple answers permitted.

^ Data may be missing (i.e. Some research participants were unable to answer the question).

There is no considerable difference between legal, bureaucratic, human resource, financial, and corruption problems experienced by Australian and PRC participants. However, a significant difference is evident between the Australian and PRC participants who experienced distribution problems. Table 5.5 also denotes that the participants in Australia may be more likely to experience distribution, taxation, product quality, tariffs, language, and cultural problems; whereas those in the PRC may be more likely to encounter problems relating to product and technology theft, and partners.

Even though similarities and differences exist between the Australian and PRC participants, legal issues were the main problem encountered by all. This finding evinces that the PRC's legal environment is marked by uncertainty, which supports previous literature (i.e. Blackman, 1997; Xin & Pearce, 1996; Yeung & Tung, 1996; Lubman, 2000). As a result of the uncertainty in the Chinese legal system, Australian businesses that rely on such a system for governance and support may face higher transaction costs

and diminished competitive advantage. Therefore, Australian businesses must consider alternative measures of support and governance (Luo, 2000a). As demonstrated in Chapter Three, one such alternative is *guanxi* (Boisot & Child, 1988; Davies, 1995; Standifird & Marshall, 2000). Thus, Guthrie's (1998) argument that the importance of *guanxi* is in decline because of the implementation of a rational-legal system at the state level and formal rational organisations at the firm level, may not hold for the PRC's foreign business environment. *Guanxi* could continue to be perceived as an important substitute for formal institutional support. Not only does the uncertainty of the PRC's legal environment increase the transaction costs of relying on such a system but it also heightens the risk of conducting business in the PRC (Chao et al 1998; Zhuang et al 1998, p. 611; AMCHAM, 2000, p. 24).

Human resource issues were the second most noted problem, with 35 percent of participants experiencing such problems. According to the American Chamber of Commerce (AMCHAM) (2000, p. 46), human resource issues are seen by foreign investors as a major determinant in the success or failure of their business ventures in the PRC. This is not to suggest that human resource issues are less critical to the success of foreign businesses operating in other countries. It is merely to indicate the impact that human resource policies and practices may have on a foreign business in the PRC.

5.2.4 Methods Employed to Initiate Contact with the PRC

To determine where and when *guanxi* is important for Australian businesses, questions were asked about the methods employed to initiate contact with the PRC, and whether *guanxi* was used after the initial contact stage. Table 5.6 displays the methods employed by the Australian participants to initiate contact with the PRC.

Table 5.6: The Methods Employed by the Australian Participants to Initiate Contact in the PRC (n=50)

Methods Used to Initiate Contact	Research Participant ^		
	South Australia (n=18)+	ROA (n=32)+	Total (n=50)
Austrade	8 (44%)	13 (41%)	21 (42%)
Chinese Government Department	-	12 (38%)	12 (24%)
Australian State Government	2 (11%)	11 (34%)	13 (26%)
Chinese Agents	-	3	3 (6%)
Existing Customer	1	1	2 (4%)
<i>Guanxi</i>	8 (44%)	24 (75%)	32 (64%)

+ Multiple answers permitted.

^ Data is missing (i.e. Some research participants were unable to answer the question).

Significant differences between participants in the ROA and South Australia are evident for the following methods utilised to initiate contact with the PRC: Chinese Government Department, Australian State Government and *Guanxi*. In other words, the participants in the ROA clearly relied more on *guanxi*, Chinese Government departments, and Australian State Governments than those in South Australia. Austrade was used by a similar percentage of the participants in South Australia and the ROA. *Guanxi*, however, was overwhelmingly the most popular method used to initiate contact with the PRC by the Australian participants.

The methods employed by the Australian and PRC participants to initiate contact with the PRC are reviewed in Table 5.7. The small number of responses from the Shanghai and Beijing participants were not included in a separate table.

Table 5.7: The Methods Used by the Australian and PRC Participants to Initiate Contact in the PRC (n=83)

Methods Used to Initiate Contact	Research Participant ^		
	Australia (n=50)+	PRC (n=33)+	Total (n=83)
Austrade	21	8	29 (35%)
Chinese Government Department	12	-	12 (14%)
Australian State Government	13	-	13 (15.5%)
Chinese Agents	3	-	3 (3.6%)
Existing Customer	2	-	2 (2.4%)
<i>Guanxi</i>	32	2	34 (41%)

+ Multiple answers permitted.

^ Data is missing (i.e. Some research participants were unable to answer the question).

The findings in Table 5.7 need to be treated with caution because of the significant amount of missing data, especially from the PRC participants. Nevertheless, Table 5.7 shows that overall *guanxi* was the primary method employed by the participants in this study. This indicates the integral part *guanxi* plays for the participants in initiating contact with the PRC. Austrade is also a popular channel.

5.2.5 The Employment of *Guanxi* after the Initial Contact Stage

The number of Australian participants who used *guanxi* after the initial contact stage with the PRC is outlined in Table 5.8.

Table 5.8: The Number of Australian Participants who Employed *Guanxi* After the Initial Contact Stage when Conducting Business in the PRC (n=50)

Research Participant	Frequency
South Australia (n=18)	8 (44%)
ROA (n=32)	30 (94%)
Total (n=50)	38 (76%)*

* Totals do not equal 50 because of missing data (i.e. Some research participants were unable to answer or the question was not applicable).

There is a considerable difference between the percentage of South Australian and ROA participants who used *guanxi* after the initial contact stage. Participants in the ROA are

more likely to rely on *guanxi* to negotiate the PRC's business environment than those in South Australia. Comparing the percentage of South Australian participants with the results in Table 5.6, we find that a similar percentage use *guanxi* during and after the initial contact stage. However, approximately 20 percent more participants in the ROA use *guanxi* after than during the initial contact stage. Overall, 12 percent more of Australian participants use *guanxi* after than during the initial contact stage. Although not a considerable increase, it does suggest that *guanxi* may be more significant for negotiating in the PRC's business environment than initiating contact.

The number of PRC participants who use *guanxi* after the initial contact stage is summarised in Table 5.9.

Table 5.9: The Number of PRC Participants who Employed *Guanxi* After the Initial Contact Stage while Conducting Business in the PRC (n=33)

Research Participant	Frequency
Beijing (n=17)	15 (88%)
Shanghai (n=16)	13 (81%)
Total (n=33)	28 (85%)*

* Totals do not equal 33 because of missing data (i.e. Some research participants were unable to answer or the question was not applicable).

Table 5.9 revealed that there is no significant percentage difference among Beijing and Shanghai participants. Overall, 85 percent of the PRC participants used *guanxi* after the initial contact stage. This is a considerable increase on the percentage of PRC participants who used *guanxi* to initiate contact. However, this comparison needs to be treated with caution because of the significant amount of PRC data missing from Table 5.7. Nevertheless, the result does suggest that *guanxi* may be more important for negotiating in the PRC's business environment than initiating contact.

Table 5.10 displays the number of Australian and PRC participants who used *guanxi* after the initial contact stage with the PRC.

Table 5.10: The Number of Australian and PRC Participants who used *Guanxi* After the Initial Contact Stage when Conducting Business in the PRC (n=83)

Research Participant	Frequency
Australia (n=50)	38 (76%)
PRC (n=33)	28 (85%)
Total (n=83)	66 (79.5%)*

* Totals do not equal 83 because of missing data (i.e. Some research participants were unable to answer or the question was not applicable).

In this study, over three-quarters of the participants have used *guanxi* after the initial contact stage, which is 38.5 percent above the percentage of participants who initiated contact with the PRC through *guanxi*. Even though this comparison needs to be treated with caution because of the considerable amount of PRC data missing from Table 5.7, it does indicate the persuasiveness of *guanxi* for negotiating the PRC's business environment, which is consistent with Yeung & Tung (1996) and Ahmed & Li (1996). It also implies that *guanxi* may be less significant for Australian businesses in the initial contact stage than for negotiating in the PRC's business environment.

5.2.6 The Importance of *Guanxi* for Conducting Business in the PRC and whether it is in Decline

To establish the importance of *guanxi* for Australian businesses, questions were asked if *guanxi* was important for conducting business in the PRC and whether the importance of *guanxi* was in decline.

Table 5.11 points out the ROA participant's responses on the importance of *guanxi* for conducting business in the PRC.

Table 5.11: The Use of *Guanxi* for Conducting Business in the PRC is Important: According to the Participants in the Rest of Australia (n=32)

Likert Scale ^	ROA (n=32)			
	Frequency	Percent	Mean	Std. Deviation
1. Strongly Disagree	-	-	4.53	0.51
2. Disagree	-	-		
3. Undecided	-	-		
4. Agree	14	46.7%		
5. Strongly Agree	16	53.3%		
Total	30*	100%		

* Totals do not equal 32 because of missing data (i.e. Some research participants were not required to answer).

^ The question used a Likert Scale, therefore, the mean and standard deviation are provided.

There was not one participant in the ROA who did not perceive *guanxi* to be important for conducting business in the PRC. This is similar for the participants in South Australia, Beijing, and Shanghai, where 47 of 51 (note data was missing) participants reported that *guanxi* is important for conducting business in the PRC. This finding further reinforces the perception of the salience of *guanxi* for negotiating the PRC's business environment, which is consistent with previous literature (i.e. Bjorkman & Kock, 1995; Ahmed & Li, 1996; Bjorkman & Schaap, 1994).

Table 5.12 and Table 5.13 summarise the ROA and South Australian participant's responses respectively on whether the salience of *guanxi* in the PRC's business environment is in decline.

Table 5.12: The Importance of *Guanxi* in the PRC's Business Environment is in Decline: A View by the Participants in the Rest of Australia (n=32)

Likert Scale ^	ROA (n=32)			
	Frequency	Percent	Mean	Std. Deviation
1. Strongly Disagree	2	6.7%	2.87	1.07
2. Disagree	12	40%		
3. Undecided	5	16.7%		
4. Agree	10	33.3%		
5. Strongly Agree	1	3.3%		
Total	30*	(100%)		

* Totals do not equal 32 because of missing data (i.e. Some research participants were not required to answer).

^ The question used a Likert Scale, therefore, the mean and standard deviation are provided.

Table 5.13: The Responses of the South Australian Participants: Whether the Importance of *Guanxi* in the PRC's Business Environment is in Decline (n=18)

Is The Importance of <i>Guanxi</i> in Decline?	Research Participant South Australia (n=18)
Yes	5 (28%)
No	6 (33.3%)
Total	11 (61%)*

* Totals do not equal 18 because of missing data (i.e. Some research participants were unable to answer the question).

Table 5.12 and 5.13 indicate that there is considerable disagreement among the ROA and South Australian participants on whether the salience of *guanxi* is in decline in the PRC. Thus, Guthrie's (1998) claim that the salience of *guanxi* is in decline is neither supported or refuted by the ROA and South Australian participants.

Table 5.14 outlines the responses of PRC participants on whether the salience of *guanxi* in the PRC's business environment is in decline.

Table 5.14: The Responses of the PRC Participants: Whether the Importance of *Guanxi* in the PRC's Business Environment is in Decline (n=33)

Is The Importance of <i>Guanxi</i> in Decline?	Research Participant		
	Beijing (n=17)	Shanghai (n=16)	Total (n=33)
Yes	9 (53%)	8 (50%)	17 (51%)
No	4 (23.5%)	6 (37.5%)	10 (30%)
Total	13	14	27*

* Totals do not equal 33 because of missing data (i.e. Some research participants were unable to answer the question).

A similar percentage of Beijing and Shanghai participants reported that the salience of *guanxi* was in decline. However, a significant difference of 14 percent is evident between the Beijing and Shanghai participants who indicated that the importance of *guanxi* was not in decline. Table 5.14 also points out that a majority of participants in the PRC believe that the salience of *guanxi* is in decline. This lends some support to Guthrie (1998).

Table 5.15 reveals the South Australian and PRC participant's responses on whether the importance of *guanxi* in the PRC's business environment is in decline.

Table 5.15: The Responses of the South Australian and PRC Participants: Whether the Importance of *Guanxi* in the PRC's Business Environment is in Decline (n=51)

Is The Importance of <i>Guanxi</i> in Decline?	Research Participant		
	South Australia (n=18)	PRC (n=33)	Total (n=51)
Yes	5 (28%)	17 (51%)	22 (43%)
No	6 (33.3%)	10 (30%)	16 (31%)
Total	11	27	38*

* Totals do not equal 51 because of missing data (i.e. Some research participants were unable to answer the question).

The majority of PRC participants reported that the salience of *guanxi* is in decline. In contrast, the majority of participants in South Australia indicated that the importance of *guanxi* was not in decline. This suggests that the South Australian participants may not be able to detect changes taking place in relation to the significance of *guanxi* because of the distance between them and their clients or operations in the PRC. Table 5.15 also reveals that most of the participants reported that the salience of *guanxi* is in decline. Having said

that, the difference between the participants that noted *guanxi* was in decline and those that indicated it was not in decline, is not significant. This suggests that there is some disagreement among the South Australian and PRC participants on whether the significance of *guanxi* is in decline.

To gain insight into the overall position of the research participants who responded on the declining significance of *guanxi*, results from Tables 5.13, 5.14, and 5.15 are combined. Thus, 14 participants in the ROA and 16 from South Australia and the PRC, which totals 30 when added together, indicated that the significance of *guanxi* was not in decline. In comparison, 11 participants in the ROA and 22 from the PRC and South Australia, which totals 33 when added together, acknowledged that the salience of *guanxi* is in decline. In other words, 48 percent of the 63 participants believe that the importance of *guanxi* is not in decline and 52 percent of the 63 participants believe it is in decline. This reveals that there is considerable disagreement among the participants as to whether the significance of *guanxi* is in decline. Despite the disagreement, Chapters Seven and Eight explore in-depth the salience of *guanxi* for Australian businesses operating in the PRC, and whether the possible decline in the salience of *guanxi* is a result of the move to a rational legal system in the PRC, or a result of an emphasis by Chinese decision makers on Western economic principles, such as price, quality and service.

5.2.7 Problems Overcome through *Guanxi*

To further establish the importance of *guanxi* for Australian businesses, the participants were asked to report problems overcome by *guanxi*. These problems are reported in Table 5.16.

Table 5.16: The Problems Overcome by the Australian Participants Through *Guanxi* (n=50)

Problems Overcome with <i>Guanxi</i>	Research Participant [^]		
	South Australia (n=18)+	ROA (n=32)+	Total (n=50)
Bureaucratic	2 (11%)	11 (34%)	13 (26%)
Legal	5 (28%)	-	5 (10%)
Language	-	5 (16%)	5 (10%)
Staffing	1	-	1 (2%)
Cultural	1	-	1 (2%)
Customer Payment	-	2	2 (4%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer).

Legal problems, more so than any other, for the South Australian participants are overcome through *guanxi*. In contrast, participants in the ROA are more likely to solve bureaucratic problems through *guanxi* than any other problem. In general, the Australian participants mainly overcame bureaucratic problems with *guanxi*. However, the percentage of the ROA participants who overcame bureaucratic problems with *guanxi* is greater than all of the Australian participants. It is also interesting to note that no research participant in the ROA reported that they overcame legal problems with *guanxi*. It may be argued that the ROA participants were reluctant to acknowledge that they overcame legal problems with *guanxi* because it may be viewed by some as corruption.

Table 5.17 reveals the problems the PRC participants overcame through *guanxi*.

Table 5.17: The Problems Overcome by the PRC Participants Through *Guanxi* (n=33)

Problems Overcome with <i>Guanxi</i>	Research Participant [^]		
	Beijing (n=17)+	Shanghai (n=16)+	Total (n=33)
Bureaucratic	6	5	11 (33%)
Legal	2	-	2 (6%)
Distribution	-	2	2 (6%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer).

Even though Table 5.17 shows that the majority overcame bureaucratic problems with *guanxi*, followed by legal and distribution problems, these findings must be treated with caution because of the significant amount of missing data.

The problems the Australian and PRC participants overcame through *guanxi* are summarised in Table 5.18.

Table 5.18: The Problems Overcome by the Australian and PRC Participants Through *Guanxi* (n=83)

Problems Overcome with <i>Guanxi</i>	Research Participant [^]		
	Australia (n=50)+	PRC (n=33)+	Total (n=83)
Bureaucratic	13 (26%)	11 (33%)	24 (29%)
Legal	5	2	7 (8%)
Language	5	-	5 (6%)
Staffing	1	-	1 (1.2%)
Cultural	1	-	1 (1.2%)
Customer Payment	2	-	2 (2.4%)
Distribution	-	2	2 (2.4%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question).

As noted earlier in this Chapter, the predominant problems were legal. However, only a small proportion of participants reported that they overcame legal problems through *guanxi*. As argued previously, the participants might have been reluctant to acknowledge this because it may have been perceived as a form of corruption. Nevertheless, the findings not only highlight the importance of *guanxi* in overcoming bureaucratic, and to a lesser extent legal problems, it also implies that *guanxi* may enable Australian businesses to gain a competitive advantage. For example, overcoming bureaucratic problems

through *guanxi* may enable the Australian businesses to complete processes or establish an operation in the PRC in less time than otherwise would be possible without *guanxi*. In essence, through *guanxi* these businesses may become first movers and enjoy competitive advantages of a monopoly until competitors are able to respond and duplicate such competitive actions (Schumpeter, 1936; Porter 1985; Porter, 1990). In addition, by using *guanxi* as a form of institutional support rather than the PRC's uncertain legal system, Australian businesses may be able to economise on transaction costs. This suggestion is consistent with Boisot & Child (1988), Davies (1995), Standiford & Marshall (2000) and Luo (2000a). Economisation of transaction costs may award the Australian business with a competitive advantage. Thus, it may be argued that *guanxi* in certain instances may continue to be important for Australian businesses operating in the PRC.

5.2.8 The Advantages of *Guanxi*

To gain additional insight into the importance of *guanxi* for Australian businesses, the participants were asked to note its advantages. These are outlined in Table 5.19, as reported by the Australian participants.

Table 5.19: The Advantages of *Guanxi* Reported by the Australian Participants (n=50)

The Advantages of <i>Guanxi</i>	Research Participant		
	South Australia (n=18)+	ROA (n=32)+	Total (n=50)
Reduced Bureaucratic Interference	7 (39%)	22 (69%)	29 (58%)
Market Information	-	23 (72%)	23 (46%)
Market Access	11 (61%)	-	11 (22%)
Access to Scarce Resources	-	4	4 (8%)
Tax Concessions	-	3	3 (6%)
Reliable Material Supplies	-	8 (25%)	8 (16%)
Cheap Material Supplies	-	1	1 (2%)

+ Multiple answers are permitted.

^ Data may be missing (i.e. Some research participants were unable to answer the question and an advantage of *guanxi* is subjective).

Participants in the ROA consider reduced bureaucratic interference as more of an advantage of *guanxi* than those in South Australia. Table 5.19 also points out that the

participants in the ROA are more likely to note that market information and reliable material supplies are advantages of *guanxi*, whereas the South Australian participants are more likely to indicate that market access is an advantage. This finding suggests that the South Australian participants may be more reliant on *guanxi* for market access than the participants in the ROA. The Australian participants pointed out that reduced bureaucratic interference was the chief advantage, closely followed by market information.

Table 5.20 summarises the advantages of *guanxi* noted by the PRC based participants.

Table 5.20: The Advantages of *Guanxi* Acknowledged by the PRC Participants (n=33)

The Advantages of <i>Guanxi</i>	Research Participant [^]		
	Beijing (n=17)+	Shanghai (n=16)+	Total (n=33)
Reduced Bureaucratic Interference	9 (53%)	8 (50%)	17 (51%)
Market Information	2	1	3 (9%)
Market Access	10 (59%)	8 (50%)	18 (54%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question and an advantage of *guanxi* is subjective).

Participants in the PRC pointed out that reduced bureaucratic interference and market access are the most significant advantages, but do not see that market information is a vital advantage of *guanxi*.

Table 5.21 displays the advantages of *guanxi* acknowledged by the Australian and PRC participants.

Table 5.21: The Advantages of *Guanxi* Noted by the Australian and PRC Participants (n=83)

The Advantages of <i>Guanxi</i>	Research Participant [^]		
	Australia (n=50)+	PRC (n=33)+	Total (n=83)
Reduced Bureaucratic Interference	29 (58%)	17 (51%)	46 (55%)
Market Information	23 (46%)	3 (9%)	26 (31%)
Market Access	11 (22%)	18 (54%)	29 (35%)
Access to Scarce Resources	4	-	4 (5%)
Tax Concessions	3	-	3 (4%)
Reliable Material Supplies	8	-	8 (10%)
Cheap Material Supplies	1	-	1 (1.2%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question and an advantage of *guanxi* is subjective).

The percentage of PRC and Australian participants who reported that reduced bureaucratic interference was an advantage of *guanxi* is similar. Significant differences, however, between the Australian and PRC participants are evident for market information and market access. The PRC participants, in other words, may be more reliant on *guanxi* to gain market access than the Australian participants, whereas the Australian participants may be more reliant on *guanxi* for market information. This may be a result of the distance between the Australian participants and their clients or operations in the PRC.

In this study, reduced bureaucratic interference, market access and market information are respectively the three most noted advantages of *guanxi*. This is consistent with previous literature (i.e. Luo, 1997; Bjorkman & Kock, 1995; Ahmed & Li, 1996; Bjorkman & Schaap, 1994). As with the data from Table 5.18 on overcoming bureaucratic problems with *guanxi*, the advantages of reduced bureaucratic interference, market access and market information may result in a competitive advantage. For example, gaining market access through *guanxi*, which ordinarily may be denied, resembles the innovative way of opening up an existing market for a foreign business (Schumpeter, 1936; Porter, 1985; Porter, 1990). This highlights the importance of *guanxi* and its advantages for Australian businesses operating in the PRC. The extent to which

these advantages of *guanxi* may be translated into competitive advantages for the Australian businesses is discussed at length in Chapter Eight.

5.2.9 The Disadvantages of *Guanxi*

Although *guanxi* has its advantages, it also has its disadvantages. Table 5.22 reviews the disadvantages of *guanxi* reported by the Australian participants.

Table 5.22: The Disadvantages of *Guanxi* Recorded by the Australian Participants (n=50)

The Disadvantages of <i>Guanxi</i>	Research Participant [^]		
	South Australia (n=18)+	ROA (n=32)+	Total (n=50)
Time-Consuming	2 (11%)	16 (50%)	18 (36%)
Costly in Monetary Terms	-	7 (22%)	7 (14%)
Ineffective	-	5 (16%)	5 (10%)
Obligation	3 (17%)	-	3 (6%)
Lost Opportunities	2 (11%)	-	2 (4%)
Competitive Disadvantage	1	-	1 (2%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question and a disadvantage of *guanxi* is subjective).

The South Australian participants reported that the leading disadvantage of *guanxi* is its inherent obligations, whereas those in the ROA pointed out that the problem was the time-consuming nature of *guanxi*. Table 5.22 also evinces that considerable differences are apparent between the participants in South Australia and those in the ROA. That is, the ROA participants are more likely to note that the disadvantages of *guanxi* are that it is time-consuming, costly in monetary terms, and ineffective. In contrast, those in South Australia are more disposed to acknowledge obligations and lost opportunities. Overall, the Australian participants indicated that the main disadvantage of *guanxi* is its time-consuming nature.

Table 5.23 summarises the disadvantages of *guanxi* noted by the PRC participants.

Table 5.23: The Disadvantages of *Guanxi* Reported by the PRC Participants (n=33)

The Disadvantages of <i>Guanxi</i>	Research Participant [^]		
	Beijing (n=17)+	Shanghai (n=16)+	Total (n=33)
Time-Consuming	5 (29%)	3 (19%)	8 (24%)
Costly in Monetary Terms	-	1	1 (3%)
Ineffective	-	-	-
Over reliance	7 (41%)	4 (25%)	11 (33%)
Obligation	3 (18%)	4 (25%)	7 (21%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question and a disadvantage of *guanxi* is subjective).

Table 5.23 shows that a higher percentage of Beijing participants than those in Shanghai reported that the disadvantages of *guanxi* are time consumption and over reliance. The obligations of *guanxi* are viewed as a disadvantage by a similar percentage of participants in Beijing and Shanghai. Although over reliance was viewed as the principal disadvantage by the PRC participants, a greater percentage of participants in Beijing felt that it was a disadvantage. It is interesting to note that no PRC participant revealed that *guanxi* was ineffective in achieving their desired goal.

The disadvantages of *guanxi* reported by the Australian and PRC participants are outlined in Table 5.24.

Table 5.24: The Disadvantages of *Guanxi* Acknowledged by the PRC and Australian Participants (n=83)

The Disadvantages of <i>Guanxi</i>	Research Participant [^]		
	Australia (n=50)+	PRC (n=33)+	Total (n=83)
Time-Consuming	18 (36%)	8 (24%)	26 (31%)
Costly in Monetary Terms	7	1	8 (10%)
Ineffective	5	-	5 (6%)
Over reliance	-	11 (33%)	11 (13%)
Obligation	3 (6%)	7 (21%)	10 (12%)
Lost Opportunities	2	-	2 (2.4%)
Competitive Disadvantage	1	-	1 (1.2%)

+ Multiple answers are permitted.

[^] Data may be missing (i.e. Some research participants were unable to answer the question and disadvantages of *guanxi* are subjective)

The participants in Australia acknowledged that the time-consuming nature of *guanxi* is its foremost disadvantage. In contrast, those in the PRC noted that over reliance on *guanxi* was its principal disadvantage. Even though *guanxi* has its disadvantages, it is,

however, not seen as ineffective in achieving its desired outcomes, as only 6 percent of participants in this study suggested that *guanxi* was ineffective. Table 5.24 also points out that the PRC participants were the only ones to report that over reliance on *guanxi* was a disadvantage. It may be argued that because of distance, Australian participants are more reliant on *guanxi* and, therefore, do not view it as a disadvantage. This may also explain why they may not perceive the obligations of *guanxi* as a disadvantage to the extent of those in the PRC, and why they view *guanxi* as more time-consuming than PRC participants.

Despite these differences, the central disadvantage of *guanxi* is its time-consuming nature, which supports previous literature (i.e. Davies et al 1995; Tsang, 1998; Yi & Ellis, 2000; Fock & Woo, 1998). Over reliance and obligations are the second and third most reported disadvantages, with 13 percent and 12 percent of participants respectively noting such disadvantages. The finding that over reliance on *guanxi* is a significant disadvantage is consistent with Bun and Kiong (2000, p. 75).

5.3 Summary

This Chapter indicated that the South Australian, Beijing and Shanghai participants acknowledged that banquets and gifts are widely used to develop and maintain *guanxi* and that it is not a form of corruption. To further enhance the understanding of *guanxi*, these complexities are examined in-depth in the following Chapter.

It also noted that in the findings there was significant disagreement over whether the salience of *guanxi* was in decline. Given that legal problems were mainly encountered by the participants, it appears from this study that the argument that the importance of *guanxi* is in decline because of the construction and implementation of a rational legal system at the state and firm level may not be applicable to Australian businesses. To determine the role and importance of *guanxi* for Australian businesses, Chapter Seven

will provide an in-depth analysis of the above argument and the legal problems encountered by the participants within the framework of transaction cost economics.

The participants in this study overwhelmingly indicated that *guanxi* was important for reducing bureaucratic interference. Market access and market information were also highly regarded as advantages. To further establish the role and importance of *guanxi* for Australian businesses, Chapter Eight reviews in-depth the applicability of the advantages of *guanxi* to the first mover theory of competitive advantage.

Even though *guanxi* has its advantages, it also has its disadvantages. The time-consuming nature of *guanxi* is the principal disadvantage, according to the participants in the study, followed by over reliance and obligations. These disadvantages, however, do not appear to detract from the effectiveness of *guanxi* in achieving desired outcomes. The disadvantages are explored further in Chapter Eight.

Chapter Nine examines the ability of discretionary policies to undermine the competitive advantages obtained by an Australian business, analysing the second and third most reported problems human resource and finance.

CHAPTER SIX: UNRAVELLING THE COMPLEXITY OF DEVELOPING AND MAINTAINING *GUANXI* AND WHETHER *GUANXI* IS A FORM OF CORRUPTION

6.1 Introduction

In analysing the qualitative data of the interview participants, this Chapter unravels the following complexities of *guanxi*: the methods used to develop and maintain *guanxi*, and whether *guanxi* is a form of corruption. Unless otherwise stated, *guanxi* refers to economic *guanxi*.

6.2 Developing and Maintaining *Guanxi*

Chapter Five indicated that there are a variety of methods used by the interview participants to develop and maintain *guanxi*, which included banquets, gifts, and regular contact. These methods are analysed in the following section to further enhance the understanding of *guanxi*.

6.2.1 Banquets

Banquets were the most widely employed method to develop and maintain *guanxi* with 57 percent of the South Australian, Beijing and Shanghai interview participants using such a method. S4's mainland Chinese General Manager stated:

The banquet is a time for you to establish good relationships in a relaxed atmosphere, and more often than not, it is done outside of working hours. This is where you get to know the person with whom you want to have a business relationship. You can relax and forget about the trivialities of work.

S4's General Manager's statement points out that it is not the banquet *per se* but the environment which the banquet creates that is important for developing *guanxi*. This is further noted by the Director of A15:

Forming a relationship is paramount to the Chinese and one way the Chinese like to do that is by having a meal together. This may range from a simple lunch with a bowl of rice and some noodles or through to a bells and whistles banquet. The type of meal varies in accordance with the people and the circumstances surrounding the need for a meal. More often than not, the relationship building starts off with a more elaborate banquet that is often a show of strength, power and wealth on the Chinese behalf. But once the relationship has developed to a level where they say 'okay lets just go up and have a bite to eat' you know it is indicative of a growing sophistication in the relationship.

Not only does this comment indicate that banquets are important for developing a relationship, it also suggests that the type of 'meal' presented may be correlated with the status of the relationship. According to A9's Export Manager, the environment of a banquet provides an opportunity for parties to develop the trust and rapport needed in economic exchange:

Banquets are a necessary part of business. It is the way the Chinese conduct business. A banquet gives you an environment where you can relax and talk on a one to one basis building up trust and rapport.

In agreement, A14's Export Manager stated:

Banquets form a major part of Chinese business lives. The Chinese view a banquet as a tool to build up the trust and rapport in a relaxed atmosphere.

Building trust appears to be central to the development of *guanxi*. According to Xin & Pearce (1996, pp. 1641-1642), Lui (1998, p. 338), Kiong & Kee (1998, pp. 84-85), Davies (1995), and Davies et al (1995, p. 207), trust is extremely important for the Chinese because of the uncertain regulatory and legal environment that governs economic transactions in the PRC. Trust, or what Kiong & Kee (1998, p. 84) refer to as *xinyong*, which literally means the use or usefulness of trust, conveys several meanings. For example, *xinyong* may refer to the integrity, credibility, trustworthiness, or the reputation and character of a person (Kiong & Kee, 1998, p. 85).

The Chinese, in general, deal with those who have *xinyong* and avoid those with little or no *xinyong*. On a business level, the Chinese are less interested in general reputations than in whether an individual may be expected to deal honestly, which is a function of whether they or their own contacts have had satisfactory past dealings with

the individual (Kiong & Kee, 1998; Lui, 1998). This suggests that one's reputation is an achievement and not an ascription based upon ethnicity or kinship ties (Lui, 1998, p. 348). When developing business *guanxi* from scratch, an individual has to build and prove his or her *xinyong*. This depends on the willingness of an individual to undertake the risk of conducting business with another, which is influenced, in turn, by the pre-existence of *guanxi* established through an intermediary, or shared *guanxi* bases. If neither of these exist, the reluctance to undertake the risk of conducting business with an individual is higher and the time involved in building *xinyong* may be protracted (Kiong & Kee, 1998, p. 85; Lui, 1998, p. 348). Worm & Frankenstein argue that it may take up to 6 months or a year for foreigners to develop *xinyong* within a relationship before business is conducted (2000, pp. 270-272).

The time-consuming process of developing *xinyong* is noted by A18's Singaporean Chinese Regional Sales Manager:

When the Chinese first meet you, they will not start conducting business. Of course, there are exceptions but by and large initially the Chinese people would like to get to know you, slowly building that trust and rapport with you. Once the Chinese have established that trust and rapport it is easier for them to conduct business with you.

Consistent with A18's Singaporean Chinese Regional Sales Manager, A4's Mainland Chinese Solicitor stated:

in dealing with the Chinese people you really need to have patience and you really need to take time to build that trust and observe the person that you want to develop that relationship with.

Therefore, developing *xinyong* and ascertaining whether there is a risk in conducting business with an individual is a time-consuming process. During this time, the Chinese may be evasive:

In the beginning of developing the relationship, the Chinese were very evasive. For example, if there was a negative answer they would dance around the issue. But as time progressed trust was developed. And now if there is a negative answer the Chinese have no qualms about giving a negative answer (A10's General Manager).

Thus, trust building is an essential element in a relationship because it influences the effectiveness of a relationship (Wong, 1997, p. 57).

Although banquets are an integral part in developing *xinyong* within economic *guanxi*, S6's mainland Chinese Chief Representative indicates that once *guanxi* has been developed banquets are not a necessity to maintain the *guanxi*:

In the beginning when you first meet your customer you need to take them out for a banquet, a drink, karaoke, etc. But once you have supplied them with good products and after sales service a couple of times, then you do not need to do that anymore. It is just an introductory type of courtesy. It gives you an opportunity to develop a relationship with the other person. This environment relaxes the tension and then they slowly realise you are a nice guy and they are willing to do business with you.

Nevertheless, a number of research participants indicate that banquets also have the purpose of conveying respect for the other party of the relationship. As the Hong Kong Chinese Owner Manger of A13 noted:

When we go and visit them [our customers or partner] you have to be able to enjoy life with them. In other words, you dine with them in the evenings to build that relationship and trust between the two parties. It is also a show of strength and respect to your partner or customer.

Likewise, S11's Operations Manager commented:

Our company policy is that you do not accept anything be that lunches or gifts. However, when it comes to our operations in Shanghai our head office in Australia turns a blind eye. This is because if you do not go to lunch, the Chinese will be very offended unless you have a good excuse for not going.

Not only does the environment of a banquet provide the atmosphere to develop *xinyong* within the parameters of the relationship, it is also a sign of respect for the other party, which is consistent with Smart (1999), Xin & Pearce (1996), and Hsing (1998). Refusing a banquet invitation may not only indicate a lack of respect for the other party, it may also jeopardise the fulfilment of the business deal, whatever it may be. Thus, banquets are important for the development and maintenance of *guanxi*.

6.2.2 Gift Giving

Gift giving was the second most popular method used to develop and maintain *guanxi*, with 35 percent of the South Australian, Beijing and Shanghai participants employing such a method. As important as gift giving is for developing *guanxi* (Yang, 1994; Hsing, 1998), according to A4's mainland Chinese Solicitor certain types of gifts are more appropriate:

I do not think that it is important to buy a big gift for some party official. But I do think that a proper gift will help. However, if you try to please someone in the initial stages of contact by giving them a big gift, it will create doubt in the receiver's mind of your intentions. If you want to give someone a gift, a medium size gift would be most appropriate. For example, if you are dealing with a director general in a Chinese governmental department and you give them a camera in the initial stages of contact, it is too much. A more appropriate gift would be something like a kangaroo skin that is symbolic and unique to Australia. But if you have already developed a relationship with this person past the business stage and more on a personal friendship to friendship basis then you can possibly give a big gift in a non-official way.

This implies that gifts which are symbolic of Australia and unique are most appropriate for developing *guanxi*, whereas large gifts may be viewed as a bribe because they do not disguise the instrumental nature of the gift (Yang, 1994; Smart, 1999). However, if the relationship incorporates both social and economic *guanxi*, then large gifts may be appropriate if they are based on friendship. The General Manager of A6 also pointed out that unique and symbolic gifts were given to develop *guanxi*:

We always give gifts but we keep it to something reasonably modest, such as an Australian flag, boomerang or a cheap opal. Something that is unique and symbolic.

Similarly, the General Manager of B12 noted:

The first couple of times I visited the PRC I took along a [cheapish] gift that was representative of Australia, such as a small stuffed kangaroo, a small plate painted with a kangaroo or a painting of Sturt desert peas.

Thus, it appears that unique and symbolic gifts are the most appropriate for developing *guanxi*. This is in accordance with Hsing (1998, p. 135) and Yang (1994, pp. 137-139) who contends that what matters is not just the gift itself but also the message carried by

the gift. Gifts also have a use value independent of their monetary value. A rare or unique, but not necessarily expensive, gift that cannot be bought just because someone has the money demonstrates greater respect and sincerity for the gift receiver. If it is something that is not available in the market and can not be obtained without making special efforts and going through special channels (again that takes another personal network to gain access to those channels), the gift will be much more valuable and appreciated (Hsing, 1998, p. 135). In other words, the type of gift presented correlates with the amount of respect shown to the receiver and the sincerity in establishing a relationship.

The notion that gift giving conveys respect for the receiver is outlined by S2's Singaporean Chinese General Manager:

We do give gifts but I think there is a lot of misconception about giving gifts. In China, it is a tradition to give gifts. For example, if I give a Chinese government official a monetary gift of A\$200 or A\$1000, normally the Chinese government official would see that they returned me a gift. It is not any dubious payment to develop *guanxi*. It is more out of mutual respect. You respect them. They respect you. Therefore, you exchange gifts.

While this comment indicates that gift giving is a mark of respect for one another, it is also adding weight to Yang's (1994, p. 129) claim that more emphasis is being placed on monetary exchange in the 'art of *guanxi*'. According to S5's Malaysian Chinese Director of the PRC, corporate gifts also convey the same message:

We give our customers and people that we have a relationship with corporate gifts. Something with the corporate logo on it to show respect.

Correspondingly, S7's Hong Kong Chinese General Manager pointed out:

we give corporate gifts with the company logo on it. We give gifts such as pens or T-shirts with the company logo on them to show respect and they are well received.

Whether the level of respect differs between a corporate gift with a company logo, a unique gift, or a unique gift with a company logo is beyond the scope of this thesis.

Nevertheless, the point is to recognise that gifts have a use value other than their monetary value.

Even though ‘unique’ gifts have a use value other than their monetary value, according to a couple of research participants it is not necessary to continually present them. As A10’s General manager remarked “we have been given advice by the Office of Asian Business in Adelaide [South Australia] that it is not necessary to continually give gifts”. In agreement, A16’s Operations Manager International noted:

Sometimes when you go to the PRC you take them a nominal Australian gift, such as wine but you would not do that every time you visit. However, we do send them gifts for Chinese New Year and other special Chinese festivals.

Although continually giving ‘unique’ gifts may not be necessary, this comment also suggests that it is important for maintaining *guanxi* to send gifts during the Chinese festivals. This is supported by S9’s mainland Chinese Customer Service Manager:

If it is Chinese New Year it is a tradition to give gifts. Therefore, I follow the Chinese traditional way and give gifts, as it is showing respect to the Chinese.

While gift giving ordinarily shows respect for the receiver, during Chinese festivals gift giving appears to heighten the relationship and respect shown because of the importance of these festivals in Chinese culture. This is consistent with Yang (1994, p. 136) who contends that Chinese festive occasions are usually the sites for the circulation of *renqing* or “expressive gifts”, which cement relations without a clear tactical advantage in mind. For this reason, their *renqing* associations are especially suitable in disguising the instrumental nature of the gifts (Yang, 1994, p. 136). Even though these festivals are especially suitable in disguising the instrumental nature of a gift, there is evidence they may be used to disguise corrupt actions. As S7’s Hong Kong Chinese General Manager remarked:

In China, there are three very important festivals: Chinese New Year, Mid Autumn Festival and the Dragon Festival. As you know trucks distribute our products. Therefore, we have to deal with the traffic police in Shanghai everyday. They expect us to give them a gift during these festivals, it is a tradition. We cannot avoid it. Because if we do not give them gifts during these festivals, they

will take our trucks off the road for any reason they think of. So we buy them a moon cake or a few bottles of wine and some fruit.

The suggestion that the actions of the traffic police may be a form of corruption is consistent with Hsing's (1997, pp. 154-155) research, and will be further highlighted later in this Chapter.

According to the Director of A17, Chinese festivals are not the only occasions that provide an opportunity for disguising the instrumental nature of a gift:

I like to disguise the gift giving process and do not want to be obvious about it. Thus prior to Christmas I would send modest gifts to our counterparts in the PRC, on the pretext of saying 'well it is our custom in Australia to give gifts to our friends at Christmas' and they reciprocate (A17's Director).

Therefore, there are many occasions that are especially suitable for disguising the instrumental nature of a gift.

The notion that *guanxi* is established purely for economic advantage and that it must be paid for, is reiterated by S15's mainland Chinese Sales Representative:

If you are trying to set up a business relationship, which means you want to obtain some benefit. You must pay for it. For example, if I want to sell a machine to a Chinese State Owned Company (SOC), I must investigate who is the person that makes the decision to buy the machinery. I must then go through certain *guanxi* to arrive at that person such as a secretary, an engineer or may be the person who is in charge of the project. Then I will entertain them. I may give them gifts and invite them to dinner or an amusement place to become familiar with them. Because I have only been in business for a short period I must set up the relationship and because I have only been in Shanghai for 4 years I do not have old relationships here. If I was in my home town I would have old relationships and the job would be easier. But our business is not always fixed in one place, it is spread all over China. Therefore, it is impossible for me to have existing relationships all over China. Thus, you always have to remember to call or send a card to them, and it is not necessary to continually send gifts. You do not send gifts when you do not need them but if you do need them you send gifts.

Notwithstanding the fact that *guanxi* may be ignored when one has extracted all one desires, no one knows when the need for favours will arise again. Thus, it is important to keep small gifts flowing during the three major Chinese festivals of the year: New Year's Day, the Dragon Festival, and the Mid-Autumn Festival (Hsing, 1998, p. 137).

Although banquets and gift giving are important tools for developing and maintaining *guanxi*, according to S12 they may be somewhat over emphasised:

I think it is a part of business that is played on enormously by the Chinese side, and we as Australian companies are often taken in by the mystique of it all. You know bloody *guanxi* and everything else. I mean ultimately in my view it is all about the deal. You know the bottom line is still the deal. And the deal is going to be done and a lot of that relationship building, as the Chinese call it is actually just cosmetic. I guess the reason for saying that is particularly given my experience in Taiwan of 7 years. That is how it is in Taiwan. If you want to do the deal, the deal is going to be done whether you can drink people under the table, go karaoke or go to night-clubs, etc. If the Chinese want to deal with you, the deal is all that matters. In the PRC, I think it is a bit more traditional but ultimately if a company wants your product or to deal with you, they will do the deal without the other stuff. For example, I do not drink. I can still do my job perfectly well. The reason people want to deal with me or I want to talk with them, is about the issue at hand and nothing else. I do not want to underestimate the importance of banquets, and gifts, etc. But I guess the main thing for Australian and Western companies is to be very wary that you do not become consumed by that side of it, and lose sight of why you are really in the PRC. That is what the Chinese are trying to do to you. To be frank they are trying to build a relationship but they are also trying to catch you off guard or get you in a situation where you are off guard. In short, it is the bottom line that counts and Australian and Western companies should not lose sight of this. They should be wary of some of the methods in which *guanxi* is developed, such as banquets, gift giving, and entertainment. And always stay focused.

In other words, the Chinese utilise the ‘art of *guanxi*’ as a facade to project to foreign parties that their primary concern is the relationship. As a result, unsuspecting foreigners may believe that the relationship is more about social *guanxi* characterised by ‘friendship’ than economic *guanxi*. This belief may enable the Chinese to extract more concessions out of the relationship that may not have been possible if the foreigners were focused and understood the complexities of developing and maintaining *guanxi*. S12 also noted that the Chinese may not only use the ‘art of *guanxi*’ to extract more benefits from unsuspecting foreigners, they may also use the Chinese concept of face (*mianzi*):

It is the ultimate card trick for the Chinese because there are very few Westerners who will stand up to it. You know in the sense, if they say ‘you have to do this deal or give me these goods at this price. Otherwise I will lose face in front of my boss’. The Chinese play that hand quite often and most Australian and Western companies will often give into it in the end. The reality of face and losing face is very important between Chinese and Chinese. But in my view between Chinese and foreigners it is not particularly important at all because the Chinese can

always write that issue off because you are a foreigner. The Chinese would not lose face in front of their boss because they could just say 'I could not do this deal because this stupid foreigner did not understand'.

Fang (1999) supports the comments on *guanxi* and *mianzi* by S12. According to Fang (1999, p. 252), the Chinese may take advantage of a foreigner's stereotypical image of the PRC and the Chinese in regard to *guanxi* and *mianzi*. These traits can often be a myth. Foreign business people should both learn to practice and understand *guanxi* and *mianzi* so they can distance themselves from them when the situation requires it (Fang, 1999, pp. 252-253).

6.2.3 Regular Contact

Regular contact was the least noted method used to develop and maintain *guanxi* by the South Australian, Beijing, and Shanghai interview participants, with 33 percent using such a method, though it by no means correlates to the perceived importance of such a method. Regular contact, banquets, and gift giving are all important in the development and maintenance of *guanxi* and should be treated as such. The General Manager of A10 remarked:

I think it is important as a good relationship building exercise that you visit the PRC regularly because it indicates to the Chinese that you are not [fly-by nighters] that are just dropping in. We have visited various people in the PRC a total of about 7-10 times over a few years. I have seen on occasions where people have just dropped in for a short period and have been given a bit of short shift by the Chinese.

In other words, regular visits disguise the instrumental nature of the relationship. According to A2's Regional Marketing Director, this may make conducting business in the PRC easier:

Regular visits to the PRC are important in building and developing the relationship and if that all clicks, it makes the job of selling or building up a business much easier.

Not only is it important for Australian businesses dealing with the PRC at arms length to regularly visit, A15's Director argues that "it is equally if not more important to keep in

regular contact when not visiting the PRC". These comments suggest that failure to disguise the instrumental nature of the relationship through regular visits and contact may be viewed in a negative light by the Chinese, which ultimately may have a negative impact on the business (Abramson & Ai, 1996, p. 42). The above comments also imply that face to face contact may enhance the relationship more so than indirect methods, such as telephone, fax, or email. The Export Manager of A9 puts the importance of face to face contact into context:

Personal connections [*guanxi*] are very important in the PRC. You should visit them at least twice a year, and see them face to face to build that rapport and bond with one another because if you do not do it, it is not a positive step in the relationship. You can do business without the face to face contact over the phone but over the table conversation is much better, as you get to know them a lot better on a personal level.

Though contact via the telephone is important, it appears that a greater level of understanding between the parties is obtained through face to face contact, which may lead to positive outcomes for the business.

Even though visiting the PRC is important for developing and maintaining *guanxi*, bringing Chinese customers, staff members, or business partners to Australia may also achieve the same result. As A14's Export Manager noted:

We bring members of the local provincial government in the PRC, customers and staff members from our PRC operations to Adelaide for training and sight seeing. Every year we would bring between 60-100 Chinese expatriates to Adelaide for 'training'. This is all about building trust and developing the relationships.

On the whole, regular contact is important for developing and maintaining *guanxi* because it enables the Chinese to become better informed of the intentions and/or operations of the business. The better informed the Chinese, the less likely a business will face obstacles in achieving its instrumental goals (Hsing, 1997, p. 154).

6.3 Whether *Guanxi* a Form of Corruption

The results in Chapter Five revealed that 80 percent of the interview participants indicated that *guanxi* was not a form of corruption. A11's Operations Manager for the Asia Pacific remarked:

Guanxi is perceived by many Westerners as corruption because it does not fit with our practices of business. This, however, does not make *guanxi* corrupt. In China, business is more about relationships and the network of relationships you have, as opposed to brown paper bags full of money being handed around. And the rules are very clear among the network of relationships. For example, if you offend someone within that network do not expect to do business with that person or possibly the whole network.

In other words, *guanxi* is more about relationships based on reciprocity than any corrupt practices. In agreement, B5's Owner Manager stated:

Guanxi would be corruption if you viewed it from a Western legal perspective. However, it is very difficult to label something that way in the PRC. For example, if your friend happens to know the ticket seller in the train station, and you need a ticket for a soft sleeper to Xian and the tickets were sold out three months ago, and your friend can obtain one if you promise something in return: Is that necessarily corruption? Again, if you know someone who has the right to sell a block of land and you put in a bid and then that person sells you the block of land based on your *guanxi*. Obviously there is some implied agreement that the seller will obtain something in return: Is that corruption?

Thus, *guanxi* should not be viewed from a Western legal perspective, it should be viewed for what it is, conducting business based on reciprocal relationships with imputed obligations (Yang, 1994, pp. 139-145). B13's Chief Representative stresses this point:

Conducting business in the PRC through *guanxi* is not a form of corruption. It is all about relationships. Furthermore, it depends if you are viewing *guanxi* from a Western position. For example, from an Australian perspective holding a banquet or going to karaoke may be seen as a bribe. However, in the PRC that is a normal part of a business relationship.

Retreating to the surrounds of a banquet or karaoke lounge to develop and maintain *guanxi* are put into context by B16's Chief Representative:

When you are selling your product you are trying to build up a rapport with your potential customer. You might take them to lunch or tennis, etc. So they become comfortable with you and your message you are trying to deliver.

This remark points out that building business *guanxi* in the surrounds of a banquet or over a game of tennis is not corruption. These activities merely provide an opportunity to develop *xinyong* and build rapport.

The Director of A15 argued that “Westerners also perceive the endless stream of favours that one another do for each other within a *guanxi* network as corruption”. The Director of A17 suggests that the exchange of favours is not a form of corruption:

We use our relationships to gain access to people, to get onto tendering lists and we do not exchange money for that. Because *guanxi* is a reciprocal relationship we may introduce them to someone or find out some information for them.

Thus, corruption through bribery is for an immediate and specific purpose, whereas *guanxi* is long term and diffuse (Lovett et al 1999). This is supported by B8’s mainland Chinese Chief Representative:

The Chinese would never regard *guanxi* as a form of corruption, unless something under the table or illegal was involved. The Chinese simply regard conducting business based on relationships as a normal business practice in the PRC.

Hence, Westerners should refrain from passing judgement on *guanxi*, and labelling it corruption, until they have gained insight into the Chinese moral traditions (Snell & Tseng, 2001, p. 172). The point that *guanxi* is more about relationships and corruption is about illicit payments is highlighted by A13’s Hong Kong Chinese Owner Manager:

Conducting business based on personal relationships is not a form of corruption. It is doing business based on who knows who. But it becomes corruption when under the table deals are done.

Similarly, the Export Manager of A14 pointed out:

Guanxi is not corruption. It is all about personal relationships and that is how the Chinese conduct business. Of course, corruption does exist but *guanxi* is more to do with personal relationships than some illicit payment.

In essence, *guanxi* differs from corruption by the virtue of illicit payments. Intertwined with this notion, is that corruption involves receiving illegitimate benefits:

Corruption is where benefits are exchanged between parties that are not legitimately due to either party in the normal course of a business relationship. Therefore, corruption is where you are exchanging a benefit in return for the

other party using their discretion or government position to advantage your business. When we build business *guanxi* with government officials we are not providing any monetary or other benefit to these officials. We are simply obtaining something that should be accruing legitimately in the normal course of business (B11's Business Investment Manager).

In other words, using *guanxi* to obtain illegitimate benefits in the course of business, is not *guanxi* but corruption. The point that illegitimate entitlements is not *guanxi* but corruption is reinforced by S7's Hong Kong Chinese General Manager:

If you want to set up a company in Shanghai you have to go through many steps to complete the process. You have a relationship with the top person and he/she lets you jump from step 1 to step 10 forgetting all the intermediary steps. Now what you have done is not fulfilled the legal requirements for establishing a company in Shanghai. In effect, you are an illegal company. There is a risk associated with jumping from step 1 to step 10 in that your friend may not be the top person forever and when another person comes along they will notice that you have missed these steps and cause you all sorts of problems. Even though you know the top guy and he is willing to help, let him help by speeding up the process from step 1 to 10.

Similarly, S10's mainland Chinese Chief Representative pointed out:

On a scale, *guanxi* is just about conducting business on relationships and that is a common practice in the PRC. However, if you really want to push it up the scale it can certainly lead to corruption. Corruption is a quick way of developing the *guanxi* it is like queue jumping. If I wanted to develop a relationship with someone and that person wanted to develop a relationship with me, it would take time. But if you only have seven days to get the bidding going on say a contract and you want to make an impression. And you take the short cut by offering illicit payments, then that is not *guanxi* but pure corruption.

Thus, *guanxi* itself is not a form of corruption, it is the illegal actions of individuals within the relationship that are corrupt, and ultimately cause *guanxi* to be mislabelled as corruption. The difference between what constitutes *guanxi*, and what constitutes corruption is outlined by Luo (2000a, pp. 199-202):

- (1) *Guanxi* is an ingredient of social norm whereas corruption deviates from social norm.
- (2) *Guanxi* is, in general, legal, whereas corruption is illegal.
- (3) *Guanxi* builds on favour exchange whereas corruption mostly involves monetary exchange.

(4) *Guanxi* involves implicit, social reciprocity whereas corruption pertains to explicit, transactional reciprocity. The deal is transactional in the sense that the terms of the briber and the corrupter are explicitly, orally specified.

(5) *Guanxi* does not involve any lawful risks if it fails, whereas corruption is linked to high legal risks and uncertainties.

(6) *Guanxi* builds on a long-term association whereas corruption is short-term transaction specific.

(7) *Guanxi* does not specify a time limit, whereas corruption often requires timeliness.

(8) *Guanxi* builds on trust whereas corruption is based on “commodity”.

(9) *Guanxi* is transferable whereas corruption is not.

Although Luo (2000a) distinguishes between *guanxi* and corruption, confusion may still be apparent when money is used as an alternative medium of exchange in a *guanxi* relationship (Yang, 1994, pp. 166-167). A litmus test to determine whether monetary exchange is corruption would be to follow Luo (2000a) and ask the following questions: (1) Does the action deviate from societal norms? (2) Is it in the eyes of the Chinese legal system deemed an illegal activity? (3) Does the action pertain to explicit, transactional reciprocity? (4) Are there high legal risks and uncertainties attached to the exchange? (5) Does the activity deal with a short-term “transaction”? (6) Does the activity specify a time limit? (7) Is the activity based on “commodity”? and (8) Is the action transferable? If ‘yes’ is the answer to any of the questions from one to seven, and ‘no’ for question eight, then it is highly likely that the monetary exchange is a form of corruption.

Even though it may be clear that *guanxi* is not corruption *per se*, two participants contended that it is difficult to separate *guanxi* from corruption. B4’s Chief Representative stated:

There is not a great deal of difference between *guanxi* relationships and corruption. They go hand in hand. It is who you know and what you know and how you can use it. Ultimately, it ends up in corruption. And the fragility of the *guanxi* system is that you have no idea whether somebody is playing the middleman for you or against you at your expense financially or commercially. There is a vale of secrecy over all these things.

B4's Chief Representative's comment implies that the reason there is no real difference between *guanxi* and corruption lies in the difficulty determining whether the intentions of individuals in a *guanxi* network are corrupt. Similarly, B6's General Manager for the PRC said:

It is very difficult to know, because of your relationships whether you have been involved in anything that may be deemed corruption. For example, I have just sold two motor cars, which I did not know how to complete the transaction in the PRC as it is different to Australia. Therefore, I gave the task to our driver, which I trust explicitly. I do not know whether the driver made A\$200 out of the deal and I am involved.

The difficulty in determining whether one has been involved in corruption may be a result of an individual's length of business experience in the PRC. This is because both B4's Chief Representative and B6's General Manager's PRC business experience is less than one year, whereas the interview participants that did not label *guanxi* as a form of corruption have been conducting business with the PRC for more than one year. Having said that, determining whether the actions of an individual are corrupt may even prove difficult for the battle hardened China business specialist because of the complex nature of *guanxi*.

Despite the above discussion focusing on the difference between *guanxi* and corruption, it is important to note that corruption does exist in the PRC. For example, some argue that corruption has become the most lethal threat to China's economic development, with a suggestion that graft may cost the Chinese economy between 4-17 percent of Gross Domestic Product (GDP) each year (Pei, 2001, p. 29; Gilley, 2001, p. 60), and being involved in corruption does have grave consequences. For example, a former Deputy Governor of Jiangxi province, Hu Changqing, was tried for taking A\$650,000 in bribes, and shot for his crimes (Ziegler, 2000, p. 13). Not only does corruption appear to have grave personal consequences, it is a zero sum game, as B2 indicates:

If you were in a situation where you are going to win a business deal by paying someone off, then you should not be conducting that business because there may be someone else that could offer a better pay off and in the long run people will double cross you.

Similarly, B16's Chief Representative stated:

There is also a practical reason why you do not bribe people or officials in the PRC. Who do you bribe? The PRC is a multicentred series of influences and trying to work out which group has more influence than the other is difficult enough. It is even harder to work out which people or officials, seen or unseen carry the most influence.

Therefore, trying to bribe someone on the pretext of gaining favourable treatment is fraught with difficulties and danger, and may not enhance a businesses' success in the PRC. Australian businesses also need to be aware that amendments made in 1999 to the Australian Criminal Code Act of 1995 make it an offence to bribe foreign public officials in external territories (Criminal Code Amendment-Bribery of Foreign Public Officials-Act 1999, no. 43).

6.4 Summary

This Chapter identified that economic *guanxi* is primarily developed through banquets, gift giving, and regular contact, which are used to disguise the instrumental nature of the relationship. It also argued that the 'art of *guanxi*' and *mianzi* are often used as strategies by the Chinese to gain a business advantage over unsuspecting foreigners. In addition, this Chapter argued that *guanxi* is not a form of corruption, and that Westerners should refrain from making moral judgements without understanding the complexities of such relationships in the context of the PRC.

The following Chapter examines whether the salience of *guanxi* is in decline and whether it is a result of the move to a rational legal system in the PRC, as argued by Guthrie (1998). It also examines the legal problems encountered by the research participants to determine whether the Chinese legal system continues to be marred by

uncertainty and whether *guanxi* may be important as a substitute for formal institutional support in the PRC.

CHAPTER SEVEN: THE SALIENCE OF *GUANXI* A TRANSACTION COST THEORY PERSPECTIVE

7.1 Introduction

The quantitative results in Chapter Five revealed that the salience of *guanxi* may be in decline, although this is not entirely clear from the findings. The quantitative results in Chapter Five also indicated that the main problems encountered by the research participants were legal, with 57 percent of participants noting such problems. Although it is not entirely clear from the research findings that *guanxi* may be in decline, this Chapter discusses whether the decline in the significance of *guanxi* may be a result of the construction and implementation of a rational legal system in the PRC. It also analyses the legal problems encountered by the research participants to ascertain whether the Australian businesses are able to obtain transaction cost advantages, despite the indication that the salience of *guanxi* may be in decline. Through this analysis the Chapter determines where and when *guanxi* is important for Australian businesses conducting business with the PRC. There was no significant difference in business size, market entry strategy, industry classification, and the length of an individual's business experience with the PRC among the research participants who encountered legal problems in the PRC. However, there was a substantial difference in the date of first entry into the PRC by the research participants who encountered legal problems (see Appendix F).

7.2 The Increasing Importance of Western Economic Principles for Conducting Business in the PRC

Even though it is not entirely clear from the findings in Chapter Five that the importance of *guanxi* may be in decline, a number of the participants comments are analysed to determine whether the decline in the importance of *guanxi* is a result of the construction

and implementation of a rational legal system in the PRC, as argued by Guthrie (1998).

B5's Owner Manager stated:

The Chinese market is moving towards a more transparent environment. As a result, the importance of conducting business on a Western business model is increasing while *guanxi* is becoming less important.

In other words, as the PRC's business environment becomes more transparent through the implementation of laws and regulations, greater emphasis is placed on Western economic principles, such as product quality, price competitiveness, and service instead of *guanxi*. Correspondingly, S12 indicated that Western economic principles are coming to the fore in the PRC:

Certainly *guanxi* is an important part of doing business. But having said that, it is something that should not be overly emphasised, if I can put it that way. It is important but it is just like other parts of the business environment. Increasingly in China, with the increasing transparency in the way business is done here, the importance of it is reducing.

This comment suggests that *guanxi* is only one factor in a range of factors that need to be considered when operating in the PRC. It also implies that as the PRC's business environment becomes increasingly transparent more weight is given to other factors, such as price, quality, and after sales service than *guanxi*. More specifically, B17's Hong Kong Chinese Chief Representative suggests that the importance of *guanxi* is in decline because Chinese decision makers are having to become more accountable for their decisions:

guanxi is becoming less of a determining factor to succeed in business in this country. These days the decision makers in the PRC are having to become more accountable for their decisions. This is based on the introduction of laws and regulations governing their decisions. Therefore, decisions can not be based on *guanxi*. They have to be made in line with certain criteria. As a result, *guanxi* is becoming less important. I would not say less important but less of a determining factor to succeed in business in this country.

Similarly, A18's Singaporean Chinese Regional Sales Manager suggested that because of the increasing transparency in decision making, the significance of *guanxi* is declining:

Because of the transparency in decision making *guanxi* is becoming less important. Even though it is declining in importance, it is still a very very serious issue here.

What the above research participants have indicated is that decision makers in the PRC are having to base their decisions more on criteria such as Western economic principles than on *guanxi*, as the PRC moves towards a rational legal system. Therefore, Guthrie's (1998) argument that the significance of *guanxi* is in decline because of the construction and implementation of a rational legal system appears to be supported by Australian businesses operating in the PRC. However, the above research participants have also suggested that in other areas, other than the decision making process, *guanxi* may continue to be important for businesses conducting business in the PRC.

7.3 Legal Problems

Over fifty percent of research participants in this study encountered legal problems whilst conducting business in the PRC. This suggests that the legal environment in the PRC may be characterised by uncertainty. The legal problems encountered by the research participants, from the most to the least noted include: enforcement, interpretation, lack of legal culture, changes to the laws, underdeveloped legal system, and lack of transparency. The research participant's comments on these legal problems are examined to highlight the uncertainty of the PRC's legal system and to determine whether Australian businesses are able to obtain transaction cost advantages through *guanxi*, despite the apparent decline in the importance of *guanxi* in formal decision making processes.

7.3.1 Enforcement

The enforcement of laws posed the greatest concern for Australian businesses operating in the PRC. This is supported by Duffy (1996, p. 557) and Potter (1995, pp. 176-177) who argued that the enforceability of laws in the PRC is often seen as a major concern for foreign businesses, which is supported by A6's General Manager:

In the PRC, there is this flexibility in the enforcement of laws and in many instances decisions are based on personal interests rather than the law. For example, if you use local laws even if the hearing was open and fair for both sides, it is always difficult for the judge to make a decision. Because if the judge made a decision that favoured the foreigner he would be worried about the repercussions from the communist party, or the local government.

This comment suggests that legal decisions may be based more on personal interests than legalities. Tay and Leung argued that the enforcement by personal interest rather than legalities stems from the control local governments exercise over the personal and financial resources of judges and the courts (1995, p. 182). Rosen (1999, p. 212) argued that it is not only the Chinese authorities that can influence the courts and judges but well-connected local Chinese. For example, a Chinese manager of Kimberly-Clark set up a rival company pilfering materials and spare parts to counterfeit Kimberly-Clark's products. Kimberly-Clark sued in a local court, but the local courts refused to take action. This, it was argued by Kimberly-Clark managers, was the result of the rogue manager's ties with local Chinese officials (Weldon & Vanhonacker, 1999, p. 99). According to the Economist (1995, Jan 7, pp. 51-52) and Behar (2000, pp. 188-195) counterfeit operations are not only run by well-connected Chinese, they are often run by the very individuals empowered to police counterfeiting (Orts, 2001, p. 71). A1's Vice President supports this suggestion:

There was an operation counterfeiting our products. But when we notified the authorities and showed them where the counterfeiting operation was, the local police were running the operation.

This comment indicates that despite the PRC formally joining the World Intellectual Property Organisation (WIPO) in 1980 and since that time making numerous improvements in its regime for Intellectual Property Right (IPR) protection (AMCHAM, 2000, p. 36; Murphy, 2001, p. 41), IPR violations still occur. The lack of enforcement may increase the cost of performing a given value activity, such as producing, marketing, delivering and supporting a product for the business (Porter, 1985). This is based on the assumption that a business, to protect its market share and reputation, will introduce

measures to increase the difficulty faced by counterfeiters copying their products. These measures, as an added expense, may lead to a competitive disadvantage.

Behar (2000, pp. 192-193) argued that if the Chinese government were to really crack down on counterfeiters, some of the Chinese cities' economies would suffer. For example, 80 percent of the goods in the Chinese City of Yiwu are counterfeited. Yiwu is the PRC's largest wholesale distribution centre, which is about a five-hour drive South of Shanghai. A crack down would damage the city's economy because many hotels, restaurants, and businesses cater to the trade (Behar, 2000, pp. 192-193). This is not to say that the Chinese government does not crack down on counterfeiters, it is merely suggesting that the objectives and policies of the Chinese Communist Party (CCP) may be above the law. In this case, it appears that Yiwu's economic prosperity may be the objective of the CCP. Orts (2001, p. 66) argued that a great number of laws do not translate into practice because a central conflict remains between the political rhetoric to establish the rule of law and the continuing tendency for parts of the government to act extra-legally through the policies of the CCP.

The point that CCP policies and objectives may be above the law is taken up by S3's PRC President:

When we came to Shanghai we were granted tax concessions a long with others in our industry. However, after about 18 months the tax authorities came to us and said, 'We are going to start charging you business tax'. I replied, 'No you are not because we do not have to pay business tax until such and such a time'. The tax authorities said, 'Well we have changed our minds'. I replied, 'That was part of the deal when we were given the license by the Chinese Central government. We were also given the okay by the Shanghai government and it is all documented'. But the tax authorities said, 'Where is the letter saying that from the tax department'? I responded, 'You know it was all done on a handshake'. The tax authorities replied, 'That is the rules and unless you produce the letter we are not only going to charge you tax. But we are going to back date it for 12 months', and that is exactly what they did. This is the rather unprofessional nonsense that you have to face in coming to the PRC.

The suggestion that tax concessions may only be upheld when they promote the state's objectives is heightened when it is considered that tax revenues in the PRC have not been

growing fast enough to offset government spending. Tax revenues in the PRC have fallen steadily in the past two decades from around 35 percent of Gross Domestic Product (GDP) in 1978 to 12 percent in the last several years (Saywell, 1999, June 17, p. 57; AMCHAM, 2000, p. 51). Although all taxpayers have been feeling the heat, foreign businesses believe that they are targets of the tax authorities because they are more able and willing to pay than many SOEs and fledgling Chinese private enterprises (Saywell, 1999, June 17, p. 57). As a result of the tax concessions conflicting with state objectives, the expenditure of Australian businesses on producing, marketing, delivering, and supporting its product or service in the PRC may have increased, leading to a competitive disadvantage.

Even though Article 10 of the Unified Contract Law (UCL) OF 1999 states that oral contracts are, in general, as enforceable as written ones, oral contracts should be avoided because it can often be unclear whether a legally binding agreement was concluded and repercussions may have an adverse impact on the business (Larusson & Sharp, 1999, pp. 69-70), as indicated by the comment of S3's PRC President. In other words, legal problems in the PRC do not only stem from the Chinese legal system but also from the choices foreign businesses make when conducting business, which is consistent with Rosen (1999, p. 198).

The point that CCP policies may be above the law is reiterated by S8's General Manager:

Our operation is owed about one million Australian dollars from a Shanghai based Chinese company. According to Shanghai's municipal law, when you lodge a case for debt collection it must be heard in court within 6 months. However, it is now getting on to 12 months and the case still has not been heard. The reason the Shanghai government is stopping proceedings is that if the case proceeds and the debt is recovered approximately 2000 workers will be unemployed. It is harrowing to break through the Chinese legal system. The issue is not that you are not legally allowed to do this. It is a land of law, as long as it does not impact on any other political development.

Although laws do exist in the PRC, this comment suggests that legal proceedings may be flouted if there is a possibility the ruling would conflict with CCP policies. In this case, the objective of the Shanghai government appears to be employment, and enforcement of the law would lead to an increase in unemployment. The reason the Shanghai government may not be enforcing the law, may be the possibility of protest from the unemployed. Protests by former SOE employees have erupted across the PRC and have been viewed as a threat to the stability of the CCP (Saywell, 1999, Feb 25, p. 47). The inability of S8's General Manager to recover the A\$1 million from the SOE may have an adverse impact on the business. In the short term, for example, the Australian businesses' production process may be halted if there is too little cash to pay the bills. In the long term, a reduced cash position may render the Australian business insolvent. Insolvency is a situation where a business is unable to meet its maturing liabilities on time. A reduced cash position may also hinder the Australian businesses' ability to increase profitability through investment in both marketable securities and longer-lived assets (Petty et al 2000, pp. 198-199).

Legal disputes between firms and buyers, suppliers, and government authorities over contracts and payment are very common in China, as elsewhere. Because of the outside influences on the courts and judges in China, by far the most common solutions to these problems are administrative or informal remedies that rely on local brokers and authorities to use their relationships to resolve disputes (Rosen, 1999, pp. 211-212). The importance of these informal measures is highlighted by A13's Hong Kong Chinese Owner Manager:

In China, if you have a contractual dispute, you can not rely on the Chinese legal system to enforce the terms of the contract because the Chinese legal system is underdeveloped. If you have a contractual dispute with your business partner, there is no other way to resolve the issue than through the relationship you have with your partner or your connections.

A3's Senior Trading Manager is in agreement:

I do not believe you can conduct business in the PRC without *guanxi*, as good *guanxi* enables you to solve problems as they arise. In addition, *guanxi* is much better than relying on the Chinese legal system. I would believe you would get more out of the Chinese people, if you received their personal guarantee than any bits of written legal documents. This is because you have a better chance of solving problems through *guanxi* than any legal recourse in the PRC.

This comment implies that *guanxi* is more important than resolving legal disputes because the PRC's legal system is open to outside influences, which is supported by A1's Vice President:

We went to court on a matter involving our company and by the time we had reached court, the judge had already typed out his conclusion, which obviously was not in our favour. Thus, there is no point going to court reading chapter after chapter of Chinese law, as it will not make any difference on the ruling. You need to solve these issues through relationships and negotiation.

A4's mainland Chinese Solicitor also supports the notion that *guanxi* is more important:

In theory, the PRC does have laws. But the question is whether those laws function effectively, because the legal system is terribly weak and the courts are not independent. This has diminished the importance of the law in the PRC. Therefore, it is more productive to rely on relationships than the Chinese legal system.

In other words, *guanxi* may be an alternative to the Chinese legal system for dispute resolution because Chinese courts and the judicial authority may be open to outside influences.

Even though *guanxi* may be a substitute for formal institutional support in the PRC, there is still no guarantee that when disputes are settled through the courts that court rulings will be enforced (Rosen, 1999; Lubman, 2000). As B2 reported:

In the PRC, there is an absence of strong laws and where there are laws they are often not enforced. For example, there may be a A\$200,000 fine against an SOE for a particular reason and an instruction to pay the fine to a foreign business. However, from my experience SOEs often ignore the ruling and nothing ever happens.

This comment suggests that foreign businesses face a battle in vindicating their claims because of difficulties in enforcing court judgements. Lubman (2000, pp. 266-267) contends that it may be local protectionism and selfish departmentalism, which make it difficult for court rulings to be executed in the PRC. Even when legal disputes arising in

the PRC are dealt by boards of international arbitration, there is still no guarantee that the Chinese courts will enforce the ruling, as was the case with Revpower.

Repower, a US-owned and Hong Kong-based battery maker was awarded A\$9 million in damages by an international arbitration board in a dispute with its Chinese JV partner. However, the Chinese courts did not enforce the ruling, and after four years Repower still had not been paid (Roberts et al 1997, pp. 142-144). The comment of B2 also implies that when legal disputes are taken to the Chinese courts, it may not be a cost-effective measure. The expensive nature of the Chinese legal system is stressed by B15's Hong Kong Chinese Assistant General Manager:

It would be a lot cheaper for us to resolve a dispute through the relationship and negotiation than to resolve the legal dispute through the Chinese legal system. This is because it is a costly process to go through the Chinese legal system and usually the Chinese will stall it as long as possible in the hope that you will become tired of it all and just forget it. Even if you win, the courts in my experience do not enforce the ruling.

This comment indicates that *guanxi* may be more cost effective in resolving legal disputes than the Chinese legal system. Legal recourse, in other words, may increase the transaction costs for Australian businesses possibly leading to a cost disadvantage for the business in performing a given value activity. This is consistent with Rosen (1999, p. 214) who argued that the capriciousness of the Chinese legal system implicitly adds to the transaction costs of operating in China, making necessary more hedging against legal uncertainties.

7.3.2 Interpretation of laws in the PRC

Inconsistency in the interpretation of laws in the PRC was one of the main legal issues reported by the research participants. This is consistent with the American Chamber of Commerce's (AMCHAM) white paper on American businesses, which reported that inconsistency is a main concern of foreign businesses in the PRC (2000, p. 24). According to AMCHAM (2000, p. 24), it heightens the risk of conducting business in the

PRC. The issues are put into context by the following research participant's comments.

B6's General Manager for the PRC contended:

If I was conducting business in Hubei I would deal with the People's Bank of China (PBOC) Hubei. And if I was conducting business in Beijing or Shanghai I would be conducting business with the PBOC of the respective cities. However, each PBOC in the respective city interprets the laws differently than the other. Black is not always black and white is not always white when conducting business in the PRC.

Although the respective PBOCs have the same book of rules, the rules and regulations are interpreted differently across provinces and cities. This suggests that inconsistencies in the interpretation of laws, rules, and regulations may make it difficult for the Australian businesses to plan and implement their strategic plans when conducting business in more than one locale. Planning entails evaluating the future prospects of the business and deciding appropriate strategies to achieve long term objectives (Deresky, 1997, p. 141). In agreement with B6's General Manager for the PRC, A5's General Manager for South East and North Asia also pointed out that interpretation problems arise in the PRC:

The local laws are pretty much static but it is the central laws of Beijing that change and take a while to come through and when they do, the interpretation is not that clear. Some of the central laws are so complicated that they are applied differently across provinces. To avoid problems of interpretation, I insist that we get something in writing from the local officials saying 'that we are complying'. But to obtain something in writing from the local Chinese officials is something they are not always happy to do.

The reluctance of the local Chinese officials to provide written confirmation on compliance suggests that the local Chinese officials may be using the complexity of the central laws of Beijing to create ambiguity for self interest. According to Li (2000, p. 208), ambiguity is a strategy employed to confer benefits on various actors within the legal system because it allows them to maximise gains whilst avoiding responsibilities. In line with A5's General Manager for South East and North Asia, S16's General Manager for North Asia stresses the point that differing interpretations of laws across cities is problematic:

We make products in Shanghai from imported components from Australia as well as components made in the PRC. We went to the customs area in Shanghai to export the products as "Made in China" for the Macau market. The customs official then asked, 'Are all the products components made here?' I replied, 'No'. The customs official then asked, 'Which parts are not?' I then said, 'These and these'. The customs official replied, 'Sorry you can not export them'. I replied, 'This is what the regulations from the central government of Beijing say'. The customs official turned around and said, 'I do not care what Beijing said this is not Beijing this is Shanghai. You can not export it. You are going to get the profit from it not a Chinese company or a Chinese'.

This comment indicates that Australian businesses may be treated differently to Chinese businesses when it comes to the interpretation of Chinese laws. It also reflects the extensive discretion officials outside Beijing exercise in implementing centrally promulgated laws (Lubman, 2000, p. 203; Potter, 1995, pp. 174-176). As a result, the Australian businesses ability to compete may have been inhibited. For example, if the Australian business was unable to source comparable components in the Chinese market at a competitive price, it may have to view alternative options which may hinder the products competitiveness.

The flexibility and discretion local provincial officials have in interpreting and implementing laws, rules and regulations in the PRC is summed up by A4's mainland Chinese Solicitor:

Beijing has a lot of power to control what happens in the provinces but there are also a lot of other local laws that you need to contend with. In Chinese we say 'a strong dragon can not overcome a local snake' because even if you are powerful but they are a local snake, it is hard to get rid of them.

Notwithstanding, local provinces are supposedly limited in their power to implement rules and regulations as long as the laws do not contravene the Chinese constitution or the administrative rules and regulations issued by the central government (Tay & Leung, 1995, p. 158). However, it appears there is not one China but many. Murphy (2001, pp. 38-39) suggests that the issues arising from the flexibility and the discretion of local provincial officials are not going to fade with the PRC joining the Word Trade Organisation (WTO). This is because powerful domestic lobbies bound up with local

provincial bureaucrats will probably work hard to protect their interests and maintain local monopolies. As a result, Murphy contends that *guanxi* will remain more powerful than rules for some time to come (2001, p. 44).

Differing interpretations of centrally planned laws, rules, and regulations by Chinese officials may not only increase the difficulty in conducting business across provinces or Chinese cities, they may also have an adverse impact on the business if conflict arises among Chinese officials due to differing interpretations. As S11's Operations Manager remarked:

We went to the customs officials and asked, 'What do we need to do to get our Value Added Tax (VAT) rebate'? The customs official said, 'This is what you do'. However, when we went to the tax department to get our VAT rebate, they said, 'No that is not what you are supposed to do'. It was only an interpretation of just a few words. There is no government to government relationship there is no link between the departments. To try and resolve the disagreement between the two Shanghai government departments, we brought the two sides together. This discussion quickly ended up in an argument over the interpretation of a few words. And it just became a power struggle between the two government departments in Shanghai. If we do not get the issue resolved, we are in trouble because our VAT rebate is basically our profit margin.

The delay in the resolution of the VAT rebate would undoubtedly have an adverse impact on the Australian business. The reduction or elimination of the Australian businesses' profit margin, for example, may hinder its ability to take advantage of market opportunities. In addition, the Australian businesses' ability to react and implement strategies to counteract their rival's competitive actions may be reduced. Thus, interpretation conflicts between Chinese officials may result in a competitive disadvantage. The comment of S11's Operations Manager indicates that businesses operating in the one locale may also face planning difficulties because of the conflicting views on the interpretation and implementation of laws, rules, and regulations among local Chinese officials.

Orts (2001, pp. 66-67) argues that the problems caused by the interpretation of laws in the PRC often stem from the confusion between the law as written and the law as

interpreted according to CCP policies. Because problems are caused by the confusion between the law as written and the law as interpreted according to CCP policies, A1's Vice President and A6's General Manager suggest that *guanxi* is important for resolving interpretation issues:

The levels of law in China are often conflicting. We operate on Beijing law and have always done so, but there is the law of Guangdong, the law of Guangzhou, and the law of the town our operation is situated. For instance, the local town interpreted the law differently than Beijing and was enforcing their interpretation of the law that resulted in problems between Beijing and the local official. Negotiations and relationships played a crucial part in solving the conflict (A1's Vice President).

This comment indicates that *guanxi* played an integral part, and is supported by A6's General Manager:

The best way to overcome interpretation issues is through personal networks. For example, if you have a problem you get the local mayor to ring someone in Beijing and get someone in Beijing to say, 'look guys back off'. Personal networks are terribly important because the legal system needs improving.

7.3.3 The Lack of Legal Culture in the PRC

The concept of Rule of Law is quite new to the PRC. Indeed, until the turn of the last century, there was no Chinese word that captured the conventional Western meaning of the word "law" (Larusson & Sharp, 1999, p. 66). Chinese legal tradition was founded on Confucianism. According to this philosophy, law and morality are indistinguishable. Instead of being ruled by written or statutory law, people are governed by moral principles, which they can learn with guidance from their teachers (Orts, 2001, pp. 51-58). Since 1979, however, the importance of written law in the Chinese economy has increased significantly with thousands of laws being enacted to modernise the country. To promote the Rule of Law, the National People's Congress (NPC) amended the Chinese Constitution on 15 March 1999, where it now states that the PRC "practices the Rule of Law, and constructs a socialist country ruled by law" (Larusson & Sharp, 1999, pp. 66-67). The NPC has the sole authority to adopt legislation, but the Standing

Committee acting alone may also issue decrees, interpretations of laws, and partial or individually focused regulations (Orts, 2001, p. 68). Although the PRC is moving to a country ruled by law, it is very slow, and according to A4's mainland Chinese Solicitor *guanxi* continues to play an important role:

I would think most of the Chinese people still have a very vague idea about playing by the rules. They have not realised the importance of having strict rules, laws and regulations in the business community. Therefore, the way of doing business in the PRC is still at a very primitive stage. This articulates the point that relationships at this stage are more important than the law.

This comment indicates that at some stage the attitude of the Chinese people to the 'rule of law' will change, and that change will see *guanxi* becoming less important than the 'rule of law'. According to Lewis (1997, pp. 508-509), this vague idea of the law and legality is rooted in the influence of Confucian philosophy. As noted above, Confucian tradition avoids prescribing the content of morality, instead an individual learns a certain way of thinking, which is known as *li* (Larussou & Sharp, 1999, p. 66). The Confucian concept of *li* expresses the view that lawful norms of behaviour described in rites were essential to good government and preferable to the enforcement of laws. Confucianist proponents of *li* believe that good morals alone are in themselves sufficient to provide social order without relying on the enforcement of laws and regulations (Orts, 2001, p. 52). This vague idea of legality influenced by Confucian philosophy may be the reason Chinese view contracts differently to Westerners, as A6's General Manager remarked:

The Chinese do not view a contract as we Westerners view it, they just regard it more like a letter of intent, an agreement based on the circumstances at that time. Therefore, when circumstances changed the Chinese would say, 'we would like to make some changes to the contract'.

Similarly, A8's Export Manager for North Asia stated:

Today in the PRC, there is still much evidence that contracts are merely a starting point. The Chinese design a contract and then start to negotiate. Whereas in Australia, we tend to think once the contract is signed, it is the end of negotiations and we can get on with business.

Correspondingly, S11's Operations Manager noted:

Nothing is ever straightforward in China. For example, you need to realise that contracts are something that are negotiated and signed off which determine where you are at any point in time. Negotiations are continuous, so even once the contract is signed they will negotiate over all sorts of issues in the contract. Here in Australia when we sign a contract, it is a valid deal and both parties abide by the contract and you get on with life.

In agreement, B9's Owner Manger commented:

We [Westerners] tend to put the issues out on the table and say, 'well these are the problems and issues how do we work around them to make sure that everybody comes out of it with some benefits'. The Chinese do not seem to do it that way. We are forced to compromise on that issue and then another issue is brought up and you never know when it is going to finish. Even after the signing stage of the contract it continues.

In short, signing a contract does not necessarily indicate completion of all negotiations for the Chinese; rather it is regarded as an incomplete expression of the first stage in ongoing negotiations to establish long-term relationships that transcend the contract. As a consequence, very general expressions of the foreign party's intentions are often taken by the Chinese side to mean the creation of obligations rather than general expectations (Ahmed & Li, 1996, p. 279). In other words, the Chinese may place the contract in a larger relational context, although they are fully capable of interpreting the contract legalistically when it suits them (Lubman, 2000, p. 203). Therefore, the signing of a contract symbolises a platform to build a relationship and establishes a forum for further negotiation and is not regarded as a limiting or a definitive legal document quite in the same sense as in the West (Ahmed & Li, 1996, p. 279; Nair, 1996, p. 28). Although there may be differences in how the Chinese and Westerners view contracts and that the expectations created by contracts are not as secure as they would be in a Western legal environment, it would be ill-advised to assume that there is something "negative" in China about carefully negotiated and well drafted contracts (Lubman, 2000, p. 200). Thus, as A12's Export Manager suggested contracts should be quite explicit:

When you write contracts in China you have to make sure they are watertight because the Chinese will continue to negotiate. Therefore, you need to stipulate in a contract what they do and do not get.

Contracts should not only be explicit because of the problems and frustration of continued negotiations, but because implicit contracts diminish the opportunity for legal recourse in the future (Rosen, 1999, p. 211).

The lack of “an attitude of legality” may not only stem from the influence of Confucian philosophy, but it may also stem from the belief held by the Chinese that court decisions are based on personal affiliations rather than a case’s objective merits (Rosen, 1999, p. 214). Thus, the health and strength of the rule of law not only depends on judges, lawyers or police who know how to read, understand, interpret, and apply laws independently, but on the attitudes of the Chinese to the rule of law (Orts, 2001, p. 66; Lewis, 1997, pp. 508-509).

7.3.4 Changes to Laws, Rules and Regulations

Rosen (1999, p. 202) and Orts (2001, pp. 66-73) contend that problems experienced because of changes to Chinese laws, rules, and regulations are to be expected from a system in transition. Although there is an expectation that problems are likely to be experienced by Australian businesses, it does not reduce their severity. As outlined by A5’s General Manager for South East and North Asia:

The duty classification of some of our imported materials has changed and the way that duty is charged has also changed. In the past you could offset incoming duty against exports but now you can not do this. You have to pay for it up front and get the offset later when you export. These changes mean our manager in China is having to constantly keep up to date with the changes and inform us on the changes, and explain to us that everything he told us last week is now irrelevant.

This comment implies that the constant changes in the Chinese legal and regulatory environment may increase the difficulty faced by the Australian business in developing sales forecasts and budgets. The sales forecast not only provides management with an estimate of the revenue to be received and the units to be sold but also serves as the basis for planning in the other functional areas (Ball & McCulloch, 1999, pp. 598-602).

Without this information, management is unable to formulate the production, financial, and procurement plans. Budgets, like sales forecasts, are both a planning and control technique. During planning, they co-ordinate all the functions within the firm and provide management with a detailed statement of future operating results (Ball & McCulloch, 1999, pp. 598-602).

In support, AMCHAM contended that the bewildering variety of fees, taxes, and fines and, the ad hoc manner in which they are imposed, results in businesses encountering planning difficulties (2000, pp. 50-52). The unpredictable nature of the Chinese regulatory environment that may cause planning difficulties is stressed by B13's Chief Representative:

Because we are a manufacturing firm in Australia we are able to obtain a tax exemption for our representative office in Beijing. Even though there is this rule, the way in which the Chinese government operates, it could turn around next week or next year and say, 'representative offices working for manufacturers do not get a tax break'. The Beijing Officials move the goal posts. One day you have to jump through this hoop, the next day you have to jump through another hoop that has become smaller or has moved position.

The unpredictability in the changes to Chinese tax rulings may not only increase the difficulty to plan, it may also increase the cost of conducting business in the PRC. Tax laws and regulations, and the changes to those laws and regulations, are part of the institutional factors that influence a businesses' cost in performing a given value activity (Porter, 1985, p. 70). They are, in other words, cost drivers. Thus, any changes to the tax laws and regulations that increase the cost of performing a given value activity may place the Australian business at a competitive disadvantage. The effects that such changes have on a businesses' ability to compete effectively in the PRC is highlighted by A9's Export Manager:

The sudden change and approximately 50 percent increase in the tax paid on our products to the PRC made our products uncompetitive. We continued to serve our clients in the PRC by exporting our products to Hong Kong. Our products are then smuggled into the PRC by our PRC customers.

Although smuggling products into the PRC is illegal, this comment indicates that sudden changes in the tax rulings may cause a business to be uncompetitive in performing a given value activity whilst serving its clients through legal means. Changes in tax legislation that reduce businesses' competitiveness may heighten the attractiveness of serving customers in the PRC through illegal means. This suggestion is supported by AMCHAM (2000, p. 52) which contends that because of the unusually high rate of VAT in the PRC, tax evasion and smuggling are encouraged. For comparative purposes, the VAT rate in Singapore is 3 percent; Taiwan, 5 percent; Canada, 7 percent; and the PRC 17 percent (AMCHAM, 2000, p. 52). However, the VAT rate in the PRC is on par with Europe.

Although changes to Chinese laws, rules, and regulations may be necessary for reform (Rosen, 1999; Lubman, 2000), in some instances, as B2 indicates, these changes may be made without due respect for the "rule of law":

A major problem of operating in the PRC is that the Chinese government changes rules after you have invested there. For example, there is a case at the moment in Guangdong where an Australian business has a quarry in that province and has been operating the quarry for approximately 8 years. Even though there is a contract for the Australian business to operate the quarry into the future, the Guangdong authorities decided to cease the operation of the quarry on environmental concerns, with limited scope for compensation. The Chinese authorities change regulations without due respect to the law.

The decision by the Chinese authorities to cease the operation on environmental concerns without compensation, despite a contract for future operation, reinforces the point that the Chinese government may be above the 'rule of law' (Orts, 2001). This is not suggesting that the Chinese authorities are the only authorities that close operations based on environmental concerns. It merely highlights the uncertainty and unpredictability of the Chinese legal system and that compensation may not be forthcoming.

7.3.5 Transparency in the Chinese Legal System

Lubman (2000, p. 203) argued that the lack of transparency in the Chinese legal system is among the most notable characteristics of the foreign business environment that presents problems for foreign investors. Transparency refers to the existence of a system of publicly available laws, which are explicitly written, widely understood, and readily accessible to the affected parties (AMCHAM, 2000, p. 24). On the issue of transparency, S6's mainland Chinese Chief representative stated:

The unclear and unpredictable regulatory environment pertaining to electricity fees in our Joint Venture (JV) in Dalian blew out our budget when the fee was received.

As a result of the lack of transparency, the Australian businesses' ability to perform a given value activity may have been hindered, resulting in a competitive disadvantage. This is because transparency, as an element of the institutional factors such as laws, rules, and regulations, also determines the cost behaviour of the value activities of a business (Porter, 1985). According to AMCHAM (2000, p. 24), transparency issues in the PRC often arise from the laws and regulations at the central government, provincial and local levels conflicting with one another. They may also arise from the use of secret directives (policy statements, notices) or regulations (*neibu*) by the Chinese government, addressed to officials charged with implementation. Foreign businesses, as well as Chinese citizens, are subject to these directives. Although these directives are only circulated inside the government and are unavailable to the public, they operate with the force of the law (AMCHAM, 2000, p. 24; Orts, 2001, p. 68; Lubman, 2000, p. 197). Lubman (2000, p. 197) noted that toward the end of the 1980s, central government officials concerned with legislative drafting indicated that the PRC would rely less on these directives, and it appeared that some steps had been taken toward greater transparency. However, Potter (1995, pp. 178-179) observed that these directives remained an important yet invisible component of the regulatory system. Foreign investors face the quandary of being told

that regulations prohibit certain activities, but then being refused access to those regulations.

7.4 The Uncertain and Unpredictable Foreign Business Legal Environment of the PRC

What the above discussion on the legal problems indicated was that the legal environment Australian businesses need to contend with whilst conducting business in the PRC appears to be marred by uncertainty and unpredictability. Australian businesses that rely on such a legal system whilst conducting business in the PRC would undoubtedly face increased transaction costs, which may lead to a competitive disadvantage for the business. This is because laws, rules, and regulations, which are institutional factors, and elements of these institutional factors such as enforcement, interpretation, legal culture, changes, and transparency determine the cost behaviour of a business in performing a given value activity (Porter, 1985). The above discussion also indicated that *guanxi*, as an alternative to the uncertain and unpredictable Chinese legal system, may economise on transaction costs leading possibly to a competitive advantage for the Australian businesses in performing a given value activity. Hence, Boisot & Child (1988), Davies (1995), Standifird & Marshall (2000), and Luo's (2000a) argument that *guanxi* may be an alternative measure of support and governance to formal institutions of support, which may allow a reduction in transaction costs and lead to a competitive advantage in performing a given value activity, appears to be supported by the participants in this study. Therefore, Guthrie's (1998) argument that the salience of *guanxi* is in decline because of the construction and implementation of laws, rules, and regulations designed to increase accountability in the formal decision making process may not be as clear as he suggests and may not be applicable for Australian businesses negotiating the Chinese legal system.

Guanxi, in other words, continues to be important for Australian businesses negotiating the uncertain and unpredictable Chinese legal system, despite the decline in the salience of *guanxi* in the formal decision making process. The uncertainty and unpredictability of the Chinese legal and regulatory environment is summarised by B10's Regional Manager for Greater China:

To get around Beijing you need to use a car. It is such a big city. You can get a licence. It will take you time as a foreigner. You can buy or lease a car, which will take you time and you can drive yourself. But if you do drive yourself and follow all the laws and road rules you will get nowhere. If you want to keep up with the traffic you have to break the laws and they will be selectively used against you at an appropriate time. Therefore, it is a high-risk strategy. How do you get around? You either use a taxi and in using a taxi you are subcontracting your transport to someone else. And if the taxi breaks the law you can get out of the taxi and get into another taxi. Alternatively, you can hire or lease a car and a driver, then the driver is responsible if he breaks the traffic laws. You are home free. But you have a contingent liability that the Car Company may not have current insurance, the car is involved in an accident and you are still liable.

7.5 Summary

This Chapter noted that the significance of *guanxi* appears to some extent to be in decline in the face of the implementation of laws, rules, and regulations designed to increase accountability in formal decision making processes. It also argued that despite the implementation and improvement of laws, rules, and regulations in the PRC, the Chinese legal system pertaining to Australian businesses continues to be marred by uncertainty and unpredictability. As a result, this Chapter argued that Australian businesses may still be able to economise on transaction costs by relying on *guanxi* rather than the Chinese legal system for governance and support. Economising on transaction costs may enable the Australian businesses to enjoy a competitive advantage. Therefore, the argument that the salience of *guanxi* is in decline because of the move to a rational legal system may not be applicable to Australian businesses when negotiating the Chinese legal system.

Having established that *guanxi* may still be important as a substitute for formal institutional support, the following Chapter examines whether the declining significance

of *guanxi* in the formal decision making process translates into a reduction or abolishment of the first mover advantages an Australian business may obtain through the advantages of *guanxi*. In examining the advantages of *guanxi*, the following Chapter ascertains where and when *guanxi* is important for Australian businesses operating with the PRC.

CHAPTER EIGHT: THE IMPORTANCE OF *GUANXI* IN THE PRC's FOREIGN BUSINESS ENVIRONMENT: A FIRST MOVER THEORY APPROACH

8.1 Introduction

Even though the implementation of rules and regulations designed to increase the level of accountability in the reform era may have caused the salience of *guanxi* to decline in formal decision making processes, this Chapter examines whether the Australian businesses in this study were able to obtain first mover competitive advantages through *guanxi*. In examining the advantages of *guanxi*, this Chapter identifies when and where *guanxi* is important for Australian businesses conducting business in the PRC. It also discusses the suggestion that as the PRC has moved from a command economy characterised by scarcity to one of increasing competition, Western economic principles have come to the fore at the expense of *guanxi*. In addition, this Chapter discusses whether the importance of *guanxi* is dependent on a businesses' target market and the location of foreign investment in the PRC. Finally, it analyses the disadvantages of *guanxi*.

8.2 First Mover Competitive Advantages of *Guanxi*

Chapter Three argued that through some of the advantages of *guanxi* foreign businesses were able to obtain first mover competitive advantages in the PRC. In the wake of the indication that the significance of *guanxi* is in decline in formal decision making processes, does this necessarily mean that foreign businesses are unable to obtain first mover competitive advantages through *guanxi*? In order to answer this question, this Chapter reviews the quantitative results in Chapter Five, which revealed that the main advantages obtained through the employment of *guanxi* by the Australian businesses included reduced bureaucratic interference, market access, and access to market information. Reduced bureaucratic interference was the main advantage of *guanxi*, with

55 percent of participants noting such an advantage. This was followed by market access and access to market information with 35 percent and 31 percent respectively.

8.2.1 Reduced Bureaucratic Interference

As indicated previously, rationalising the Chinese bureaucracy through the employment of *guanxi* was its main advantage. This is highlighted by A13's Hong Kong Chinese Owner Manager:

Guanxi is paramount to doing anything in the PRC. *Guanxi* enables you to facilitate the Chinese bureaucracy. For example, if you want to set up a business in the PRC it will take you between four to ten times longer if you do not have *guanxi*. Although laws and regulations exist, through *guanxi* you are able to streamline the legal process allowing you to complete your task in less time than it would take without *guanxi*.

Although *guanxi* may enable the bureaucratic process in the PRC to be rationalised, it does not imply, however, that steps in the process may be missed, as this would be illegal (see Chapter 6). What it does suggest is the steps in the process are completed in a more timely fashion than otherwise would be the case. The establishment of an operation in less time may enable the Australian business to enjoy a monopoly position in the supply of its products or services (Schumpeter, 1936; Porter 1990). Hence, the Australian business may have become a first mover, possibly enjoying first mover competitive advantages, such as a cost or differentiation advantage if there is a proprietary learning curve in the value activities that are affected by the early move (Porter, 1985; Porter, 1990).

In line with A13's Hong Kong Chinese Owner Manager, A15's Director stated:

In the PRC, you need to develop *guanxi* with people in positions of influence. For example, in a Chinese province we deliberately set out to make contact and establish relationships with a range of people from the planning authority, design institutes to the mayor of the Chinese city. Because if you just go in there with a design for a building site and you submit it to the planning department without any of that relationship building. It may take you 2 years to work your way through the Chinese bureaucracy, as opposed to two weeks to gain approval. But of course before you get started you need to have a referral from someone who recommends to the person that you are worth seeing.

The ability to gain planning approval through *guanxi* in a more efficient manner than otherwise would be the case may be likened to the breaking up of a monopoly over the approval process (Schumpeter, 1936; Porter, 1990). Breaking up a monopoly position may also enable the Australian business to be a first mover and gain first mover competitive advantages, such as unique channel access for their products or services (Porter, 1985; Porter, 1990). This comment also highlights the importance of intermediaries in the establishment of *guanxi* with a third person, which Yeung & Tung (1996, p. 61) refer to as altercasting. In addition, it suggests that the development of *guanxi* with individuals with power and influence is critical for conducting business in the PRC. But identifying individuals who have the necessary power and influence is often difficult and time-consuming (Wang & Ralston, 2000, p. 697; Yi & Ellis, 2000, p. 27). Notwithstanding the difficulties, the importance of establishing *guanxi* with individuals of power and influence to rationalise the Chinese bureaucracy is outlined by B11's Business Investment Analyst Manager:

If you want things accomplished at a lower level in the Chinese bureaucracy things will move very quickly if you have *guanxi* with someone at a higher level. The reason things become bogged down at the lower levels of the Chinese bureaucracy is that they do not know what their role is in the transaction. In addition, at the moment there is this feeling in the lower levels of the Chinese bureaucracy that you can not get into trouble if you do not make a decision. Thus, it is critical to establish *guanxi* with higher level officials.

According to the above comment, it appears that lower level officials may hold up the bureaucratic process because of fear of reprisals from higher level officials in the bureaucracy, which further highlights the importance of developing *guanxi* with individuals of power and influence. The reluctance of Chinese in making decisions is further explored in Chapter Nine.

Continuing on the rationalisation of the Chinese bureaucracy S2's Singaporean Chinese General Manager indicated that *guanxi* may enable permits to be granted in less time than otherwise would be the case:

The advantage of having *guanxi* is that you are able to get things done faster and easier. For example, if you are dealing with government departmental officials for permits and you have *guanxi* with the right officials in that department you get things done in 3 months rather than 6 months. In addition, if you are going about it in the wrong way, they will advise you how to correct it. However, if you went through the official channels, they will tell you after two weeks that it can not be done and they will never advise you what is the best course of action to take.

Obtaining a permit through the employment of *guanxi* in less time than usual may also be likened to the breaking up of a monopoly over the process to obtain permits (Schumpeter, 1936; Porter, 1990). As a result, the business may become a first mover and obtain first mover competitive advantages, such as above average returns until other competitors are able to duplicate or respond effectively to the competitive action (Porter, 1985; Porter, 1990). Correspondingly, the General Manager of A6 pointed out that *guanxi* may enable access to distribution channels:

Guanxi is important everywhere, in Australia or China. But having said that you can not conduct business in the PRC without *guanxi*, which is in contrast to Australia. For example, the infrastructure in the PRC is in most cases inadequate, thus as in a number of cases we needed our products transported by rail to our customers in Guangzhou. But you were never quite sure if you were going to be allocated a rail car for your goods. To solve this bureaucratic problem we needed to cultivate *guanxi* with the people in charge of the rail cars and once we had done this our dilemma was solved. And you can not just go bugger it, we will ship the goods to our customers because you would be in the same boat if you had no *guanxi* with the officials on the wharf.

Despite the PRC's recent infrastructure improvements (Luo, 2000b, p. 195; Wang & Ralston, 2000), this comment indicates that infrastructural difficulties still exist. Utilising *guanxi* to gain access to a distribution channel that ordinarily would be denied may also be likened to the breaking up of a monopoly position, enabling the Australian business to gain unique channel access to their customer (Porter, 1985; Porter, 1990). In line with A6's General Manager, S5's Malaysian Chinese Director noted that they overcame bureaucratic hurdles through the *guanxi* of one of their employees:

We had an employee who was a member of the Chinese People's Consultative Committee (CPCC). Supposedly a person on that CPCC can sit and whinge about government policy, maybe nothing will happen but you can say something. This person also gets an identity card stating that they are a member of the CPCC. In

the PRC, the Chinese Central Government promotes the use of local materials and applies quotas to protect its commodities, such as steel. We need to import raw steel strip into the PRC for the production of our products, and to do that we need to go through a quota system. The required amount of steel needs to be applied for a year in advance. If we need 100,000 tonnes of raw steel strip, we send our CPCC employee. The CPCC member whinges to the official and states that he is representing the CPCC, as a result we get what we need.

The employment of the CPCC member was a deliberate strategy by the Australian business to tap into his *guanxi* network. Thus, bureaucratic obstacles were overcome resulting in access to a new source of supply of raw materials (Schumpeter, 1936; Porter, 1990), perhaps enabling the Australian business to obtain a competitive advantage by creating a barrier against competition (Porter, 1985; Porter, 1990).

Rationalising the Chinese bureaucracy through *guanxi*, which may lead to first mover competitive advantages, may also lead to cost advantages for the business. According to Porter (1985, p. 62), a cost advantage is one of the competitive advantages a business may possess. This is not limited to a cost advantage obtained through a proprietary learning curve. It can also encompass the drivers of cost behaviour, such as institutional factors underlining laws, rules, and regulations (Porter, 1985, p. 62). B1's PRC Manager commented:

Once we were late lodging our tax forms and we received a phone call from this guy in the tax office, who obviously had been taken out to dinner and had too much to drink, as he was very abusive on the phone and told us that we would have to pay a fine directly to him. We went down to the tax office with a senior Chinese consultant and we saw the head of the tax department in the corridor. The senior Chinese consultant discussed with the head of the tax department on how a lot of companies do not understand the laws of the tax system and how to lodge them in the correct manner. The senior Chinese consultant suggested to the head of the tax department that he should conduct a seminar for these companies on how to lodge tax forms and the laws pertaining to them. The head of the tax department replied, 'that he had not thought of it' and was pleased he was being invited to give a seminar to foreign companies on taxation law. The senior Chinese consultant then brought up the issue of our tax problem and explained it to the head of the tax department. He replied, 'leave it with me and I will fix the fine'. The head of the tax department saw that the idea of giving a seminar was a favour to him and gave a favour in exchange. This would not have happened if we did not have any *guanxi* with him in the beginning.

The actions of the tax official created an environment of uncertainty and unpredictability in the implementation of tax laws and regulations. Tax laws and regulations, and their implementation are institutional factors, which influence a businesses' cost in performing a given value activity, such as producing, marketing, delivering, and supporting a product or service (Porter, 1985, p. 70). In other words, they are cost drivers. Hence, the Australian business in overcoming a bureaucratic hurdle through *guanxi* was able to eliminate the possibility of a fine, resulting in a cost advantage.

B5's Owner Manager also suggested that they might have been able to obtain a cost advantage through the employment of *guanxi*:

Guanxi enables you to obtain things that are difficult to be done through the official channels. You are able to work around the Chinese bureaucracy. In addition, you are able to obtain things that may have been difficult to obtain through the official channels. For example, we had a customs issue in the city of Nanjing and we could have used the official channels. But I had a relationship with someone that knew someone in Nanjing who knew the customs official. In the end we managed to obtain a reduction in the customs duty back in line with the legislation, which may not have been obtained through the official channel.

The employment of *guanxi* rather than the official channel conjures up the notion that *guanxi* is some dubious method to attain one's goals. This, however, is not the case. The unofficial channel is merely using *guanxi* to negotiate the necessary steps within the official channel in a more cost-effective manner. The reduction of the customs duty in line with legislation again highlights the uncertainty and unpredictability of the Chinese legal and regulatory environment. Without *guanxi* to overcome the excessive customs duty, the Australian businesses' ability to produce, market, deliver and support their product may have been hindered. In essence, rationalising the Chinese bureaucracy via *guanxi* possibly allowed the Australian business to obtain a cost advantage. This comment also reiterates the point that uncertainty and unpredictability plague the PRC's business environment.

The importance of *guanxi* in rationalising the Chinese bureaucracy is further supported when it is considered that 29 percent of participants in this study reported that they overcame bureaucratic problems with *guanxi*.

8.2.2 Market Access

Market access was the second most noted advantage of *guanxi*, with 35 percent of participants reporting such an advantage. The ability of *guanxi* to reward Australian businesses with market access and first mover competitive advantages is brought to attention by A16's Operations Manager International:

You will not get anywhere in the PRC without *guanxi*. For example, if you went in 'cold' so to speak you will not have a great deal of success. We used our *guanxi* in the initial stages of entering the PRC to open the political doors, as many deals would be out of our reach without them. Then once we gained access and had a good reputation our connection would introduce us to their connections and it just flowed on from there.

It appears that access to market opportunities would be denied without *guanxi*, which in this case resembles the innovative way of opening up an existing market for a foreign business (Schumpeter, 1936; Porter, 1990). As a result of this competitive action, first mover competitive advantages may have been forthcoming (Porter, 1985; Porter, 1990). The comment also indicates that a number of market opportunities would not be attainable without political *guanxi*, which is put into context by B9's Owner Manager:

The Chinese government is involved in business in a very significant way and if you have political *guanxi* you can access the business opportunities. In simple terms, the chief advantage of having *guanxi* in the PRC is that you can access better quality commercial opportunities.

According to A8's Export Manager for North Asia, "political *guanxi* is important in the PRC because a lot of power is vested in the political actors".

Political *guanxi* and its importance for access to market opportunities is further put into context by B1's PRC Manager:

Someone rang our office one-day that I did not know. They were a friend of a friend, which I had not met. This person was high up in the State Council and

suggested we go out to lunch together. I declined the offer for lunch. I then spoke to one of my Chinese colleagues and they said, 'It is a two way street and he may have been able to help me and I may have been able to help him'. It is not like Australia where the government is obliged to help you. If you do not have *guanxi* in the PRC, doors will be closed for you.

Not only do the political actors have the power and influence to control access to market opportunities, there is no obligation on their behalf to offer assistance. This does not suggest that a business would be successful by just relying on political *guanxi*. It merely suggests that Chinese officials hold the keys to many doors leading to certain market opportunities that would remain locked without *guanxi*. The point that relationships alone are no recipe for business success in the PRC is discussed in-depth in Chapter Nine.

B3's Owner Manager continues on the importance of *guanxi* for access to market opportunities in the PRC:

Our market is predominantly Chinese business people and Chinese individuals and we find that the best way of attracting Chinese customers is through *guanxi*. Because the Chinese usually do not go to a company that is advertising for our services, especially when it is a foreign company. They will only come once a connection of theirs has vouched for our integrity and trustworthiness.

While highlighting the importance of *guanxi* in opening up an existing market for the Australian business and increasing the possibility of first mover competitive advantages (Schumpeter, 1936; Porter, 1985; Porter, 1990), this comment also reinforces the importance of altercasting in establishing *guanxi* (Yeung & Tung, 1996, p. 61; Yang, 1994, pp. 123-126). In addition, it also implies that when a foreign business is targeting Chinese customers rather than foreign customers in the PRC, *guanxi* may be more important. Whether the importance of *guanxi* may be dependent on a businesses' target market is discussed in more detail later in the Chapter. In accordance with B3's Owner Manager, S10's mainland Chinese Chief Representative pointed out that without *guanxi* their ability to conduct business may have been hindered:

We have *guanxi* with many people that we can just ring up and say our budget this year does not look good. For example, we ask, 'Have you got anything in your basket we can dig out'? They will ask, 'How much are you looking for'? I say 'about A\$500,000'. They may say 'that is a large order'. I would then say

'A\$100,000 is fine'. They get back to you and tell you they have found some work for you. To do that sort of thing is very difficult without *guanxi*.

Again, this stresses the point that with *guanxi* access to market opportunities may be forthcoming and lead to first mover competitive advantages. Rationalising the Chinese bureaucracy may also enable a business to open up an existing market, as A1's Vice President highlighted:

Guanxi is very important in the PRC and it is also very important to know who is connected to whom. For example, it was decreed by the Chinese Central government that all hospitals could only buy 30 percent of their products from foreign businesses. Although this was not legislation, many of the hospitals conformed. But we were able to step around this issue with the help of our *guanxi*.

Overcoming the bureaucratic hurdle through *guanxi* enabled the Australian business to break up the monopoly position of the local Chinese suppliers and open up an existing market possibly resulting in first mover competitive advantages (Shumpeter, 1936; Porter, 1985; Porter, 1990).

The importance of *guanxi* for gaining access to market opportunities was the reason that A15's Director signalled that the significance of *guanxi* was not in decline:

I do not think the importance of *guanxi* is in decline because in our field it would be impossible to conduct business in the PRC without *guanxi*. This is because when you are selling a product or service, especially a service, you will not get to the contract stage unless the client has confidence in what you promise to deliver.

This comment also implies that foreign businesses that provide services view *guanxi* as more important than those that supply physical products. This is consistent with Yeung & Tung (1996, p. 62) who argued that tertiary businesses in the PRC placed greater weight on *guanxi* than manufacturers and importers of physical products. However, the comment of A15's Director needs to be treated with caution because it is only one research participant's opinion in a study with a small sample size. In line with A15's Director, A5's General Manager for South East and North East Asia also revealed that the significance of *guanxi* is not in decline because it is vital in gaining access to market opportunities in the PRC:

I do not think it is possible to conduct business in the PRC without *guanxi* and if you do not have *guanxi* you do not conduct business. So I think *guanxi* is still very important and that has not changed.

These two comments stress the point that *guanxi* is far from insignificant for Australian businesses in the PRC, despite suggestions to the contrary.

8.2.3 Access to Market Information

Access to market information was the third most noted advantage of *guanxi*, with 31 percent of participants reporting such an advantage. The comments of a number of these participants are discussed to ascertain whether this advantage may lead to first mover competitive advantages. According to A13's Hong Kong Chinese Owner Manager, without *guanxi* access to market information would be difficult to obtain:

If you want something you can just ring up the people you have *guanxi* with and they will find the information for you without you having to go through all the levels of bureaucracy.

Obtaining information in a timely and efficient manner may award the Australian business a monopoly position over this information (Schumpeter, 1936; Porter, 1990), which may enable the Australian business to act upon this information before their competitors, thereby awarding the business first mover competitive advantages (Porter, 1985; Porter, 1990). Similarly, B17's Hong Kong Chinese Chief Representative reported “*guanxi* gives you access to information that you otherwise would not have until it is published in the press”, again possibly enabling the business to obtain a competitive advantage. In essence, the employment of *guanxi* has enabled the Australian businesses to create a new source in the supply of information (Schumpeter, 1936; Porter, 1990).

Despite the suggestion that the significance of *guanxi* is in decline because of the implementation of rules and regulations designed to increase the level of accountability in the formal decision making process, *guanxi* appears to be significant in rationalising the Chinese bureaucracy, overcoming bureaucratic hurdles, gaining market access and access to market information. Therefore, it is argued that *guanxi* is far from insignificant for

Australian businesses operating in the PRC during its transitional phase of market development. But to sustain the competitive advantages derived from *guanxi*, it must be rare and difficult to imitate. This may be achieved by developing *guanxi* outside the organisation with a wide range of individuals of differing levels of authority, and converting individual *guanxi* into interorganisational *guanxi* (Tsang, 1998, pp. 68-69). Basically, effective *guanxi* can be likened to a core competency. A core competency is a value creating skill within a business that helps the business establish some strength relative to its competition (Miller & Dess, 1996, p. 266-267).

8.3 Western Economic Principles versus *Guanxi*

Guthrie argued that as the PRC moves away from a redistributive system, where all the costs for firms in the command economy were covered by the state, to a system where efficiency and competitiveness on the open market are important, and where tight fiscal constraints exist and SOE are forced to take responsibility for their own economic positions, bureaucrats are increasingly likely to consider product quality, price competitiveness and service instead of *guanxi* for economic decision making in the reform era (1998, p. 274). To determine whether Guthrie's (1998) claim is applicable to and supported by the Australian businesses in this study, the following research participant's comments on the declining significance of *guanxi* are examined.

According to B12's General Manager for the PRC, *guanxi* was important for conducting business but it is changing in the face of the growing importance of quality products at a competitive price:

Guanxi is very important. It is insurmountable. But that was before. Today the market has become more quality driven where the importance of *guanxi* has succumbed to the increasing importance of quality products, after sales service at a competitive price.

Although this comment does not dismiss the importance of *guanxi*, it does suggest that due to increased competition in the PRC, decision makers are placing greater emphasis

on the overall competitiveness of a product than *guanxi* alone. In agreement, S10's mainland Chinese Chief Representative commented:

Today more emphasis is placed on demonstrating your product's capability than *guanxi*. For example, ten years ago you meet up with your classmate and you ask, 'Do you want to buy a cup?' and he says 'Yes'. You reply 'Jesus I happen to be able to provide you with some cups'. No questions asked sell me some cups. You do not need references or a branded cup or whatever as long as it holds water. Today they will say 'Yeh' but you still have to bring your cup and do a demonstration and run through the capabilities of your cup compared to other people's cups. If your cup is no good, even though your *guanxi* is good they will not purchase your product.

This suggests that as competition has increased, the decision to purchase one product over another depends more on the attractiveness and competitiveness of the deal than *guanxi*.

The increasingly competitive environment of the PRC is noted by S2's Singaporean Chinese General Manager:

For years there was no competition in the Chinese market and the consumers did not have any choices but now the consumers have plenty of choices. If your quality is not good or your marketing does not attract them, they will source other suppliers. No matter how good your *guanxi* is.

In other words, as the PRC's economy has moved from a centrally planned economy characterised by scarcity to one that has become increasingly competitive, buyers are basing their decisions more on Western economic principles, such as quality, price, and after sales service, than *guanxi*.

The above analysis reveals that the significance of *guanxi* may be in decline when competing products or services are not equal in every facet. This, however, raises the question of whether *guanxi* is more important when competing products or services are equal in every facet. This point is outlined by B7's PRC Manager:

Guanxi is somewhat over emphasised in many situations to the exclusion of other basic elements of business, such as good service and delivery of a quality product at a competitive price. If your customer's ability to purchase your product or service is open to influence by *guanxi*, then your business is at risk if someone else's *guanxi* is better than yours. For example, if you have *guanxi* but you have a low quality product at an uncompetitive price and someone comes in with a

better quality product at a competitive price, your *guanxi* will be sorely tested. *Guanxi* only makes a difference if all other things are equal, such as price, quality and service. The one thing about *guanxi*, it is amazingly fickle because it blows with the wind.

In line with B7's PRC Manager, B8's mainland Chinese Chief Representative contended:

If you have a superior quality product at a superior competitive price then *guanxi* becomes less important. But if everything else is equal, *guanxi* becomes more important and without it making a sale is difficult.

In agreement, B17's Hong Kong Chinese Chief Representative stated:

You know that in your industry you have the best product. But the people who will decide to buy your product take factors other than quantitative factors into consideration such as *guanxi* when making a decision. Therefore, even if you have the best product at a competitive price there is no guarantee that the decision maker will purchase your product because somebody may have a personal relationship with the decision maker and you do not, then they will purchase from them.

Guanxi, in other words, becomes the competitive advantage that Australian businesses need to enhance their success in the increasingly competitive environment of the PRC.

This is reiterated by B3's Owner Manager:

The importance of *guanxi* is definitely not in decline because the Chinese market is becoming more competitive. Therefore, to gain a competitive advantage everyone needs to use their *guanxi* to assist them.

While Guthrie's (1998) argument that the salience of *guanxi* is declining might logically be supported as the PRC moves away from a redistributive system to a system where efficiency and competitiveness on the open market are important when competing products or services are not equal in every facet, his argument does not appear to be supported when competing products or services are equal in every facet. In other words, the salience of *guanxi* has increased rather than decreased as competition has intensified and economic efficiency has come to the fore in the reform era. What this also indicates is that *guanxi* can operate effectively within the laws, rules and regulations of the PRC, which is acknowledged by S16's General Manager for North Asia:

The importance of *guanxi* is not in decline, it is as important now as it ever was and it always will be in the future. For example, look at Hong Kong and Singapore they will like to tell you that it is not full of *guanxi* but it is.

As the PRC moves to an environment governed by the rule of law and economic efficiency similar to that of Hong Kong and Singapore, *guanxi* will be far from insignificant. This is consistent with Smart & Smart (2000, p. 260) who argued that while *guanxi* has been domesticated in such a way as to be more or less limited by the rule of law and economic efficiency in Hong Kong and Taiwan, it still continues to affect business decisions. As the economic environment of the PRC is changing, it may be argued that *guanxi*, as a part of Chinese culture, is not necessarily in decline but evolving and adapting to meet the challenges of the global economy.

The suggestion that *guanxi* is not static is based on the notion that culture is viewed as being created by individuals of a particular society in response to the challenges the society's environment presents (Tylor, 1871; Linton, 1961; Barnouw, 1963; Hofstede, 1980; Root, 1984; Harris & Moran, 1987; Bradley, 1995; Harris, 1980; Goodenough, 1970). Hence, as *guanxi* adapts and evolves to meet the challenges of the PRC's business environment, its importance for Australian businesses is unlikely to diminish.

One such challenge to the PRC's business environment is its accession into the WTO, which according to S9's mainland Chinese Customer Service Manager will see an increase in the significance of *guanxi*:

Our market is very competitive and it will be even more so after China is accepted into the WTO because the market we are in will be opened up even more to foreign companies. They will all be trying to work with the Chinese state company in our industry. So who is going to get the deal when everyone is competing against each other. If you have a good relationship with them, then they trust you and they know you are doing good things for them. Therefore, in the end they know you better than the other companies and that will be the difference (S9's mainland Chinese Customer Service Manager).

Although the PRC was accepted into the WTO after the research was undertaken, this comment does raise an important point: is the salience of *guanxi* going to become increasingly important as a competitive advantage, as foreign and domestic competition intensifies in the PRC.

8.4 The Importance of *Guanxi*: A Customer Variable

Earlier in this Chapter it was suggested that the level of importance attached to *guanxi* might be dependent on a businesses' target market in the PRC. B1's PRC Manager supports this suggestion:

For businesses that are dealing with the Chinese market or interacting with the Chinese government *guanxi* becomes more important. However, if you were dealing with the expatriate community in the PRC, *guanxi* is less important.

The point that *guanxi* is more important when foreign businesses deal with the Chinese government than foreign businesses in the PRC, is put further into context by B13's Chief Representative:

Our office conducts two types of business. One is the construction industry and the other is trading. The trading business entails selling machinery to SOEs and this is where the *guanxi* is more important than in our construction business. Our construction business mainly deals with foreign clients. Therefore, *guanxi* is not really an issue with our foreign clients.

Similarly, B5's Owner Manager reported:

We do not need to rely on *guanxi* to get things done. Our company's customers are primarily Western companies. Therefore, we are conducting business on a Western business model. Although we do have relationships with our customers, they are more on a rapport than anything else and certainly not *guanxi*. In addition, we are not forced to conduct business with the government. Our involvement is limited to the necessary documentation. Thus, *guanxi* is not so important for our company. But for companies that are dependent on the Chinese government and the Chinese market, *guanxi* is more important.

This is not to suggest that Chinese officials do not operate according to Western economic principles, as noted in Chapter Seven. It is to merely indicate that they may give more credence to *guanxi* than such principles. This needs to be viewed in the context that the PRC's economy is in a transitional stage of development and that compliance of regulatory reforms may take a while to filter through the Chinese bureaucracy and economy; hence, the difference in emphasis placed on *guanxi* by Chinese officials and Chinese businesses, as opposed to Western businesses.

In agreement with B5's Owner Manager, S12 stated:

The level of importance of *guanxi* is dependent on what sector you are in, what business you are doing and the level of government involvement in that type of business. Therefore, if you are dealing with an SOE or governmental department, it is likely the importance of *guanxi* will be greater than if you were dealing with a foreign company.

Similarly, S5's Malaysian Chinese Director for the PRC commented:

The importance of *guanxi* is dependent on what type of business you are dealing with whether it is a foreign owned company or a SOE. For example, if you are conducting business with a SOE and you want to win their supply business you really have to know who to speak to and how to get through the back door. Thus, *guanxi* is important but if you are dealing with a foreign owned company *guanxi* is not so important. For example, when the General Motors corporation came into Shanghai in 1998 if you wanted to conduct business with them whether you were a Chinese company or not you had to follow the strict Western principle of price, quality, and after sales service.

Not only does this comment indicate that *guanxi* is less important when foreign businesses target other foreign businesses, and is more important when foreign businesses deal with a Chinese company in the PRC, it also implies that it may also be applicable for Chinese companies. In other words, if a Chinese company's target market is a foreign business in the PRC, greater emphasis may be placed on Western economic principles in securing that business than *guanxi*. Conversely, if the Chinese company's target market is a SOE, for example, then more weight may be given to *guanxi* than Western economic principles in securing that business. It must be pointed out that Western companies are in a minority among foreign owned companies in the PRC as most Joint Ventures (JVs) are part-owned by Hong Kong Chinese or Overseas Chinese (Tracy, 1995; Tracy, 2000). Therefore, *guanxi* may still be important in this arena.

What these research participants have indicated is that the level of emphasis placed on *guanxi* may be dependent on a foreign businesses' target market and a Chinese company's target market in the PRC. However, this finding must be treated with caution because of the small number of research participants in this study who observed such differences. Therefore, whether the level of emphasis placed on the importance of *guanxi* is dependent on a foreign businesses' target market or a Chinese company's target market in the PRC is an area that needs further attention.

8.5 The Importance of *Guanxi*: A Foreign Investment Variable

A number of research participants in this study pointed out that the level of importance of *guanxi* in the PRC might also be dependent on an areas' exposure to foreign investment. S5's Malaysian Chinese PRC Director stated that "the further inland you go and the more remote, the greater the dependency on knowing the right people". As the research participant was based in Shanghai, the comment is interpreted to imply that individuals in cities located inland of Shanghai that have little or no exposure to foreign investment may place greater emphasis on *guanxi* in the decision making process than Chinese individuals in cities such as Shanghai. B5's Owner Manager noted that "major cities are more sophisticated and the further you move away from major cities the greater influence of *guanxi*". Sophisticated is interpreted to mean that Chinese individuals in the major cities conduct business more on Western economic principles than *guanxi* because of the level of exposure to foreign investment. This is supported by A7's Export Officer:

In Beijing and Shanghai, the Chinese have a better understanding of the way Westerners conduct business. I mean it is just much more Westernised but of course the further you get out of Shanghai or Beijing, for example, the more things stay the same.

This implies that because Shanghai and Beijing have a greater level of exposure to foreign investment, individuals in these cities have a better understanding of the way Westerners conduct business and place less emphasis on *guanxi* when targeting foreign businesses, whereas those in areas that have little or no exposure to foreign investment rely more on *guanxi*.

According to S12, you do not need to go out of Shanghai to observe such differences in the level of emphasis attached to *guanxi*:

The level of *guanxi* is very much dependent on where you are doing business whether you are doing business in Shanghai outside Shanghai or whatever. Other places in the PRC that are more traditional if you like. However, you do not need to go far outside Shanghai to notice the difference in the levels of *guanxi*. For example, there is a difference if you are conducting business on the *Puxi* side of the river than if you are conducting business in the Pudong New Area. The

Pudong New Area is quite different because it is more international and much more transparent and much less based on *guanxi* than it is on the *Puxi* side.

What the above research participants have indicated is that more emphasis may be placed on Western economic principles than *guanxi* in areas that are more exposed to foreign investment, such as Shanghai and Beijing, than areas that receive little or no foreign investment, such as Qinghai (Chinese Statistical Yearbooks, 1996-2000). Even though only a small number of participants reported such differences, it raises the question of whether the declining salience of *guanxi* is dependent on an area's exposure to foreign investment rather than the implementation of a rational legal system, or whether the level of exposure to foreign investment heightens the move towards a rational legal system, which in turn affects the salience of *guanxi*? If this is the case, why do so many foreign businesses report that Beijing and Shanghai are difficult places to conduct business?

In short, foreign businesses that fail to recognise that the salience of *guanxi* may be dependent on a businesses' target market in the PRC or an area's exposure to foreign investment, and implement strategies effectively and efficiently may be at a competitive disadvantage (Deresky, 1997; Donaldson, 1995).

8.6 The Disadvantages of *Guanxi*

Chapter Seven argued that relying on *guanxi* as an alternative to formal institutional support in a state of uncertainty may reduce transaction costs. This Chapter also argued that utilising *guanxi* to rationalise the Chinese bureaucracy, gain market access, and access to information may enable Australian businesses to obtain first mover competitive advantages. It also argued that as competition has intensified *guanxi* may be the competitive advantage that Australian businesses need to succeed in the PRC. Notwithstanding these benefits, *guanxi* still has its disadvantages, which need to be considered. The quantitative results in Chapter Five revealed that the main disadvantage of *guanxi* was that it is time-consuming to develop and maintain, with 31 percent of

participants reporting such a disadvantage. This was followed by over reliance on *guanxi*, the obligations of *guanxi*, and that *guanxi* is costly in monetary terms, with 13 percent, 12 percent, and 10 percent respectively of participants highlighting such disadvantages. To highlight the disadvantages, some of the comments of the research participants on its time-consuming nature, over reliance on *guanxi*, and the obligations of *guanxi* are examined.

8.6.1 Time-Consuming

The time-consuming nature of developing and maintaining *guanxi* was viewed by the participants as the main disadvantage of *guanxi*, which is consistent with previous literature (i.e. Tsang, 1998; Yi & Ellis, 2000; Fock & Woo, 1998; Pearce & Robinson, 2000). Although Chapter Six discussed how building *xinyong* in a relationship is a time-consuming process (Worm & Frankenstein, 2000, pp. 270-272), it did not, however, examine the time-consuming nature of *guanxi* in its negative light. Therefore, this discussion views the time-consuming nature of developing and maintaining *guanxi* in its negative light, which is highlighted B7's PRC Manager:

To develop *guanxi* you need to develop relationships and that means taking time out yourself. You have to take time out of your day that you would not otherwise take to cultivate those relationships. You have to spend time and money in say taking people out to lunch or dinner on the cultivation of those relationships.

This comment suggests that time taken to develop and maintain *guanxi* is often time that is not available, and may distract an individual from the main task of running the business (Goshal & Moran, 1996, p. 34). This is also implied by B10's Regional Manager for Greater China: "*guanxi* does have some penalties in that I often can be out for 3-4 breakfasts, 3-4 lunches and 3-4 dinners per week". The above comments also reveal that developing and maintaining *guanxi* may be an expensive exercise and that it may not be constrained by office hours. The point that developing and maintaining *guanxi* is not

constrained by office hours is underlined by S6's mainland Chinese Chief Representative:

I tried to break into several competitor's customers, which takes a lot of time and effort before the *guanxi* can be established before you can conduct business. A lot of people always say 'it is very difficult to break into the Chinese market'. Another part of the reason is that you have to spend much much more time than usual taking care of your customer rather than just support them from the face value of your products such as quality, technology, and service. Not only do you need to spend long hours with your customers and distributors after working hours, you also have to take time to get to know their family.

More specifically:

The disadvantage of *guanxi* is that you have to sacrifice a lot of your personal time to build up your *guanxi*. It is not only built up during office hours but over the weekend and during public holidays (B8's mainland Chinese Chief Representative).

Thus, the time-consuming nature of developing and maintaining *guanxi* may not only distract an individual from the main task of running an operation in the PRC, it may also impinge on an individual's personal time, which may cause family problems. Family problems and in particular a spouse's ability to adjust to a new environment have been found to be major causes for the failure of expatriate managers in US and European companies (Deresky, 1996, p. 288-289).

The time-consuming nature of developing *guanxi* having a possible negative impact on a business is outlined by B4's Chief Representative:

International companies that tend to rotate their staff every three years in the PRC have only just put their toe in the water in the sense of developing *guanxi*.

What this comment implies is that rotating expatriates every three years, when they have only just begun to develop and understand the complexities of *guanxi*, may have a negative impact on the business. This is because rotation may occur before their *guanxi* is developed to a stage where it can be used to its fullest potential. Bjorkman and Schaap (1994, p. 151) suggest that a 'transfer period', the period during which the successor and the predecessor work together in the business, may resolve some of these issues. During the transfer period, the successor can learn about the local Chinese conditions and

possibly continue developing and maintaining the *guanxi* his/her predecessor had developed (Bjorkman & Schaap, 1994, p. 151). However, this may be difficult if the *xinyong* within the relationship has not been built to a point where the Chinese individual is comfortable accepting the predecessor's word on the integrity and trustworthiness of the successor. Therefore, in the case of the PRC, expatriate rotation should be greater than every three years.

Even though developing and maintaining *guanxi* is a time-consuming process and is often viewed as a disadvantage, the time it takes to develop *guanxi* may be reduced. As indicated by S6's mainland Chinese Chief Representative:

When I meet a new person and I detect an accent. I use the same dialect. Immediately, I have achieved 50 percent of my *guanxi*.

In other words, cultural similarities may reduce the time it takes to develop and maintain *guanxi*, which is also supported by S7's Hong Kong Chinese General Manager:

It is even more difficult for a Westerner to develop a relationship with a Chinese because there are not many similarities, such as language and culture. Therefore, it makes it harder and it takes longer for a Westerner to develop a relationship.

Although these remarks appear to be directed at individuals, such as overseas Chinese, foreigners who speak Mandarin, for example, will also be able to develop *guanxi* faster and easier than someone without any cultural similarities. As indicated by B13's Chief Representative "it is difficult and time-consuming for a Westerner to develop *guanxi* but it becomes quicker and easier if they are able to speak Mandarin". Even though cultural similarities may enable *guanxi* to be developed more quickly and easily, it must be pointed out that reliance on such similarities, in the case of overseas Chinese, may be no guarantee for business success in the PRC (Bjorkman & Schaap, 1994, p. 149). For example, cultural similarities often lead to misunderstandings when mainland Chinese incorrectly assume that overseas Chinese are familiar with the PRC's way of doing business. In addition, overseas Chinese often lack an understanding of how to deal with the PRC's officials, colleagues, and subordinates. They may even fail to adhere to social

protocols (Bjorkman & Schaap, 1994, p. 149). While the cultural differences between a Western expatriate and a mainland Chinese are great, their failures are often overlooked because it is presumed they are ignorant of correct social behaviours. However, failures of overseas Chinese are likely to be counted against them (Bjorkman & Schaap, 1994, p. 149).

8.6.2 Over Reliance on *Guanxi*

Although over reliance on *guanxi* was only viewed as disadvantage of *guanxi* by 13 percent of participants, it was the second most noted disadvantage of *guanxi*. The dangers are underlined by B7's PRC Manager:

If you do not understand *guanxi* then it can be disadvantageous. I mean there are a number of people who think they have *guanxi* and tell you that they know this guy or that guy. This is often bullshit as a lot of their stated *guanxi* is illusory because when you come to push the button to exercise an imputed obligation. It is not there and it suddenly evaporates. A number of people have hung their business on *guanxi*. For example, our consultant is a son of a senior cadre or something like that but when something goes wrong, suddenly it becomes all a bit too hard and the *guanxi* evaporates very quickly. A number of people do not understand *guanxi* and through this they over rely and place too much emphasis on it.

In essence, individuals who have a misguided understanding of *guanxi* may place too much emphasis on it, which may make them more susceptible to overtures of unscrupulous individuals claiming to have the necessary *guanxi* for their business to succeed. Similarly, S7's Hong Kong Chinese General Manager asserted:

There are a number of people in the PRC all claiming that they have *guanxi* with this person or that person and in fact they do not have what they say they have. The reason these people claim to have *guanxi* is simple. Is that they are poor and they will cheat you whether it be for a dinner or money or whatever they can get, as they see Westerners as walking banks. Therefore, you must conduct a thorough search on these people to find out whether they have the *guanxi* they claim to have. Otherwise you may become stuck with someone that does not have what you thought causing you all sorts of problems.

This is consistent with Pearce and Robinson (2000, p. 36) who contended that the Chinese often overstate their *guanxi* to extract what they can to supplement the little

income they receive. In avoiding such traps, one of the participants in Wang et al's (1999, p. 293) study indicated that they would ask the Chinese to help them with small favours that, nevertheless, required good *guanxi*. Based on the speed and the ability of the individual to perform the 'favour', they could then assess the potential of the individual's *guanxi* (Wang et al 1999, p. 293).

According to B4's Chief Representative, over relying on an employee's *guanxi* is fraught with dangers:

One of the reasons we changed our staff in the office was because a particular Chinese staff member went about his job and kept all the information in his head. The disadvantage of this was that the Chinese person may go out and be hit by a bus and all the *guanxi* this person had and used to gather information is eliminated because he was protective of his information. In addition, it is a disadvantage as well if the staff member is head hunted by competitors. Furthermore, there is no accountability or responsibility for the information that is gathered and presented. For example, if I went back to our staff member and said, 'This information you gave was incorrect and flawed'. They would turn around and say 'I did not give you that information: somebody else told me and I told you'. Thus, there is no way of knowing if that information is correct especially when you are working in an environment where the machinations of the bureaucracy are so extraordinary. It seems that information is power.

Overcoming such difficulties might be achieved by converting an employee's *guanxi* into organisational *guanxi*, as argued by Tsang (1998, p. 70). However, converting an employee's *guanxi* into interorganisational *guanxi* may not be as simple as it seems because the Chinese view information as power. As such they are reluctant to divulge their *guanxi* connections (Walsh et al 1999, p. 78). According to some of the Western respondents in Bjorkman & Kock's (1995, p. 530) study, this problem was also encountered. The Chinese seemed to view their *guanxi* as an asset that they neither wanted to share with Westerners or with other Chinese employees. Yeung & Tung (1996, p. 54) in their study also concluded that the Chinese are reluctant to divulge their *guanxi* because they consider it as a personal asset. Despite the apparent difficulty in converting individual *guanxi* into organisational *guanxi*, it is something that foreign businesses should persist with in order to enhance their chances of success. As discussed in Chapter

Two, this may be achieved through regular meetings and social activities, where senior staff become involved with the *guanxi* (Tsang, 1998, p. 71).

Even though it may be a disadvantage when an employee is poached by a competitor, according to S6's General Manager for the PRC it may also be an advantage:

The disadvantage of *guanxi* is that if your staff have cultivated it with people in the Chinese ministries or bureaucracies and they are poached by a competitor, then you have to rebuild that *guanxi*. However, it may be an advantage because now you would have a contact somewhere else that you previously did not have.

Having a contact somewhere else is only an advantage if that person is in a position of power and influence that is valuable to the business. If the former employee is not in a position to be valuable to the business, and his or her individual *guanxi* has not been converted to interorganisational *guanxi*, then the Australian business would be in a precarious position. In addition, over reliance on a former employee's *guanxi* or any individual outside the organisation is also a risky strategy, as highlighted by S5's Owner Manager:

If you are too reliant on *guanxi*, there is a risk that the people you have *guanxi* with may be promoted or moved to another department, where they may not be as valuable and then you have to rebuild the *guanxi*.

Correspondingly, B11's Manager Business Investment Analysis indicated:

Some companies have *guanxi* with a senior person in a Chinese ministry, which has given them some priorities in access to potential business opportunities. However, the disadvantage is that the person may move on to another department.

More specifically:

The Chinese administration is changing rapidly in terms of senior and middle level management positions. People are moved around at quite a rapid pace and if you only have or rely on one relationship in the place you are doing business. You can be very exposed (B9's Owner Manager).

Thus, over reliance on any one individual's *guanxi*, inside or outside the business, may have a negative impact on the business, which is consistent with Bun & Kiong (2000, p. 80). *Guanxi*, in other words, should be developed with a wide range of individuals in differing occupations and positions of authority because the more diverse the *guanxi*

network, the better one's manoeuvrability becomes in accessing resources and opportunities (Yang, 1994, p. 123; Tsang, 1998, pp. 70-71).

8.6.3 Obligation

Although *guanxi* is a reciprocal relationship with imputed obligations (i.e. Yang, 1994; Hsing, 1997; Yeung & Tung, 1996), they were viewed by 10 percent of participants as a disadvantage. The Owner Manager of B3 indicates that it is not the obligation that is the disadvantage but the type of payment requested:

In the PRC, if you have *guanxi* it is a relationship where you scratch my back and I will scratch yours. Those obligations might be quite simple ones, such as buying medicine. But often you are caught with a favour that you do not really want to do or find difficult to accomplish.

The type of repayments Australian businesses may view as a disadvantage of *guanxi* are outlined by A11's Operations Manager for the Asia Pacific:

Time to time you will have requests made of you and you have to decide whether those requests are reasonable or not. For example, I have had a request from somebody who was keen to get a visa and come to Australia, and they wanted to come on their own, not as a business. They wanted our company to write and say 'we know him personally and you should give him a visa'. Well, we would not do that. If it had been a business to business arrangement then we would have done it. We had to try and explain to him that while we had a relationship we can not use our business because that would put us in disrepute with the Australian immigration department. And when we genuinely wanted someone to go to Australia for business the Australian immigration department would make it difficult.

Although the above comment indicated that the Chinese often request a visa to Australia as repayment of a debt, it did not point out the consequences, if any, of not fulfilling a request. This, however, is taken up by S5's Malaysian Chinese PRC Director:

Guanxi does have a disadvantage because it works both ways. In the sense that you are obliged to return a reward to the other party whether that be a favour, gift, or banquet. For example, I receive a lot of phone calls from my *guanxi* connections that say 'I have my niece, my nephew or close friend who is out of a job can you do something'. In addition, they often say 'such and such is selling this and that can you help'. If I say 'no' it will strain the *guanxi* and it may have repercussions later.

In agreement, S14's General Manager noted:

In our attempts to import our plant and import it duty free, we had to work through the foreign investment review board. The guy that we were dealing with from the foreign investment review board was pretty indifferent to the whole thing, but in the end we got what we wanted through him. At the end of it all he said, 'I have some friends in high places. I can help you sell your product'. Well that sounded great to me and then about a month later we received this phone call from him saying 'everything is fixed up' and we asked, 'Would you like to come to lunch'? He replied, 'Oh there is something that I would like to talk to you about'. Anyway the gist of it was he has got this nephew who is looking for a job. Basically he was asking if we could give his nephew a job. I was not going to employ his nephew because he has just left school and he can not do anything we want him to do. But we are probably looking at repercussions. He was after a favour because he had just done his job.

This comment highlights the differing perception of a relationship held by a Westerner and a Chinese. What a Westerner may perceive as fulfilling one's duties may in fact be perceived by the Chinese as doing a Westerner a favour. Hence, in the Chinese eyes they are entitled to repayment of that favour, and refusal to repay may have repercussions for the business.

It also suggests that Westerners should be better prepared when dealing with the Chinese in the PRC, which is indicated by S12:

Guanxi is a two way street and if somebody is using their *guanxi* to assist you in getting a deal done or whatever, you might think that the *quid pro quo* for that is something fairly straight forward, such as money. But one of the biggest difficulties and differences between the Chinese and Westerners is the psyche in that often Westerners do not actually see what the Chinese want in return. More often than not, what the Chinese want in return you are unable to deliver. For example, if government officials are helping you with something in the PRC to do deals, they might want a visa for their son or daughter to study in Australia. But as a company you have no power to influence the Australian government's process. The Chinese will not tell you that is what they want for doing the deal. Then all of a sudden after a while you get this request out of the blue. They will not say it to you blatantly but that is what they are after. To possibly obtain a better understanding of where the other party is coming from and what their objectives are is to spend time developing the *guanxi*. For example, the Chinese do not like doing business with strangers and they do like to have some understanding of the people they are going to be doing business with.

Although developing *guanxi* is a time-consuming process and is often viewed as a disadvantage, it should be used to the advantage of the foreign business. In other words,

the time taken to develop *guanxi* should be used not only to determine what the Chinese can deliver for the Australian business but what the Chinese expect as repayment for their assistance. And, it should also be used to dispel any perceptions held by the Chinese on what the Australian business is willing and able to deliver as repayment, which should be done in an indirect manner to avoid damaging the relationship building process (Yang, 1994, pp. 133-139). Request for payment is indirect and the repayment appears not to be constrained by time, which is consistent with previous literature (i.e. Yang, 1994; Yeung & Tung, 1996; Hsing, 1997).

S12 takes up the point that repayment of a debt is not constrained by time, where it is also implied that during the time a favour is given and request for repayment is made, the business may no longer be willing or in a position to fulfil the request:

I was given some assistance on a matter and then years later some person came out of nowhere. By this time I had forgotten this thing had ever happened. All of a sudden there was this Chinese guy on my doorstep asking, again asking in a very subtle manner, but I knew he was asking for his repayment. Just because you did some deal with some guy a couple of years ago and you have gone back to Australia forgetting about China. It does not mean the Chinese will forget about their repayment, as your successor, more often than not, will get that guy you did a deal with on their doorstep looking for his repayment.

Australian businesses that give favours in the hope of securing some benefit must also be aware that by the time they request repayment, the Chinese individual may not be willing or able to repay. This again highlights the dangers of relying on *guanxi* alone for business success in the PRC. In essence, it is not the obligation to repay that is the disadvantage of *guanxi*, it is the consequences stemming from an inability or unwillingness to fulfil the imputed obligation. Such consequences may include limiting access to scarce goods, services, and opportunities by the Chinese, or increased bureaucratic interference (Alston, 1989; Yang, 1994; Davies, 1995; Hsing, 1997).

8.7 Summary

This Chapter has argued that *guanxi* is important for Australian businesses in rationalising the Chinese bureaucracy, gaining market access, and access to market information, which may lead to first mover competitive advantages, despite the indication that the salience of *guanxi* is in decline in formal decision making processes. It also argued that as the PRC's market has become increasingly competitive the salience of *guanxi* has increased rather than decreased, as argued by Guthrie (1998). Hence, the significance of *guanxi* may not be affected by the move to a rational legal system and economic efficiency in the PRC. Furthermore, it noted that the importance of *guanxi* may be dependent on a businesses' target market, and an area's exposure to foreign investment in the PRC. Moreover, it established that despite the benefits of *guanxi*, it does have its disadvantages that need to be considered when conducting business in the PRC.

Although this Chapter and Chapter Seven have argued that *guanxi* may enable Australian businesses to obtain competitive advantages, these may be undermined by the discretionary policies of a business, such as human resource and finance policies. The following Chapter examines the human resource and financial problems encountered by some of the participants, arguing that competitive advantages, whether derived from *guanxi* or other competitive actions, are no guarantee for business success in the PRC.

CHAPTER NINE: COMPETITIVE ADVANTAGES ALONE ARE NO GUARANTEE FOR BUSINESS SUCCESS IN THE PRC

9.1 Introduction

Chapter Seven argued that Australian businesses may economise on transaction costs by relying on *guanxi* rather than the Chinese legal system for governance and support, and that this may lead to competitive advantages. Chapter Eight also argued that Australian businesses may obtain first mover competitive advantages from *guanxi*, such as rationalisation of the Chinese bureaucracy, market access, and access to market information. Informants in this study, however, did not seem to recognise that competitive advantages derived from *guanxi* may be undermined by discretionary policies. According to Porter (1985, pp. 80-83), the cost of a value activity is always affected by policy choices, quite independently of other cost drivers. Some of the policy choices and practices that tend to have the greatest impact on cost include product configuration, delivery time, buyers served, wages paid, and human resource policies and practices. Human resource and finance issues were the second and third most noted problems encountered by the participants in this study, with 35 percent and 31 percent respectively reporting such issues.

This Chapter analyses the human resource and some of the finance problems reported by the participants, to highlight the point that discretionary policies may threaten the competitive advantages derived from *guanxi* or other sources. For the purpose of this Chapter reference is only made to the competitive advantages stemming from *guanxi*. However, the analysis is applicable to competitive advantages derived from other sources. The research findings indicated that there was no significant difference among the business size, industry classification, and market entry strategy of the participants who encountered human resource problems. But a significant difference was revealed between the length of an individual's business experience with the PRC and the date of

first entry into the PRC (see Appendix G). The findings also indicated that there was no substantial difference between the length of an individual's business experience with the PRC, the market entry strategy, and the date of first entry into the PRC among the participants who reported financial problems. A considerable difference, on the other hand, was revealed among business size, and industry classification for the participants who noted financial problems (see Appendix H).

9.2 Human Resource Policies and Practices

The human resource management function of any organisation, domestic or international, presents many challenges. However, given the greater complexity of managing international operations, the decisions required on the staffing policies suitable for a particular kind of business, its global strategy, and its geographic locale are even more critical than in domestic operations (Deresky, 1997, pp. 218-282). According to Deresky (1997) and Dowling, Welch and Schuler (1999), International Human Resource Management (IHRM) is being recognised increasingly as a major determinant of success or failure in international business. The human resource problems encountered by the participants in this study include productivity and staffing policies and practices. These issues are examined in the succeeding section to stress the point that competitive advantages stemming from *guanxi* may be jeopardised by discretionary policies.

9.2.1 Productivity

Productivity can be defined as the relationship between real output and the quantity of inputs used to produce it; thus productivity = output/input (Jackson et al 1998, p. 150). Suppose 20 units are produced, the input quantity needed to produce that output quantity is 5, and the price of each input unit is A\$2.00. Total input cost = A\$10.00. Productivity-output per input is 4 (20/5). The per-unit cost of output can be found by the following formula: per-unit production cost = total input cost/units of output (Jackson et al 1998, p.

150). In this case, per-unit cost is A\$0.50 found by dividing A\$10.00 of input cost by 20 units of output. Now, suppose that output declines to 10 units, while the input price and quantity remain constant at A\$2 and 5 units. This results in productivity falling from 4 (20/5) to 2 (10/5). Because the total cost of inputs remains at A\$10, the per-unit cost of the output increases from A\$0.50 to A\$1.00. In other words, if productivity falls then the per-unit cost of production increases. As a result, the cost of performing a given value activity of a business increases. If this was to happen, the competitive advantages obtained through *guanxi* might be undermined.

According to S12, “productivity in the PRC might be 10 percent of what it is in Australia and that increases the costs of conducting business in the PRC”. The differing productivity levels is also noted by S5’s Malaysian Chinese PRC Director:

In Shanghai, if you have a good production manager, they would probably be on about A\$12,000 a year but then you need to add 67 percent to the cost that goes into government levies. This brings the cost of the production manager to around A\$20,000. It still looks good compared to manufacturing costs in Australia. However, the productivity of the worker is not the same as the Australian worker.

This comment suggests that at first glance labour costs in labour intensive operations in the PRC may be low compared with Australia. Notwithstanding, once the productivity levels of Chinese workers in labour intensive operations are taken into consideration the gap between labour costs may be reduced or eliminated. As a result of the lower productivity levels in labour intensive industries in the PRC, the cost of performing a given value activity for the Australian business may increase, possibly threatening any competitive advantage obtained through *guanxi*. This is consistent with AMCHAM (2000, p. 48) and Wang & Ralston (2000, p. 696) who argued that low productivity levels coupled with mandatory benefits and subsidies puts the cost of labour in the PRC into the top bracket for workers and professional staff when compared with other areas in Asia, such as Malaysia, Vietnam, and Indonesia.

Productivity issues were also a concern for S11's Operations Manager "One of our areas did not have a bonus system, they come to work late, took longer for lunch and just lazed around". To increase productivity levels S11's Operations Manager introduced a bonus system based on piece rates:

We have two shifts. One starts at 7:30 am and these workers are here at the factory at 7:00 am. We change shifts at 4.00 p.m. and the night shift starts at 4:15 p.m. The night shift is here at 3.30 p.m. and we have to lock them out. When the time comes to change over we let the night shift in and what you find is that the day shift wants to finish their products and earn a bonus. Then what happens is that if there is someone on the machine and the night shift people come in, they virtually toss that person off the machine.

It appears that this bonus system based on piece rates was effective in increasing the productivity levels of Chinese workers. This supports Ding & Warner (1999, p. 251) who argued that piece rates are an effective measure to increase productivity levels in labour intensive industries in the PRC.

B9's Owner Manager suggests that productivity levels may also be enhanced if a foreign business controls the selection process of employees in the PRC:

Hire your staff because in my experience it is very difficult to take on somebody else's work force, particularly if it is staff from an old SOE. Even if you go through them and do a skill gap analysis and try work out what you have got and what you need, it is an imperfect science in China. You will end up with a work force that you do not really feel is yours. My staff are all hand picked and I feel that they are mine. Hand picked staff rather than an inherited monolithic work force may give you a better chance of success in this market.

Ding et al (1997, p. 598) pointed out that if recruitment were under the control of a Chinese partner, very often they would simply transfer employees from the SOE, recruit more staff than was actually required, sometimes including relatives or friends who are not qualified for the position, and this would result in a power structure aligned to the Chinese partner. Chow (1998) also argued that maintaining control over the selection process is necessary for a foreign business because most SOE employees are ingrained with habits of absenteeism and idleness, and it is often difficult in a Joint Venture with a

Chinese partner to dismiss inherited SOE employees. As indicated by S8's General Manager:

The productivity of our workers suffers because these workers cannot be dismissed. These workers are from the SOE of our partner. In two years we have achieved about 70 percent capacity and to get the next 30 percent is a very slow process. The way we are going, it will take a number of years to get there. That is if we ever get there. Most organisations are like that in that they do not reach 100 percent. The first two years were a slow process because the employees from our partners SOE all wondered why they had to work while other workers from a different section sat and drank tea all day.

As a result of the inability to dismiss inherited SOE employees, productivity levels would fall leading to an increase in the cost of performing a given value activity, which may threaten the competitive advantages derived from *guanxi*. The difficulty in dismissing inherited SOE employees, according to Chow (1998) and Ding et al (1997, pp. 598-599) arises for a number of reasons: senior managers of the SOE receive considerable status and prestige as a result of their patronage in proffering employment to local families.

Discharging employees may cause trauma and anxiety for the local community, bringing considerable embarrassment to local managers as well as loss of prestige. There is also pressure from local governments to keep employment high to reduce the pressure on social welfare services. In addition, for local governments national interests are implicated if a large number of employees are to be dismissed (AMCHAM, 2000, p. 48). Even though Ding et al (1997) and Chow (1998) make reference to Joint Venture operations in the PRC, it is argued that regardless of the type of operation (i.e. Representative Office) Australian businesses should exercise control over the recruitment process because a Chinese human resource officer may still have a tendency to recruit friends and relatives who are not suitable for the position. Having said that, dismissing or not hiring individuals who are associated with one's *guanxi* network may impact on one's ability to derive competitive advantages from their *guanxi*.

Productivity levels of low-skilled and semi-skilled Chinese employees may be influenced not only by the recruitment policies and practices of a foreign business but

also by the following: a lack of initiative by Chinese employees, reluctance of Chinese employees to make a decision, and the reluctance of Chinese employees to take responsibility for their actions (Walsh et al 1999, p. 77, Child & Yu, 1996, pp. 78-79).

This is supported by a number of research participants:

In Hong Kong if you give a direction, it will be carried out 90 percent effectively but in the PRC it can be a very small percentage that actually is done. You have to keep chasing them and checking what they have done to make sure they understand what you have asked them to do and how to do it, all the way through to completion. It is very time-consuming and difficult (S7's Hong Kong Chinese General Manager).

Similarly, S3's PRC President contended:

The Chinese staff may be keen learners but generally they do not use initiative. They are all mechanical. They will do exactly what you want them to do. They will not go outside the square and that can be a real risk because you think something has been completed. There is also a definite reluctance by the Chinese to make a decision if one of the department managers or I am not around. They will not necessarily make a decision by themselves.

In agreement, B6's General Manager for the PRC remarked:

The Chinese staff need direction, they need to be told what to do. That is why we have job descriptions, which define what they are expected to do, when they are expected to do it and how to complete the task. The problem with one of those is that the Chinese staff think that they only need to do what is on the document. They have a real problem with initiative and teamwork. For example, we have a supervisor for trade finance and that is all she will do even to the extent where she will not answer the phone that rings next to her because it is not her phone. Another example, after the May holidays (2000) we had two weeks of work to complete in one week. One of our sections was very busy and needed assistance. In Australia, most employees would note they are busy and think 'they need a hand I will go ask them if they need any help'. Here you have to ask them to go and help. They will do it once they have been told to do so but they will not use their initiative.

Although job descriptions may alleviate some productivity issues, they do not appear to address the productivity problems resulting from the lack of initiative of Chinese employees. On this problem, B11's Manager Business Investment Analysis remarked:

Incredibly there is a real lack of responsibility for any tasks that are delegated to the Chinese. In fact, you have to go to extreme measures to get people to take responsibility. That is one of the most difficult things. I have to make a job list for the Chinese workers on what they have to do, the date it needs to be completed and the day it is completed because I find without that they would not

do the job. They are also extremely quick to blame somebody else or even just not accept responsibility even when there is nobody else to blame.

In agreement, B8's mainland Chinese Chief Representative pointed out:

When our Chinese staff make mistakes they do not take responsibility for their mistakes. If something goes wrong, they always try to blame someone else and I am the same. I do not take responsibility for my mistakes. I try shift the blame to someone else. The Chinese need to be directed what to do, they do not take the initiative to do things. They are always waiting for your direction. But once you give them the direction, they are able to perform the task.

The possible reason for the lack of initiative, and risk aversion among the mainland Chinese employees is put forth by S13's Managing Director:

It is partially cultural. I mean it is better with younger people because they are not accustomed to the SOE culture. I mean the way the old SOE system worked, unless the boss was there and made a decision nothing would be done and if you made a decision you probably would get into trouble. This would probably be seen as threatening the boss, belittling his authority and making him lose face. So, it is partly cultural. I think that it will change as younger people work more in foreign companies because they will become accustomed to the foreign way of doing business.

What this comment suggests is that the lack of initiative and reluctance to make decisions is partially cultural. It also reveals that to enhance productivity levels young people unaccustomed to socialist working practices should be employed rather than old employees indoctrinated with a socialist work ethic.

The contention that the lack of initiative and reluctance to make decisions by Chinese employees is partly cultural is supported by B8's mainland Chinese Chief Representative:

The lack of initiative I feel comes from the way we are brought up in society. We are told what to do and not encouraged to ask questions. If you do ask questions people would look at you and think 'what is wrong with this guy'. The teacher is supposed to be right and supposedly the master or the teacher who is conveying the message is superior or unquestionable. Therefore, students have the tendency to just accept things.

These findings are consistent with Weldon & Vanhonacker (1999, p. 95) who contend that the Chinese lack of initiative and risk aversion has been attributed to various facets of Chinese culture, including traditional socialisation practices where obedience, impulse

control and acceptance of social obligations are encouraged, while independence, assertiveness and creativity are not. The lack of initiative and risk aversion has also been attributed to the Chinese education system, in which students are taught what to think, not how to think; and the PRC's hierarchical society, where status and precedent must be respected (Weldon & Vanhonacker, 1999, p. 95). The reluctance of the Chinese to make decisions and take responsibility may also be attributed to a political system where mistakes were associated with penalties, often severe (Pye, 1992, p. 64; Fang, 1999, pp. 104-105; Wong et al 1999). For example, mistakes would often jeopardise benefits provided by a Chinese *danwei* (work unit), which included the allocation of housing, arrangement of jobs for children of retiring employees, family planning control, medical care, the pension system and other welfare programs (Fang, 1999, p. 104; Warner, 1987, p. 115).

Productivity issues stemming from the lack of initiative and risk aversion of Chinese employees may be overcome by training (Bucknell, 1994, p. 104). According to Rosen (1999, pp. 93-94), training younger rather than older Chinese employees is easier and brings better results because younger employees are more open to new ideas and are not already accustomed to outmoded work practices. In support, B6's General Manager for the PRC noted:

There are huge differences between Chinese nationals aged between 26-35 and 20-25, such as education, the way they approach life, and the way they can discuss things. The younger Chinese nationals have a broader knowledge and are better prepared, and this is reflected in their work ethic.

In other words, productivity levels in the PRC may be enhanced if an Australian business introduces a bonus system based on piece rates for labour intensive operations, maintains control over the recruitment process and targets younger Chinese employees who are not inculcated with a socialist work ethic. As a result, a businesses' ability to sustain a competitive advantage stemming from *guanxi* may be strengthened.

9.2.2 Executive Staffing Policies and Practices

The above discussion indicated that inappropriate staffing policies and practices pertaining to semi-skilled and low-skilled employees in the PRC may increase the cost of performing a given value activity, which may undermine the competitive advantages obtained through *guanxi*. Inappropriate executive staffing policies and practices may also have the potential to increase the cost of performing a given value activity and threaten the competitive advantages obtained through *guanxi*.

Four approaches to executive staffing policies for international businesses can be identified as ethnocentric, polycentric, geocentric, and regiocentric (Ball & McCulloch, 1999, pp. 520-522; Dowling et al 1999, pp. 30-31). An ethnocentric approach to staffing results in all key positions in the international operation being filled by parent-country nationals (PCNs). Sound business reasons for pursuing an ethnocentric staffing policy include a lack of qualified host-country nationals (HCNs) and the need to maintain good communication, co-ordination and control links with corporate headquarters. The disadvantages of such an approach may include the time adaptation to a host country by a PCN, imposition of an inappropriate style of management, and higher compensation for PCNs than HCNs, causing animosity between the local staff and the PCN (Dowling et al 1999, pp. 70-77). A polycentric staffing policy is one in which HCNs are recruited to manage international operations in their own country. The main advantages of a polycentric approach, some of which address the shortcomings of an ethnocentric approach, are elimination of language barriers avoiding the adjustment problems of expatriate managers and their families; removing the need for expensive cultural training programs; reducing hiring costs; and adaptation of a low profile in sensitive political situations. The disadvantages of a polycentric approach may include conflicting national loyalties and a range of cultural differences (i.e. personal value differences and differences in attitudes to business), possibly isolating the headquarters staff from the HCN. It also restricts PCNs from gaining international experience and limits the career

opportunities of the HCN, which over time may constrain decision making and resource allocation (Dowling et al 1999, pp. 70-77).

The geocentric approach uses the best people for the key roles throughout the organisation, regardless of nationality. The main advantages include the development of an international executive team, and overcoming the nominal links between headquarters staff and the international operation. The main disadvantages are that it may be expensive because of increased training and costs, and large numbers of PCNs, HCNs, and Third Country Nationals (TCNs) need to be sent abroad to build and maintain the international team required to support a geocentric staffing policy (Dowling et al 1999, pp. 70-77). Third country nationals are neither citizens of the home country nor the host country but they may come from a culture similar to that of the host country and may have work experience in the host country (Ball & McCulloch, 1999, p. 522). A regiocentric approach to staffing uses managers from the geographic region to be responsible for the businesses' operations in that region (Roffey & Lau, 2001, p. 170). The main advantages of the regiocentric approach are that it allows interaction between executives transferred to regional headquarters from subsidiaries in the region, reflects some sensitivity to local conditions, since local subsidiaries are mainly staffed by HCNs, and it may be a way that an international business can gradually move from a purely ethnocentric or polycentric to a geocentric approach. The main disadvantages are that it can produce federalism on a regional rather than a country level constraining the organisation from taking a global stance, and staff may advance to regional headquarters but seldom to positions at the parent headquarters (Dowling et al 1999. pp. 70-77).

In the case of the PRC, Woodward and Liu (1993, p. 88) argued that the use of individuals of Chinese extraction in senior positions is beneficial to the operation in terms of managing the human resource to the greatest economic benefit. As noted in Chapter Eight, however, the use of overseas Chinese may be fraught with difficulties.

Notwithstanding, Woodward and Liu's (1993) argument is supported by B8's mainland Chinese Chief Representative:

I do identify many areas that Australians and Chinese operate differently in a business environment. My personal understanding is that it would be far easier for people who have a very thorough understanding of the local culture, the politics and the local environment to run the office and manage the local people. Because foreigners who come from Australia or other Western countries that have a very limited knowledge on how to handle the situation, sometimes create a lot of tension between the staff in the office. The way they manage Western staff is totally different to the way you manage Chinese staff. For example, I seem to notice that the foreigner tries to make a very simple decision, they do not care too much about the personal reaction, the human feelings of their decision. They just say what is right and what is wrong. Theoretically, if they think it is the right thing to do they will do it. But as we know in Chinese culture if the Chinese can tolerate something they will not say 'no', even if they do not feel very happy about this situation. Conversely, if they do not say 'yes', it already means 'no'. However, Westerners may say 'no' from time to time to your face and this makes people feel very uncomfortable. Therefore, my personal understanding is that if you promote localisation and if you can trust local people or people with local background to run the office rather than spending huge amounts of money for Westerners to stay on site in China, it can save money and achieve a better result in staff relationships.

This comment is consistent with Dowling et al (1999, p. 14), who argued that expatriate managers who are culturally insensitive and behave in a manner based on ignorance or misguided beliefs ("my way is best," or "what works at home works here") are not only inappropriate for foreign assignments but often cause international business failure. The comment of B8's mainland Chinese Chief Representative also suggests that staffing key positions in the PRC with HCNs rather than PCNs may lead to an economic benefit in managing the human resource in the operation. Given that many expatriates find it difficult to work and live in the PRC, increasing the possibility of expatriate failure (Wong & Law, 1999, p. 28), HCNs rather than PCNs may enhance a businesses' ability to sustain competitive advantages obtained through *guanxi*. Hiring HCNs rather than PCNs may also provide a strategic advantage for a foreign business. This is because a foreign business may gain access and use of a HCN's *guanxi* network before a PCN could develop *guanxi*, which is a time-consuming process, to a level that could be

valuable to the business. Having said that, Chinese managers, as is the case with non-executive staff, often lack decision-making skills and are wary of taking personal initiatives (Dowling et al 1999, p. 271).

It must be pointed out that to date no measures have been undertaken by the business referred to as B8 to address the problems arising from cultural insensitivity by their Australian expatriate (pers.comm., 8th March, 2002). What this indicates is that the business has not reached its potential in terms of managing its human resource to the greatest economic benefit, and that the business does not recognise that their discretionary policies may have a negative impact on their ability to compete in the PRC.

9.3 Financial Issues

Twenty-five percent of research participants reported financial problems whilst conducting business in the PRC. They include, from most noted to least: customer non-payment, repatriation of monies out of the PRC, and finance availability. Although repatriation and finance availability were problems, this Chapter examines only the problem of customer non-payment to highlight the possibility that the financial policies and practices of an Australian business may threaten the sustainability of competitive advantages obtained through *guanxi*.

9.3.1 Customer Non-Payment

Porter (1985, pp. 80-83) argued that the cost of a value activity is always affected by the policy choices a business makes, such as product configuration, delivery time, wages paid, human resource policies and practices, and buyers served. Buyers served may be extended to encompass the policies and practices of a business pertaining to the terms and conditions of a sale. On customer non-payment, B10's Regional Manager for Greater China stated:

One of the biggest problems for most companies in the PRC, and ours included, is not being paid. This is perpetuated by the practices of foreign companies where they conduct business on credit terms, as they would in Western countries. In the PRC, it is better to sell a lower volume where you will know you will be paid than to sell a larger volume where you may only receive a small percentage of the money owed.

In other words, customer non-payment is perpetuated by inappropriate business policies and practices governing the terms and conditions of a sale in the PRC. The consequences are underlined by A1's Vice President:

Our operation has been making heavy losses of approximately A\$2 million per year. This project from the initial stages was oversold on what it could do. In addition, the company was delivering goods to customers and payments were not received until they had sold the product. As a result, there was no cash flow in the business. But we have made the necessary changes and have turned the A\$2 million losses to a break-even stance in the past few years.

As a result of cash flow difficulties, the Australian business may not have been able to meet its short term debt obligations, and if the situation was not rectified closure of the business may have been imminent (Petty et al 2000, p. 199).

The importance of appropriate policies and practices governing the terms and conditions of a sale is heightened when one considers the problem of triangular debt in the PRC:

Payment difficulties caused by triangular debt in the PRC are one of the biggest risks of conducting business in the PRC. However, if our customers do not meet our credit requirements or do not purchase with cash. I would rather sell no products than sell them and not get paid for them (S15's mainland Chinese Chief Representative).

Triangular debt is explained by S5's Malaysian Chinese Director for the PRC:

Say you sell your goods to company A and company A gives you only 30 percent of the money owed. Now company A is owed money from company B and will only be able to pay you when company B pays company A. It does not just end here because company B is owed money from company C and will only be able to pay company A when company C pays company B. However, company A can not approach company C because he does not have any influence over him paying company B and when company C pays company B company A will only receive a percentage of the money given to company B. More often than not, company A is owed money from a number of different companies making the collection of money owed more difficult. You can be guaranteed that because of triangular debt part of your value outstanding will not be recovered.

To reduce customer non-payment S16's General Manager North Asia stated "we demand a 30 percent down payment of the purchase price of the goods and an irrevocable letter of credit for the remaining amount". Similarly, S8's General Manager commented, "we now tie our customers to the venture with equity, therefore, minimising the risk of non-payment". Utilising one's *guanxi* network may also provide an avenue to recover monies outstanding. *Guanxi*, however, may be limited in its power and influence because of the infinite nature of triangular debt and the limited resources one may have at one's disposal for 'favour exchange'.

9.4 Summary

This Chapter has argued that competitive advantages may be threatened by productivity levels pertaining to low and semi-skilled Chinese employees, and inappropriate executive staffing policies and practices. It also argued that inappropriate policies and practices governing the terms and conditions of a sale in the PRC may undermine a businesses' competitive advantage. In addition, this Chapter suggested that to sustain a competitive advantage a business should consider the following: implementing a piece rate bonus system for labour intensive operations, maintaining control over the recruitment process of Chinese employees; employing young Chinese who are more responsive to training and are not indoctrinated with a socialist work ethic for non-executive positions; hiring Host Country Nationals for executive positions; and not implementing Western credit practices in the PRC. What these measures indicate is that competitive advantages derived from *guanxi* or other sources are no guarantee for business success in the PRC.

The Concluding Chapter discusses the significance of this study, the study's contribution to knowledge, the implications of the findings for Australian businesses operating in the PRC, the limitations of the study, and suggestions for further research.

CHAPTER TEN: CONCLUSION, LIMITATIONS, AND SUGGESTIONS FOR FURTHER RESEARCH

In a sense, this chapter is an epilogue, as the main conclusions of the study have been enunciated during the discussion on how to develop and maintain *guanxi*, whether *guanxi* is a form of corruption (Chapter Six), the salience of *guanxi*: from a transaction cost perspective (Chapter Seven), a first mover theory approach to the importance of *guanxi* in the PRC's foreign business environment (Chapter Eight), and the observation that competitive advantages derived from *guanxi* or other sources are no guarantee for business success in the PRC (Chapter Nine). Accordingly, from this point the focus will be on the significance of the study for the major area of interest: the role of *guanxi* for Australian businesses operating or seeking to operate within the PRC.

10.1 The Significance of the Study

The first significant contribution this study makes is that *guanxi* is not static. Although this may suggest a decline in the salience of *guanxi*, it is merely an adaptation of *guanxi* to the challenges of the surrounding environment. For example, as the PRC has moved from a command economy characterised by scarcity to one of increasing competition, where decision makers are having to become more accountable for their decisions due to the implementation of rules and regulations, the decision to purchase one product or service over another depends more on the attractiveness of the deal than *guanxi* alone. If competing products or services are equal in every facet then it may be *guanxi* that becomes the deciding factor. In other words, the salience of *guanxi* in the decision making process has merely shifted to a new position and not declined, as argued by Guthrie (1998).

This study's analysis of the human resource and financial problems encountered by the research participants demonstrated that the discretionary policies of an Australian

business may undermine the competitive advantages derived from *guanxi* or other sources. The discretionary policies of a business, its competitiveness in the PRC market, and *guanxi* combined may enhance a businesses success in the PRC.

This study contributed significantly to the general theory of competitive advantage by analysing the main advantages of *guanxi*, which include reduced bureaucratic interference, market access, and access to market information, obtained by the Australian businesses in terms of pioneering discoveries or innovative competitive actions that may lead to first mover competitive advantages (Schumpeter, 1936; Porter, 1985; Porter, 1990). Evidence suggested that first mover competitive advantages obtained from *guanxi* may not have been abolished or reduced, because the salience of *guanxi* has adapted and evolved to meet the challenges of the PRC's business environment. However, even though first mover competitive advantages continue, and that the importance of *guanxi* has adapted to meet the challenges of the surrounding environment, *guanxi* continues to have its disadvantages.

Moreover, this study contributed significantly to the theory of transaction cost economics by analysing the legal problems faced by Australian businesses in the PRC. Findings in this study suggest that the PRC's legal environment pertaining to Australian businesses continues to be marred by uncertainty and unpredictability, despite legal reform. As a result of this, the salience of *guanxi* as an alternative to the market, hierarchy and hybrid forms of governance continues, supporting Davies (1995), Boisot & Child (1988), Standifird & Marshall (2000), and Luo (2000a). In other words, *guanxi* as a substitute for formal institutional support may continue to economise on transaction costs. Even if the PRC moves to an environment governed by the rule of law and economic efficiency, such as in Hong Kong and Taiwan (Smart & Smart, 2000), where *guanxi* has been domesticated in such a way as to be more or less limited by the rule of law and economic efficiency, evidence suggests that *guanxi* will be far from insignificant.

This study has made a number of contributions to knowledge in the area of *guanxi*, transaction cost economics, and the first mover theory of competitive advantage. These are summarised below. A further strength of this study is that it provides a clear outline of the methods used, allowing replication in the future.

- Insight into the salience and role of *guanxi* for Australian businesses.

Most studies on the importance and role of *guanxi* have been primarily dominated by evidence from Overseas Chinese, North American, and European companies. No previous studies have examined the role and importance of *guanxi* for facilitating investment in the PRC by Australian businesses. This study adds to the literature by filling this gap and establishing a foundation for comparison.

- Development of a theoretical model of transaction cost economics based on the legal problems faced by the Australian businesses in the PRC.

Most research debating the ways in which *guanxi* may be an alternative to the market, hierarchy, and hybrid forms of governance concentrates on theoretical modelling. This study uses the theoretical model of transaction cost economics to determine the extent to which *guanxi* is an alternative form of governance for Australian businesses operating in the PRC. It is not a test of the theoretical model of transaction cost economics but an example of the use of the model to determine where and when *guanxi* is significant.

- Development of a theoretical model of competitive advantage in relation to *guanxi*.

While prior studies have affirmed that the advantages of *guanxi* may be a source of competitive advantage for foreign investors in the PRC, most do not provide a clear link between the advantages of *guanxi* and the first

mover theory of competitive advantage. This study extends an existing model to provide such a link, and to ascertain where and when *guanxi* is important for Australian businesses operating in the PRC.

These three contributions to knowledge fill the gap in the literature on the importance of *guanxi* for Australian businesses. They have some important implications for theory and practice, and provide the foundation for a great deal of further research. These implications are discussed in the following section.

10.2 Implications of the Findings for Australian Businesses Conducting Business within the PRC

This study has implications for the success of Australian businesses in the PRC. Examination of the results suggest that Australian investors should be conscious that the Chinese may utilise the ‘art of *guanxi*’ to create the impression that the primary concern is the relationship and not the instrumental goal. As a result, Australian investors may be led into a false belief and act accordingly, with extra concessions being granted to the Chinese.

Evidence from this study also indicates that failure to partake in *guanxi*, because of one’s moral standing or belief that it is corrupt, may result in a competitive disadvantage for the business. This is not suggest that *guanxi* alone is a guarantee for business success in the PRC, as the competitive advantages derived from *guanxi* or other sources can be undermined by discretionary policies or *guanxi*’s disadvantages (see Chapter Eight and Chapter Nine). Rather, it is to suggest that *guanxi* may heighten a businesses’ chance of success.

The findings in this study further demonstrated that failing to recognise that the salience of *guanxi* may be dependent on a businesses’ target market or the exposure of an

area in the PRC to foreign investment, and that *guanxi* is not static, may hinder a businesses' ability to compete effectively.

10.3 Limitations

The limitations of scope in this study are outlined in Chapter One, and limitations of the methods employed are discussed in Chapter Four. A few additional limitations of the study appeared once the analysis was undertaken: a market entry strategy response-bias, a size response-bias, and an industry classification response-bias, which were discussed in Chapter Five.

10.4 Suggestions for Further Research

The study has revealed a number of important areas for further research, which are outlined below.

Gift giving is an important aspect of Chinese culture where the type of gift presented correlates with the amount of respect shown to the receiver, and the sincerity in establishing a relationship (Jacobs, 1979). Unique or rare gifts, but not necessarily expensive, demonstrate greater respect and sincerity for the gift receiver (Hsing, 1998). A number of research participants in this study gave either a unique or corporate gift with company logos to show respect and sincerity for the relationship. This raises the following questions: Does a corporate gift with a company logo convey a similar level of respect and sincerity than a unique or rare gift? Does the level of respect and sincerity a unique or rare gift with a company logo conveys differ from a unique or rare gift without the logo?

Evidence in this study indicated that the PRC's legal environment continues to be marred by uncertainty and unpredictability arising from the lack of enforcement, inconsistent interpretation of laws, the lack of legal culture, changes to the laws, the underdeveloped legal system and the lack of transparency. It was suggested that issues

arising from the flexibility and the discretion local provincial officials have interpreting and implementing laws, rules and regulations are not going to fade with the PRC joining the WTO implying that *guanxi* may continue to be important for negotiating the PRC's legal environment. The findings in this study provide a foundation for further research on the impact China's accession to the WTO may have on the PRC's legal environment and the significance of *guanxi*.

A small number of research participants in this study indicated that the level of importance of *guanxi* might be dependent on a businesses' target market in the PRC. Thus, further research is needed to confirm the suggestion that foreign businesses which deal with Chinese companies need to place greater emphasis on *guanxi* than if they were targeting foreign companies, and whether Chinese companies need to place greater emphasis on *guanxi* when dealing with other Chinese companies than if they were dealing with foreign companies.

A small number of research participants in this study also indicated that the significance of *guanxi* may be dependent on an area's exposure to foreign investment. This raises the question of whether the level of exposure to foreign investment in a certain locale heightens the move towards a rational legal system? If so, does this have any impact on the salience of *guanxi*, and if so, why do so many foreign businesses report that Beijing and Shanghai are difficult places to conduct business? It also raises the question whether *guanxi* is more or less significant in rural China than urban China? If so, does this have any implications for foreign investment in rural and/or urban China?

As this study concentrated on economic *guanxi*, it provides a foundation for comparison on the role and importance of social *guanxi* during China's economic transition.

Finally, the variable nature of *guanxi* and the continued economic reform process in the PRC provides all the more reason for continued research, inquiry and debate.

APPENDIX A: MAIL SURVEY COVER LETTER AND QUESTIONNAIRE

Dear Sir/Madam,

LETTER OF INTRODUCTION

This letter is to introduce Andrew Scott Whitehead who is a PhD student in the School Of Political and International Studies at Flinders University.

Andrew Whitehead is undertaking research leading to the production of a thesis on the subject of Australian Business in the People's Republic of China.

Andrew Whitehead would be most grateful if you would be prepared to spare the time to assist in this project, by completing the attached questionnaire, which touches upon certain aspects of his thesis topic. No more than 15-20 minutes will be required to complete the questionnaire.

Be assured that any information provided will be treated in the strictest confidence and none of the participants will be individually identifiable in the resulting thesis, report or other publications. You are, of course, entirely free to decline to answer particular questions. If you are not responsible for your firm's Chinese activities could you please forward the questionnaire to the appropriate department or person.

Any enquiries you may have concerning this project should be directed to the Head of the School of Political and International Studies (Dr David Plant) at the address given above or by telephone on (08) 8201 2186, fax (08) 8201 5111

This research project has been approved by the Flinders University Social and Behavioural Research Ethics Committee. The Secretary of this Committee can be contacted on (08) 8201-3513, fax (08) 8201-5034, e-mail Kim.Jones@cc.flinders.edu.au.

Thank you for your attention and assistance.

Yours sincerely,

Dr David Plant
Head
School of Political and International Studies

APPENDIX A: QUESTIONNAIRE

AUSTRALIAN BUSINESS IN THE PEOPLE'S REPUBLIC OF CHINA (PRC)

This questionnaire seeks information about your firm's experiences in conducting business with or within the People's Republic of China (PRC). Of particular interest is the role and importance of Guanxi. **Guanxi** refers to the establishment of personal connections between individuals to enable bilateral flows of social or economic transactions.

SECTION I: PRELIMINARY QUESTIONS

A: Does your firm currently conduct business with or within the People's Republic of China?

(Please circle the most appropriate answer)

Yes

No

**Please continue from
QUESTION B**

**Please Return The Uncompleted
Questionnaire In The Enclosed Stamp
Addressed Envelope**

B: Is your firm:

(Please circle the most appropriate answer)

(1) Wholly Australian owned →

**Please continue from
QUESTION C**

(2) Partly Australian owned →

(3) Wholly Foreign owned



**If circled wholly foreign owned please return the uncompleted
questionnaire in the enclosed stamp addressed envelope.**

C: Is your firm listed on the Australian stock exchange?

(Please circle the most appropriate answer)

Yes

No

PLEASE CONTINUE WITH SECTION II

SECTION II

(1) What was the most recent market entry strategy used to enter the PRC?
 (Please circle the most appropriate answer)

(1) Joint Venture	(2) Licensing Agreement
(3) Wholly Owned Operation	(4) Turnkey Operation
(5) Contract Manufacturing	(6) Management Contract
(7) Export	(8) Franchise Agreement
(9) Other (Please specify).....	
.....	

(2) Please choose the business classification which most closely describes the main activity of your firm with or within the PRC?
 (Please circle the most appropriate classification)

(1) Agriculture, Forestry and Fishing	(2) Mining
(3) Electricity, Gas and Water Supply	(4) Construction
(5) Retail Trade	(6) Accommodation
(7) Manufacturing	(8) Wholesale Trade
(9) Restaurants	(10) Cafes
(11) Transport and Storage	(12) Communication Services
(13) Finance and Insurance	(14) Property and Business Services
(15) Government Administration	(16) Defence
(17) Education	
(18) Other (Please Specify).....	

(3) In which year did your firm first conduct business with or within the PRC?
 (Please specify)

.....

(4) Has your firm's involvement with or within the PRC been continuous?
 (Please circle the most appropriate answer)

Yes

No

↓
 Indicate timing and years of discontinuity.....

(5) Did your firm encounter any of the following problems when conducting business with or within the PRC?
 (Please circle the most appropriate answer/s)

(1) Labour Yes No

(2) Bureaucratic Yes No

(3) Legal Yes No

(4) Taxation Yes No

(5) Product quality Yes No

(6) Distribution Yes No

(7) Other (Please specify).....

.....

(6) When entering the PRC what methods did your firm use to initiate contact?
 (Please circle the most appropriate answer/s)

(1) Austrade Yes No

(2) Australian State Government Yes No

(3) Chinese Government Department Yes No

(4) Other (Please specify).....

(7) **Did your firm use any form of ‘personal connections’ (guanxi) to initiate contact with the PRC?**

(Please circle the most appropriate answer)

Yes

No

(8) **Did your firm use ‘personal connections’ (guanxi) when conducting business with or within the PRC after the initial contact stage?**

(Please circle the most appropriate answer)

Yes



**Please continue from
QUESTION 9**

No



**Please continue from
QUESTION 15**

INSTRUCTIONS: From your business experience please indicate your agreement or disagreement with each of the statements in Q9, Q10 & Q11.

(9) **The use of ‘personal connections’ (guanxi) for conducting business with and within the PRC is important:**

(Please circle the most appropriate answer)

5	4	3	2	1
Strongly Agree	Agree	Undecided	Disagree	Strongly Disagree

(10) **The importance of ‘personal connections’ in the business environment in the PRC is declining:**

(Please circle the most appropriate answer)

5	4	3	2	1
Strongly Agree	Agree	Undecided	Disagree	Strongly Disagree

(11) **The most effective way of overcoming problems associated with business in the PRC is by using ‘personal connections’ (guanxi):**

(Please circle the most appropriate answer)

5	4	3	2	1
Strongly Agree	Agree	Undecided	Disagree	Strongly Disagree

(12) Did your firm overcome any problems by using ‘personal connections’ (guanxi) when conducting business with or within the PRC?
 (Please specify what problems)

.....

(13) Did your firm obtain any of the following benefits by using ‘personal connections’ (guanxi) when conducting business with or within the PRC?
 (Please circle the most appropriate answer/s)

(1) Access to Scarce Resources	Yes	No
(2) Market Information	Yes	No
(3) Reduced Bureaucratic Interference	Yes	No
(4) Tax Concessions	Yes	No
(5) Cheap Material Supplies	Yes	No
(6) Reliable Material Supplies	Yes	No
(7) Other Benefits (Please specify).....		

(14) Were any of the following a disadvantage of using ‘personal connections’ (guanxi) in the course of business with or within the PRC?
 (Please circle the most appropriate answer/s)

(1) Time Consuming	Yes	No
(2) Costly in money terms	Yes	No
(3) Ineffective	Yes	No
(4) Other (Please specify).....		

.....

(15) How would you describe yourself?

(Please circle the most appropriate answer)

(1) Australian

(2) Chinese

(3) British

(4) Australian-Italian

(5) Australian-Greek

(6) Australian-Chinese

(7) Other (Please specify)

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Page 10 of 10

(16) What is your current position in the firm?

What is your
(Please specify)

.....

(17) How long have you held your current position?

(Please specify)

.....

How long ha

How many people are employed in your firm?

How many p (Please specify)

How long have you personally been engaged in doing business with the PRC?

(Please specify)

If you would like to comment further on any of the above questions, **please** do so below

.....

For more information, contact the Office of the Vice President for Research and the Office of the Vice President for Student Affairs.

.....

**HOW LONG DID IT TAKE YOU TO COMPLETE THIS
QUESTIONNAIRE.....**

**PLEASE RETURN THE COMPLETED QUESTIONNAIRE IN THE ENCLOSED
STAMPED ADDRESSED ENVELOPE**

**Flinders University-Adelaide
Department of Political and International Studies
Andrew Scott Whitehead
GPO BOX 2100
Adelaide SA 5001**

**THANK YOU FOR YOUR ASSISTANCE WITH THIS IMPORTANT
RESEARCH**

APPENDIX B: INTERVIEW LETTER, CONSENT FORM AND INTERVIEW GUIDE

Dear Sir/Madam

This letter is to introduce Andrew Scott Whitehead who is a PhD Candidate in the Department of Political and International Studies at Flinders University.

He is undertaking research leading to the production of a PhD thesis on the subject of Australian Businesses in the People's Republic of China.

He would be most grateful if you would volunteer to spare the time to assist in this project, by granting an interview which touches upon certain aspects of this topic. The interview will run for approximately 1 hour.

Be assured that any information provided will be treated in the strictest confidence and you will not be individually identifiable in the resulting thesis. You are, of course, entirely free to discontinue your participation at any time or to decline to answer particular questions.

Since Andrew Whitehead intends to make a tape recording of the interview, he seeks your consent, to record the interview, to use the recording or a transcription in preparing the PhD thesis, on condition that your name or identity is not revealed, and the recording will not be made available to any other person. It may be necessary to make the recording available to secretarial assistants for transcription, in which case you may be assured that such persons will be advised of the requirement that your name or identity not be revealed and that the confidentiality of the material is respected and maintained.

Any enquiries you may have concerning this project should be directed either to me or the Head of the School at the address given above or by telephone on 8201 2186, fax 8201 5111

This research project has been approved by the Flinders University Social and Behavioural Research Ethics Committee. The Secretary of this Committee can be contacted on 8201-3513, fax 8201-5034, e-mail Kim.Jones@cc.flinders.edu.au.

Thank you for your attention and assistance.

Yours sincerely,

Associate Professor Noel Tracy
Department of Political and International Studies
Flinders University-Adelaide

APPENDIX B: CONSENT FORM FOR INTERVIEW

I

being over the age of 18 years hereby consent to participate as requested in the interview for the research project on Australian Investment in the People's Republic of China.

1. I have read the information provided.
2. Details of procedures and have been explained to my satisfaction.
3. I agree to my information and participation being recorded on tape.
4. I am aware that I should retain a copy of the Information Sheet and Consent Form for future reference.

5. I understand that:

- * I am free to withdraw from the project at any time and am free to decline to answer particular questions.
 - * While the information gained in this study will be published as explained, I will not be identified, and individual information will remain confidential.
 - * I may ask that the recording be stopped at any time, and that I may withdraw at any time from the interview.

Participant's signature.....Date.....

I certify that I have explained the study to the volunteer and consider that she/he understands what is involved and freely consents to participation.

Researcher's signature.....Date.....

**APPENDIX B: GUIDE FOR SEMI-STRUCTURED INTERVIEWS IN
ADELAIDE, BEIJING AND SHANGHAI, SEPTEMBER 1999-JUNE 2000**

Interviews with Business Executives of Australian Businesses Conducting Business with
or within the People's Republic of China (PRC)

1. What is your position, and how long have you been in your current role?
2. How long have you worked for your current employer?
3. What is your length of business experience with the PRC?
4. Do you speak any Chinese languages?
5. Are you an Australian?
6. What market entry strategy did your firm use to enter the PRC, and when did the firm first conduct business with the PRC?
7. Has your firm's involvement with the PRC been continuous?
8. What industry is your business in?
9. How many people are employed in the business?
10. What methods were employed by your business to initiate contact with the PRC?
11. How would you define *guanxi*?
12. Did the firm use *guanxi* at any time during the initial contact stage with the PRC?
13. Have you used *guanxi* in the course of business in the PRC? (Examples)
14. How have you developed, and maintained your *guanxi*?
15. What problems have you encountered while conducting business in the PRC? (Eg. labour, bureaucratic, contractual, infrastructure, government, product quality, storage, distribution, taxation, legal, etc.).
16. Have you used *guanxi* to overcome any problems? (Examples, Effectiveness)
17. Is *guanxi* important for conducting business in the PRC?
18. Have you seen a decline in the importance of *guanxi* for conducting business in the PRC?
19. What are the advantages, and disadvantages of *guanxi*?
20. Some people have labelled the usage of *guanxi* as corruption and others see it as the normal way of conducting business in the PRC. What are your thoughts?

APPENDIX C:
AUSTRALIAN AND NEW ZEALAND STANDARD INDUSTRIAL
CLASSIFICATION (ANZSIC) CATEGORIES

1993 Edition

Agriculture, Forestry and Fishing

Horticulture and Fruit Growing
 Grain, Sheep and Beef Cattle Farming
 Dairy Cattle Farming
 Poultry Farming
 Other Livestock Farming
 Other Crop Growing
 Services to Agriculture
 Hunting and Trapping
 Forestry and Logging
 Marine Fishing
 Aquaculture

Mining

Coal Mining
 Oil and Gas Extraction
 Metal Ore Mining
 Construction Material Mining
 Other Mining
 Exploration
 Other Mining Services

Manufacturing (M)

Meat and Meat Product (M)
 Dairy Product (M)
 Fruit and Vegetable Processing
 Oil and Fat (M)
 Flour Mill and Cereal Food (M)
 Bakery Product (M)
 Other Food (M)
 Beverage and Malt (M)
 Tobacco Product (M)
 Textile Fibre, Yarn and Woven Fabric (M)
 Textile Product (M)
 Knitting Mills
 Clothing (M)
 Footwear (M)
 Leather and Leather Product (M)
 Log Sawmilling and Timber Dressing
 Other Wood Product (M)
 Paper and Paper Product (M)
 Printing and Services to Printing
 Publishing
 Recorded Media Manufacturing and Publishing
 Petroleum Refining
 Petroleum and Coal Product (M)

Basic Chemical (M)
 Other Chemical Product (M)
 Rubber Product (M)
 Plastic Product (M)
 Glass and Glass Product (M)
 Ceramic Product (M)
 Cement, Lime, Plaster and -
 Concrete Product (M)
 Non-Metallic Mineral Product (M)
 Iron and Steel (M)
 Basic Non-Ferrous Metal (M)
 Structural Metal Product (M)
 Sheet Metal Product (M)
 Fabricated Metal Product (M)
 Motor Vehicle and Part (M)
 Other Transport Equipment (M)
 Photographic and Scientific -
 Equipment (M)
 Electronic Equipment (M)
 Electrical Equipment and Appliance
 Industrial Machinery and -
 Equipment (M)
 Other Manufacturing

APPENDIX C:
AUSTRALIAN AND NEW ZEALAND STANDARD INDUSTRIAL
CLASSIFICATION (ANZSIC) CATEGORIES

1993 Edition

Electricity, Gas and Water Supply

Electricity Supply
 Gas Supply
 Water Supply, Sewerage and Drainage Services

Construction

Building Construction
 Non-Building Construction
 Site Preparation Services
 Building Structure Services
 Installation Trade Services
 Building Completion Services
 Other Construction Services

Wholesale Trade

Farm Produce Wholesaling
 Mineral, Metal and Chemical Wholesaling
 Builders Supplies Wholesaling
 Machinery and Equipment Wholesaling
 Motor Vehicle Wholesaling
 Food, Drink and Tobacco Wholesaling
 Textile, Clothing and Footwear Wholesaling
 Household Good Wholesaling
 Other Wholesaling

Accommodation, Cafes and Restaurants

Accommodation
 Pubs, Taverns, and Bars
 Cafes and Restaurants
 Clubs (Hospitality)

Retail Trade

Supermarket and Grocery Stores
 Specialised Food Retailing
 Department Stores
 Clothing and Soft Good Retailing
 Furniture, Houseware and -
 Appliance Retailing
 Other Personal and Household -
 Good Retailing
 Household Equipment Repair -
 Services
 Motor Vehicle Retailing
 Motor Vehicle Services

Transport and Storage

Road Freight Transport
 Road Passenger Transport
 Rail Transport
 Water Transport
 Air and Space Transport
 Other Transport
 Services to Road Transport
 Services to Water Transport
 Services to Air Transport
 Other Services to Transport
 Storage

Communication Services

Postal and Courier Services
 Telecommunication Services

APPENDIX C:
AUSTRALIAN AND NEW ZEALAND STANDARD INDUSTRIAL
CLASSIFICATION (ANZSIC) CATEGORIES

1993 Edition

Finance and Insurance

Central Bank
 Deposit Taking Financiers
 Other Financiers
 Financial Asset Investors
 Life Insurance and Superannuation Funds
 Other Insurance
 Services to Finance and Investment
 Services to Insurance

Property and Business Services

Property Operators and Developers
 Real Estate Agents
 Non-Financial Asset Investors
 Machinery and Equipment Hiring and Leasing
 Scientific Research
 Technical Services
 Computer Services
 Legal and Accounting Services
 Marketing and Business Management Services
 Other Business Services

Government Administration and Defence

Government Administration
 Justice
 Foreign Government Representation
 Defence

Education

Pre-school Education
 School Education
 Post School Education
 Other Education

Health and Community Services

Hospitals and Nursing Homes
 Medical and Dental Services
 Other Health Services
 Veterinary Services
 Child Care Services
 Community Care Services

Cultural and Recreational Services

Film and Video Services
 Radio and Television Services
 Libraries
 Museums
 Parks and Gardens
 Arts
 Services to the Arts
 Sport
 Gambling Services
 Other recreation Services

Personal and Other Services

Personal and Household Goods -
 Hiring
 Other Personal services
 Religious Organisations
 Interest Groups
 Public Order and Safety Services
 Private Households Employing -
 Staff

**APPENDIX D: CODING SCHEME FOR CLASSIFYING AND TAGGING
SIGNIFICANT TOPICS/THEMES IDENTIFIED IN TRANSCRIPTS AND FIELD
NOTES AND EXAMPLE OF CODING SCHEME**

INDIVIDUAL CHARACTERISTICS

Business Experience with the PRC:

5 Years or less	BXF
6-10 Years	BXS
11-15 Years	BXE
16 Years or greater	BXSX

Nationality:

Australian	NAST
British	NBTS
Hong Kong Chinese	NHKC
Mainland Chinese	NMLC
Singaporean Chinese	NSGC
Malaysian Chinese	NMYC
Australian Chinese	NASC
Other	NOT

Chinese Languages Spoken:

Mandarin	CLM
Shanghainese	CLS
Cantonese	CLC
Other	CLO

Position Held:

Owner/Manager	PHOM
Executive	PHEX
Senior Management	PHSM
Middle Management	PHMM
Lower Management	PHLM
Other	PHOT

Time in current position:

5 Years or less	TPHF
6-10 Years	TPHS
11-15 Years	TPHE
16 Years or greater	TPHSX

INDIVIDUAL CHARACTERISTICS

Time with current employer:

5 Years or less	TCEF
6-10 Years	TCES
11-15 Years	TCEE
16 Years or greater	TCESX

BUSINESS CHARACTERISTICS

Market Entry Strategy:

Joint Venture	MEJV
Export	MEEX
Licensing Agreement	MELA
Franchise Agreement	MEFA
Strategic Alliance	MESA
Wholly Owned Operation	MEWOO
Contract Manufacturing	MECM
Management Contract	MEMC
Turnkey Operation	METO
Representative Office	MEREP
Acquisition	MEAC
Combination	MECB

Business Classification:

Primary	BCP
Secondary	BCS
Tertiary	BCT

Date of entry into the PRC (Range in decades):

1940-1950	DEFF
1951-1960	DEFS
1961-1970	DESS
1971-1980	DESE
1981-1990	DEEN
1991-2000	DENT

BUSINESS CHARACTERISTICS

Business size (Depicted by employee numbers):

Small	BZS
Medium	BZM
Large	BZL

Method of initial contact with the PRC:

Austrade	ICAUS
Australian State Government	ICAST
Chinese Government Department	ICCGD
<i>Guanxi</i>	ICGX
Chinese Agents	ICCA
Existing Customer	ICEC
Other	ICOT

GUANXI RELATED CODES

<i>Guanxi</i> defined	GDF
<i>Guanxi</i> a normal business practice	GNB
<i>Guanxi</i> a form of corruption	GFC
<i>Guanxi</i> is important for conducting business in the PRC	GIMP
Importance of <i>guanxi</i> is in decline	GIMPD
Importance of <i>guanxi</i> is not in decline	GIMPN
<i>Guanxi</i> overcomes problems	GOPR

Advantages of *guanxi*:

Access to scarce resources	GASR
Market information	GAMI
Reduced bureaucratic interference	GARBI
Tax concessions	GATC
Cheap material supplies	GACMS
Market access	BMKA
Other	GAOT

Disadvantages of *guanxi*:

Time Consuming	GDTC
Costly in monetary terms	GDCM
Ineffective	GDIE
Obligation	GDOB
Over reliance	GDOR
Other	GDOT

GUANXI RELATED CODES

Development of *guanxi*:

Banquets	GDVB
Gift giving	GDVGG
Regular contact	GDVRC
Other	GDVOT

Maintenance of *guanxi*:

Banquets	GMBQ
Gift giving	GMGG
Regular contact	GMRC
Other	GMTOT

PROBLEMS ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC

Human resource:

Productivity	HRPR
Staffing Policies	HRSP
Labour shortage	HRLS
Other	HROT

Legal:

Enforcement	LGEN
Interpretation	LGINT
Lack of legal culture	LGLLC
Changes	LGCH
Underdeveloped	LGUND
Lack of transparency	LGTRN
Other	LGOT

Financial:

Customer non-payment	FNCNP
Foreign exchange	FNX
Finance availability	FNAV
Other	FNOT

Bureaucratic

PRBC

Taxation

PRTX

Product quality

PRPQ

Distribution

PRDST

Theft

PRTFT

PROBLEMS ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC

Tariffs	PRTFS
Infrastructural	PRINF
Supply of materials	PRSUP
Corruption	PRCOR
Cultural:	
Cross cultural	PRCCL
Within (e.g. Among the Chinese)	PRCW
Competition	PRCOMP
Language	PRLAN
Partner	PRPTN
Other	PROT

EXAMPLE OF CODING SCHEME

Interview A0002

Q1. How long have you worked for this firm?

I have been with this company for thirteen years (TCEE)

Q2. What is your current role, and how long have you held that position?

I am the regional marketing director (PHEX), and I have been in the role for about 5 years (TPHF).

Q3. What is your length of business experience with the PRC?

About 5 years (BXF).

Q4. What market entry strategy did the firm use to enter the PRC, and when did the firm first conduct business with the PRC?

We went into China in 1987 (DEEN) when we formed a joint venture (MEJV) with xxxx which is a large Chinese company.

EXAMPLE OF CODING SCHEME

Q5. Is *guanxi* important for conducting business in the PRC?

All businesses. I am always careful to say that because I think it is exaggerated. I think we Westerners and Asians exaggerate the importance of it. Having said that the uniqueness of *guanxi* is a standard requirement of conducting business in China (GIMP).

Q6. Have you seen a decline in the importance of *guanxi* for conducting business in the PRC?

Unfortunately I am unable to answer that question.

Q7. How do you maintain your *guanxi*?

Well in most cases it is a standard common practice, as seen in many Asian countries where it is keeping in contact with the customer (GMRC), and making regular visits to the customer (GMOT). Also we go out to dinner which is no different to what we do in a Western society (GMBQ).

Q8. What problems have you encountered while conducting business in the PRC?

When we have not been paid (FNCNP) and we take our customer to court, the law is of very little support to us as a Western company. Often the law is on the side of the local instead of the outsider (LGEN).

Also, I think if you look at the environment in which you work where there is enormous demand for good people, which are taken up by other companies. There is enormous competition for well-trained staff with good experience. The problem most companies have in China and ours included is finding good people (HRLS). As a result of this competition for well educated, trained and experienced local Chinese, the cost of hiring them has increased (HROT).

APPENDIX E:
**THE BUSINESS AND INDIVIDUAL CHARACTERISTICS OF THE ADELAIDE,
 BEIJING AND SHANGHAI BASED RESEARCH PARTICIPANT**

Adelaide Based Research Participants Business Characteristics

Research Participants	Market Entry Strategy	Industry Classification	Market Entry Date	Business Size
A001	Acquisition	Secondary	1994	Large
A002	Joint Venture	Secondary	1987	Large
A003	Export	Primary	1994	Large
A004	Export	Tertiary	1994	Medium
A005	Acquisition	Secondary	1995	Medium
A006	Joint Venture	Secondary	1987	Large
A007	Export	Primary	1986	Large
A008	Export	Primary	1997	Medium
A009	Export	Primary	1987	Medium
A010	Export	Tertiary	1997	Large
A011	Export	Services	1995	Medium
A012	Export	Secondary	1985	Medium
A013	Export	Tertiary	1995	Small
A014	Joint Venture	Secondary	1987	Large
A015	Export	Tertiary	1992	Large
A016	Export	Tertiary	1989	Large
A017	Export	Tertiary	1994	Large
A018	Export	Secondary	1992	Large

* Chinese cities in the People's Republic of China (PRC).

APPENDIX E:

Adelaide Based Research Participants Individual Characteristics

Research Participant	Position Held	Business Experience with the PRC	Nationality
A001	Vice President	2 years	Australian
A002	Regional Marketing Director	5 years	Australian
A003	Senior Trading Manager	6 years	Australian
A004	Solicitor	5 years	Mainland Chinese
A005	General Manager South East and North Asia	7 years	Australian
A006	General Manager	15 years	Australian
A007	Export Officer	6 years	Australian
A008	Export Manager North Asia	8 years	Australian
A009	Export Manager	less than 1 year	Australian
A0010	General Manager	2 years	Australian
A0011	Operations Manager Asia Pacific	4 years	Australian
A0012	Export Manager	14 years	Australian
A0013	Owner-Manager	4 years	Hong Kong Chinese
A0014	Export Manager	3 years	British
A0015	Director	8 years	Australian
A0016	Operations Manager International	1 year	Australian
A0017	Director	6 years	Australian
A0018	Regional Sales Manager	5 years	Singaporean Chinese

APPENDIX E:
Beijing Based Research Participants Business Characteristics

Research Participants	Market Entry Strategy	Industry Classification	Market Entry Date	Business size
BJ1	Rep Office	Tertiary	1993	Small
BJ2	Rep Office	Tertiary	N/A	Small
BJ3	Rep Office	Tertiary	1998	Small
BJ4	Rep Office	Tertiary	1997	Large
BJ5	Joint Venture	Tertiary	1995	Small
BJ6	Rep Office	Tertiary	1986	Large
BJ7	Rep Office	Primary	1984	Large
BJ8	Rep Office	Primary	1973	Large
BJ9	Rep Office	Tertiary	1999	Small
BJ10	Rep Office	Tertiary	1992	Large
BJ11	Rep Office	Primary	1984	Large
BJ12	Rep Office	Primary	1986	Large
BJ13	Rep Office	Secondary	1985	Medium
BJ14	Rep Office	Tertiary	1973	Small
BJ15	Rep Office	Tertiary	1995	Large
BJ16	Rep Office	Tertiary	1994	Large
BJ17	Rep Office	Tertiary	1994	Large

APPENDIX E:

Beijing Based Research Participants Individual Characteristics

Research Participants	Position Held	Business Experience with the PRC	Nationality
BJ1	PRC Manager	7 years	Australian
BJ2	N/A*	13 years	Australian
BJ3	Owner Manager	7 Years	Australian
BJ4	Chief Representative	3 months	Australian
BJ5	Owner Manager	8 years	Australian
BJ6	General Manager PRC	6 months	Australian
BJ7	Manager PRC	20 years	Australian
BJ8	Chief Representative	10 years	Mainland Chinese
BJ9	Owner Manager	15 years	Australian
BJ10	Regional Manager Greater China	8 years	Australian
BJ11	Manager Business Investment Analysis	2.5 years	Australian
BJ12	General Manager PRC	10 years	Australian
BJ13	Chief Representative	10 years	Australian
BJ14	PRC Correspondent	8 months	Australian
BJ15	Assistant General Manager PRC	7 years	Hong Kong Chinese
BJ16	Chief Representative	6 years	Australian
BJ17	Chief Representative	6 years	Hong Kong Chinese

* BJ2's position held is not available due to confidentiality reasons.

APPENDIX E:Shanghai Based Research Participants Business Characteristics

Research Participant	Market Entry Strategy	Industry Classification	Market Entry Date	Business Size
SH1	Rep Office	Tertiary	1993-1994	Large
SH2	Joint Venture	Secondary	1993	Large
SH3	Rep Office	Tertiary	1993	Large
SH4	Joint Venture	Secondary	1994	Large
SH5	Joint Venture	Secondary	1987	Large
SH6	Rep Office	Secondary	1996	Large
SH7	Co-op Joint Venture	Primary	1991	Medium
SH8	Joint Venture	Secondary	1994	Large
SH9	Rep Office	Tertiary	1999	Large
SH10	Rep Office	Tertiary	1995	Medium
SH11	Joint Venture	Secondary	1992	Large
SH12	Rep Office	Tertiary	N/A	Small
SH13	Rep Office	Tertiary	1994	Medium
SH14	Joint Venture	Tertiary	1996	Large
SH15	Rep Office	Secondary	1998	Large
SH16	Equity Joint Venture	Secondary	1995	Medium

APPENDIX E:

Shanghai Based Research Participant's Individual Characteristics

Research Participant	Position Held	Business Experience with the PRC	Nationality
SH1	Chief Representative	5 years	Mainland Chinese
SH2	General Manager	15 years	Singaporean Chinese
SH3	President of PRC	3 years	Australian
SH4	General Manager	4 years	Mainland Chinese
SH5	Director for PRC	6 years	Malaysian Chinese
SH6	Chief Representative	9 years	Mainland Chinese
SH7	General Manager	14 years	Hong Kong Chinese
SH8	General Manager Asia	3 years	Australian
SH9	Customer Service Manager	1 year	Mainland Chinese
SH10	Chief Representative	5 years	Mainland Chinese
SH11	Operations Manager	3 years and 6 months	Australian
SH12	N/A	9 months	Australian
SH13	Managing Director	5 years	British
SH14	General Manager	4 years	Australian
SH15	Sales Representative	2 years	Mainland Chinese
SH16	General Manager North Asia	11 years	Australian

* SH12's position held is unavailable due to confidentiality reasons.

**APPENDIX F: CROSS TAB ANALYSIS OF LEGAL PROBLEMS
ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC**

Table 1F: Market Entry Strategy and Legal Problems

	Foreign Direct Investment (n=25)	Non-Foreign Direct Investment (n=58)	Total (n=83)
Legal Problems	14 (56%)	33 (57%)	47*
			*

* Totals do not equal 83 because of missing data (i.e. The other research participants did not experience legal problems)

Table 1F indicates that encountering legal problems may not be dependent on the market entry strategy employed to enter the PRC.

Table 2F: Industry Classification and Legal Problems

	Primary (n=16)	Secondary (n=22)	Tertiary (n=45)	Total (n=83)
Legal Problems	9 (56%)	13 (59%)	25 (55.5%)	47*
				*

* Totals do not equal 83 because of missing data (i.e. The other research participants did not experience legal problems).

It appears that encountering legal problems may not be dependent on a firm's business classification.

Table 3F: First Date of Entry Into the PRC and Legal Problems

	1971-1980 (n=6)	1981-1990 (n=22)	1991-2000 (n=51)	Total (n=79)^
Legal Problems	4 (67%)	16 (73%)	27 (53%)	47*
				*

^ Totals do not equal 83 because of missing data (i.e. No Australian business that entered the PRC during 1940-1970 experienced legal problems).

* Totals do not equal 83 because of missing data (i.e. The other research participants did not experience legal problems).

Table 3F shows that businesses, which entered the PRC during 1971-1990, are more likely to experience legal problems than those that entered the PRC during 1991-2000. This may be the result of continual improvements and changes to Chinese legislation since the opening to foreign investment in 1979. This is not to suggest that the Chinese legal environment is not characterised by uncertainty and unpredictability, as noted in this study, it is merely indicating that the PRC's legal environment has improved, albeit at a slow pace.

**APPENDIX F: CROSS TAB ANALYSIS OF LEGAL PROBLEMS
ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC**

Table 4F: Business Size and Legal Problems

	Small (n=18)	Medium (n=17)	Large (n=48)	Total (n=83)
Legal Problems	10 (55.5%)	9 (53%)	28 (58%)	47*

* Totals do not equal 83 because of missing data (i.e. The other research participants did not experience legal problems).

This table demonstrates that encountering legal problems may not be dependent on the size of the business.

**Table 5F: The Individual's Length of Personal Business Experience with the PRC
and Legal Problems**

	5 Years or Less (n=38)	6-10 Years (n=24)	11-15 Years (n=14)	16 Years or Greater (n=5)	Total (n=81)[^]
Legal Problems	21 (55%)	15 (62.5%)	8 (57%)	3 (60%)	47*

[^] Totals do not equal 83 because of missing data (i.e. Some research participants were unable to answer).

* Totals do not equal 81 because of missing data (i.e. The other research participants did not experience legal problems).

Table 5F indicates that encountering legal may not be dependent on an individual's length of business experience with the PRC. This result coupled with the above conclusions suggests that the Chinese legal system itself may be the cause of many legal problems encountered by Australian businesses.

APPENDIX G: CROSS TAB ANALYSIS OF HUMAN RESOURCE PROBLEMS ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC

Table 1G: Market Entry Strategy and Human Resource Problems

	Foreign Direct Investment (n=25)	Non-Foreign Direct Investment (n=58)	Total (n=83)
Human Resource Problems	9 (36%)	17 (29%)	26*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or may have not experienced human resource problems).

Table 1G indicates that encountering human resource problems may not be dependent on the firm's market entry strategy.

Table 2G: Industry Classification and Human Resource Problems

	Primary (n=16)	Secondary (n=22)	Tertiary (n=45)	Total (n=83)
Human Resource Problems	4 (25%)	8 (36%)	14 (31%)	26*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or may have not experienced human resource problems).

Experiencing human resource problems does not appear to be dependent on the classification of the Australian businesses.

Table 3G: First Date of Entry into the PRC and Human Resource Problems

	1971-1980 (n=6)	1981-1990 (n=22)	1991-2000 (n=51)	Total (n=79)^
Human Resource Problems	3 (50%)	7 (32%)	16 (31%)	26*

* Totals do not equal 83 because of missing data (i.e. No Australian business that entered the PRC during 1940-1970 encountered human resource problems).

^ Totals do not equal 83 because of missing data (i.e. Some research participants were unable to answer).

Human resource problems encountered by the Australian businesses in this study seem to be more prevalent among businesses that entered the PRC during 1971-1980 than 1981-2000. This is interesting as one may expect the businesses that entered the PRC during 1981-2000 may have experienced a greater proportion of human resource problems than those that entered during 1971-1980 because of an experience curve affect. One possible explanation may be that the individual in charge of the PRC operations may not be the most suited individual. Thus, increasing the likelihood of encountering human resource problems. Nevertheless, this is an area that needs further research.

Table 4G: Business Size and Human Resource Problems

	Small (n=18)	Medium (n=17)	Large (n=48)	Total (n=83)
Human Resource Problems	7 (39%)	5 (29%)	14 (29%)	26*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or may have not experienced human resource problems).

Table 4G shows that encountering human resource problems may not be dependent on the size of the Australian business.

Table 5G: The Individual's Length of Personal Business Experience with the PRC and Human Resource Problems

	5 Years or Less (n=38)	6-10 Years (n=24)	11-15 Years (n=14)	16 Years or above (n=5)	Total (n=81) [^]
Human Resource Problems	13 (34%)	6 (25%)	5 (36%)	2 (40%)	26*

* Totals do not equal 83 because of missing data (i.e. Some research participants may not have experienced human resource problems).

[^] Totals do not equal 83 because of missing data (i.e. Some research participants were unable to answer the question).

It appears that experiencing human resource problems may not be dependent on an individual's length of business experience with the PRC.

**APPENDIX H: CROSS TAB ANALYSIS OF FINANCIAL PROBLEMS
ENCOUNTERED WHILE CONDUCTING BUSINESS IN THE PRC**

Table 1H: Market Entry Strategy and Financial Problems

	Foreign Direct Investment (n=25)	Non-Foreign Direct Investment (n=58)	Total (n=83)
Financial Problems	7 (28%)	14 (24%)	21*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or did not experience financial problems).

Table 1H indicates that encountering financial problems may not be dependent on the market entry strategy of the Australian businesses.

Table 2H: Industry Classification and Financial Problems

	Primary (n=16)	Secondary (n=22)	Tertiary (n=45)	Total (n=83)
Financial Problems	2 (12.5%)	11 (50%)	8 (18%)	21*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or did not experience financial problems).

It appears that Australian businesses that are classified as primary businesses are less likely to experience financial problems. However, this result must be treated with caution because of the small proportion of research participants who experienced financial problems. In addition, the research participants who are employed by secondary businesses may be more inclined to acknowledge financial problems than those employed by primary or tertiary classified businesses. Thus, possibly distorting the financial problems experienced by secondary classified businesses.

Table 3H: First Date of Entry into the PRC and Financial Problems

	1971-1980 (n=6)	1981-1990 (n=22)	1991-2000 (n=51)	Total (n=79) [^]
Financial Problems	2 (33%)	5 (23%)	14 (27%)	21*

[^] Totals do not equal 83 because of missing data (i.e. No Australian business that entered the PRC during 1940-1970 experienced financial problems).

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or did not experience financial problems).

Table 3H shows that experiencing financial problems might not be dependent on the date of first entry into the PRC.

Table 4H: Business Size and Financial Problems

	Small (n=18)	Medium (n=17)	Large (n=48)	Total (n=83)
Financial Problems	1 (5.5%)	10 (59%)	10 (21%)	21*

* Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer or did not experience financial problems).

Table 4H indicates that medium sized businesses are more inclined to experience financial problems than large and small sized businesses. However, this finding needs to be treated with caution because of the small number of research participants who acknowledged that they encountered financial problems. In addition, the research participants from medium sized businesses may be more inclined to acknowledge financial problems than research participants from large or small sized businesses. Therefore, overstating the financial problems experienced by medium sized businesses.

Table 5H: The Individual's Length of Personal Business Experience with the PRC and Financial Problems

	5 Years or Less (n=38)	6-10 Years (n=24)	11-15 Years (n=14)	16 Years or above (n=5)	Total (n=81) [^]
Financial Problems	11 (29%)	6 (25%)	3 (21%)	1 (20%)	21*

[^] Totals do not equal 83 because of missing data (i.e. Some research participants chose not to answer).

* Totals do not equal 83 because of missing data (i.e. Some research participants did not experience financial problems).

It appears that experiencing financial problems might not be dependent on an individual's length of business experience with the PRC.

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