

The Effects of Guanxi on Doing Business in
China

By

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Attestation of Authorship

I hereby declare that this submission is my own work to the best of my knowledge and belief. It contains no material previously published or written by another person (except where explicitly defined in the citations and reference list), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

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Abstract

Guanxi is one of the major issues for doing business in China. This dissertation defines the concept of guanxi, analyses its characteristics and functions, and presents the similarities and distinctions between guanxi and Western relationship marketing principles. This paper argues that guanxi has a major and positive impact on business performance. Finally, the paper creates a model for developing and retaining guanxi as a guideline for foreign marketers looking to succeed in China.

1. Introduction

Since China opened the door to the outside world, marketing issues have been of increasing importance. The Chinese term *guanxi*, which means good relations, is regarded as the major issue for Chinese people doing business. Due to the relatively higher significance of *guanxi*, compared with the conditions and enforcement of contracts in the West, doing business in China is considered to be more complicated than in it is in the West. To do well in the Chinese market, foreign businessmen must understand how *guanxi* is constructed and determine a practical way of building and maintaining *guanxi* in the Chinese context. This dissertation finds that quality *guanxi* is built on face, reciprocity, empathy and trust. The development of *guanxi* is a process by which two individuals start a potential relationship as *outsiders*, with this relationship developing into an *insider* stage, to become old friends.

This dissertation defines the concept of *guanxi*, analyses its characteristics and functions, and presents the similarities and distinctions between *guanxi* and Western relationship marketing principles. This paper argues that *guanxi* has a major and positive impact on business performance. Finally, the paper creates a model for developing and retaining *guanxi* as a guideline for foreign marketers looking to succeed in China.

2. The Importance of Guanxi in Doing Business in China

Wu (1994) described guanxi as a willingness to gain mutual benefits. Guanxi includes trust, personal friendship and commitment. People in guanxi have affection for one another, do favours for one another, maintain the relationship and fully repay all favours received. Actually, guanxi is not exclusive to China, but is universal. So, why is guanxi used more widely and importantly in China than in other countries?

Bjorkman and Kock (1995) stated that China is an extremely bureaucratic country and that its process of administration is ill defined. Each body, from central government to local government, has overlapping decision making authority with one or more others. Often, in order to get things done, people are required to get many official licenses and approvals from various government bodies, and this process is often difficult and slow. Moreover, Arias (1998) suggested that commercial law has not been properly defined in China. This means that the enforcement of business exchanges cannot depend on the legal and judicial system. Often, those who enforce policies and contracts are involved in these business deals. Thus, increasing business and personal connections and developing guanxi networks are more important than simply relying on any legal contracts to bond parties to a business relationship. As a result, businessmen trust that, by creating a guanxi relationship, they can obtain many benefits such as; information regarding government policies; receipt of administrative approvals; the smooth running of routine business operations; and the procurement of necessary resources such as land, raw materials and import licenses (Lee and Ellis, 2000).

Recently, researchers have argued the significance of business relationships in China. Some researchers, such as Ambler (1994) and Yeung and Tung (1996) have described the different means and unique features of relationships in the Western World and in China. Others, such as Davies, Leung, Luk and Wong (1995) and Leung, Wong and Wong (1996) present the advantages and disadvantages of guanxi in China. On the other hand, few researchers have shown a full understanding and/or given a clear explanation of the concepts of guanxi in China. There is an unclear measurement of the quality of guanxi in

particular situations. Despite repeated emphasis of the standpoint that building guanxi is essential for managers to be effective in China few studies have offered a comprehensive model for developing and maintaining guanxi. This research paper discusses definitions, principles and guanxi in China's unique context, but also presents a distinctive view of four guanxi constructs (face, reciprocity, empathy and trust) in order to assist businessmen in fully understanding the interaction among Chinese businesspeople and the significance of guanxi, with the goal of offering a new process of guanxi development and a practical guideline for foreign marketers doing business in the Chinese environment. The key research question of the paper is how foreign marketers establish and maintain guanxi with their Chinese partners in China. In order to achieve this purpose, this paper examines guanxi by providing answers to the following five questions:

- (1) What is the difference between Western relationship marketing and Chinese guanxi?
- (2) What is the principle of guanxi?
- (3) What impact does guanxi have in the Chinese environment, including the Social, Legal, Political and Business contexts?
- (4) How do the guanxi constructs (Face, Reciprocity, Empathy and Trust) affect the quality of relationships?
- (5) What are the practical approaches which can be used by foreign marketers to establish and sustain guanxi with their Chinese partners?

Methodology – This paper utilises a literature review to analyse and evaluate the currently available research in order to synthesize a conceptual framework for guanxi; to provide recommendations for Western managers; and to test the hypotheses raised in the paper.

3. The differences between Western Relationship Marketing and Chinese Guanxi

Hofstede (1992) contends that management techniques may not be carried out worldwide without modification, because values defined in various cultures have different impacts on their effectiveness. Boyacigiller and Adler (1991) argued that management practices in the Western World may not be particularly appropriate for China, due to the cultural differences. Yue (1993) stated that Western views should match Chinese circumstances before their correctness and rationality will be possible. Thus, it can be concluded that it is necessary to identify the differences between Western relationship marketing and Chinese guanxi.

Yau, Lee, Chow, Sin and Tse (2000) indicated that, in a Western context, a marketing person tends to start a business with his/her contacts, agents, or network of channels, then evaluates the company's advantages and disadvantages, finally focusing on the relationships at a later stage. In contrast, Chinese businesspeople begin by evaluating their relationships and emphasizing how to integrate those relationships into their business plans. Goals and shared values do not seem to be the basic criteria for beginning a business. The Chinese think that people are willing to make a good relationship first, and once guanxi is successfully built, exchanges will start. People in the West, however, prefer to make exchanges first. If they are satisfied with the outcomes, they will then form a relationship. Similarly, Ganesan (1994) stated that Westerners might primarily consider buyer-seller relationships as short term transactions in which one aims to gain profit from others' expenditure. Later in the business transactions, Westerners may think it is profitable to develop trust and commitment, in order to form a relationship. In contrast, Chinese usually highlight cooperation, alteration and good relations prior to business transactions. Moreover, Luo (1997), Fock and Woo (1998) and Leung and Wong (2001) express the idea that relationship marketing operates within groups or organisations, but guanxi is a personal relationship among individuals, rather than an inter-group or inter-organisation relationship. Guanxi may play a role at the

organisational level, but only once the personal relationship is utilised by the organisation. If the key guanxi persons resign from the companies, guanxi between the two companies will disappear, but the philosophy of relationship marketing will still remain.

In conclusion, the emphasis on relationships as a key factor for doing business is a cultural characteristic of China (Hamzah-Sendut, Madsen and Thong, 1990), and it differentiates business practices carried out in China from those in Europe or North America (Wu, 1994). These differences must be taken into account in business relationships.

4. Principles of Guanxi

This section presents a comprehensive explanation of the principles of guanxi. It consists of three sub-sections: Defining guanxi; categorising the basis of guanxi; and clarifying guanxi features.

4.1 Definition of Guanxi

Guanxi in Chinese language is related to the conception of creating personal relationships intended to protect personal interests. Literally, the word *guanxi* contains two Chinese characters; *guan* and *xi*. Tim (1995) explained that the original meaning of *guan* was a *gate*, with its extended meaning being *to close up*. If you are inside the door, then you may be in the group; but if you are outside of the door, your existence will not be recognised by those in the group. Today *guan* joined with other Chinese words often means *to do someone a favour*. For example, *guan zhao* implies *to take care of*; *guan xin* implies *to show consideration for*; and *guan huai* implies *to show tender care for*. *Xi* indicates hierarchy and formalisation. It implies binding together and expanding relationships such as those with family members and other kin. *Xi* can also refer to retaining long-term relationships; for example, *wei xi* implies *to keep*.

Guanxi is developed imaginatively and energetically in China. Guanxi is a complicated and persistent relationship; including promise, perception, shared obligations, and directing attitudes and behaviours towards nurturing relationships (Luo, 1997). In the English language, there is no single word with equivalent meaning to *guanxi*, and there is not a consensual definition of the term *guanxi*. Bian (1994) stated that *guanxi* can be translated to one of three meanings: (a) People have an existing relationship because they are all related to a same person, or they have the same status within the group; (b) there are real links and regular communications between two individuals; or (c) individuals interact indirectly. Tsui and Farh (1997) explained that *guanxi* simply means relationships, or connections. The term *guanxi* means that familiar people play an infinitely repeated game with each other within the group (Davies, 1995). King (1991)

suggested that guanxi is a kind of interpersonal network which is built mainly on particular ties, or criteria. Similarly, Luo (1997) stated that guanxi refers to the interpersonal relationship which bonds people together through the exchange of reciprocal favours and mutual obligations. Others (Tsang, 1998; Bell, 2000) consider guanxi as being more than a pure interpersonal relationship, but also as a mechanism that can be used by people to obtain political or economic benefits, as well as to achieve personal, family, or business goals.

By reviewing the existing literature, this dissertation offers a comprehensive definition: *Quanxi is a personal relationship, cultivated by individuals through continued exchange of favours, in order to gain personal needs and wants and establish reciprocity within networks, as well as creating obligations within the relationships.*

4.2 Guanxi Base

The existence of a guanxi base determines whether guanxi exists between two people. According to Jacobs (1979, cited in Tsui and Farh, 1997), as long as two or more people have a similar shared identity, origin and characteristics, a base for guanxi can be found. People with such a base share a portion of their personal identification, which is significant to them as individuals. The identification can be through kinship, place of birth/dialect, educational institutions, workplaces, social clubs, sworn brotherhoods, friendship, and so on (Tong and Yong, 1998). For instance, two people with a workmate guanxi share recognition of a working experience important to both of them.

King (1991) divided all major guanxi bases into two categories: Predetermined bases; and voluntary bases. Predetermined bases, including locality and kinship, represent inherited guanxi (such as son-father and brother-sister) which are prearranged for the person, and his/her status and obligations are fixed according to the relationship. Voluntary bases are achieved through individuals' either activated, or voluntarily created, activities. Chen and Chen (2004) stated that voluntary bases consist of three kinds of guanxi bases: Common social identities, such as workplaces; a common third party, who

has a mutual friendship with both parties, and can vouch for either party; and anticipatory bases, which are created by exchanging partners through making an agreement, or showing intentions for joint ventures, future transactions and/or cooperation. Chen and Chen (2004) further state that the three forms of voluntary bases differ, but are not unrelated. Two persons who have an anticipatory basis realize the common identities they share through their connections. People who have common identities may also find they both have guanxi with an intermediary (Chen and Chen, 2004).

Similarly, Tsang (1998) stated that guanxi bases have two types: blood bases and social bases. Blood bases refer to kinships, such as members of the same tribe, relatives and family members. Blood bases are predetermined for members and cannot be changed. Members with blood bases are relatively tight. Since the family is the basic element of Chinese society, family guanxi is the most significant type of guanxi. On the basis of an empirical study of the recent cultural changes in China, Tsang (1998) found that relationships between family members are stronger than those between friends or other individuals. People like to rely on family members and also trust them more than they do other individuals. Social bases consist of other guanxi bases, which occur mostly as the result of social interactions at the place of work, study, or entertainment.

Different Guanxi bases define different types of guanxi relationships. Hwang (1987, cited in Lee and Ellis, 2000) stated that expressive ties, instrumental ties and mixed ties are three basic types of guanxi relationships. Expressive ties are very personal and effective. Family members and relatives are primarily involved. Such ties are permanent and involve stable relationships. In contrast, instrumental ties are impersonal and utilitarian. This kind of tie is formed temporarily, and is also performed frequently in order to achieve material goals. Instrumental ties are considered as more distant types of guanxi bases, such as the relationship between salesmen and customers. Mixed ties are relatively stable relationships compared with instrumental ties. People linked by this kind of tie; such as classmates, neighbours and colleagues; have overlapping social networks, with their behaviour bound by the obligation to take into account the reciprocity of favours and face saving when making requests (Lee and Ellis, 2000).

Consistent with Hwang's (1987) view, Yang (1994) classified guanxi into three groups according to their bases: (1) Relationships among family members, which is similar to expressive ties; (2) relationships with familiar people (e.g. friends, classmates and neighbours), which refers to mixed ties; and (3) relationships with mere acquaintances, or strangers (with, or without, common demographic attributes), which equates to instrumental ties. Yang (1994) claimed that these three groups of relationships are managed by interrelated rules, and that those involved have entirely different psychological and social senses. Fan (2002) also divided guanxi into three similar forms: Family guanxi; helper guanxi, which refers to mixed ties; and business guanxi, which means that people utilise their personal relationships for business purposes. People have little trust and commitment towards this type of relationship; they are concerned about their own business interests and how to take advantage of the other party.

In summary, guanxi begins with guanxi bases. The key elements for building guanxi bases are kinship, friendship and other personal relationships. Guanxi bases can be discovered and generated through inherited identifications, such as kinship and locality; and cultivated identifications, from the work place, friendships, etc. Guanxi bases classify guanxi with three groups: Family members with expressive ties; familiar people with mixed ties; and strangers with instrumental ties. Leaving out the consideration of the family business, business relationships are made between strangers, or familiar people. The boundaries between strangers and familiar people are convertible (Hwang, 1987). Strangers can become familiar people and vice versa. This dissertation focuses on how a foreigner (as a stranger) can build guanxi with Chinese partners and transform the relationship from one of instrumental ties to one of mixed ties.

4.3 *Guanxi features*

4.3.1 Guanxi is transferable

Guanxi can be transferred from one person to another through a third party. For instance, if Mr. A is a friend of Mr. B, and Mr. B has a good relationship with Mr. C, Mr. C can be recommended, or introduced, to Mr. A by Mr. B to easily form a new guanxi between them. Without Mr. B, contact between A and C would be difficult, or even impossible. The success of the transfer of guanxi depends on how important Mr. B considers his relationships with Mr. A and Mr. C to be.

4.3.2 Guanxi is intangible

Guanxi is built on people exchanging unlimited favours and making unspoken commitments to maintain long-term and stable relationships. Anderson and Weitz (1992) stated that an unspoken commitment plays a major role in guanxi relationships. Two persons in a good relationship need to make commitments to each other by following unseen and intangible rules of reciprocity and fairness. Failing to regard this commitment may seriously damage the party's social reputation and result in a loss of prestige.

Guanxi fundamentally stresses utility over other values. Guanxi ties two parties together through the exchange of favours rather than through emotion. If the guanxi can no longer bring profit to the parties, their relationship is easily broken.

4.3.3 Guanxi is virtually personal

Relationships are personal, and guanxi works basically on the personal level. Guanxi between organisations is primarily made and maintained based on a personal relationship. Yau et al. (2000) pointed out that, in Chinese cultures, a personal relationship resulting in business is more attractive than business resulting in a personal relationship. Chinese tend to complete a deal if a previously existing personal relationship is involved. Trust and friendship can help in overcoming conflicts within the decision making process. As long

as the guanxi lasts, nothing cannot be negotiated, compromised and, eventually, solved. In China, the application of guanxi is pervasive and intensive. Joseph Denaro, general manager of Shanghai Xerox, described his company's distribution system in China as excellent. He stated that, "We are the top seller in China because of our distributors. The network is constructed by our friendships that have been formed for many years" (Batson, 1994, p. 95).

In summary, guanxi is the social interactions within a particular network where members have perceived similarities as bases and each member makes infinitely repeated exchanges of favours equally with each other member.

5. An overview of guanxi in various Chinese contexts

This section discusses the significant impact of guanxi in four of China's contexts: Social; legal; political; and business. It explains why people who are doing business in China should pay more attention to guanxi.

5.1 Guanxi in the Social context

Guanxi is not a new concept in twenty-first-century China. It is a network of personal relationships emerging from the fundamentals of Chinese culture, traditions and social organisation (Parnell, 2005). During the sixth century BC, one of ancient China's most famous philosophers, Confucius, created the social norms by which people should practice guanxi. Confucius philosophy still directs guanxi based exchanges in China today (Standifird and Marshall, 2000). In order to understand why guanxi is important, and how it operates in Chinese societies, one must understand the Confucius philosophy and the moral code it defines.

Confucius believes that the social norms should be based on *li*, *ren* and *xiao* (Hackley and Dong, 2001). These three key principles provide the framework for the development of Chinese society.

The Confucian concept of *li* is described as a set of formal prescriptions, which defines the boundaries in which to search for personal needs and interests, with the intention of maintaining a stable social order and harmony (Cua, 1989, p. 215). *Li* indicates that individual relationships exist in all hierarchical orders and statutes, and that the individual must follow a proper way and a proper ritual for conducting and sustaining relationships in social interaction. Confucius defined five main relationships, named *wu lun*, in the society: Lord-civilian; husband-wife; father-son; elder brother-younger brother; and friend-friend (Chen and Chen, 2004). Each party in the social structure relationship circle has a unique position. Some are in higher positions, while others are in relatively lower positions. For instance, a lord can make an order to a civilian, and a son always has to obey his father. In addition, *li* also stresses social obligations and rights. An individual

has an unequal set of obligations and rights according to his/her social position. For example, a lord always has more power than a civilian; a husband has more benefits than a wife, etc. Li provides *guanxi* with favourable structures and allows social resources to take root. After an individual is born, he/she will be integrated into a natural *guanxi* network in his/her socialisation process, because humans are essentially relationship-oriented (Tung and Worm, 2001). With this principle, Chinese always consider themselves in a position of mutual dependence with the society, and the individual's experience is related to the experiences of others.

Tsui and Farh (1997) point out that the Chinese view of an interdependent self is just the opposite of the Western view of an independent self. The latter holds that every single person is self-contained and autonomous. People are independent of each other, and human behaviour is influenced by internal attributes such as values, motives, character and capacities, rather than outside relationships (Markus and Kitayama, 1991). This opposite view of a person is one of the most primary differences between China and the West in social relationships.

The Confucian concept of *ren*, which refers to gentleness, love and kindness, indicates that individuals should always be nice to each other, and be willing to treat each other in a friendly manner. The concept of *xiao*, which refers to loyalty and obedience, means that people at the lower level of the hierarchy must obey and respect those who at the higher level of the hierarchy. For example, a citizen must be loyal to his/her lord, and a wife has to respect her husband.

Ren and *xiao* foster people's positive attitudes towards each other, and create harmony for *guanxi* to develop (Hackley and Dong, 2001). Harmony is an important characteristic to promote and pursue in Chinese society (Buttery and Wong, 1999), and to achieve harmony is the central goal of Confucianism (Carlisle and Flynn, 2005). Therefore, Chinese people always emphasize harmony and try to retain harmony in interpersonal relationships, even though sometimes they may need to sacrifice some of their own benefits (Huang, 2004). Harmony will be achieved once one receives something which is

expected from others in order to protect one another's face. Face is a key element of guanxi, and it is an intangible form of social resources and personal status. People without a certain amount of prestige cannot establish a guanxi network (Luo, 1997). Another concept related to guanxi is renqing. One who wants to be ren to others is not only willing to help others, but also needs to return other's favours genuinely, because people within a guanxi relationship have to commit to each other with an unspoken code of reciprocity (Luo, 1997). Renqing (meaning human obligation) provides leverage in interpersonal exchange of favours (Yang, 1994). To achieve harmony, responsibilities are enforced. Individuals believe that they have the obligation to maintain human relationships. Renqing forces each individual to fulfill the obligation. When one disregards renqing, he/she loses face, hurts exchange partners, and eventually damages the guanxi network.

5.2 *Guanxi in the legal context*

China's legal system is not well developed. "Problems of federalism, administration and corruption plague the nascent legal system and enforcement of judgments or even national statutes remain chancy" (Dunfee and Warren, 2001, p. 193). Every year, China adopts many rules and regulations, but seldom enforces them properly and/or consistently. People who are in positions of power or authority interpret these rules, regulations and policies freely, and often impose harsher justice than do the courts.

While reforming its economy, the Chinese government admits that the legal system needs to be redesigned and is carrying out a gradual transformation of the legal system. This is, however, a long term project that cannot be carried out overnight. In 1994, Rongji Zhu, China's Vice Premier, estimated that China needed at least 300,000 lawyers to make the legal system effective, compared with there only being about 100,000 actual licensed legal professionals in China at that time. During this transitional period, Chinese people rely on personal connections to resolve disagreements. They assume that disputes can be solved more effectively and efficiently through guanxi, rather than through the legal system.

The Chinese legal system provides little protection in business transactions. The commercial laws in China are often indefinite, changeable and inconsistently enforced. The legal contract carries no sense of commitment. Business people who have formed good relationships with key persons in government departments can break contractual commitments without any punishment or payback. People have to rely on *guanxi* to provide the required assurances that another party will fulfill its obligations. Thus, *guanxi* offers people a much more effective way to produce trust than does any formal legal contract (Lovett, Simmons and Kali, 1999), and it plays a substitute role for commercial law in China (Ambler, 1994).

Guanxi can also provide businessmen with a legal advantage in order to gain favourable treatment. Pearce and Robinson (2000) report an example: McDonald's lost its legal battle with Ka Shing Li, one of Hong Kong's billionaires. A property in central Beijing was first offered to McDonald's by the Beijing government with a signed contract. Later, Ka Shing Li took a fancy to the property and wanted to use it for his real estate development. Li had well-built *guanxi* with high position officers in China's central government. Through these relationships, he eventually gained the property. McDonald's was forced to find another location for its business in Beijing.

Thus, it is important for foreigners to realise the differences in commercial laws and practices between China and the Western World, and understand how important *guanxi* is in the Chinese legal context.

5.3 Guanxi in the Political Context

The political system in China is based on the principle of public ownership. Government institutions and departments connect with every aspect of business activity. China has been transforming its economy since the 1980s. One of the important aspects of this reform is regional decentralisation, which has given local government greater autonomy in decision making (Blejer and Szapary, 1990). The central government now delegates three functions to local government: Fiscal responsibility and taxation authority;

investment and financing authority; and the authority to manage enterprises (Li, Qiu and Sun, 2002). As a result, local governments take control over forming businesses, distributing resources and approving bank loans. Nonetheless, a few powerful people are still in charge of key economic and financial resources. They distribute resources based on their own preferences. Moreover, Pearce and Robinson (2000) pointed out that obtaining approvals, or licenses, takes a long time because few deadlines for making decisions are enforced and many overlapped government bodies are involved.

In such circumstances, it is essential for people to develop a close business relationship with government officials prior to doing any business. With such *government guanxi*, a company can gain competitive advantages over its rival when seeking licenses and approvals, and can obtain information on market trends, business opportunities and government policies. Government *guanxi* becomes a company's competitive advantage over companies who do not have this connection, and also allows unfair competitive practices by those companies.

The downside of *guanxi* is related to corruption. Fan (2002) suggested that, in China, this special Government *guanxi* refers to an exchange, or deal, involving money and power. Since the economic reforms, corruption has been rife in China. In 2000, a total of 45,000 corruption cases were investigated; which was 15% more than in 1999 (Fan, 2002). Corruption has become a cancer in Chinese society. It has penetrated all levels of government and has a negative impact on carrying out any form of business. Maintaining *guanxi* with the government is very expensive. Huge bribes to government officials continually increase company's total costs and may even increase its debts. The Hong Kong Independent Commission Against Corruption estimates that *guanxi* made through outright bribes, gifts, or payments was up to 5% of companies' total expenses (approximately US\$5 billion) in foreign investments in China (Su and Littlefield, 2001). *Guanxi* is risky as well. In China, there is a saying that, *Water can carry a boat, and also water can overwhelm the boat*. If a company relies heavily on *guanxi* to run its business, it can get what it wants. On the other hand, once this *guanxi* disappears for any reason; such as the government official losing his political power, or even being arrested for his

corrupt behaviour; the firm will find its business threatened because it can no longer easily acquire rare resources and obtain protection and permits. For example, in 1995, Xitong Chen, the former mayor of Beijing city was convicted of corruption charges. As a result, any firms associated with him lost their investments (Tsang, 1998). Recently, the Chinese government has launched several anticorruption campaigns in order to crack down on corruption, but bigger cases are still emerging. Guanxi-related corruption will continue to exist in Chinese society, and it will continue to affect people doing business in China for a long time.

5.4 Guanxi in the Business Context

In the Chinese business context, Davies (1995) points out three significant functions for guanxi: (1) Individuals are able to form social bases (such as salespeople and customers) with mutual obligations regardless of whether they have blood bases or not; (2) Guanxi compensates for inefficient systems and weak institutions. It offers motivation and behavioural norms for relationships; and (3) Guanxi is a tool used for private gain in communist systems. Luo and Chen (1997) have carried out an empirical survey regarding local and foreign investment enterprises in China, and concluded that guanxi is like a lubricant, used in order to help firms operate more efficiently and effectively in China. State-owned companies, which face planned and fixed limitations on products, prices, promotions, wages and capital expenditures, will try to find unofficial levels of these constraints possible through guanxi-based personalised exchanges (Child, 1990). At the same time; in comparison to state-owned companies; collectively and privately owned companies have less ability to acquire scarce raw materials and other resources controlled by government, and are also less likely to obtain governmental support and assistance. In this circumstance, good guanxi has been proven to be a substitute for governmental support, to help those firms to survive (Xin and Pearce, 1996).

Other researchers, such as Leung, Wong and Tam (1995) and Davies et al. (1995) name three main benefits of guanxi in the Chinese business system: 1. It assists in reducing, or avoiding, uncertainty; 2. It assists in getting information on government policy, business

opportunities and market trends; and 3. It saves time and provides required operating resources, thus improving efficiency.

China's economic reform needs these guanxi-based business connections. The Chinese economic transformation is characterised by underdeveloped market structures, unspecified property rights and unstable institutional policies, which make market exchanges uncertain and expensive (Nee, 1992). Inevitably, this reform has caused a quick rise in opportunistic behaviour and has increased transaction costs. In such a context, companies will try to *internalise* transactions to avoid turbulence. The main logic of relying on personalised exchanges is that it guides companies to choose a guanxi-based strategy of development, creating relationships to assist business transactions. A study conducted by Standifird and Marshall indicated that: Guanxi has significant potential and great ability to reduce transaction costs related to an uncertain environment, such as communicating, negotiating and coordinating transactions, as well as maladaptation and/or failure to adapt. Guanxi-based exchange also offers transaction cost advantages by guaranteeing that exchange partners will not act opportunistically.

Undeveloped information markets in uncertain environments also require the emergence of guanxi. In the Western World, people can gain information easily through public published media, such as newspaper, magazines and phone books, or through radio and television. Information in China, however, is often released through government controlled media channels, and the process is very people-intensive. Therefore, people have to build guanxi with those key information holders. Once the guanxi network is built, information gained from reliable sources is more useful, richer and more trustworthy. Thus, guanxi-connected members are able to make more informal decisions with lower search costs (Luo, 1997).

A guanxi-connected business network aids a company in overcoming its shortage of resources to support its growth, while reducing substantial bureaucratic costs through internalising its processes. Peng and Luo (2000) stated that boundary spanning can improve firm performance. In such an environment, boundaries between firms are not

clearly demarcated. A firm undertakes broad networking activities based on guanxi and often makes verbal agreements resulting from exchanging favours and building trust. By making these efforts, companies can form multiple network connections in order to organise their activities, collect resources together and chase joint growth (Peng and Heath, 1996).

In summary, Wong (1998) suggested a *4 S* approach in understanding the importance of guanxi in Chinese contexts. Owing to the poor institutional legal systems in China, plus the unstable political systems of the existing PRC government, most Chinese tend to have a feeling of scarcity of individual personal economic resources. They tend to accumulate more social capital - guanxi – in order to create a psychologically safe environment. On the other hand, the psychologically insecure environment pushes them to gain network synergism. Wong (1998) mentions that guanxi in the Chinese context lies in the skillful mobilisation of some Chinese moral and cultural imperatives, which construct guanxi and play important roles in doing business in China.

The next section illustrates the dimensionality of guanxi constructs and how each factor works.

6. The Dimensions of Guanxi Constructs

In the interpersonal relationship context, Hwang's (1987) resource allocation model expressed the theory that guanxi consists of several concepts: Emotional feelings of attachment; the receipt of reciprocal favours; and the giving of *face*. Kipnis (1997), Lovett, Simmons and Kali (1999) and Park and Luo (2001) all agreed with Hwang's (1987) view, and also proposed that affection, reciprocity of favours and the preserving of face are the necessary components of guanxi. Further, Parnell (2005) expressed the idea that trust is the creation and consolidation of the triangularity of face, reciprocal favours and affection. This makes the informal unofficial phenomenon of guanxi tangible and lasting. Indeed, Lee and Dawes (2005) suggested that trust is the outcome of guanxi, however, the majority of the guanxi literature (e.g. Redding and Ng, 1982; Tong and Kee, 1998; Wong, 1998) stated that trust is an important component of guanxi. Tsang (1998) identifies ganqing (empathy), trust and credibility and face as three important ingredients of guanxi. Yau et al. (2000) compared Chinese guanxi with Western relationship marketing. They concluded that trust, reciprocity, empathy and bonding are required for building holistic relationships in China, but that shared values and goals, which were identified by Abramson and Ai (1997) as one of the key aspects of relationship marketing, are not necessary conditions in building these types of relationships. Hutchings and Murray (2003) and Parnell (2005) also stated that the Chinese social values which determine the effectiveness of guanxi are face, reciprocity based on renqing, empathy (ganqing) and trust. Thus, by putting these ideas together to present a broad perspective of the dimension of guanxi, this dissertation proposes that a true, healthy and lasting guanxi consists of four elements: Face; reciprocity; empathy; and trust. Each factor of guanxi has a significant impact on people doing business in China.

6.1 Face

The word *face* is an intangible commodity which is very important to a person's reputation, dignity and prestige, and is affected by one's social position and material wealth (Park and Luo, 2001). Face also refers to an individual's positive image in his, or her, social environment. Face is obtained by performing some well-recognised social

roles (Tsang, 1998), or through success and ostentation during a particular contact (Lee and Dawes, 2005).

The Chinese concept of face is called *mianzi* in Chinese language, which is defined slightly differently than what Westerners understand as the twin concepts of losing, and saving, face. It includes what you think of yourself, how you work with others, what others think of you and what kinds, and levels, of relationship you have. Giving and accepting *mianzi* is to respect one, and recognise one's moral reputation and social status (Buttery and Wong, 1999) and enhance one's esteem through compliments, flattery, or a show of respect (Seligman, 1999). When you *put gold* on someone's face, it enhances one's status and reputation. When you *throw dirt in their face*, these aspects are negatively affected. A person loses face when his/her actions fail to meet those requirements determined by his/her social position (Ho, 1976, cited in Lee and Dawes, 2005). On the other hand, causing others to lose face is considered an aggressive and violent act (Tung and Yeung, 1996). *Losing face* socially is similar to physical damage to one's eyes, nose, or mouth; it brings shame to the individual and even to his/her family, or to the whole group.

Face is vital for Chinese, not only in their personal lives, but also in their business lives. For example, Redding and Ng (1982, cited in Lee and Dawes, 2005) discovered that businesspeople in Hong Kong see face as always being essential to deliberations in their professional exchanges, and that Chinese people often prefer to use informal systems of contracts and agreements due to the fear of losing face. They further discovered that face has important power in business negotiations. During a business negotiation, it is highly desirable to give face to someone, and it is highly undesirable to challenge, or jeopardize, the other's face.

The thought of having a reputation of not losing face and, at the same time, saving the other's face, is an important element in *guanxi*. Face becomes the leverage for people to operate and enlarge a *guanxi* connection. Without having a certain amount of face, one cannot build up *guanxi* networks. On the other hand, *guanxi* networks partly determine

how much face one has (Standifird and Marshall, 2000). One has strong face if his/her guanxi network is large and there are more powerful people connected with it. Preserving face in Chinese society encourages people to carry out appropriate social roles, meet essential requirements, be part of the same associated group and allow all members to look good in the group. As a result, harmony within the group is improved and conflicts within the group are minimised.

6.2 *Reciprocity*

In the Western context, the concept of reciprocity has been heavily influenced by Gouldner (Westwood, Chan and Linstead, 2004). Gouldner (1960, cited in Chen and Chen, 2004) stated that the very basic meaning of reciprocity is that people should help, rather than harm, those who have helped them, and makes reciprocation occur directly and immediately. Lebra (1976, cited in Yau et al, 2000) agreed that people receiving favours from others need to return similar favours immediately during social exchanges. He further pointed out that, normally, the one doing a favour for another may intend to gain a specific need from the recipient. Even though reciprocity is a universal social phenomenon, it is subject to different cultural manifestation in social exchanges and social relationships (Smith, 1998), and is highly influenced by the cultural social norms of the society (Chen and Chen, 2004).

In China, reciprocity is deeply rooted in Chinese social relationships and has remarkable influence in social institutions. It is an integral part of li and is the moral tenet governing peoples' behaviour in all relationships and situations (Westwood et al., 2004). The concept of li requires mutual interdependence in all relationships. This is the case even in imbalanced relationships, where higher power holders have not only rights, but also obligations. If people do not reciprocate the mutual obligations inherent in the position, the balance of harmony is damaged.

Reciprocity in Chinese is named *bao*. The basic meaning of *bao* is to response and to return favours. Reciprocal favours in Chinese is called *renqing*. *Renqing* provides strong rules binding Chinese social life. A person who does not return favours will be

considered to be a mean person without credibility, and he/she will lose face, reputation and eventually lose personal relationships. The rule of renqing requires all group members in the relationship network to give favours and to help people in need, with the favours being returned as soon as the opportunities arise. Renqing is a social mechanism which is used by people to gain desirable resources within a stable social environment, rather than only as a normative standard for adjusting social exchanges (Hwang, 1987, cited in Ordonez and Pablos, 2005). Wong and Tam (2000) pointed out that, in Chinese culture, the word *Renqing* has three implications: (1) It is a person's emotional reaction to various situations, or life events; (2) it can be a gift presented by one person to another during social interactions; and (3) it is the social norms which encourage a person to get along well with others. Renqing, with its rules and implications, assists each member to survive within the group.

In order to build a positive cycle of favour exchanges, reciprocity based on renqing has some special features in China.

First, renqing in China has a long-term orientation; i.e., no return should be made immediately. Chinese people think that quickly repaying a favour will have a negative effect on an ongoing relationship; one might not accept any future demand, because he/she no longer owes a debt of gratitude. Thus, keeping people indebted is a way to maintain the relationship. Extending the repayment period, or delaying the return, indicates a willingness to continue guanxi. Although debts should not be repaid quickly, great efforts for remembering the debt have to be made and these exchanges must be equal in the long-term.

Second, renqing in China is an unbalanced exchange. Chinese people do not highlight the equality of reciprocity. In the process of exchanging favours, the value of the gift is never fixed and will keep increasing. If two parties intend to contribute more toward guanxi, the value of what is reciprocated to the receiver must be greater than what was received. This also requires a good understanding of the other party's expectations, and a concern for the other's desires. Such generous return aids in maintaining guanxi. On the other hand,

any favours returned are aimed at relieving oneself, without considering that the value to the receiver would harm the guanxi relationship. Some popular Chinese sayings can illustrate this unspoken rule: *One person honour another person a linear foot, another person must honour him ten feet in return; and you should repay like a gushing spring, if you have received a droplet of generosity.* It means that people should return favours with higher value, than those they received. Another implication is that, in order to maintain guanxi, people should put others into debt by increasing the value of the favours.

Third, renqing in China is relationship-orientated, rather than task-orientated. Chinese people do not intend to gain any specific benefits from others when they present gifts, or offer favours. Instead, they may intend to develop a good relationship in the future.

In conclusion, renqing provides leverage for those who exchange favours with others, and is a prerequisite for developing guanxi in China. Reciprocity based on renqing, is a complex mixture of mutual obligations, favours, emotions, and mutual support and protection, all of which together are the real dynamic behind the practice of guanxi in China (Parnell, 2005).

6.3 Empathy

The concept of empathy is universal because it refers to human feelings. It is related to enduring and affective commitments made by group members (Lee and Dawes, 2005). In order to create an exclusive relationship, two members have to develop a personal relationship with each other and develop empathy towards each other. This can include showing personal concern for each other, sharing personal feelings and understanding the other person's needs and wants. In the business context, empathy has several applications: Identifying the business partner's strengths and weaknesses; understanding the business partner's desires and position; and appreciating the business partner's efforts made in terms of the business relationship (Yau et al., 2000).

Empathy is important in building relationships in China, due to the special interpersonal behaviour of Chinese society. Chinese culture promotes great self-restraint and frowns

upon self-disclosure. Chinese people do not engage in verbal expression of their preferences, but wait for others to understand their desires. They try to avoid making any judgments regarding others, but they are restrained and reserved in their interactions, because they tend to try to not offend, or be rejected by, others (Chen, 1995). Such behaviour requires empathy among people. Yum (1988) named this kind of behaviour, *receiver-centred*, or *anticipatory*, communication. This is in contrast to the *sender-centred*, or *self-disclosure*, communication style highlighted in the West.

In Chinese language, empathy is called *ganqing*. *Ganqing* is related to the level of emotional understanding and bonding. People involved in *ganqing* share their feelings of happiness and their fears. Moreover, *ganqing* is related to loyalty, unity and willingness to sacrifice oneself to take care of others (Chen and Chen, 2004). Tsang (1998) suggested that, a key measurement of *guanxi*, whether it is formed by blood bases, or social bases, is the degree of closeness, which depends upon the element of *ganqing*, or affection. Therefore, once *ganqing* is created between partners, the *guanxi* will become closer. On the other hand, without *ganqing*, *guanxi* is less valuable and less dependable.

Guanxi bases may be easily found, but it does not necessarily lead to a close *guanxi* relationship. Both the occurrence of *ganqing* and the development of close *guanxi* hinge upon time and continued personal interaction and mutual help. For Chinese people, a ten-year friendship is much tighter than a one-year relationship, because people have cultivated *ganqing*. The long-term relationship has been tested and evaluated during personal interactions and has been considered reliable and stable through adjustment. In the terms of doing business, long-term relationships offer a steady environment for business transactions. Firms are more comfortable doing business with long-term partners, and tend to maintain relationships longer (Wann, Chwan, Ya and Hui, 2004).

6.4 *Personal Trust*

Personal trust is defined as a willingness to act for a partner in whom one feels confident (Moorman, Deshpande and Zaltman, 1993). Morgan and Hunt (1994) believe that a

trustworthy party has high integrity and is reliable, honest, fair, responsible, helpful and consistent.

Personal trust in the Chinese language is called *xinyong*, which implies the use, or usefulness, of trust. It also indicates a person's credibility, integrity, trustworthiness and reputation.

In China, people normally employ defensive mechanisms in the development of relationships, particularly in the early stages of its development. This is due to the worries of potential relationship termination costs and opportunistic reactions (Wong, 1998). Thus, in order to avoid any future losses, Chinese people prefer to contact those who have *xinyong*, rather than those who do not have *xinyong*. When starting a new relationship, it can first rely on *guanxi* parties' general *xinyong*. Both parties have to build and prove *xinyong*. The initial establishment of *xinyong* depends on the willingness of others to undertake risk to provide one with work. This willingness is influenced by the past experience and shared bases. Generally speaking, there is higher perceived *xinyong* between family members and relatives than between non-kin. Moreover, people can build up their *xinyong* and increase their credit through the quality of their work.

Xinyong is also associated with the importance of one's word over the importance of legal documents. Chinese people prefer to take a *gentleman's word*, or *personal guarantee*, rather than legal bonding (Leung, Lai, Chan and Wong, 2005). When *xinyong* has been established, one's word can be taken in business transactions and verbal agreements, based on *xinyong*, are desired. One example of this is found in Leung et al. (2005). In 2002, sales personnel in Green Group Corporation, one of the largest electrical appliance manufacturers in China, relied only on their personal *xinyong*, rather than on any legal contracts. Through this method, they successfully generating annual turnover of approximately RMB \$10 billions for their company.

The significance of personal trust in *guanxi* is due to poorly specified property rights, undeveloped market structures and cultural reasons which are concerned with

collaboration rather than rivalry (Ambler, 1995; Palmer, 1995; Thorelli, 1990). People carrying out business in China cannot rely on the legal system to enforce business deals. Moreover, people who are in charge of enforcing regulations are often part of business deals. Such circumstances make market exchanges uncertain and costly. As a result, trust between business partners is more important than any legal contractual rules, or any external referees. Trust offers the way, which reduces uncertainty and brings stability to exchange relationships in order to manage and guarantee business transactions (Yau et al., 2000). Thus, Bjorkman and Kock (1995) advised that people should develop trust with their potential business partners before any business, or information, exchange occurs.

In summary, these four dimensions are not meant to be comprehensive factors of guanxi, but they are critical elements and act as major factors in establishing guanxi in China. Moreover, they are not mutually exclusive, but supplement each other. Consecutive reciprocity progressively increases trust between members. Trust and empathy are required to sustain face and guarantee reciprocity, so that neither partner will act opportunistically. A sound perception of these four dimensions can help the development of guanxi.

7. The process of guanxi development

Many studies (such as Davies et al., 1995; Luo, 1997; Abramson and Ai, 1999; Pearce and Robinson, 2000) have shown that guanxi is the most important ingredient in strategies for doing business in China, and that foreigners can gain a competitive advantage over their rivals in Chinese markets by utilizing guanxi. Therefore, fully understanding the process of guanxi development, and finding an effective and practical way that is most suitable for foreign investors to develop guanxi, are crucial factors for Western firms who intend to successfully do business in China.

Buttery and Wong (1999) suggested that the development of guanxi is a process by which two individuals start a potential relationship as outsiders, and then develop into the *insider* stage to becoming old friends.

Wong (1998) outlined the route to build guanxi as four outsider-insider, *F* psychological concepts: Fencer; Fiancé; New Friend; and Old Friend. In the *Fencer* stage, each member tests the others' intentions and reactions, and treats the other as an outsider; in the *Fiancé* stage, each member bargains for power, and evaluates the dependence on, and the level of trust in, the other party. If the basis for friendship has been found, then they move into the *New Friend* stage. If the friendship has been fully proven and a strong guanxi has been formed, both parties enter into the *Old Friend* stage as insiders. At this stage, loyalty and trust have been proven, and any business deals between parties will be bound by their words without the need for any legal contacts.

Foreigners doing business in China are initially considered to be strangers and outsiders. In China, one of the features that Chinese take into account when dealing with foreigners is *centrality*. This is the concept that people's social interactions are moderated through networks, and encourages Chinese people to treat foreigners as outsiders who are not to be trusted (Wong and Tam, 2000). Furthermore, Wong and Tam (2000) believe that when Chinese people deal with foreigners, the Chinese people tend to over-emphasize self-protection due to the lack of institutional trust. They also primarily focus on

pragmatism, because Chinese people believe that their nation's economy influences its survival and well-being.

In order to cultivate a good relationship with Chinese partners, and transform from an outsider to an insider, it is important for Westerners find a practical model through which to start a guanxi with their Chinese business partners. They then need to develop the guanxi relationship over time.

How is guanxi started? Jacobs (1980, cited in Xin and Pearce, 1996) suggested that guanxi depends primarily on shared identification with family, hometown, region, school, or place of work. The possibilities are varied enough that people who are motivated to build guanxi can find a common basis. Jacobs (1980, cited in Xin and Pearce, 1996) stated that two individuals may not need to have a common background to develop a good relationship, however, without a shared common background, people will have a lesser basis for developing guanxi than do individuals who do have a common background.

Chen and Chen (2004) expressed a similar view to Jacobs (1980), stating that it is important to identify and create bases through familiarisation in order to start guanxi. They proposed a three stage model of guanxi development: (a) Identifying and creating bases through familiarisation in order to start guanxi; (b) after two persons find their common bases a wide variety of transactional activities take place in order to move both parties from new friend status to old friend status; and (c) once trust and empathy are created during expressive and instrumental interactions, both parties can eventually use guanxi by requesting favours and giving favours.

Yeung and Tung (1996), Tong and Yong (1998) and Yau et al. (2000) agree that guanxi begins with a guanxi base. Differently, however, they believe that direct interpersonal bases through familiarity are important for building guanxi, but that indirect bases created through an intermediary are also important, especially where a shared common guanxi base cannot be located. A similar view is also expressed in Fock and Woo (1988) and in

Su and Littlefield (2001). Li and Wright (2000) interviewed forty-three Chinese managers and confirmed that, “Guanxi included relationships created through an intermediary” (p. 374).

In terms of building and maintaining guanxi, guanxi varies in its closeness. In fact, guanxi in China contains different levels of intensity, which can be arranged according to the level of closeness as follows: Family members; distant relatives; close friends; workmates; other Chinese; and foreigners. In the business area, the company self is similar to a family, followed by the company’s principal alliances; such as suppliers, distributors, and customers; followed by other Chinese businesses, and then the outside world. The main task for a foreign marketer wanting to success in doing business in China is to get as closely into the inner circles as possible (Steidlmeier, 1997).

Jacobs (1980, cited in Xin and Pearce, 1996) argued that guanxi can be made closer, either by a social interaction which contributes to positive affection (ganqing), or by relying, to some extent, on giving gifts to indicate respect and goodwill.

Tong and Yong (1998) expressed a similar view with three requirements for maintaining guanxi: (1) Continual social interaction, such as social visits, invitations to dinner and the preferment of gifts, facilitates this process; (2) mutual rendering of help, which does not necessarily have to be equally beneficial to both parties; and (3) an ongoing demonstration of reliability and trustworthiness.

In order to find out what the approaches for building and maintaining guanxi from the Western perspective are, Yeung and Tung (1996) interviewed executives from nineteen non-Chinese companies which were currently operating in China, and offered four basic strategies: Tendering favours; nurturing long-term mutual benefits; cultivating personal connections; and cultivating trust. Fock and Woo (1998) conducted a survey of 128 Hong Kong business executives. They found that most of the respondents conceived guanxi as involving; personal relationships, trust, mutual co-operation, exchange of favours/benefits, social activities, giving face, and exchange of information. These factors

are similar to Yeung and Tung's (1996) four strategies. Yau et al. (2000) offered five approaches for Western marketing managers in building guanxi with Chinese businesspeople, which are also consistent with the findings of Yeung and Tung (1996). These five approaches are; social interaction, informal discussions, gift-giving, non-business favours, and cultivating trust.

Based on reviewing the previous literature, the paper proposes four approaches for foreigner investors looking to develop guanxi in China: Intermediary; social interaction; personal involvement; and giving favours.

A foreign investor should initially use **Intermediaries** in order to establish contact with relevant government, or business, organisations in China. After making the initial contact, he/she needs to build guanxi through **Social Interaction**, such as gift giving and dinner invitations. Furthermore, he/she needs to express good intentions to improve guanxi quality, which further assists in creating a basis for a gradual conversion from a stranger to a close friend, such as a family member; through **Personal Involvement**, such as cultivating personal relationships and building trust. Sooner or later, the foreign investor should nurture guanxi by **Giving Favours** in order to make guanxi more productive and long lasting.

7.1 Use of Intermediaries

Guanxi starts with a guanxi base; either predetermined, or voluntary. Since most foreign marketers do not have any predetermined bases (such as kinship, or locality) with Chinese businesspeople most of them have to rely on creating some voluntary bases in order to build guanxi. To find intermediaries who are familiar with Chinese relationship networks and have a good relationship with both partners is the most efficient approach for a foreign marketer to quickly form a voluntary basis with the targeted Chinese partners, and to further extend their business links to others. Bian (1994) suggested that Western companies can successfully build guanxi if they know how to obtain help from intermediaries. Abramson and Ai (1999) further state that using intermediaries to

establish guanxi relationships could cultivate the basis for connecting with key groups of customers, developing effective supply and distribution channels, and making contact with key decision makers who have the political power and authority to influence negotiated agreements, and even government regulations. There is evidence supporting this point. Book (1994) presented a case regarding an intermediary. In 1992, the head of US-based firm McMahan Securities became aware that China's Huaneng Group was looking for international funds in order to fund one of its developing projects. McMahan was interested in this project as a great opportunity to gain a foothold in China. Despite the fact that some of the world's largest financial companies competed for the project, McMahan secured the contract and successfully entered the Chinese financial sector. McMahan used the power of an intermediary, Pufang Deng, who is the head of the Disabled Persons' Federation in China. In the past, McMahan made significant efforts to help disabled children in China, and in other countries, by donating a large number of computers. Thus, Pufang Deng deemed McMahan to be a good company and a friend of China. When McMahan told Deng his intentions, Deng recommended McMahan to Rongji Zhu, China's Vice Premier. With the help of this intermediary, McMahan was able to enter into the Chinese finance market, and further created guanxi within the banking industry in China.

Chan and Wright (1999) created a *buffered approach* through case-based research. They suggested that small North American/European firms can use Hong Kong as a buffer to form a distributorship, or an agency basis, in order to enter into Mainland China's markets. Later, Li and Wright interviewed forty-three Chinese managers and suggest that, "Any organization can gain guanxi through an intermediary" (2000, p. 7). Furthermore, Li and Wright (2000) found that the social status of an intermediary has a variety of impacts on establishing guanxi: "...the higher the social status of the intermediary, the greater the commitment by the parties involved" (p. 374). An intermediary with higher social status is considered to have more *face*. In order to give more face to the intermediary, both parties have to build up greater social obligations and sustain their guanxi. Thus, higher profile intermediaries would be more useful in establishing guanxi. For instance, Pufang Deng was able to successfully help McMahan enter the Chinese

market, not only because he is the head of China Disabled Person's Federation, or because he knows Rongji Zhu, China's Vice Premier, but most importantly because his father, Xiaoping Deng, was the second most powerful leader in Chinese Communist Party history. According to Victor Fund, Chairman of Prudential Asia, a Hong Kong investment bank, has made an interesting statement regarding to the usage of intermediaries: 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 (Kraar, 1994, cited in Jiang and Prater, 2002).

7.2 Social Interaction and Personal Involvement

The maintenance of guanxi relationships is about understanding expectations and performing continuity. A person expects his/her guanxi partner to possess moral integrity, to not create any challenges, to not misuse the guanxi, and to take care of the partner. In other words, to constantly maintain the guanxi. Many foreign marketers think that once a guanxi is built, they can phone the guanxi partner only when help is needed, however, guanxi is not an emergency brake. If one triggers the guanxi only when trouble arises, one deprives the partner of opportunities to build roadblocks to avoid trouble. Once problems already exist, it is often too late to fix the situation and the partner may not be willing to act on your behalf.

To support the development of a strong guanxi and maintain a close guanxi, both parties must make greater efforts and show willingness during their interactions. Social interaction; such as gift giving, dinner invitations, and other entertainments; and personal involvement; including cultivating personal relationships and establishing trust; facilitate this process. Without these factors, the guanxi becomes distant and may gradually fade away.

7.2.1 Gift giving and dinner invitations

During social interactions with Chinese business partners, foreign managers must be aware that the concept of face is very important. Giving face will increase a person's reputation and status. Once face has been given, *ganqing* will be fostered and a strong *guanxi* relationship will follow. On the other hand, if someone makes another person lose face, *guanxi* between them will be in danger. Two of the most frequently used tactics to give face and enhance *guanxi* in Chinese society are presenting a gift to, and holding a banquet for, the other party (Hwang, 1987).

For Chinese people, gifts indicate gratitude and goodwill, and are often used to maintain a closer *guanxi*, while enhancing social interaction. Gift giving shows respect to another person, which will nurture personal relationships and reinforce reciprocity, trust and caring between both parties (Steidlmeier, 1999).

The most difficult aspect of gift giving is how to assess and balance obligation and reciprocity. People often hardly make the correct decision about what kind of gift is appropriate, when it is the proper time to present a gift and/or what social obligations a gift imposes. Presenting an incorrect gift at the wrong time may cause the receiver to lose face, or have too great an obligation. The result of refusing to accept the gift would also cause the sender to lose face.

For small personal businesses it is best to use gifts, or souvenirs. It is also best to present the same gift to everyone in the same group, reserving a better and bigger gift for the group leader, or a decision maker. This gift should be presented in private. Foreigners should also be aware of some notable exceptions for selecting and giving gifts in China. For example, one must never give a clock as a gift, because in Chinese culture, the word is associated with death, and can be related to the end of a life, or a relationship.

The wise way to give gifts is to present a gift at the right occasion; such as at an anniversary, at Chinese New Year, the mid-autumn festival, the lantern festival, or other occasions such as birthday parties, wedding receptions and housewarmings. The kind of

gift depends on the situation and the local custom. In such circumstances, a gift is acceptable because it expresses a personal concern without any clear purpose of taking advantage of a relationship. On the other hand, presenting a gift aimed at getting something done will bring only a short-term benefit, and will even be considered to be bribery. For instance, offering a certain amount of money to a governor in order to get a deal signed off is not considered to be a gift. Such bribery may be good to get a one-off business transaction done, but it won't cultivate an emotional relationship between parties.

Foreign managers can also enhance interrelationships, maintain the bonds of a relationship, and create affection for their guanxi partners by hosting appropriate dinners, or by inviting the other person to birthday banquets. Steidlmeier (1999) suggests that during a dinner meeting with Chinese people, it is very important to notice some unspoken rules in the practice of etiquette. For example, it is important to have the important person sit next to you, give him many toasts, and never refuse a toast, even if only a small sip is taken. When you make a toast, firstly, you should toast his/her company's future, then toast the good future of the business between you, and also toast his/her health and his/her family. Other etiquette to show respect for Chinese people in eating and drinking include: Never starting until they all arrive; letting the important person seat the centre seat; waiting for him/her to sit first; always using their surname with their title; and never using their first name.

Other types of social interactions may be used in order to develop a guanxi relationship with the potential target: Including offering a free trip for Chinese partners to visit the headquarters; supporting and sponsoring their children studying overseas; and so on.

7.2.2 Cultivating personal relationships

Although gifts and dinner invitations are necessary, they are not enough to form a sustainable guanxi. If foreign businessmen overemphasize the giving of gifts and wining and dining to form guanxi with their Chinese partners, it is often considered as constituting bribery, or they will become known as *meat and wine friends*. This means that the relationship is considered to be unstable and unreliable. Creating personal

relationships with the guanxi partner is more useful than any gifts and/or dinner invitations. To value guanxi, foreign marketers should know the needs and main concerns of their Chinese partners, games that they like, food that they prefer, and topics that they like to talk about (Pearce and Robinson, 2000). A similar view was also found in the interview study conducted by Yeung and Tung, who interviewed the heads of nineteen non-Chinese firms operating in China in 1996. Most of the respondents revealed that, because competitors can repeat short- and long-term gains, guanxi relationships solely based on material benefits could be easily broken. As a result, forming personal relationships with partners, which cannot be easily duplicated by rivals, is vital to sustaining long-term guanxi.

Personal has specific meanings to both members in guanxi, including sharing personal secrets, or feelings (Yeung and Tung, 1996). Yau et al. (2000) suggested that one way that foreigners wish to create a personal relationship with their Chinese partners is through informal discussions. Making a deeper level of honest and emotional disclosures in the relationship will be considered as a signal of being committed to the guanxi. Chinese are more willing to expose detailed information about themselves during an informal discussion. It is a good opportunity for a foreigner to understand and express concerns for the Chinese partner's preferences, priorities and needs.

In real life, however, Chinese people do not tend to make connections quickly with strangers, and do not want to make the first contact, or trust people they are not familiar with.

Foreign marketers, as strangers in China, have to realize this fact, and must always take the first step to committing to the guanxi relationship, showing their desire, sincerity and frankness. By following the unspoken rule of reciprocity, Chinese business partners will return similar commitments, which will encourage the forming of a formal relationship, or friendship.

7.2.3 Building trust

Standifird and Marshall (2000) argued that guanxi is first and foremost in cultivating long-term personal relationships, but that it will not succeed unless trust is established. Trust is a prerequisite for establishing a successful and enduring guanxi.

How is such trust built? According to Zucker (1986), and Lane and Bachmann (1996), a person can, over time, draw on prior exchanges, common characteristics, and/or institutions as three trust bases to produce trust with others. Prior exchanges-based trust is based on previous experience, reputation and credibility. Common characteristic-based trust grows from ethnicity, or familial ties. Institutionally-based trust relies on the legal system to produce trust.

In the West, people doing business rarely rely on agreed words, or personal trust, because these factors do not have legal sanctions. Institutionally-based trust, however, is heavily relied on in Western business transactions (Leung et al., 2005). In contrast, Chinese business practices emphasize personal trust (xinyong), rather than institution trust (Tong and Yong, 1998). Continued and repeated business exchanges between two companies in China are more likely to start from a personal relationship between the two companies' decision makers. This differs from the impersonal nature of transactions conducted in Western countries. As a result, cultivating personalised trust is a key element to developing harmonious relationships in China (Lee et al., 2001). Han (2003) points out that, since the Chinese legal framework for the enforcement of a contract is not well developed and the institutional environment is very uncertain, having personal contact with the head managers of a partner company, past exchanges, and/or identity signals of the head managers, are three bases for Chinese to build relationships of trust in China. For foreign investors, because they are not able to easily take advantage of this type of close personal relationship and will not receive any substantial support from Chinese institutions, building trust with their Chinese business partners should focus on increasing perceived similarities, and creating and maintaining their reputation and credibility based on prior exchanges.

In order to develop similarities, foreign investors should try to understand Chinese business culture. This includes business behaviours, business interests and business values, as well as being familiar with how the Chinese partners operate their firms. Moreover, foreign investors from different countries are still able to find a certain level of similarity with their Chinese business partners by increasing their cultural affinity and making efforts to avoid isolation in the relationship; such as enhancing language capabilities and cultural understanding (Lee et al., 2001).

On the other hand, Chinese partners will focus on the long-term relationship. Received favours are not necessarily immediately returned. It is a long-term commitment, which requires guanxi parties to have the belief that others have enough reliability and competence to return favours in the future. Thus, foreign firms have to show their reliability and ability in the delivery of favours to their Chinese partners during their interactions. Foreign firms should also avoid any opportunistic behaviour in order to maintain, and increase, reputation and credibility.

Moreover, Child and Mollering (2003) suggested that people should not only base relationships on certain foundations, but should also play a more active role in producing trust, especially where those foundations for trust are weak. Child and Mollering (2003) carried out an empirical study and stated three strategies for foreign investors in actively developing trust with their Chinese business partners and staff. The first strategy is to develop personal rapport with them; the second strategy is to recruit local managers to deal with them; and the third strategy is that foreign investors should transfer their own business standards, functions and practices to its joint venture operations in China, in order to substitute for the lack of institutional foundations, and eventually increase trust with local staff.

7.3 Giving Favours

In China, the emphasis on face saving and reciprocity based on renqing has a great influence on how Chinese deal with things, especially when giving a favour to someone. For Chinese people, face indicates a person's social status. A person giving favours to

others signifies his/her power, or ability, beyond his/her normal peers. Thus, he/she gains face. Related to face, renqing relates to a person's social obligation and the sense of reciprocity. Giving favours can develop an unpaid obligation, and these obligations can extend to entire networks. While enjoying the favours, a receiver takes on a reciprocal obligation. He/She has to fulfill the obligation and return favours in the future, otherwise, he/she will be considered to be a mean person, and loses face.

Renqing and face can help the exchange partners to avoid opportunistic behaviours (Ganesan, 1994), and giving favours allows the exchange partners to mutually depend on each other (Huang, 2004). High interdependence allows the exchange partners to adjust the existing guanxi in order to handle uncertain Chinese environments more successfully (Heide, 1994). On the other hand, the exchange partners who have high interdependence are willing to collaborate and contribute more to the relationship. Thus, giving favours can help the exchange partners to make greater commitments to the relationship and maintain the on-going guanxi network.

Su and Littlefield (2001) suggest that, in China, there are two different ways of giving favours, which could cause the receiver different levels of appreciation. One of these is called *Xue Zhong Song Tan*, which means giving appropriate assistance to people in time, such as delivering charcoal to people in snowy weather. Another is called *Jin Shang Tian Hua*, which means to embroider extra flowers on the brocade. In real life, people giving favours with *Xue Zhong Song Tan* are much more valued than those offering *Jin Shang Tian Hua* favours, because *Xue Zhong Song Tan* shows genuine and timely help for people in trouble and, at the same time, exposes true feelings toward them. *Jin Shang Tian Hua*, however, seems to be unnecessary and extra help for the receiver. Therefore, timely giving of a favour tends to increase the appreciation and build up of a relationship.

In the business context, China welcomes foreign companies to give *face* to China, to understand China's social reality, and will offer treats to those foreign companies who offer great favours, or genuine help, to them as insiders. On the other hand, by giving

more favours to their Chinese exchange partners, foreign companies can gain more face for themselves and increase mutual dependence between them.

In general, foreign firms should adjust their marketing and manufacturing plans to help Chinese partners achieve their economic developmental goals by supplying capital, introducing foreign advanced technology, equipment and management skills. As a result, Chinese partners can recognise that these foreign firms are making a great commitment and are willing to make a good relationship. Moreover, foreign marketers should set up a presence in the local community and be aware of the governmental expectations. Local and regional Chinese governments would like foreign firms to make a contribution to their towns and cities. For example, foreign companies should carry out sympathetic plans and arrange community activities, such as donating to and/or funding schools, refurbishing historic buildings, or sponsoring sports events. These efforts, plus their social interactions, would help foreign marketers create and sustain guanxi with top local officials and governments. In return, the Chinese government would be more likely to take good care of these companies by approving companies to market products in the local area, and by providing incentives such as raw materials, cheap rent and lower taxes, thereby increasing the foreign company's overall performance.

In conclusion, the proposed model of guanxi development by which foreign investors can build and maintain guanxi reflects the four fundamental dimensions of guanxi: Face; reciprocity; empathy; and trust. The four proposed practical approaches: Using intermediaries; social interactions; personal involvement; and giving favours: are complementary of each other, rather than exclusive. They should always work together in order to build and maintain strong guanxi, because none of them alone has this capability. Social interactions alone cannot secure guanxi, because other competitors can make similar efforts. Personal involvement alone, however, without giving gifts, hosting dinners and doing personal favours, cannot maintain guanxi. If guanxi excludes the use of intermediaries, some foreign companies that do not have strong personal ties (e.g. blood basis) may have difficulty creating guanxi, because they cannot make direct contact with Chinese companies. Yeung and Tung's (1996) empirical study indicated that, in general,

42% of foreign firms have used intermediaries to locate suitable joint venture partners. Companies that engaged in exporting and service sectors were likely to emphasize bestowing favours, whereas importing and manufacturing companies preferred to nurture long-term mutual benefits. Six of the nineteen firms which had more experience of doing business in China usually used the integrated four approaches to build and maintain guanxi. As a result, they achieved considerably higher levels of financial performance.

8. Conclusion

Business is conducted differently in China than in the Western World. Obviously, if people do not pay enough attention to Chinese cultural preferences, their business success in China may be put in danger. Foreign businessmen have to make and employ strategies for engaging in China's unique business environment. The essential part of these strategies is to cultivate a strong guanxi network, which is critical for foreign marketers wanting to successfully do business in China.

Foreign marketers should pay more attention to building and maintaining the formation of personal relationships. They must realise that guanxi is vital, not only for the creation of new business partnerships, but also for their subsequent effectiveness. By adopting and analysing existing studies, this dissertation aims to help foreign marketers to understand guanxi. By putting together the constructs of guanxi, the study develops an integrated model for building and maintaining guanxi for foreign marketers, as a guideline to success in the Chinese business environment. The model demonstrates the fact that guanxi itself consists of face, reciprocity, empathy and trust. The development of guanxi is a process by which two individuals start a potential relationship in the *outsider* stage as strangers, and then develop until they become old friends in the *insider* stage of the relationship.

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