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Table of Contents

I. Table of Figures	III
Abstract.....	1
1. Introduction	1
1.1. CHINA’S DEVELOPMENT AND CURRENT SITUATION.....	2
1.2. THE CHINESE SOCIETY	3
2. Guanxi.....	4
2.1. DEFINITION, CLASSIFICATION AND INTERPRETATION.....	4
2.2. THE CHARACTERISTICS OF GUANXI	5
2.3. THE PROCESS OF GUANXI.....	7
2.4. THE UNDERLYING IMPORTANCE OF THE CHINESE GUANXI	12
2.4.1. History, roots and development of guanxi	12
2.5. THE RELEVANCE OF GUANXI FOR BUSINESS	15
2.5.1. Establishing guanxi	17
2.5.2. Guanxi usage.....	19
2.5.3. Distinction between B2B and B2G Guanxi	21
2.6. THE BENEFITS AND DRAWBACKS OF GUANXI	24
2.6.1. The time perspective.....	24
2.6.2. Guanxi’s competitive advantage	26
2.6.3. The significance of face and transaction costs	27
2.6.4. Guanxi’s side effects	29
3. Stock Markets and Corporate Governance.....	31
3.1. INTRODUCTION TO CORPORATE GOVERNANCE	31
3.2. CHINESE STOCK EXCHANGE	32
3.3. LEGAL FRAMEWORK AND CORPORATE GOVERNANCE CODES.....	34
3.4. OWNERSHIP STRUCTURES, SHAREHOLDER PROTECTION AND THE EFFECTIVENESS OF BOARDS	36
3.4.1. Ownership structure and minority shareholders.....	36
3.5. INFLUENCE OF THE STATE	40
3.5.1. The problem of politics in corporate governance	41
3.5.2. Tunnelling in China.....	42
3.5.3. Pyramiding.....	43

4. The Influence of guanxi on Corporate Governance	43
4.1. THE SELECTION OF BOARD MEMBERS	44
4.2. THE ROLE OF DISCLOSURE	45
4.3. THE PROBLEM OF ENFORCEMENT	46
5. The interrelation between corruption and guanxi	47
5.1. INTRODUCTION TO CORRUPTION IN CHINA.....	47
5.2. THE INTERRELATIONSHIP BETWEEN GUANXI AND CORRUPTION	48
5.2.1. Two different concepts by nature	48
5.2.2. Gift-giving	50
5.2.3. Corruption, guanxi and business	51
5.3. THE CONNECTION BETWEEN CORPORATE GOVERNANCE AND CORRUPTION.....	53
5.3.1. Examples	56
5.4. ETHICS OF CHINESE BUSINESS PRACTICES AND GUANXI	57
6. Corruption and guanxi in Singapore, Taiwan and Hong Kong	59
7. Guanxi and networking.....	64
7.1. GUANXI AND WESTERN NETWORKING	64
7.2. NETWORKING THROUGHOUT ASIA	68
8. The connection between guanxi and profitability	69
9. The connection between guanxi and corporate culture	73
10. The changing significance of guanxi and future development.....	74
11. Meta-analysis.....	78
12. Conclusion.....	96
II. Appendix I – Deutsche Zusammenfassung	99
III. Appendix II – Lebenslauf	101
IV. References	102

I. Table of Figures

Figure 1: How guanxi works (based on Fan 2002)	10
Figure 2: Person X’s guanxi net, Chen and Chen (2004)	11
Figure 3: Board members recommendation, Heidrick and Struggles (2007)	44
Figure 4: Comparison of the four dimensions of relationship Marketing between Western and Chinese (Yau et al., 2000).....	67

Abstract

The goal of this thesis is to analyze the influence of “guanxi” on (the development of) the Chinese economy and on business practices through an exhaustive literature review. The origin of guanxi in the teachings of Confucianism and reason for its prevalence despite the opening of the Chinese economy such as lack of legal institutions and law enforcement will be evaluated. Also, the influence of the Cultural Revolution and the consequently, political and social unrest on the development of guanxi as an alternative to a functioning market system is of interest.

Benefits of guanxi especially in connection to the reduction of transaction costs as a result of minimized opportunistic behaviour and more efficient access to resources resulting in a competitive advantage will be explained. Nevertheless, side-effects such as the costliness of guanxi especially in terms of risks and intangible, unpredictable outcomes as well as the deterrence of competition and the negative influence on the development of a competitive market economy will also be taken into consideration.

The obvious tie between B2G guanxi and corruption as a result of the great amount of influence still prevalent in the hands of the government and the monopolistic position of bureaucrats will be evaluated as well as the consequences on the proper implementation of and adherence to Corporate Governance Codes. The problem of tunnelling of resources out of companies, especially as a result of complex pyramiding and unrestrained management as well as the lack of complete privatisation and the resulting challenges for the economy will be treated. The changing significance of the dynamic concept of guanxi and its predicted future development as well as connections between guanxi and other (Western) types of networking will be of interest in the later section of this thesis.

1. Introduction

Frequently, Western firms that have entered the Chinese market have not been successful with their business operations which is often blamed on the difference between Chinese and Western negotiation styles that are assumed to be culture-

based (Ghauri and Fang, 2001). Through the development of China’s economy and consequently the enhanced interest in its business opportunities guanxi, a Chinese specific concept, has obtained an increment of attention. Guanxi which in its simplest definition is an “interpersonal relationship” has a significant influence on Chinese social behaviour and business practice (Luo, 2000). Guanxi’s roots are said to date back to Confucius (c. 552 – c. 479 BC) when the teachings of Confucianism were commonly believed, which emphasise the importance of relationships, morality and the attainment of social harmony (Yao, 2000). This concept is often defined as an absolutely necessary condition for successful business operation in China, its importance being accepted and recognized by many Western scholars. The objective of the subsequent chapters lies in the examination of how this concept influences business operations in China and what significant it actually exhibits.

1.1. China’s development and current situation

China, comprising approximately 20% of the world’s population, has established itself as one of the world’s leading economies through rapid growth and significant development. Being one of the most important economies on the globe it attracts interests of global investors and academics. As China’s significance for worldwide business is undeniable, the special issue of Chinese business conduct has received an increased amount of attention.

In December of 1978, the People’s Republic of China (PRC) opened its economy under the rule of Mao Zedong’s successor Deng Xiaoping, developing a centrally planned economy that was mostly closed to international trade into a market oriented economy. The reforms included the liberalization of prices, fiscal decentralization, enhanced freedom for state-owned enterprises (hereafter SOEs), establishment of stock markets and the opening to foreign trade and investment. Through this, output quadrupled by the year 2000, poverty has been reduced to a great extent and living standards as well as personal freedom have increased. With the enforcement of a joint venture law in 1979 China opened its borders to foreign investment (Luo, 2000: 159) and since then, many Western companies have established joint ventures or wholly owned subsidiaries in China. The

officially recorded GDP growth rate in 2006 of 11.1%¹ makes China the fastest growing major nation with GDP growth rates steadily well above 10% in recent history. 70% of China GDP was produced in the private sector in 2005 whereas the public sector is dominated by SOEs. Concerning purchasing power parity, China was the second largest economy in the world after the US in 2006, although when measured on per capita, the country has lower middle income levels and still retains a poverty rate of 10% (est. 2004) or 130 million Chinese that still fall below international poverty lines².

The ambition behind China's transition was the reduction of influence available to the party and government concerning the management of the economy which has been achieved to a certain degree (Fan, 2007). The Chinese government has reduced its direct influence in running businesses, privatizing enterprises and reducing its control in certain industries. Despite improvements, political control nevertheless remains tight, the government still exerting a great amount of political influence in his interest. The government still holds the majority shares of many SOEs or indirectly controls decision making processes of SEOs through pyramiding or controlling resources and managers.

1.2. The Chinese society

Chinese society, culture, values and behaviour are based on Buddhism, Taoism and Confucianism although the latter is seen as retaining the greatest amount of influence in China's society and as the origin of guanxi practices. The teachings of Confucius (or Confucianism) highlight the importance of relationships and emphasize that individuals exist in relation to each other rather than being separate identities. Each individual takes a position in a complex social system and needs to fulfil his position's requirements to be able to achieve social harmony and order which, according to Confucius, resembles the ultimate goal. Consequently, great emphasis is placed on the group instead of the individual and these relationships with others are what define people. Further, relationships are hierarchically structured and the concept of morality is important (Bond, 1991:

¹ <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html> (27.11.07; 21:53)

² <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html> (05.01.08; 22:43)

215). Individuals exist in a delicate balance with their social environment (Steidlmeier, 1999) through which they are defined, contrary to Western assumptions of independent, autonomous individuals that are self-defined (Bond, 1991: 215).

Taoism highlights the attainment of harmony through minimal interference and opposes the use of punishment or force (Jing et al., 2005), exhibiting parallels to the Chinese believe of the “rule by man” instead of the “rule by law”, and the typically weak law enforcement and reliance on relationships and trust instead.

2. Guanxi

2.1. Definition, classification and interpretation

The process through which relationships are established and the importance attributed to these relationships differentiates between Eastern and Western societies as this to a large extent depends on cultural values (Buttery and Wong, 1999). Guanxi, a special way to form relationships in China has become a recognized and accepted cultural phenomenon throughout the world, increasingly in the past years as China’s economic importance and consequently, the interest for business in this country has increased. Western academics have recognized the relevance of this concept, especially for business as it seems to be hardly possible to achieve success without an adequate guanxi network. Many academics, Chinese as well as Western have focused on this Chinese peculiarity, devoting numerous empirical research and academic articles to this topic. As guanxi is a complex concept it makes a clear and exhaustive definition and explanation necessary in order to fully understand this thesis. Due to its uniqueness and peculiarity, it is often misunderstood however, its importance for foreigners entering the Chinese market should not be neglected and a clear understanding of its application is essential.

Existing literature and studies on guanxi can be divided into two major categories. First, academic research on guanxi focuses on evaluating its benefits and pitfalls and its implications for business. The other stream of guanxi research concentrates on the comparison between guanxi and Western concepts of networking and relationship marketing (Fan, 2002b; Fock/ Woo, 1998). The field of

research focusing on the creation, process and result of guanxi is also called *guanxiology*. *Guanxi xue*, a similar concept, focuses on the practical implementation of guanxi development and maintenance, including gift giving and favour exchange to establish a relationship.

The word guanxi can be analyzed according to the two Chinese characters it contains, namely guan 关 and xi 系. Guan can be defined as “to connect” or “a pass or a gate” (Yang, 1994: 49) whereas xi basically means to tie up and extend relationships (Lou, 2000: 2). The simplest definitions of guanxi characterize it as a sort of special social relationship however, the English word relationship by far does not cover the complex nature and the binding power of guanxi (Bell, 2000). Numerous definitions can be found in existing literature for the complex phenomenon of guanxi. For instance, “guanxi refers to the concept of drawing on connections in order to secure favours in personal relations” (Luo, 1997). Lovett et al. (1999) consider guanxi the “glue that holds Chinese society together”. Chen and Chen (2004) state that “guanxi operates in different life spheres, so there are family-, friendship-, political-, and business-guanxi.”

2.2. The characteristics of guanxi

Guanxi connections are based on trust, friendship, reciprocity and honesty and are established on a long-term basis, each guanxi being highly personal and particular. Especially the concepts of xing (trust) and ganqing (feeling or emotional commitment to each other) play an important role for determining the quality of a guanxi connection. Guanxi is a dynamic process that changes and develops over time. Further, it is not determined by social class or status but rather is class-independent. Using or pulling a guanxi connection is also known as *la guanxi*, or commonly also referred to as to “walk guanxi”.

According to Lou (2000: 10-14) guanxi typically exhibits seven main characteristics. Guanxi is a *utilitarian* process, i.e. a personal gain for at least one party is always involved, which is the underlying drive for the exchange of favours. Through the *reciprocity* of guanxi, both parties at some point profit from their connection with the other party as a bond for mutual exchange upon request is formed. This mutual exchange of favours is typically established to *last long*

without an advanced determination on the endurance of the relationship. Building a guanxi connection tends to be a time and effort consuming process, therefore it is expedient to build guanxi on a long term basis and for the future. Nevertheless, a connection can be easily terminated if it is no longer of use to both parties. Guanxi is a highly *personal* concept which is established through face-to-face interaction between individuals to build up a personal relationship. Personal attachment in terms of a trustworthy and reliable special relationship needs to be established. Guanxi that is only based on material exchange is considered fragile or can be regarded as corruption or bribery. Although highly personal, guanxi is to a certain degree *transferable*. For instance, a person could acquaint two of his guanxi contacts if one could be helpful to the other and vice versa. They could then establish their own guanxi connection which will be predetermined by the quality of guanxi they have with the intermediary. Guanxi is *intangible* which means that the members are connected through an invisible bond. The members are not de facto obliged to fulfil their guanxi obligations of reciprocity and equity, if however they do not, they must reckon that their reputation will seriously be damaged and that they lose their face (*mianzi*), which is of significant importance for Chinese choice of guanxi. *Mianzi* is a person's public or social image gained by performing social roles and is determined by the dimension of one's guanxi network. Someone's face depends on the status of the persons one has relationships with; the more powerful and respected they are the more face one will have himself which in turn is necessary to establish new guanxi. A loss of face is quickly spread through the guanxi network and, depending on the connectedness can result in losing all one's network members. Finally, the cultivation of guanxi is *concept-specific*, its meaning varies depending on the situation in which it is used.

Through the influence of Confucianism, Chinese tend to be very group oriented and accordingly, people will be treated either as insiders or outsiders of their groups. Guanxi relationships are built on guanxi bases which are basically some form of a pre-existing relationship or commonality concerning an aspect of personal identification that connects individuals. As a result of the existence of this base or relationship, a guanxi process is made possible through the establishment of *ganqing*. Nevertheless, it is important to recognize that the existence of such a

guanxi base does not necessarily mean that guanxi will develop but an existing base only facilitates the development of guanxi (Fan, 2002b).

A base can either be established through blood relationships (i.e. family members or kin), a relationship by nature (for instance school mates, work colleges or neighbours) or an acquired relationship (through acquaintances, intermediaries or friends). Yang (1994: 64) also called these categories of guanxi *chia-ren* (family guanxi), *shou-ren* (familiar person) and *sheng-ren* (acquaintances). Depending on the base, a relationship is defined whose interaction and outcome varies accordingly (Chen and Chen, 2004). According to Luo (2000: 6), friendship itself, however, is not a guanxi base but it is other commonalities that trigger friendship and friendship in turn is necessary to establish a stronger and close guanxi relation.

2.3. The process of guanxi

Chen and Chen (2004) question the borderline between guanxi and guanxi bases and claim that with guanxi base models it is difficult to distinguish guanxi bases from guanxi itself, questioning whether a base is only a potential for establishing guanxi or can already be considered a guanxi itself. They therefore propose a 3 stage model of initiating guanxi, building guanxi and using guanxi.

In the first stage, personal backgrounds are exchanged, focusing on the possibility of identifying an existing common social identity base. Future objectives are also communicated in order to identify mutual goals and utility of the guanxi and great emphasis is placed upon impressing the other party with the utility one could bring through a future guanxi relationship. Here the concept of self-disclosure plays a significant role as it is absolutely necessary for the detection of common bases, yet too much self-disclosure too early can be dangerous and a failure to reciprocate this openness might signal a lack of interest in a future relationship to the other party.

In the second phase the goal lies in establishing guanxi and enhancing its quality. As mentioned, *reciprocity* is an important precondition for successful guanxi development however, on a *long-term* basis. In other words, it is not necessary or even a clever move to “repay” the other immediately as this would close the guanxi

circle rather than leave opportunities open for the future. The repayment is further based on the principles of *other-oriented reciprocity* (i.e. what is given in return must be valuable to the other party exhibiting consideration of the other person's needs) and on *unequal exchange* (i.e. more than one has received is given in return, thus further stimulating the guanxi exchange through the creation of feelings of indebtedness). If the favour returned, of whatever nature it be, is not of greater value than what has been received, the Chinese counterpart will not be considered as “gentlemen” and a state of psychological balance will not be reached (Yau et al., 2000).

In the last stage, guanxi is used to obtain benefits through favours and through asking a favour, the quality is evaluated and readjusted. Here the principle of long-term equity is applied; it might be the case (especially amongst family member and close friends) that one party asks a favour of the other several times consecutively but, care is at all times taken to keep the long-term equity in balance.

Hwan (1987) proposes a classification of three kinds of guanxi, but according to its purpose and nature, not the base. The *socio-affective guanxi*, corresponding to the guanxi based on blood relationship above, focuses on the exchange of feeling and emotion within the family to satisfy the primary need for love, affection and belongingness. *Instrumental guanxi* can be compared with the above categorization of a stranger or a guanxi acquired through relationship and is meant to fulfil material needs through utilitarian interaction and exchange. *Mixed guanxi* is analogous to guanxi with a familiar person, i.e. a relationship by nature, and is used for both, the exchange of feelings as well as for material advantages (Chen and Chen, 2004).

Guanxi with a familiar person is based on a relationship by nature through which some social characteristics are shared. In the West, social identities tend to be formed through a categorization of age, gender, race, education, income level etc. whereas in China commonalities based on e.g. birthplace, college or workplace are significant. Whereas Western concepts of social identity are based on stable demographic criteria, Chinese social identities are based on social institutions with clear boundaries, although these can be enlarged and reinvented (Chen and Chen, 2004). In China, a greater and different meaning is assigned to social

relationships as social relationships do not just help a person as in the West but define who the individual is (Vanhonacker, 2004).

Fan (2002b) proposes that guanxi should be seen as a dynamic process of social interaction which initiates with two players but may involve an undefined number of actors. In Figure 1, A and B have a constant relationship but the guanxi process itself is activated through A asking B for a favour, i.e. it is the need of something that triggers the guanxi process. B may then turn to C for help who in turns asks D for assistance. Various scenarios are possible, for instance A might get to know C or D (represented by the dotted arrow lines) and build up an own relationship or, on the other hand, C and D may remain completely unknown to A. A has no pre-existing base with C or D, however here B takes over the role of the intermediary or matchmaker. Each of the actors will receive a reward for the assistance offered directly or indirectly to A. This reward can either be given directly by A if a connection has been established, or directly through each actor immediately in front (then A would reward B, B would reward C and C would reward D).

This chain of relationships can be endlessly long and lengthy chains tend to be comprised of a number of sequential dyadic relations where each actor helps his guanxi directly because of their personal connection. The participants of this chain do not assist in order to aid the initiator of the request and might as well not be aware of this person or never meet them. In this case, debt is also only owned to the individual personally asked, not to the whole chain (i.e. if A does not become acquainted with the other actors, A will only owe to B). Through this, a person can indirectly use the resources of a vast amount of people without creating a large debt (Luo, 2000: 248).

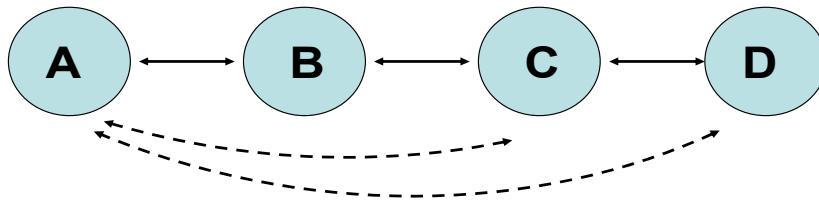


Figure 1: How guanxi works (based on Fan, 2002b)

This explanation demonstrates that with one guanxi relationship, a whole network of other guanxi connections is made available. Through the connection A has with B, A has indirect access to B's guanxi network³, assuming B is willing to assist. The more connections A establishes, the more possibilities for new guanxi are available, in accordance with Yang (1994) description on the cumulative effects of guanxi. As Steidlmeier (1999) stated: “duo yige guanxi, dui yitiao lu – one more connection offers you one more road to take”.

Through these connections A secures resources that might be useful in the future thus building up a sort of social investment or social capital. This unfulfilled obligation to repay, which is also described as a form of social capital by Luo (2000: 14) is also known as *renqing*. According to Fan (2002b: 549) “to develop and maintain a guanxi relationship is like putting one's money into a savings account or purchasing an insurance policy so that one could get help whenever needed”. The more guanxi connections a person has i.e. the more integrated and dependent someone is on their guanxi network, the more possibilities and independence one obtains (Yang, 1994)

³ This network of social connections that a person has is also called *Guanxiwang*

Another interesting concept I want to introduce at this point is that of Chen and Chen (2004) on the determinants of guanxi quality resembled below in Figure 2.

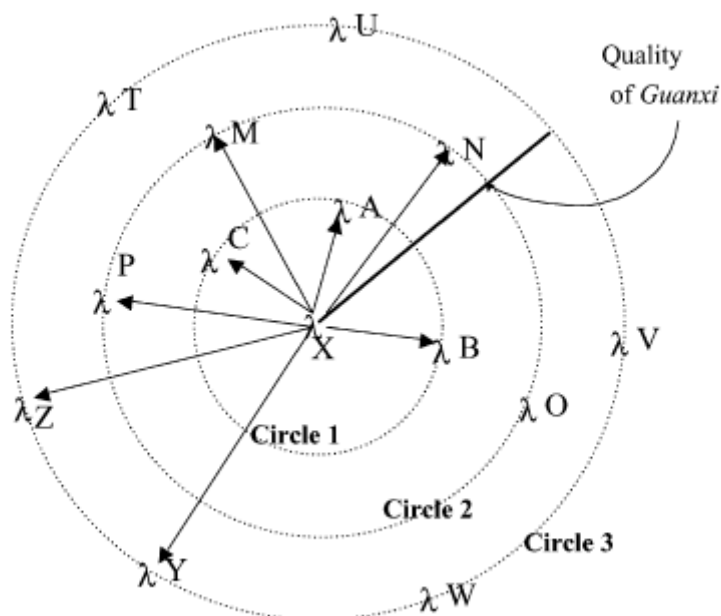


Figure 2: Person X's guanxi net, Chen and Chen (2004)

Figure 2 represents the psychological net space of person X's (located in the centre) guanxi. The quality of a person's guanxi is determined through the distance between X in Figure 2 and the other, corresponding individual so the closer to X the other person is located the better is the quality of their guanxi connection. For instance, in Figure 2, person X has a better connection to A, B or C than to M and N or even worse, Y or Z. This follows out of the assumption that, the closer an individual is to X, i.e. the more inner the circle, the smaller is the psychological distance and therefore the better the quality of their relationship. The focus lies on the individual X and its connections to other members, which may or may not be aware of each other, know each other or de facto themselves have a connection between each other. However, this diagram is not meant to resemble an interconnected guanxi network but merely highlight the connections between X and the other parties. Through the establishment of a closer guanxi a movement to inner circles is feasible, however, a movement in the opposite direction is also possible if the quality of guanxi is decreased. The higher the quality of the guanxi, the more likely it is that a failure to return a favour or obligation to assist will be forgiven (Luo, 2000: 256).

Similar to Figure 2 is the explanation offered by Luo (2000: 13). Chinese society functions within clan-like networks which can be represented through concentric circles. Depending on the degree of trust.⁴ and the distance of relationship, guanxi relationships are placed on the circles. The closest connections will be placed in the centre, the other individuals are placed moving away from the centre similar to Figure 2, representing a person’s guanxi network. A desirable goal, especially for foreigners conducting business in China, is to position oneself as close to the centre as possible (Steidlmeier, 1999).

Luo (1997b) also distinguishes between “predetermined” and “voluntary” relationships. Predetermined relationships are determined through a common base such as the relationship to family members. In this case, certain behaviour is expected and possible derivations are very limited. In voluntary relationships however, a person can define their own role and determine the nature of the relationship and exchange.

2.4. The underlying importance of the Chinese guanxi

2.4.1. History, roots and development of guanxi

Various suggestions concerning the origin of guanxi and its development have been made. Yang (1994: 148) surveyed Chinese on when they believed guanxi first became important and realized that most respondents believed in the emergence of guanxi during the time of the Cultural Revolution (1966-1976). At this time of social and political unrest, people needed to rely on their personal connections in order to survive, until social order and discipline had been restored by the state. Anything from housing to groceries could only or much easier be acquired through the use of ones social contacts. Within this highly centralized bureaucratic state, the only way to get things done was through the use of personal connections (Arias, 1998). Similarly, Xin and Pearce (1996) argue that guanxi can be seen as a transitional agreement until the institutional system was better established. These views however, conflicts with the fact that guanxi became more and more prevalent over the past years and has not diminished after

⁴ The positive relationship between trust and relationship quality has been shown by Wong (1998).

social order had been at least partially restored. Similarly, Luo (2000: 21) states that the extensive use of guanxi in China is due to the strictly controlled, top-down allocation of resources by the government and primitive legal infrastructure that was common until recently. Guanxi can be considered a result of the monopoly position of few powerful governmental individuals over certain rights along with an economic system that produced scarcity instead of abundance. Through the combination of monopoly and scarcity, guanxi established as an unofficial way of resource allocation for society (Chang 1993). Also Guthrie (1998) considers guanxi as dependent on the institutional structure of society rather than on culture which changes and adapts according to institutional changes. At this point a distinction suggested by Su and Littlefield (2001) is worth noting. Accordingly, two types of guanxi exist in this regard, namely favour-seeking guanxi and rent-seeking guanxi. The former is prevalent in Chinese society as roots of Confucianism and characteristics of a collectivist society while the rent-seeking alternative is institutionally defined and often synonymous with corruption. Also the distinction between family, helper and business guanxi should be drawn, each of these types of guanxi being distinctive in its nature, goals, base and values. Family guanxi is considered to be based on Confucian values through which affection is exchanged and reciprocity only plays a secondary part whereas helper guanxi has its origin in the social and political developments in China and, as it is utilitarian, is based on the mutual exchange of favours (Fan, 2002b). Personal connections can also be used in business as a means to enhance transactions, obtain advantages and find solutions.

Many respondents surveyed by Yang (1994: 148) claimed that guanxi is a deeply rooted phenomenon which has always been present to some degree in the Chinese society. Here, the influence of Confucianism (see chapter 1), which still has a significant meaning in China, must be considered. Confucianism highlights the relevance of relationships and the position each individual takes in a complex social network in order to obtain social harmony which is considered the ultimate goal. These teachings undeniably have a connection with China's contemporary relationship building processes and might be considered the ancestor of guanxi as it is known today. In fact, the word *lun* stems from Confucian principles and has a

similar meaning to guanxi, referring to traditional social relationships⁵ and their differentiation depending on the individual (Luo, 2000: 8). A clear connection is also drawn by Dunning and Kim (2007) between guanxi and Hofstede’s collectivism dimension⁶. Chinese typically score high on this dimension, highlighting their emphasis on the in-groups before the individual and importance of building up relationships. The collectivism of Chinese seems to be an essential ingredient for guanxi, resulting in the creation of an interdependent self.

Interesting is the fact that the word guanxi does not appear in classic Chinese dictionaries⁷ which, according to Yang (1994: 49) suggest that it has developed during the socialist period. Nevertheless, the word “guan” can be found which is defined as “to pass a gate” or “to make a linkage”, whose meaning is undeniably connected with today’s notion of guanxi. Further, the term guanxi only appeared in Chinese newspapers around 1978 which may although also have been influenced by a lack of freedom of press and speech.

Concluding, it seems that the concept of guanxi as a special way of forming relationships has existed for centuries and is deeply rooted in Confucian teachings which still have a significant influence in present China. Nevertheless, the concept of guanxi as it is known today, a way to use one’s personal relationships in order to obtain certain economic or political privileges (especially in connection with business) is a relatively new concept which at least to a certain extend was triggered through the political and social developments in China.

Guanxi can be considered a result of Chinese culture, institutional weakness and corruption. We have seen the importance of the influence of Confucian teachings on relationship establishment and attitudes towards relationships. Typically, Chinese rely and belief in each other rather than in a legal system and in fact rather an animosity against law and its enforcement is the case. Further, the Chinese legal system is typically weak and lacks enforcement and transparency (Dunfee and Warren, 2001). The question now is, what relationship these

⁵ Five traditional relationships exist which are also referred to as wu-lun exist: prince-subject, father-son, older brother-younger brother, husband-wife, friend-friend.

⁶ One of Hofstede’s dimensions of culture is the collectivism vs. individualism dimension.

⁷ E.g. the word guanxixue does not appear in the 1947 edition of the Chinese dictionary „The Sea of Words“(Ci hai), which is similar to the English Oxford dictionary (Yang 1994; 49). Lou (2000; 2) also states that the word guanxi cannot be found in the classic Chinese dictionary “Source of Words” (Ci Yuan) published in 1915.

concepts exhibit. Has the weakness of legal and judicial systems and the lack of its enforcement fostered the use of relationships to solve problems instead? Or have Chinese typically always relied on relationships and therefore never realized the necessity of a well-determined and functioning legal institution?

Three main causes for guanxi as it is known today can be identified. First, guanxi is a concept deeply rooted in Chinese society and a result of thousands of years of feudalism and totalitarian regime. Second, guanxi is identified as a response to the Cultural Revolution and the resulting lack of social order. Finally, guanxi is also said to be caused by the economic reforms and opening of China's doors as this developed the money seeking economy (Yang, 1994: 147). Many authors have claimed that guanxi is not only a cultural phenomenon, inherited in Chinese traditions but rather a result of adaptation to social pressure resulting from influence by the Chinese Communist Party (CCP) (Kipnis, 1997), penetrating all areas of life and all regions of the huge country with its power.

2.5. The relevance of guanxi for business

Current academic research and opinions on the importance of guanxi seem to be in accordance, emphasizing the relevance of guanxi for achieving business success in China (Davies et al., 1995; Yang, 1994; 2002; Yeung and Tung, 1996; Luo, 2000; Lovett, 1999). It seems that without an adequate guanxi network, one is condemned to fail in China. This is particularly relevant for foreigners entering the Chinese market, as they often do not understand the significance and commonness of this phenomenon. The concept of guanxi is not an easy one to comprehend and the lack of comprehension of this profound cultural uniqueness often results in enormous difficulty when doing business in China and, in the long run, often leads to failure. Doing business in China is only possible if an appropriate guanxi network is built up, not only with business partners to secure trade but also with government officials. Here the differentiation between business to business guanxi (B2B) and business to government guanxi (B2G) is drawn, the former focusing on business partners and the latter consisting of relationship building with government official and policy makers.

In the business world, guanxi means “a network of relationships among various parties that work together and support one another” (Fan, 2007). The description of preferential treatment regardless of market rationality pictures a more negative image (Luo and Chen, 1997). Business guanxi can be used in a great variety of ways, accordingly, definitions, description, benefits and pitfalls will vary.

As Chinese society is in general still based on Confucian values such as trust and sincerity, this also influences businesses and managerial processes. Therefore, Chinese generally are only willing to do business with those they trust, respect and know. Trust exhibits such a high significance in this context because business negotiations often only rely on verbal agreements and reputation (face or mianzi) and not on contract (Ramasamy et al., 2006). This is a result of the lack of trust Chinese exhibit towards the traditionally weak legal system, subsequently they have developed their own way of safeguarding them from uncertainties, dealing only with those one has a good relationship with (Kiong and Kee, 1998). As Buttery and Wong (1999) highlighted, the aim is to get to the status of “old friend” based on trust which makes business transactions quick and flexible. Guanxi’s significance was highlighted through numerous studies for instance by Yeung and Tung (1996) who showed that among a list of factors important for long term business success in China, guanxi was the only factor consistently ranked as a key success factor. This importance of guanxi was attributed to the ambiguity and weakness of legal institutions with numerous loopholes left for interpretation.

Consequently, if one wishes to conduct successful business in China, the focus a priori needs to lie on building up and maintaining a sufficient long-term guanxi network as this is a key determinant of firm performance. Without guanxi, it is challenging to find business partners and bureaucratic procedures require an awful long time, the outcome often being unfavourable. Millions of firms are connected through guanxi networks which, to a large extent, determine their performance thus to be confronted with guanxi dynamics is unavoidable. If a firm has managed to establish a rich guanxi network, exercising these connections can make up for other deficiencies the firm faces such as lack of distribution channels, competencies, product quality or marketing experience. The correct implementation of one’s network will result in the achievement of competitive

advantage and assist to expand the firm’s markets resulting in superior firm performance (Luo, 2000: 134).

2.5.1. Establishing guanxi

Guanxi is build up through the exchange of favours and gifts and encompasses the obligation to assist the other upon request without hesitating. According to Pearce and Robinson (2000: 31), members of a guanxi network are “committed to another by an unwritten code. Disregarding this commitment can destroy a business executive’s prestige and social reputation”.

Guanxi is always developed with the intention to last long and can be initiated through gift giving, doing a favour or offering assistance to someone in need. However, as mentioned before, a strong base much facilitates the development of a guanxi relationship. Nevertheless, the intension and interest in a guanxi relationship should clearly be communicated and the creation of a feeling of obligation and indebtedness is desirable in order to activate and continue the guanxi exchange (Ai, 2006). In the business context, the term *guanxi hu* is common referring to firms with an extensive guanxi network. Of course, it is impossible to establish guanxi with everyone, therefore a careful selection of important and powerful connections needs to be made. In order to preserve guanxi, continuous social interaction is required through which reliability and trustworthiness should be communicated. In the business world, dinners, festivities and social gatherings are especially important as this is when negotiations most often take place. Further, such assemblies are ideal to strengthened and extended guanxi networks.

Vanhonacker (2004) suggests four steps involved in the process of building an own guanxi as a businessperson in China: targeting, scouting, signalling and packaging. In the first step, the person with whom a relationship should be built up needs to be identified, considering the possibility and benefits of a long term relation instead of a one-time interaction. Next, the identification of a common base or a trusted intermediary supports the establishment of guanxi. Once these steps have been conducted, signals need to be given to the person with whom guanxi is desirable, preferably through broader social events. Finally, once the

target has received the signal, packaging is the last step however asking for a favour in a straightforward manner is not appropriate therefore one can only hint at what is desired from the target.

Ghuri and Fang (2001) conclude their paper that explained the peculiarity of doing business in China on the basis of the Swedish multinational corporation Ericsson with a few, interesting managerial implications on “Priority, Patience, Price, and People”. Business in China is conducted according to the priorities, plans and policies of the government. Foreign firms need to be aware of these guiding principles for China’s social and economic development and consider them before establishing new business in China. Many businessmen consider patience amongst the most important qualities when doing business in China. Negotiations usually require an awful long time as various organisations, decision makers and departments are involved and bureaucratic decision take long. Additionally, Chinese do not negotiate with everyone, a sense of familiarity, trust, respect and friendship first needs to be established before negotiations are possible which also requires time. Attention needs to be paid to pricing as prices can not be reduced drastically by the foreign firm since this will cause suspicion however, a certain price discount should be allowed as Chinese gain face through this and otherwise would probably feel insulted. A senior Ericsson executive in China once said: “To do things in China you must do people first.” In fact, Chinese are very people oriented and believe in people before contracts, another survival of Confucian values.

The Chinese market is usually entered through joint ventures or through wholly foreign-owned subsidiaries, although joint ventures tend to be preferred. The choice of an adequate and well-established partner with the required skills and connections is essential for the investor. Since the Chinese partner supposedly already has business guanxi connections he can be used as an intermediary (as seen in illustrations of previous chapters), facilitating quick acceptance of the foreign partner into the existing guanxi network of the Chinese colleague which tends to be more efficient than self-initiated acquaintance. The foreign colleague can learn how to cultivate guanxi and use the partner’s country specific knowledge to generate his own guanxi through the Chinese partner’s connections. This relationship with the Chinese entrepreneur can be a valuable base for the

foreigner to assemble his new connections on. The advantages resulting from the joint-venture alternative and hence from better and easier access to influential guanxi are cheap and reliable material supplies, favoured tax treatment, lower land rent, priority in obtaining infrastructural services, market access and support of authorities when needed (Luo, 2000: 176). Joint ventures are an easy way to gain access to the partner's knowledge which can enhance firm performance (Ramasamy et al., 2006). Intermediaries are in addition often hired by firms as advisor or agent to aid with the development of a guanxi network and bridge the gap between personal relationships. If the intermediaries face is valuable this will shed a positive light on the person that wishes a connection, guaranteeing his trustworthiness and sincerity (Yau et al., 2000). However, once a connection has been established, a great amount of time, effort and devotion is needed to keep the guanxi upright and valuable.

Empirical evidence has been found in a study by Luo (1997a) for the above made assumptions. He has shown that market entrance through joint ventures is positively correlated with the use of guanxi and firm performance. Attention needs to be paid to the choice of the local partner as his connections and face (mianzi) within his network will determine future firm performance to a great extend.

2.5.2. Guanxi usage

Chinese society can be considered hierarchical, suggesting that resources are controlled by only by a few powerful players. To these, one should establish guanxi as when resources are scarce they tend to be distributed on the basis of connections and relations rather than official rules (Luo, 2000: 43).

In the time after the Cultural Revolution, simple goods and services that were often in short supply could not or only rarely be purchased without guanxi. Guanxi was also commonly used by ordinary people to obtain access to consumer goods. For instance, certain train tickets were extremely difficult to acquire for “normal” persons without the appropriate connections. Special ticket booths used to exist at train stations for those people buying a ticket with guanxi connections (Yang, 1986: 40). Guanxi acquaintances could also help to obtain better and faster medical care, determined whether one obtained a job assigned that's either near

or far away from ones home or city or received housing which usually was in short supply in urban areas and included long waiting lists. Parents still use their influential connections to get their children into recognized colleges and universities.

Yang (2002) realizes newer developments in the possibilities of guanxi's usage. For instance, acquiring exit permits to leave the country and passports, obtaining loans, attracting overseas Chinese investors and finding prospect job opportunities are all easier tasks when guanxi connections to the responsible counterparts exist. Yang (2002) further emphasizes that guanxi's usage has moved from simple consumer good acquisition to the business and urban-industrial arena where it is common in negotiations between entrepreneurs, entrepreneurs and state managers or entrepreneurs and (local) officials. As consumer goods no longer are characterized by shortage and China has developed into a consumer economy, it is now in business where managers still need to deal with the remains of the state economy in order to obtain permits, favourable tax conditions, loans, valuable market information and many more scarce resources. Today's guanxi is used for a lot more than buying a bicycle, determining over deals worth millions, entry or exit of markets and competition (Seligman, 1999). Since it is used in all aspects of life, an effective guanxi network needs to sufficiently represent all the members of the society, from clerks to cadres (Luo, 2000: 20).

Information is often passed through social connections rather than through other media. In a survey conducted by Pearce and Robinson (2000) a high rank executive recounts that information such as facts and figures is less relevant for Chinese decision making than is guanxi. According to Ramasamy et al. (2006), guanxi can be considered a bridge to knowledge transfer in China. Chinese typically are very suspicious of strangers or out-group members and reluctant to share valuable information with them as this might cause a loss of competitive advantage. In the conducted study, trust and communication crystallized as the important factors enhancing knowledge transfer which are also bases that guanxi is built on. A stranger therefore needs to establish a relationship based on trust or guanxi in order to be considered as an in-group member and obtain relevant information. Guanxi therefore influences the degree of knowledge transfer and the quality of transmitted knowledge as information transferred between guanxi

connections is considered reliable, useful and trustworthy. This again reduces search costs for the receiver and results in more informed decision making (Luo, 1997; Yau et al., 2000).

2.5.3. Distinction between B2B and B2G guanxi

As mentioned, guanxi can either be established between businessmen (B2B) or may involve government official(s) and a businessman (B2G). The distinction between B2B and B2G guanxi is important as the latter (also termed venal guanxi) is the concept mostly considered unethical, unfair and frequently brought into connection with corruption. B2G guanxi is considered as a way to by-pass laws and obtain preferable treatment or privileges as a result of one's special relation to government officials. Fan (2002b) features a definition of business guanxi by the Dictionary of New Words and Phrases (1989: 92), according to which it is defined as “the use of someone's authority to obtain political or economic benefits by unethical persons”.

The establishment of guanxi with government officials is particularly important in China as bureaucratic procedures are rather ill-defined but complex as decision making is stretched out over a great number of officials. Often this includes provincial, local and central government authorities as well as party officials and the army. Further, regulations often vary from place to place. Without connections, achieving one's goals such as obtaining licenses or permits becomes a challenging task and these procedures can take endlessly long and turn out very costly. Guanxi with high government officials will prove to be helpful in many occasions, however, as these connections may involve illegal elements or be considered bribery, trust and a personal guanxi relationship needs to be established beforehand (Arias, 1998). Whereas the Chinese bureaucracy often tremendously slows processes down, guanxi can be a useful way of facilitating processes. Basically, governmental guanxi connections are either used to obtain rare resources or protection. Some possibilities for usage include obtaining business or import-export licences, cheaper or more favourable conditions for bank loans, enter the stock market, authorization of projects, confidential

information, land and other scarce materials as well as securing distribution channels (Fan, 2002b, Hong, 2002).

A study by Xin and Pearce (1996) shows that guanxi is used as a substitute for weak legal frameworks, government and law enforcement, especially by newer, smaller private businesses. Surveying high-ranked executives of various key functional units in different types of enterprises in China, they found that especially smaller, privately-owned companies use guanxi connections to substitute for a lack of institutional support, having more government connections and emphasizing their importance especially concerning protection from threats such as appropriation and extortion compared to state-owned or collective hybrid companies. Su et al. (2003) in accordance with findings of the study by Xin and Pearce (1996) have shown through a survey on purchasing managers of various types of Chinese enterprises⁸ that a significant difference exists between the guanxi orientation of various types of enterprises. Privately owned Chinese enterprises have exhibited the strongest level of guanxi orientation, having most government connections and emphasising their importance the most. This is explained through the assumption that SOEs have direct access to resources whereas privately owned enterprises need to use the “back door” and their relationships to obtain required resources. Also, Millington et al. (2005) showed in a study of UK-owned enterprises in China that the relationships with private Chinese enterprises exhibited more of an association with guanxi than that with SOEs.

A study on Australian expatriates in China showed that the appreciation for guanxi for businessmen depends on the time of operation and experience in China and the size of the organization that one works in. Those expatriates in larger organizations claimed that guanxi has no or little significance for them whereas businessmen in smaller organizations stressed the importance of establishing relationships. This suggests that larger organization automatically have guanxi through their size and international influence whereas smaller organizations need to work hard to obtain guanxi. Because of their economic power, employees of

⁸ The classification of Chinese enterprises was based on Nee's (1992) distinction between state-owned, privately owned, collective-hybrids and joint ventures. For more information see: Nee, V. 1992. Organizational Dynamics of Market Transition: Hybrid Firms, Property Rights, and Mixed Economy in China, Administrative Science Quarterly 31, 1-27.

large, influential organizations therefore do not need to put in the same amount of effort as many business partners desire negotiating with them, regardless of their guanxi. Depending on how long expatriates had been doing business in China (the distinction being between more or less than three years) their views concerning the importance of establishing guanxi varied. Those that had been doing business in China for longer (majority spoke Mandarin) did not stress a need to develop guanxi whereas those that had not been doing business in China for a long time highlighted guanxi's importance and time consuming nature. This suggests that length of service and language skills give guanxi in a similar way as reputation of working for a big multinational (Hutchings and Murray, 2002).

The Chinese legal system traditionally was not well developed as a result of the influence of Marxist theory in China that stresses that law is an offensive device used by capitalists against the working class. Furthermore, the government's central planning policy added to the diminishing significance of contract law. With the opening of the economy and development of a market economy, the government has realized this deficit and has put effort into rebuilding the legal system (Wong et al., 1999). Considering the inherent weakness of the legal system, a lot of room for the interpretation of laws has always been available in China therefore it is not surprising that disputes were often resolved through personal connections. Although numerous regulations and laws have been passed, Chinese still tend to rely upon interpretation. Davies et al. (1995) state that China is an economy based on relationships, not on laws or regulations. McDonald's recognized this when, despite of a 20-year contract, it was evicted from a central building in Beijing because it had not managed to maintain good guanxi with the government (Luo, 2000: 142).

Guanxi should be considered as a form of relationship marketing by foreigners and as a consequence, as a form of investment. Depths are not repaid immediately but sometime in the future when needed, somewhat like an insurance. Through guanxi, abstract credits are established comparable to a credit system of a free market economy. If monetary resources do not suffice (i.e. possibilities), a bank loan or credit (i.e. guanxi connection) can be taken (Chang, 1993). This balance between favours is also known as “guanxi equity” (Fan, 2002b). Through

conducting a favour an investment for the future is made that can be utilized whenever necessary through the principle of reciprocity no matter of what nature it will be (Chang, 1993) This is an, as mentioned, morally binding obligation which could cause a person to loose mianzi or face if not adhered to, a risk few Chinese will be willing to take (Yau et al., 2000).

2.6. The benefits and drawbacks of guanxi

The opinions and arguments about the benefits and drawbacks of guanxi are often found to be inconsistent. Further, aspects that have initially been considered benefits often emerged into hindrances through newer empirical inquiries. Guanxi has been recognized as one of the key factors determining business success by numerous authors (Davies et al., 1995, Luo, 1997a, Tsang 1998). However, guanxi does not only exhibit benefits but a great amount of costs and side effects become involved through its establishment. Fan (2002b) stresses that no clear-cut evidence has been found that could verify the benefits of guanxi for firm performance. The following paragraphs will present a summary of ideas, believes and empirical research on the positive and negative aspects of Chinese business guanxi.

2.6.1. The time perspective

Particularly for foreigners in China, building up a guanxi network is not an easy task. Establishing and maintaining guanxi takes a lot of time, money and effort. In a survey conducted by Pearce and Robinson (2000), a high Chinese executive admits to spending an average of two-thirds of his time cultivating guanxi with important people he meets. Also Luo (2000: 2) mentions that entrepreneurs, managers, officials and even college students spend a substantial amount of their time cultivating and preserving guanxi relationships. Tsang (1998) interviewed managers in the course of his study and highlights a comment of a Chinese manager on a business deal in which he states that it takes years in order to properly establish a good relationship with “them”. This time perspective is of great importance to guanxi establishment as it takes time to develop ganqing which is an essential element of a qualitative guanxi relationship.

Fan (2002b) seems to agree in this regard with his likeminded, stressing Fock and Woo (1998) and Lovett et al. (1999) studies, highlighting the time consuming and expensive process of guanxi establishment. On the one hand, guanxi has the advantage of being relatively flexible, however, the time needed to establish it results in limiting its growth and diversification capacity (Lovett et al., 1999). A great amount of sociability and communication skills are required for guanxi network establishment which can only be constructed through face-to-face interactions in the course of which trust and friendship can be assembled. In order to acquire a sufficient network, many people must be interacted with intensively.

Especially for foreigners in China, guanxi is often even more time consuming as they typically exhibit difficulties in identifying the decision makers needed. On the other hand, Chinese are by nature suspicious of out-group members and foreigners and will take even longer to carefully examine the foreign counterpart before establishing trust, friendship and, somewhere in the long run, business deals. Consequently, business processes can become very slow and wearisome (Fock & Woo, 1998). Another point concerning the time perspective of guanxi has been emphasized by Fan (2002b). It should also be considered that the favour is usually not returned immediately, leaving the participant in an uncertain position of when the future transaction will take place and of which quality and value the returned favour will be.

Nevertheless, whenever arguing on the time perspective, the different attitudes of Chinese compared to Western businessmen need to be taken into consideration. Whereas Western attitudes towards time are based on the ideology “time is money”, a valuable and limited resource one must thoughtfully employ, Chinese unhesitatingly and readily devote most of their time to relationship establishment (Steidlmeier, 1999). What Westerners need to recognize is that “the essential characteristic of a successful relationship in China is the trading of efficiency and autonomy (political or institutional) for personal dependence” (Vanhonacker, 2004).

2.6.2. Guanxi’s competitive advantage

Although developing and sustaining a good guanxi network consumes a lot of time and effort, according to Luo (2000: 139), these marginal costs compared with the marginal benefits of sales are rather low. A powerful and exhaustive guanxi network can save time, improve efficiency and facilitate the attainment of valuable and scarce resources (Fock & Woo, 1998). If a firm has managed to establish a rich guanxi network, exercising these connections can make up for other deficiencies the firm faces such as lack of distribution channels, competencies, product quality or marketing experience (Luo, 2000: 134). Even if its products are not competitive, sales force marketing through personal relationships can lead to successful business outcomes (Luo, 2000: 138). Although this might be very convenient for the favoured firms, in the long run this behaviour will influence competitiveness and market development negatively. Despite, if implied correctly and effectively, guanxi can be a source of sustainable competitive advantage (Tsang, 1998). That “guanxi creates long-term synergies or net economic rents for all participants involved” (Luo, 2002) is commonly believed by many authors.

The establishment of guanxi can be considered a form of social investment or social capital for the future, expanding ones potential and resources (Pearce & Robinson, 2000). Through this strategic alliance between individuals and companies, a general access to resources of all kinds is acquired by its members (Lovett et al., 1999). If managed effectively, this social capital can provide competitive advantage through access to resources, reduction of opportunism and transaction costs, also on global markets through the extension of relationships beyond borders (Hitt et al., 2002). As seen in previous chapters, dealing with the government and bureaucracy in China can be extremely complicated and time intense. Undeniably, guanxi can be an immense benefit in this context, from permission seeking to dealing with the government and obtaining scarce resources or raw materials.

According to Luo (2000: 247), if one maintains good guanxi with the important business players, competitive advantage is achieved in the form of smoothly running business operations, endorsement of governmental authorities and obtaining information on government policies. In order for guanxi to create competitive advantage it needs to be valuable, rare and imperfectly imitable (Tsang,

1998). Established personal relations can be seen as an entry barrier to outsiders and competition as these special relations that require a lot of time, consideration and effort can not easily be imitated (Yau et al., 2000). Nevertheless, especially when considering foreigners in China, insider competition often manages to achieve better and closer guanxi, driving the other foreigner out (Fock & Woo, 1998).

2.6.3. The significance of face and transaction costs

Neglecting ones guanxi obligations can result in the loss of valuable contacts and reputation, the above mentioned “face”. As a result, the quest for future business partners may turn difficult and already established guanxi may vanish. Furthermore, the disreputability will quickly spread through the closely knitted guanxi network and, depending on the connectedness, might pervade to all guanxi. Re-establishing ones reputation and guanxi networks is likely to prove more difficult than initial efforts of guanxi network development. The obtained negative image will keep many Chinese businessmen suspicious and it will take long to regain the trustworthy image once established. Nevertheless, Vanhonacker (2004) claims that Westerners have an advantage when doing business in China since making a mistake such as not fulfilling obligations from guanxi is often excused. As foreigners might not know how to act properly, a few initial mistakes will not cause a loss of face and tend to be dismissed.

The richer and more valuable a person’s guanxi network is, the more mianzi or face they will have and the easier it will be to establish new relationships. Chinese place much emphasis on the social image of a person when it comes to the choice of guanxi partners. Therefore, the more favourable someone’s face is, the more the person will be known as a valuable, respected and worthy business partner and the more people will desire the establishment of guanxi with this person (Tsang, 1998). Transaction cost advantage in form of reduced opportunistic behaviour (Lovett et al., 1999) justifies the implementation of guanxi connections for market exchange (Luo, 2000: 138). As already mentioned, opportunistic behaviour could result in a loss of face and a rejection by all network members. The more connected and richer the network, the quicker will the news about opportunistic

ways of the member spread and opportunistic behaviour with one insider is easily interpreted as opportunistic behaviour with everyone. Therefore, the tighter connected and richer a guanxi network, the more valuable and consequently the less likely one will be willing to risk precious connections and exclusion from the network. The two underlying reasons for this are that one does not want to sacrifice the investment costs that were essential for the network's establishment and that if a connection is detached once due to self-interested behaviour it is almost impossible to re-establish. Therefore a guanxi network itself can be considered as a sort of insurance against opportunistic behaviour which in turn reduces monitoring costs of transactions (Standifird & Marshall, 2000). As a result of the communication of the business partner's reputation, face and character through the guanxi network, transaction costs concerning screening and identifying an appropriate partner are decreased. Constant feedback and information about the partner's behaviour and performance is submitted through the network, further reducing monitoring costs and uncertainty (Standifird & Marshall, 2000).

As a result of basing ones business deals on trust, transaction costs are reduced further as contracting costs do not exist since contracts do not need to be established (Lovett et al., 1999). Because principles of bounded rationality make the establishment of complete contracts impossible, it might as well be wiser to rely on relationships in the first place, saving the time that is needed to set up contracts.

If a valuable face is acquired, guanxi can easily be used as a successful and economic promotional tool to promote an organization and its products often more effectively than through conventional means of advertising (Fan, 2007). Company image and reputation can be drastically influenced through guanxi (Fock & Woo, 1998).

Protection from potential troubles and difficulties is a major driver behind the establishment of guanxi with government officials. As officials are those that enforce governmental regulations, businessmen realized that having good relations with them will yield protection (Hong, 2002). Often, problems are easily resolved through the influential power of a bureaucrat, no matter if it concerns a tax increase or a court dispute (Fan, 2002b). Guanxi can in addition be a source of information on markets and trends, business opportunities and government

policies such as import regulations and restrictions (Fock & Woo, 1998; Davies et al., 1995). Additionally, guanxi connections reduce business partners uncertainty through obtaining more, better and reliable information (Fock & Woo, 1998).

A study conducted by Davies et al. (1995) amongst Chinese and Hong Kong executives, revealed that in general, benefits concerning the smooth operation of routine business, such as payment and transport, were seen as the most important benefits established from guanxi followed by the benefits in securing information on policies and administrative approvals from government officials. Guanxi can reduce transaction costs connected to environmental uncertainties such as communicating, negotiating and coordinating transactions. Attention however needs to be paid to if what has been given in return for the received information does not outweigh the benefits (Fan 2002b).

2.6.4. Guanxi’s side effects

Although guanxi has many benefits for Chinese business life, awareness needs to be paid to the fact that a guanxi connection can become worthless within a very short period of time once the partner loses his status, position or power. The investment provided is then lost and the guanxi connection may even turn into a liability (Tsang, 1998). This is especially significant because guanxi is a highly personal concept established between individuals, it is often difficult to incorporate it into an organisation. When an employee leaves the organisation, valuable guanxi contacts are frequently lost (Tsang, 1998). Managers need to pay attention to this in advance, considering the exercised impact if certain employees leave the company taking their guanxi with them. If appropriate, managers can try to become involved in the relationship as a means of avoiding its loss if the employee desolates.

Through guanxi, vital and scarce resources can be obtained much easier through the favouritism of government officials. However, this often establishes major disadvantages for other business players, stifling competition, not a desirable condition for the development of the economy. Competition becomes unfair, violating the principles of an open market economy.

One final predominant disadvantage is that conducting business through or with the aid of guanxi networks is a costly procedure. Guanxi is reciprocal and favours tend to incline with every transaction. Costs are additionally increased when relying on guanxi connections for conducting business as one commits to a certain degree of risk. As mentioned, the interconnectedness of the guanxi network provides a great amount of information on business partners and any important Chinese businessman will be cautious not to jeopardize his face or reputation. Nevertheless, the seldom reliance on ones personal connection might prove troublesome as a business partner may emerge as unreliable and not comply with his obligation, leaving the other only with a verbal agreement. Accordingly, complete reliance on guanxi connections might be a risky strategy to pursue. This is especially the case when most managerial and financial resources are employed for the cultivation of guanxi networks. In this case, as Fan (2002b) stresses, the expenses in terms of risks are likely to outweigh the potential benefits of guanxi.

As can be seen, guanxi offers a variety of benefits especially in the area of reducing transaction costs from business partner research, information research, reduction of contract and monitoring costs. Regardless of its benefits and drawbacks, guanxi is considered a necessary condition for successful business in China by most authors and sometimes the only way to achieve certain objectives. In order to be able to negotiate in China, guanxi first needs to be established and if that is achieved successfully, business negotiations will follow. Despite its relevance, guanxi alone is not sufficient to achieve business success as emphasis also needs to be placed on competitiveness and efficiency. However, numerous examples are found in literature where a firm's products are chosen regardless of higher price or poorer performance, merely because good guanxi existed between the partners. Nevertheless, as China has become more and more market oriented, the importance of efficiency has increased. However, guanxi can still be considered a mean to enhancing firm performance and reducing costs (Fan, 2002a).

Although the necessity as well as benefits of guanxi have been highlighted, it needs to be kept in mind that all benefits obtained from ones connections are

gained at the expenses of other individuals or firms, disadvantageous to society as a whole and raising ethical concerns. As Fan (2002a) states, social good is sacrificed for personal gains in China through the use of guanxi.

Fan (2002b) raises the question whether guanxi actually reduces or increases uncertainty. As the outcome of the relationship and the returns of the investment are very intangible and unpredictable (Leung et al. 1995), the elaborate investment into guanxi may not be worthwhile. Consequently, one might consider the suggestion made by Tsang (1998) and carry out a cost-benefit analysis before establishing guanxi connections, as the proper realization of this phenomenon requires a great amount of investment.

3. Stock markets and Corporate Governance in China

3.1. Introduction to Corporate Governance

When analysing corporate governance in China, the country's transition from a planned economy to a market economy needs to be taken into account. Corporate Governance in China is becoming a topic of great interest as the country opens up to foreign investment, privatises former SOEs and reduces its influence in some previously completely state controlled industries. With the World Trade Organization membership in 2001, the interest of this topic has further enhanced. The ultimate objective behind the establishment of a capital market by the CSRC was the implementation of a modern, efficient and transparent company management system (Roche, 2005, pg. 51). As part of the transition, numerous SOEs have been restructured under Company Law into joint stock companies to profit from capital invested through initial public offering (IPO). This goal has been realized by over 1200 companies that have been listed at one of either two Chinese stock markets (CFA Institute, 2007).

Generally speaking, corporate governance can be divided into two representative systems, the Anglo-American and the German-Japanese model. China falls into the second category typically exhibiting very concentrated ownership in the hands of the state or institutions (Xu and Wang, 1999). China has adopted the two-tier board system consisting of a board of directors and a supervisory board, creating a business and a monitoring division. The business leadership consists of the

management, the board of directors and the shareholders' meeting. The monitoring leadership contains the party committee, trade union and the supervisory council. The board of directors works closely with the executive management, representing the decision making organ while the supervisory board is independent and monitors the actions of managers and directors (CFA Institute, 2007). The board of directors has authority to appoint CEOs and senior management, call shareholders' meetings, implement resolutions of shareholder meetings, determine internal management systems and undertake necessary decisions (Dahya et al., 2003; Xiao et al., 2004). The required size of the board of directors lies between three to thirteen members while the supervisory board requires a minimum of one to at least three members (for larger companies). The members of the board of directors and supervisory board are appointed by the shareholders, where a supervisory board member cannot hold the position of a CEO, CFO or board of directors simultaneously (Xiao et al., 2004).

“China's stock market is worse than a casino. At least in a casino there are rules” – Wu Jinglian, a famous Chinese economist, 2001 (cited in Liu, 2005). In fact, many rankings provided by organizations (e.g. S&P, CLSA, Asian Development Bank, IMD Switzerland) have shown that China underperforms in the corporate governance aspect, China usually acquiring one of the last positions in a survey of numerous countries. The typical results exhibit poor shareholder protection, usually not taking shareholder interest in the form of value maximisation as a priority and insider trading is widespread (Liu, 2005). Especially minority shareholders are faced with a challenge as this control based model in which the government usually is the controlling shareholder, expropriates them and uses the companies in his best interest. Guanxi along with the continuous influence of the government has an undeniable influence on the impediment of the implementation and adherence to corporate governance codes and regulations.

3.2. Chinese stock exchange

“The Chinese stock market was organized by the government as a vehicle for its SOEs to raise capital and improve operating performance” (Green, 2003, cited in

Liu, 2005). Capital was meant to be raised through the investment of household savings into stock and, as a result of a separation of SOE management and government, efficiency was supposed to be improved (Roche, 2005: 50; Clarke, 2003). Although these goals have been achieved to a certain extent, an absence of major institutional investment has been recognized (Roche, 2005: 50) as one major drawback. The two mainland China stock exchanges are the Shanghai Stock Exchange (SHSE located in the city of Shanghai) and the Shenzhen Stock Exchange (SZSE located in the city of Shenzhen). The Shanghai stock exchange, inaugurated in December 1990, is the largest in mainland China and fifth largest in the world. By the end of 2006, 842 companies were listed on the SHSE (together both stock exchanges list about 1400 companies) and market capitalization reached a total of US\$915 billion.

The Chinese Securities Regulatory Commission (CSRC), an institution of the State Council of the PRC and the main security regulator of the PRC has similar functions to the US Securities and Exchange Commission. Amongst its functions are the establishment of a centralised system for supervision of securities and futures markets as well as the formulation of policies and regulations⁹. The CSRC along with the State Economic and Trade Commission, the Ministry of Finance and the People’s Republic of China are the key decision making organs concerning the law making (Roche, 2005: 52).

Various types of shares exist in the listed firms in China, namely state shares, legal person (institutions) shares and public (individual) shares, of which only public shares can be traded freely whereas state shares and legal person shares are strictly controlled by the state (Liu, 2005; Xu and Wang, 1999) and held by local government and administrative or functional departments (Jing et al., 2005). These shares are all considered A-shares or domestic shares which, until reforms in December 2002 could not be held by foreigners. Through the reform in December 2002, the Qualified Foreign Institutional Investors (QFII) programme was introduced to allow for foreign investment (with limitations) into Chinese securities (A-shares, treasuries, convertible bonds and corporate bonds) (China Corporate Governance Survey, 2007). B-shares are quoted in dollars and may be held by foreigners and, since 2001 by domestic investors.

⁹ <http://www.csrc.gov.cn/n575458/n4001948/n4004898/n4026463/index.html> (07.01.08; 15:11)

Until the end of 2006, the CSRC has arranged for the conversion of non-tradable shares into tradable shares through the Split share structure reforms of listed companies (also called “Administrative Measures on the Split Share Structure Reform of Listed Companies”) and banned non-tradable shares into new initial public offerings (IPOs) which are all supposed to increase shareholder power (Heidrick and Struggles, 2007)

Despite the initial growth of the Chinese stock market, its further development has proven troublesome. Although China’s GDP grew by 53% in the years from 2000 to 2004, the Shanghai and Shenzhen stock indexes fell by more than one third each. In fact, an online survey conducted by sina.com in March 2005 on 25,675 Chinese investors showed that 94.28% had lost money through their investment in the Chinese stock market, whereas 67% had lost more than half of their investment (cited in Liu, 2005). Furthermore, the market capitalization of tradable shares was reduced by one trillion Yuan in the years from 2000 to May 2005 (Liu, 2005).

3.3. Legal framework and Corporate Governance Codes

The improvement of corporate governance regulations to enhance the development of the financial market has been one of the top priorities of the government over the past years. Since the establishment of the CSRC in 1992, approximately 300 guidelines and regulations have been passed to regulate the Chinese securities market (CFA Institute, 2007). Despite the introduction of numerous regulations and laws, many of these are very vague and difficult to interpret which challenges compliance and their enforcement. The weak legal system including lack of law enforcement in China in general has been discussed. This needs to be taken into consideration when analysing the development and implementation of corporate governance codes as these were placed into a legal system where most of the requirements for a well-functioning financial market were missing (i.e. law enforcement, regulatory agencies, well-defined legal system) (CFA Institute, 2007). Nevertheless, in the past years, China has witnessed a great improvement and progress of Corporate Governance partially

due to increased competition and the determination of the central government to improve regulations concerning public companies.

Current corporate governance is based upon key legal frameworks including the Audit Law passed in 1994, Company Law (1994), Commercial Bank Law (1995), People’s Bank of China Law (1995), Securities Law (1998) and Accounting Law (1999) (Roche, 2005: 52). In 2002, the Code of Corporate Governance for Listed Companies was issued, taking a great step into the right direction concerning shareholder protection through the emphasis on credibility and integrity. China’s new Company Law passed with 2006 endows more rights to shareholders and increases standards of conduct and competence for corporate directors. Basic accounting standard for business enterprises (ASBE) based on International Financial Reporting Standards (IFRS) were introduced in the beginning of 2007 with the objective of further developing the market economy, improving the quality of financial information disclosure and enhance investor confidence. Quarterly and annual disclosure requirements have been intensified.

The positive correlation between good corporate governance and firm performance has been proven by numerous studies (Roche, 2005: 245). This influence between good governance equals good management which in turn delivers high shareholder value also further attracts (new) investors. In fact, according to the International Financial Cooperation (IFC), Chinese managers and entrepreneurs realize that improved CG codes lead to higher investment and enhanced firm performance (China Corporate Governance Survey, 2007). “China’s legislators and the CSRC have done an admirable job of establishing a framework for disclosure and shareholder protection” (Roche, 2005: 210). Nevertheless, the key to further improvement of Chinese firm’s profitability lies in well-defining shareholder rights, enforcement and control of codes adhered to, higher transparency through enhanced disclosure and an independent, efficient board of directors. Only clear signalling of effective corporate governance regulations will attract long-term investors.

3.4. Ownership structures, shareholder protection and the effectiveness of boards

3.4.1. Ownership structure and minority shareholders

Corporate governance can be summarized as a set of mechanisms aimed at establishing a balance between the interests of the owners of a company (shareholders) which resembles maximizing company profits, and the requirements of the board and management. Through corporatization, efficiency improvements of management of SOEs were meant to be achieved as a result of separating ownership and control. Managers should be “freed” from bureaucratic interferences (Clarke, 2003) through transferring shares to shareholders other than the state. Nevertheless, the state still controls most of SOEs directly or indirectly through pyramiding. Consequently, corporate governance in China is best characterized as a control-based model. Despite advanced corporatization and decentralization, the state often is the controlling shareholder (i.e. holds more than half of the shares), exerting a great amount of influence to tightly control the firms (Liu, 2005), sometimes even holding up to 80% of a company’s shares (Roche, 2005: 51).

The number of individual shareholders in China is relatively high. However, their share ratios are rather low and the shareholders themselves are very dispersed. The large amount of influence of the state and the lack of power of shareholders results in expropriation and exploitation of minority shareholder. As investors seek long-term profitability upon investment, this continuous unjust treatment of minority shareholders eventually results in a reduction of confidence in the stock market of the public and, as a result, in a reduction of investment. Xu and Wang (1999) found that the average holding period of shares in China is one to two months compared to eighteen months in the United States. Similarly, Roche (2005: 67) states that Chinese do not “buy to hold” but rather “buy to trade”, as stock prices do not reflect actual performance values due to manipulated figures. The aim of new CG codes therefore needs to lie in the improvement of shareholder rights in order to increase trust in the Chinese financial market and attract investors, leading to growth in the long run.

Upon investment, the primary motivation of shareholders lies in the future prospect of an increase in stock market valuation. The government's interest may diverge from that of the smaller shareholders and possibly work against an increase in stock market valuation. Generally, a large disparity between the amount of shares held by the largest and the second largest shareholder exists, leading to neglect of other shareholders by the majority shareholder. The majority shareholder can use its powers and information asymmetries¹⁰ to exploit and take advantage of the company (Roche, 2005: 210).

Liu (2005) mentions results of Tian in his paper according to which, the large shareholders besides the controlling shareholder (i.e. institutional investors, holders of legal person shares), have a positive influence on the firm's market valuation as other large shareholder have adequate motivation and means to monitor the majority shareholder. This concentration in the form of institutional investors is needed for the protection of minority shareholders who have no incentive to monitor on their own, especially in a country like China where the legal protection of minority shareholders is weak due to institutional determinants or historical reasons (Xu and Wang, 1999). Minority investors are hardly represented on the board of directors whereas representatives of legal person shareholders are elected onto the board of directors and supervisory committee. Further, through their representatives on the board, voting powers and the right to call a shareholder meeting can be exercised and institutional investors gain access to corporate inside information (Xu and Wang, 1999). The CFA Institute (2007) also showed that participants believed, through increased QIFF quotas, more foreign institutional investors would be attracted, having a beneficial result on the value of the firm and the economy as a whole, and improving corporate governance.

Monitoring of institutional shareholders will prevent tunnelling¹¹ of the resources to the majority shareholder and increase the value of the company for the remaining shareholders. The fact that market valuation suffers from the state being the controlling shareholder has been shown through various studies (Bai et al., 2004; Xu and Wang, 1999). Xu and Wong (1999) have realized that an increase in legal

¹⁰ Directors and Managers have access to information before minority shareholders do, opening possibilities for falsifying numbers in order to deceive smaller investors and maintaining the possibility of attracting new investors.

¹¹ The term tunnelling is often used to describe the process of expropriation of minority shareholders through the transfer of resources from the firms to controlling shareholders

person shares is positively correlated with profitability of a firm. As a result, they consider the reduction of government shares and consequently its influence as a Pareto improvement. SOEs need to be restructured and the influence of other large shareholders including institutional investors needs to be intensified. Bai et al. (2004) empirically investigated the relationship between governance mechanisms and the market valuation of all publicly listed firms on both stock markets based on the annual reports between 1999 and 2001. They found a positive effect of a high concentration of non-controlling shareholders and the issuing of shares to foreign investors on market valuation. The positive influence of foreign investors could be a consequence of increased and effective monitoring by the more sophisticated outsiders and the increased disclosure and financial transparency required for international listing. Large holdings by the controlling shareholder, the CEO being the chairman or vice chairman of the board of directors and the largest shareholder being the state were all found to have negative effects on market valuation. However, the “Guidelines on the Establishment of a System of Independent Directors in Listed Companies” issued by the CSRC in August 2001 required the independence of at least 2 members of the board of directors by June 2002 and the independence of 33% or 3 members of the board of directors by June 2003 (Roche, 2005: 83).

The foundation of the conflict of interest lies in the separation of management and ownership in corporations which typically results in a Principal-Agent Problem. The owners of the firm, i.e. the shareholders or the principal are in conflict with the agent, i.e. the manager that controls the firm. Managers of firms often use their position and influence in their best interest instead of that of the shareholders who they are agents for. In China, especially minority shareholders are faced with difficulties as the controlling shareholder, (often the state) used its power to its benefit in connection with the management on behalf of the minority shareholders. Internal and external mechanisms are supposed to resolve the principal-agent problem between shareholders and managers and between controlling and minority shareholders (Liu, 2005). Internal mechanism are ownership structures, an independent board of directors, incentive-related executive compensation and financial as well as information disclosure. Examples of external market

mechanisms are appropriate legal frameworks, market competition and effective takeover market (Liu, 2005).

CEOs are often chairman of the board of directors, challenging its independence and effectiveness and limiting the influence board members have on the choice of CEOs. The lack of skilful managers on the market is often blamed as a reason for unifying CEO and chairman of the board by companies. In 74% of SOEs the role of CEO and chairman is separated and relatively many members of the board of directors are outsiders. In fact, according to Heidrick and Struggles (2007), more than 30% of boards now include independent directors often from research institutions or universities, however, these tend to have little or no decision making power and are only used to fulfil legal obligations. Being the controlling shareholder, the state still has great influence over the appointment of influential positions such as CEO, senior management, independent directors and chairman resulting in boards dominated by state representatives (Liu, 2005). Hence, board composition varies depending on whether the enterprise is a SOEs, Private Enterprises (PEs) or Foreign-Invested Enterprises (FIEs) where boards of SOEs tend to be occupied by state bureaucrats and government officials.

As previously mentioned, the supervisory board as an independent organ fulfils a supervisory and monitoring function. Supervisors may be insiders (i.e. work for the company full time) or outsiders. According to their status, a balance between information and independence needs to be found as one is traded for the other. An insider supervisor will likely have superior access to information than an outsider however, independence is substituted in its place. The difficulty of properly informed supervisory board members has been realized by numerous studies. Interviews by Xiao et al. (2004) between 1999 and 2002 among high executives and board members typically showed that the supervisory board rather fulfilled a subordinated advisory role, typically lacking information from the board of directors and management. The greater the independence of the supervisory board members, the more likely they suffered from lack of insider information and were treated as outsiders.

3.5. Influence of the state

The influence of the government has decreased to some extent through economic transformation to a market economy, nevertheless tight control remains over certain industries. In his paper on business ethics, Ip (2003a) calls SOEs giant economic black holes which swallow everything in their paths. Although the transformation of SOEs into corporate entities has to a great extent advanced in the past years, this process does not necessarily include privatisation since the government still holds most of the SOEs shares (Roche, 2005: 146). This “state paternalism” retains the ultimate control in the hands of the government of most stock companies (Child and Tse, 2001), consequently state objectives are being followed (Clarke, 2003).

80% of companies in China are government controlled, i.e. the government being the largest shareholder and as the state holds over 48% of listed companies' shares it is evident that interests of minority shareholders play a secondary role. For the government, the ultimate objective is not value maximisation, although of course an interest in efficiency exists, it is not always the centre of attention. Rather goals such as maintaining urban employment, improving efficiency of SOEs, direct control of sensitive industries, politically motivated job placement or obtaining more capital are of interest. As mentioned in the above principal-agent model, a conflict of interests is created between the state and other shareholders. Because of the influence the government has (i.e. the controlling shareholder, more than 50% of shares), it will follow its goals on behalf of the other (minority) shareholders, reducing the return on their investment on which they are dependent on as investors. Although the actual goal was to reduce the state's influence through the corporatization of companies, the state actually remains in the same amount of control while it has influence over a greater amount of capital which investors have brought in, while the investors themselves remain powerless (Roche, 2005: 147). Liu (2005) states that “concentrated ownership, management friendly boards, inadequate financial disclosure and inactive take-over markets have been the governance norms in China”.

3.5.1. The problem of politics in corporate governance

Most of the listed companies used to be or evolved from state-owned or state-controlled enterprises. Upon public offering, only a relatively low percentage of shares were traded on the market because of market capacity restrictions which resulted in the promoters i.e. the state holding more than 50% of shares (CSRC).

Since the government consequently is frequently the controlling shareholder of Chinese enterprises (in over 80% according to Liu, 2005; Bai et al., 2004) corporate governance becomes a topic closely connected to politics. CEOs are frequently found to be former or current government bureaucrats, which are often appointed through their connection and relationships to powerful government officials. In fact, Fan and Wong (2004) found that within their sample, 28% of CEOs were former or current government bureaucrats. Their research on their sample consisting of 625 firms further showed that in the time period of three years after IPO these politically connected companies underperformed on their average stock market return by 20%. Compared to non-politically connected listed companies they even underperformed by 30%. Also, these politically connected CEOs tend to appoint other bureaucrats to other board positions more frequently, leading to a domination of state representatives on boards, further challenging the firms independence (Liu; 2005). Consequently, board membership is not proportional to ownerships and the state is heavily overrepresented in most boards (Xu and Wang, 1999). “A properly functioning managerial labour market may discipline managers and solve incentive problems caused by the separation between ownership and control” (Xu and Wang, 1999). This functioning labour market however, is rarely found to be the case in China as managers are not appointed due to their skill and know-how but rather based on their relationships with powerful government officials, as it is frequently the government that has ultimate control of companies.

Regardless of the reduction of the government’s influence and the establishment of a market economy, the state is not willing to give up control over certain industries including natural monopolies, national security-related industries, high-technology sectors or goods and services of great importance to the public (Roche, 2005: 146). This refusal of the government to reduce its control in many industries results in the government being both, controlling shareholder and

regulator which has been shown to reduce overall firm performance and severely damage minority shareholders (Liu, 2005). Consequently, SOEs can be seen as little more than state departments adhering to government prescription even falsifying their books in order to be in accordance with governmental demands¹².

3.5.2. Tunnelling in China

Tunnelling can be defined as “actions taken by the controlling shareholder to increase her private benefit at the expense of other shareholders” (Bai et al., 2004). Especially in emerging markets, this concept exhibits particular relevance as inferior corporate governance mechanisms such as lack of independent board members, poor protection of dispersed shareholders, malfunctioning takeover markets and low disclosure quality provide prospects for abuse of controlling shareholders (Liu and Lu, 2004). Liu (2005) states that 78% of listed companies are controlled by some parent company or belong to a group, which again, facilitates the tunnelling of resources.

A number of empirical evidence and real world examples of scandals can be found verifying the actuality and magnitude of this common behaviour amongst controlling shareholders. In 2001 the largest shareholder of Meierya (a then profitable company) colluded with other insiders to embezzle US \$ 44.6 million, 41% of the company’s total equity. Also in 2001, the largest shareholder of Sanjiu Pharma (a one time blue chip in China) extracted US \$ 309.1 million, 96% of the listed company’s total equity. A study by Shanghai based Shenyin and Wangguo Securities Co., Ltd surveyed 130 listed companies and found out that those firm’s controlling shareholders on average own the listed companies US \$ 40 million in the form of accounts receivables or outright parent borrowing (Source: Caijing Magazine, June 5, 1992) (cited in Liu, 2005). Cheung et al.’s (2007) study also highlighted the prevalent expropriation of minority shareholders through the state. Resources are tunnelled out of listed companies from minority shareholders to the state through connected transaction between the listed company and the SOEs shareholder i.e. the state. On average, 45% of the value of these connected

¹² <http://www.ethicalcorp.com/content.asp?ContentID=3440> (08.01.07. 14:20).

transactions is lost. The CSRC agrees that the SEOs owned by central ministries account for the major cases of company's cash exploitation (Roche, 2005: 52).

3.5.3. Pyramiding

Pyramiding is a concept common amongst Chinese enterprises. Listed companies are often majority owned by a holding company of which in turn the government is the controlling shareholder. This although can often include numerous layers of intermediate companies (Fan, 2005). Therefore, the ultimate controller of companies tends to be the government whose interests might diverge from those of the listed company, especially those of minority shareholders. Although the government does not directly hold any shares of the listed companies he controls the company indirectly, giving him the power to have any decisions implemented, even if these exploit the listed companies. The way to solve this problem would be the privatization of the holdings company's ownership (Watanabe, 2002). Most companies, regardless of whether they are state-or-entrepreneur- owned in China are controlled through pyramids.

The control-based government model deeply rooted in China's institutional setting (Liu, 2005) hurts economic and stock market development in China. The government is not efficiently using its influence in connection to the management of companies but rather this type of ownership often inhibits the development of functioning and profitable corporate governance systems (Roche, 2005: 51). Yet worse, through a deficit of enforcement and minority shareholder protection, resources are tunnelled out of SOEs through state shareholders which despite of corporatization frequently remain the controlling shareholder (Clarke, 2003). Low business ethics, weak legal systems and enforcement and managerial opportunism are the main cause for low standard of corporate governance (Jing et al., 2005).

4. The influence of guanxi on Corporate Governance

The challenge that has arisen through corporatization is the separation between ownership and management. Shareholders that now own the firm have a right to its profits which are frequently used by managers and controlling shareholders to

obtain benefits through guanxi connections. During the liberalization of Chinese enterprise ownership through stock issuing, Chinese enterprises received a great amount of monetary inflow which managers often invested into other, frequently inefficient firms in the area instead of using it as investment for their company. These investments into other firms were often influenced by the government, who pursued its own goals such as maintaining employment, which resulted in a loss of money that could have been used for productive investment by the issuing firm (Dunfee and Warren, 2001).

4.1. The selection of board members

It is common for board of directors members to be elected according to their relationship with the majority shareholder, not their skills. For instance, in SOEs where the controlling shareholder is the state, the CEO and board members tend to be former or current government officials chosen on the basis of their guanxi to government officials. In fact, Heidrick and Struggles (2007) see Figure 3 below; have shown that 66% of board of directors member selection is based on close ties with majority shareholders and the chairman. The better someone’s relationship to majority shareholders or chairman of the board, the more likely he or she will be elected onto the board. The selection of board members tend to be made based on relations or guanxi instead of know-how and skill.

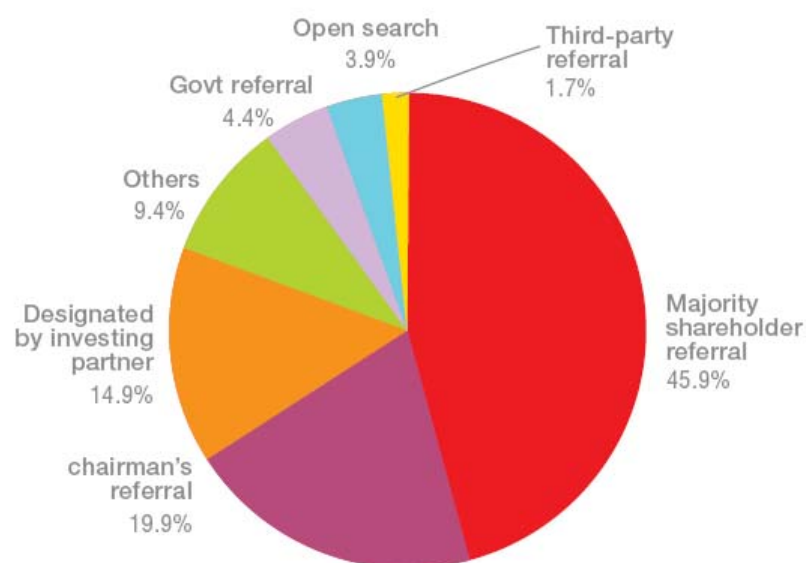


Figure 3: Board Members Recommendation, Heidrick and Struggles (2007)

Through this selection of board members and CEOs and following, the under representation of minority shareholders, future investment potential is severely harmed. Trust of foreign investors in the Chinese financial market dwindles, suppressing China’s growth potential. Corporate Governance Codes need to, amongst other factors, focus on well-defining shareholder rights in order to regain confidence of domestic and foreign investors.

4.2. The role of disclosure

Disclosure is essential for informed decision making of investors, a fundamental necessity of good corporate governance. Further, honest disclosure facilitates the attainment of investor confidence and as a result increases capital opportunities. Nevertheless, a distinction between material information (i.e. information that has the potential to influence investor decision making) (Roche, 2005: 173) and less important information needs to be drawn, good disclosure focusing on material information as to avoid information overload of investors.

The already mentioned regulations on information disclosure in particular of financial nature and the introduction of uniform accounting standards in the beginning of 2007 known as Accounting Standards for Business Enterprises has assisted the increment of transparency and improvement of disclosure through increasing pressure on management (Heidrick and Struggles, 2007). Especially because pyramiding enjoys such great significance in China, whose complexity makes it easy to tunnel resources out SOEs, financial information becomes necessary for investors in order to get a clear picture of what is happening to their investment. High transparency levels and appropriate disclosure of related party transactions are vital to reduce tunnelling. According to Hong (2002), due to fraudulent accounting practices books do not reflect performance of companies and transparency is still very low (Liu, 2005).

Chinese listed companies’ annual reports are required by the CSRC to include a supervisory board report. The usefulness of the supervisory board report depends largely on the usefulness of the function the supervisory board has adopted in the public company. Depending on whether the supervisory board is desirably an independent supervisory organ over the management or not, the usefulness of the

supervisory board report will vary. If the supervisory board is merely an “honoured guest”, a “friendly advisory” or a “censored watchdog”, all of which are heavily dependent on the CEO or the board of directors, have little or no expertise and thus almost no monitoring or actual supervisory powers, the usefulness of the supervisory board report is likely to suffer. If however, the supervisory board can be identified as an “independent watchdog”, fulfilling the function of monitoring and supervising independently and effectively, the supervisory board’s usefulness is likely to be reflected and transferred to the supervisory board report. The independence of supervisory boards is common amongst companies predominantly issuing B-shares, H-shares or that are listed in foreign exchanges, as they are confronted with stricter auditing and monitoring. Therefore, the improvement of the supervisory board report requires an underlying melioration of supervisory boards function, competence and independence (Dahya et al., 2003).

4.3. The problem of enforcement

Numerous regulations and codes have been issued attempting to improve corporate governance practices in China. Consequently, the problem cannot only lie in the laws themselves but rather in their enforcement. According to Roche (2005: 257) “regular inspections, ad hoc inspections, fraud task force, independent scrutiny, active international investment with vigorous shareholders, a lively investigative media unhampered by state control and censorship, and guarantees of severe punishment for offences coupled with a high clear-up rate” are a precondition for successful compliance to corporate governance regulations. The factor corruption needs to somehow be debarred in order to ensure compliance. As can be seen in European and US scandals such as Parmalat and Enron respectively, even if the appropriate enforcement mechanisms are in place, compliance is often not secured resulting in the creation of scandals and corruption affairs.

A major issue constituting to the challenge of enforcement is that in order for the CSRC and other regulatory organs to monitor all listed companies efficiently, a drastic increase in monetary and human resources would be needed. The costs of these additional investments into CSRC resources compared to the costs of

weaker corporate governance systems need to be outweighed and compared, especially to much more urgently needed investments (e.g. health care, infrastructure) (Roche, 2005: 258). Further, the CSRC has too much responsibility; it is not only responsible for IPO but also for monitoring and de-listing firms if their performance is not adequate. Jing et al. (2005) suggest giving responsibility for listing to the stock markets themselves which would improve performance as stock markets would have an initiative to monitor and attract valuable companies.

5. The interrelation between corruption and guanxi

5.1. Introduction to corruption in China

Definitions of corruption vary depending on the context but “there is consensus that corruption refers to acts in which the power of public office is used for personal gain in a manner that contravenes the rules of the game” (Jain, 2001). Corruption in China is prevalent in the public sector amongst government officials as well as in the private sector (Hoenig, 2006). The cadre’s goals through behaving corruptly lie in achieving their personal aims or benefits while fulfilling their mutual obligations and avoiding state regulations. The reason for this behaviour is at least partially due to income discrepancies between bureaucrats and businessmen (Chang, 1993). As a result of the large amount of bureaucrats living on a limited fiscal budget, bureaucratic income was typically low although still higher than that of most other work groups (Luo, 2000: 209). This low income became a problem as a result of economic development after the 1980s, when the discrepancy between bureaucrats’ salary and other income groups increased and government officials became one of the poorest groups in the country (Luo, 2000: 209). Additionally, they also lost their feeling for superiority and their privileges, businessmen now often enjoying higher living standards (Hong, 2002).

At the heart of Chinese corruption lies the problematic phenomenon of guanxi, causing rampant nepotism through the admission of favours and privileges. The Chinese tradition of rule by man instead of by law highlights the crucial importance of establishing good connections also with high government officials. Especially at times of the Cultural Revolution and the Big Leap Forward were these connections a necessary precondition for survival. However, as previously mentioned, the way

these connections are used has changed over time and new fields of application have been identified.

Luo (2000: 92) suggests that corruption might be a result of weak institutional protection of business. Yao (2002) argues with the support of numerous scholars and economists that the core of current Chinese corruption is caused by the government's struggles against loss of control over certain industries and procedures while at the same time opening the economy. Through this lack of separation between business and government, the government retains the role of the leading actor concerning the allocation of resources, placing officials at the centre of the market and enabling them to draw profits out of companies into their own pockets (cited in Yao 2002, reference to BBC News 13.09.00). Consequently, China's received Corruption Perception Index (CPI) score of 3.4¹³ in 2004 does seem surprising.

5.2. The interrelationship between guanxi and corruption

5.2.1. Two different concepts by nature

Guanxi is distinctive from bribery in that renqing, trust and friendship, which are essential elements of guanxi, cannot be bought. Guanxi is a personal relationship deeply rooted on the principles of trust, friendship, reciprocity and indebtedness. As Vanhonacker (2004) argues in his paper, guanxi is different from corruption because it is relation-focused whereas corruption is transaction-focused. Yang (1994) also stresses that in bribery, loss-gain calculation is of much greater relevance than in guanxi relationships. Furthermore, morality, a concept central to guanxi is more than stressed or challenged through corrupt behaviour which destroys human values (Vanhonacker 2004, Luo 2002: 201). Another primary disparity is that whereas guanxi is oriented to create long term synergies and tends to be used repeatedly without time specification concerning reciprocity, bribery is immediate requiring timeliness and is frequently merely a one term transaction. Further, guanxi's reciprocity is not necessarily equivalent and only

¹³ Source: www.transparency.org, 29.12.07, 00:52.

The Corruption Perception Index (CPI) Score relates to perceptions of the degree of corruption as seen by business people and country analysts and ranges between 10 (highly clean) and 0 (highly corrupt).

socially binding, i.e. a lack of accomplishing guanxi duties only has social consequences.

Guanxi is considered a complement to contract law, bridging gaps of legal institutions when necessary while corrupt activity violates laws, consequently is illegal and therefore involves a high amount of risk and uncertainty (Luo, 2000: 199-201). As these two diverse concepts have similar means of execution (e.g. gift giving) (Luo, 2000: 200) guanxi can easily be used as a tool to hide corrupt behaviour (Vanhonacker, 2004) or disguise bribery (Lovett et al., 1999). Consequently, guanxi can also be seen as a protection for corrupt actors from punishment for their illegal behaviour (Luo, 2000: 209).

Guanxi is meant to ease social and economic exchanges through favour exchange, on the other hand, corrupt exchanges are usually of monetary nature (Luo, 2000: 200). Whereas it has been illustrated that guanxi is to a certain degree transferable through the utilization of intermediaries, corruption typically remains hidden between a determined number of individuals, i.e. as a result of its risky nature the fewer know about it the better (Luo, 2000: 202). Guthrie (1998) draws the borderline between guanxi and corruption in the following way. The distinction is defined as “establishing good business relations” and “using social relations to take care of situations” where the former is a prevalent part of business conduct and the latter is considered corrupt. The challenge, especially for international companies is to distinguish good from bad guanxi (Fan, 2000b; Vanhonacker, 2004).

I have raised the question concerning guanxi’s roots, whether it is a phenomenon deeply rooted in Chinese society or has developed out of a necessity at times of the Great Leap Forward and the Cultural Revolution or through the opening of the Chinese economy in combination with the state’s reluctance to release control over certain industries and enterprises.

Although a definite answer could not be given, it has been shown that guanxi’s basic values are deeply rooted in the Chinese culture and are in accordance with or a remainder of Confucian teachings. Consequently, the Chinese traditions of relying on relationships and the accentuation of the rule by man instead of the rule by law can be considered the socially accepted source/ spring of corrupt behaviour

and practices. Luo (2000: 209) states that through social chaos China has experienced in the past, the imperial government become less and less trustworthy, leading people to rely on their relationships to achieve their ambitions, regardless of what kind.

Yao (2002) addresses Mao’s responsibility for the creation of the political system (Chinese Communist Party) responsible for China’s corruption problems, a system that grants and protects privileges. Accordingly, Sun (2004) claims that recent corruption problems can be traced back to post-Mao reforms, further activated by economic incentives and structural opportunities in the emerging market place. Guanxi basically is favouring persons depending on their relationships, i.e. as Yao (2002) would call it, privileging, which is the core of the corruption problem in China, causing social unfairness and economic inefficiency.

5.2.2. Gift-giving

Although not essential for relationship establishment, gift-giving is an undeniable part of the guanxi building process and of Chinese tradition, communicating good will and respect (Luo, 2000: 28). However, Western businessmen often do not understand how to use this concept and what needs to be achieved in terms of contacts and relationships before hand. Steidlmeier (1999) identifies this component of the lesson foreigners need to learn concerning business processes in China the most difficult one. Whether gift exchange is considered bribery depends on the objective of the gift giver, the type of exchange and the time perspective (for instance, gifts are often given on occasion such as New Year or the birth of a child). Gift giving remains secondary though, in first place stands the pre-existing relationship between the participants (Luo, 2000: 29). Foreigners often overemphasized the gift giving element which can easily be interpreted as attempted corruption or bribery by the Chinese counterpart (Standifird & Marshall, 2000). On the other hand, gift giving which is used as a way to nurture and strengthen relationships, increasing trust and conveying respect to one another by Chinese (Steidlmeier, 1999) is often immediately construed as bribery by foreigners that are not familiar with the processes and occasions of gift giving.

However, many authors have argued that Chinese are well aware of the thin borderline between the two and the fine differences.

In a study of 49 UK-owned manufacturing companies and their relations to their local component suppliers, Millington et al. (2005) realized that gift-giving was often brought into relation with corruption, bribery and illicit payments. However, such illicit payments are not associated with guanxi and companies realize the difference between gift-giving in connection with guanxi relationship to strengthen the bond and trust and on the other hand, illicit payments which are based on personal gain motives.

5.2.3. Corruption, guanxi and business

Through the establishment of relation-based business practices, the borderline between guanxi and corruption, in particular between guanxi related gift giving and bribery has blurred. Although the concepts are based on completely different values, might guanxi not induce corruption or even lead the way into corrupt practices? Guanxi may be based on completely respectable and honourable values but it is implemented based upon self-interest and motivated through the gain from social relationships. One might therefore consider guanxi the origin or at least a trigger for corrupt behaviour in China. Although there are differences, the underlying motivation needs to be considered, i.e. is a gift really given out of friendship and reciprocity or is it merely used to conceal an act of bribery or corruption.

High ranked officials bribe each other with the resources that have been allocated to them based on their position and accordingly, privileges. In order for “normal” people to do business with them, frequently horrendously costly bribes are necessary with which one must comply in order to achieve ones goals (such as obtaining permits or licenses). Yao (2002) makes a particularly interesting comment when he claims that they have become price searches, demanding higher and higher bribes for doing business with ordinary people and that the privileged have learned the two-part tariff of a monopolist.

Su and Littlefield (2001) highlight the problem of a hybrid socialist market economy which has developed in China through economic reforms in the late 1970s,

representing a dual system not only for the exchange of goods for goods but also power for goods. In fact, many authors believe that these economic reforms and the emergence of capitalism are responsible for an increment in the usage of guanxi and consequently, bribery and corruption (e.g. Yang, 1994, Luo, 2000: 208). Still others argue that such economically underdeveloped, gift-giving societies with scarce resources need to accept corruption as a by-product of political and economical modernization. Unavoidably, structural transformation provides loopholes for corruption (Luo, 2000: 207; Chang, 1993).

Relatively few influential government officials control the state property or public good and its distribution, themselves unjustly receiving most of it and considering corruption as a source of income (Luo, 2000: 207). The ordinary public is only left with the possibility of establishing good guanxi with powerful officials in order to receive at least a part of their share of the public good. Following, guanxi, more precisely rent-seeking guanxi, has become synonymous with corruption in China's imperfect market conditions (Su and Littlefield, 2001). Resources are allocated below market equilibrium prices through powerful officials. Sometimes companies are even blackmailed into guanxi based corruption. In such cases the responsible government officials with which one has guanxi demand high bribes (or “gifts”) for a company to retain its permits or further receive valuable resources (Fan, 2002b). As Yao (2002) states, unless privileges granted and protected by the Chinese Communist Party are eliminated, China will never dispose of its corruption problem. Unethical guanxi-based conduct, the core of the problem, needs to be abolished (Fan, 2002b). Further, powerful cadres that have monopoly position over scarce resources create a bottle-neck situation which allows them to use their position to generate profits for themselves. Cadres further establish networks of relationships to advance their power through connections with other cadres (Chang, 1993). Although the concept of guanxi as a special form of relationship has existed for centuries and is deeply rooted in Confucian teachings the concept of guanxi as it is known today, a way to use one's personal relationships in order to obtain certain economic or political privileges is a relatively new concept which at least to a certain extend was triggered through the political and social developments in China and the consequently weak market structure, lack of legal

systems and enforcement, absence of political opposition, media scrutiny and transparency.

According to Fan (2002b), corrupted guanxi and guanxi-based corruption are inseparable, business guanxi always involving (at least some degree of) corruption and there is no corrupt behaviour without the use of guanxi.

Money ← Guanxi → Power → Corruption

According to this relationship above, guanxi connects the two parties, acting as a matchmaker (Fan, 2002b). The guanxi relationship between businessmen and individuals results in the exchange between money and power, also known as venal guanxi (Jing et al., 2005). Businessmen only have money which they trade for the power officials have to offer.

Anti-corruption codes passed by foreign countries tend to prohibit gift giving by enterprises completely, also when conducting business abroad. These regulations, however, pose a difficulty for foreign businesses in China as they ignore the Chinese customs and business practices (Steidlmeier, 1999), for instance, through the Foreign Corrupt Practice Act (FCPA), US firms might lose significant business opportunities (Norton, 2006). In general, foreign companies adhering to such imposed anti-corruption codes would then clearly be facing a competitive disadvantage. Nevertheless, the abolishment of favouritism through relations and gift giving, the core of China’s corruption problem, is essential. However, it needs to be fought simultaneously at all ends in order to achieve adherence by all parties.

5.3. The connection between Corporate Governance and corruption

From an economic macro level view, some corruption might be considered as good because policy makers do not always imply regulations that are Pareto optimal, corruption then moving the partial equilibrium towards Pareto optimality. If regulations however are optimal, corruption will not be good and move the market away from Pareto optimality. These assumptions however clearly demand a (too) high amount of rationality from actors (Luo, 2000: 211). Further, scholars have

argued that corrupt behaviour might to some extent be useful as it overcomes inefficiencies, resembling “grease for the wheels of China’s economy” whereas others argue that this grease creates a “slippery road to nepotism and lost opportunities” (Luo, 2000: 207-211).

The central issue of corporate governance in relation to corruption is the usage of investors’ money for inadequate purposes. Frequently, management diverts money from state and company accounts into their own pockets or uses it in their own interest for instance for travelling abroad on “business trips” (Roche, 2005: 53). (Cited in Roche 2005: 62) Laura Cha, Vice Chairman, CSRC, said in 2001: “Some recent cases in China show that some controlling shareholders have all along used their listed companies as their own little ATM machines. When this is discovered, they say they cannot repay, so it is the listed company that suffers.”

What needs to be taken into consideration when looking at bribery is not only that it is illegal and risky but also that it is expensive. Gift-giving, bribes, commissions or gratuity all require monetary assets, money that actually does not belong to managers that use it to get their will but to shareholders, the owners of the company. As mentioned, also tunnelling through the controlling shareholder is an issue in Chinese SOEs.

Another concern that additionally intensifies the principal-agent problem between shareholders and managers is that manager earnings on shares are fixed at high levels, regardless of performance, yielding dividends to managers even if firms are operated at a loss (Sun, 2004: 94). Sun (2004: 94) also highlights the growing opportunity to embezzle money through the issuing of SEOs shares, not complying with state regulations or market mechanisms. The majority of shares are split between the management, whereas some are given to officials in state agencies as “gifts” to buy their silence in case of irregularities. Often, employees are forced into buying shares through threats of dismissal if they do not abide, the money then used by management in its own interest. Management styles remain the same after the issuing of shares as employees do not participate in shareholder meetings.

Sun (2004: 94) illustrates an example of how four high executives (head of board of directors, CEO and two deputy CEOs) of the Dongguo Shareholding Group, Inc. (East Boiler), a large SOE, decided to use the prosperous performance of their enterprise in 1996 for their own benefit, dividing 1.32 million shares of IPOs between themselves, paying for the shares only after they had been sold on the market. Each executive earned over 2 million Y. Two of them had to face a life sentence whereas the other two were punished with a death sentence.

Often shareholding companies (typically corporatized SOEs) have the problem of one individual holding all the trivial management and controlling positions, responsible for all the corporate governance issues of a company. This leaves the manager all possibilities for fraud, without having to bother about internal control (Hoenig, 2006). Managers have gained almost ultimate control over personnel appointment decisions, leading to kinship appointment being a frequent sight. Job placement then tends to be largely influenced through ones guanxi connections, often more than through ones expertise. Placing relatives into positions such as accountancy and supervision leads to further potential of firm exploitation without notice from outside. As Sun (2004: 95) states, books are kept according to management instructions, not according to receipts, making valuable supervision and monitoring of firm assets almost impossible. Additionally, shareholders are often employees of the company, which reduces the likelihood of them raising their voice in the shareholders' meeting as they are threatened through layoffs (Sun, 2004: 162).

Corporate governance is an important factor for the functioning of a transition economy's financial market, necessary for an efficient allocation of resources and consequently for economic growth. The well-functioning and efficient financial market then further promotes good corporate governance practices (Roche, 2005: 42).

“A society dominated by corruption cannot hope to achieve high standards of corporate governance” (Roche, 2005: 257). On the other hand, Roche (2005: 17) also cites that low corporate governance breeds corruption. This suggests an interrelationship between the two: low corporate governance on the one hand might enhance corruption while on the other hand, high corruption prevents corporate governance codes adherence. The competitive environment that

surrounds private enterprises where the mobility and transferability of resources is given, corruption can be restricted which however is not the case in state enterprises as corruption can hardly be influenced through competition (Luo, 2000: 207). Business ethical standards in China are too low to ensure fair and effective transactions which leads to costs of illicit behaviour outweighing the benefits, highlighting the necessity of a stable legal system and enforcement of corporate governance codes (Jing et al., 2005)

Negative guanxi causes inefficiency and a reduction of growth through jeopardizing private sector investment (Luo, 2000: 200) and can seriously damage corporate reputation (Fan, 2007).

5.3.1. Examples

Scandals in China's public companies and amongst high ranking officials are numerous, some already have been mentioned in previous chapters. Often, the poor corporate governance of the firms involved has been emphasized and blamed to have left certain room for the corrupt behaviour. However, these scandals have also had an influence within the improvement and promotion of corporate governance in China. Investors have exerted their pressure on the demand for better corporate governance and new reforms, hoping to secure their investment through closer monitoring. Frequently, death sentences are imposed on the involved officials, a clear and strong signal that China is determined to diminish corruption and fraud and regain investor's confidence.

Especially in the drug and food industry¹⁴, scandals have been rampant¹⁴. The former head of the Food and Drug Administration Zheng Xiaoyu was sentenced to death in May 2007 for accepting bribes worth \$850,000 from various pharmaceutical companies to aid them with the approvals. As the New York Times stated in July 2007, he and his family accepted “gifts” and bribes in return for such favours. He was accused by the government of approving 227 medicines in return for bribes out of which six were forged. In July 2007, Cao Wenzhuang who was responsible for drug registration approvals at the State Food and Drug

¹⁴ http://www.breitbart.com/article.php?id=D8PAHT0G2&show_article=1&cat=0
<http://www.nytimes.com/2007/06/02/us/02toothpaste.html> (05.01.08, 12:16)
<http://www.nytimes.com/2007/07/07/business/worldbusiness/07drug.html> (08.01.08, 17:32)

Administration until 2005 was sentenced to death for accepting bribes worth \$ 300,000 from two pharmaceutical companies. Both cases clearly harmed the credibility of the government and hurt the image of the Food and Drug Administration, an institution founded to protect consumers from unsafe medication now has adopted the picture of a corrupt and crooked organisation that can easily be bribed into approvals, resulting in the damage and death of Chinese.

The toothpaste scandal in June 2007 where toothpaste that had been spread around the world was found to contain poisonous diethylene glycol (which killed 200 people in Haiti and Panama) as well as a great recall of pet food triggered through Chinese exported pet food ingredients contaminated with industrial chemicals and the recent Mattel recall of toys made in China which were covered with lead paint further damaged China's image and that of its products.

The examples of corruption scandals in connection with government officials are endless. For instance, the Premier Wen Jiabao's son Wen Yunsong was accused by the 21st Century Economic Report, a newspaper based in Guangdong province and owned by a Shanghai entrepreneur to have taken about \$ 900 million in shares under a false ID. A number of officials were involved in this bribery scandal which was meant to facilitate listing of China's second largest insurance company and to avoid regulations that limit foreign ownership to 50%¹⁵. Zhou Zhengyi a property developer who used to be ranked the 11th richest man in China was arrested for bribery and forging value added tax receipts early 2007. Corruption in China is considered one of the greatest threats to the nation's economic and political stability and costs China about \$86 billion every year¹⁶. All big corruption cases and organised crimes are traced down to guanxi (Fan, 2002a).

5.4. Ethics of Chinese business practices and guanxi

“Seen as one of the forms of “Asian values” contributing to the abuses of crony capitalism, guanxi is both righteously condemned and reluctantly accepted as an unfortunate, though necessary, evil for those wishing to succeed in business in China” (Dunfee and Warren, 2001). As B2G guanxi has become a synonymous for

¹⁵ <http://www.wsws.org/articles/2004/aug2004/chin-a03.shtml> (06.01.08, 10:30)

¹⁶ Carnegie Endowment for International Peace stated in <http://chinadigitaltimes.net/tag/Zhou+Zhengyi> (06.01.08, 11:23)

bribery, corruption, fraud and nepotism all of which describe unethical behaviour, accordingly guanxi must raise ethical concerns (Su et al., 2003). Even if not ultimately connected to illicit behaviour, through guanxi outsiders are excluded and discriminated, which is unfair and unethical.

When analysing the ethics of guanxi, the differentiation between various categories of guanxi (e.g. family, helper and business guanxi) is fundamental. Whereas guanxi between persons for private purposes (e.g. family and helper guanxi) is usually considered morally unquestionable, business guanxi is considered bad and unethical, often resulting in unfair competition, nepotism and fraud (Fan, 2002b).

Concerning the ethics of guanxi networking for business it is important to consider the diverging views between Western and Chinese societies on what is regarded as ethical or unethical. Often, the favouring of one business partner over the other by Chinese based on guanxi contact will be considered as unfair and unethical by Western partners (Lovett et al., 1999). This is due to the differences in values the societies built their opinions about ethics on. Western ethics are founded on the basis of equality and fairness which is resembled in the principles for perfect competition, namely equal opportunities, access to trading partners, information and factors of production (Luo, 1997). Chinese however have a different perception about certain aspects of ethics. Concerning business, they believe that it is more important and fair to establish a relationship and trust first. Through this, respect for the trading partner is generated which is essential for successful business transactions and the keeping of one's promise. Western focus however, lies on the contractual obligation and on performance. Why should Chinese ethics then be worth less or not as moral as Western ethics? “Westerners see guanxi as “using” others, which according to Western morality is unethical” (Vanhonacker, 2004). However, in Chinese eyes, as long as you repay your debt or obligation in an adequate and considering form sometime in the future, this behaviour is anything but unethical. Through this network of relationships in which each person takes a distinctive role, the “use” of other people is, under Confucius, considered to help in achieving social harmony through caring and respecting others.

As especially business guanxi between businessmen and government officials is often undeniably linked to corrupt activities it is no surprise that current B2G

business practices are considered unethical and unacceptable by Chinese ethical standards. Even if the special treatment is not de facto breaking the law, the preferential treatment of some and not of others is unfair and unethical and triggers corrupt behaviour. As mentioned, B2G guanxi is either used to gain valuable but rare resources or protection. Either one permits a special treatment of an insider on the expenses of the general public. The distribution of resources on the basis of relationships is not only unfair and unethical but also refuses the adherence to basic principals of open market economy and competition. Protection, be it from tax increases, court disputes or other provides immunity to certain individuals and positions them above the law. Again, the interest of the general public and social well-being is sacrificed for a few.

“The downside of this pervasive guanxi phenomenon is rampant nepotism which compromises justice and fairness. Ethics based on guanxi is arbitrary and capricious” (Ip, 2003a). Guanxi constitutes privileging certain individuals and taking advantage of others. Those that are not privileged, for instance through their connections to the party, state, influential parents, etc., i.e. the normal people, are found left aside and exploited. The privileged use their monopoly power to exploit the ordinary people’s wealth (Yao, 2002). Through the establishment of a deal between them they place their interests above those of other people acting to other’s disadvantage. There is no need to raise the question of ethics in this context, as it is clear that such behaviour is unfair and causes social unrest. Many different types of guanxi exist, their effect having varying influences on Chinese economy and efficiency. One needs to also take the ordinary Chinese into account and pay attention to their well-being (Dunfee and Warren, 2001). Only if no third party, known or unknown, is in any way disadvantaged through the use of guanxi can the action be considered ethical (Fan, 2002b).

6. Corruption and guanxi in Singapore, Taiwan and Hong Kong

Although guanxi is a common phenomenon through many Asian countries, its significance, the way it has established itself and is dealt with varies. As guanxi is a concept typical to Chinese culture, other Confucian countries besides the Peoples Republic of China must also be confronted with the notion of guanxi.

75.2 % of Singapore citizens are Chinese¹⁷ and although the country is multi-religious, 51% practice Buddhism or Taoism. 98% of Taiwanese (also known as The Republic of China) citizens are of Han Chinese ethnicity, consequently conducting business in Taiwan is often considered as dependent on guanxi as business conduct in mainland China. As has been explained, these gift-giving (with the thin borderline between gift-giving and bribery) and networking cultures often resemble a breeding ground for corruption (Luo, 2002).

Nevertheless, Singapore is considered the least corrupt country in Asia and always found amongst the ten least corrupt countries in the world on the Transparency International's Corruption Perception Index. The 2007 Corruption Perceptions Index ranked Singapore the fourth (9.3) least corrupt country worldwide, Taiwan received 35th (5.7) place whereas China only scored 72nd (3.5)¹⁸. These countries are all in a sense Chinese and consequently, are confronted with guanxi as a remainder of Confucianism to some extent. Consequently, assuming that these countries are all confronted with the phenomenon of guanxi and that guanxi triggers and raises corruption then why is China so much more corrupt compared to other, similar countries such as Singapore and Taiwan?

Singapore, China and Hong Kong are all found to cultivate personal relationships and tender favours to preserve and support guanxi establishment. However, Chinese highlight group identification and emotional investment more than the Singapore and Hong Kong counterparts (Tang). Nevertheless, authors have often argued that with the development of legal institutions, the relevance of guanxi decreases, looking at the well-established legal systems of Singapore or Hong Kong in comparison to China (Tsang, 1998). It is often argued that the concept of guanxi used to be important in other Confucian societies, e.g. Singapore and Taiwan, but its significance has decreased with market development¹⁹.

According to Quah (1999), the degree of corruption in a country depends on the skills of the government to identify causes for corruption and implement effective measures to reduce such behaviour to a minimum. Corruption is triggered if low

¹⁷ <http://en.wikipedia.org/wiki/Singapore#Population> (05.02.08, 13:18)

¹⁸ <http://www.icgg.org> (04.02.08, 15:32) Scores range from 1 (most corrupt) to 10 (no corruption)

¹⁹ <http://www.diligencechina.com/blog/?p=78> (04.02.08, 11:48)

salaries are received, opportunities for corrupt behaviour are provided and the probability of getting caught is low or even if one is caught, the punishment is not severe. Consequently, in order for corruption to be reduced to a minimum these conditions need to be set at an optimal level, i.e. salaries need to be adequate, opportunities for corrupt behaviour need to be diminished and the probability of detection paired with the harshness of punishment needs to be high. Further, greater transparency in all areas of government practice would be a useful mean to avoid corrupt practices (Luo, 2002).

This is especially problematic in China as the issue of underpayment, in particular of bureaucrats which used to belong to the wealthiest part of Chinese society received a relatively low salary specially when compared to wealthy businessmen, has been mentioned. People realized incomes through other means such as establishing a stock of obligations or owned favours to secure the future²⁰. If salaries are high enough, the risk of losing one's job as a result of corrupt practices will restrain from such actions.

The probability of detection and the severeness of punishment deviate across Asian countries. Singapore, the least corrupt country in Asia also has one of the highest execution rates in the world for which it has frequently had to face international criticism from diverse human rights institutions such as Amnesty International. Nevertheless, also Singapore has had problems with corruption especially among the Singapore Police Force as a result of low salaries (Quah, 1999). In fact, corruption was unrestrained until 1959 when measures adopted by the People's Action Party (PAP) reduced corruption through altering the public's perception from a low risk-high reward strategy to a high risk-low reward strategy. Singapore as a relatively poor country at that time could not afford to raise salaries so it implemented a single independent anti-corruption agency (Corrupt Practice Investigation Bureau, unlike China where numerous anti-corruption agencies are at work and not necessarily independent)²¹ which due to its independence performs outstandingly, reduced opportunities and increased penalties (Quah, 1999).

²⁰ <http://www.diligencechina.com/blog/?p=78> (04.02.08, 11:48)

²¹ http://www.transparency.org/news_room/in_focus/2007/nis_in_east_and_southeast_asia (04.02.08, 12:48)

Through the anti-corruption strategies Singapore has implemented, corruption is considered a high risk-low reward strategy in Singapore whereas in China, where the probability of getting caught in the complicated and entangled bureaucratic net is relatively low, corruption being considered a low risk-high reward strategy is pursued by many lower paid bureaucrats. Therefore, the ideal strategy for regulations against corruption should lie in the creation of a high risk-low reward perception of corruption (Quah, 1999). The punishment weighed with the probability of getting caught must outweigh the utility someone might obtain from acting corruptly. However, it is of ultimate importance to eliminate the protection often given to party officials from their protectors in the party hierarchy (Quah, 1999).

Recent scandals in China and the strict punishments actors were faced with illustrates China’s attempt at generating a system in which the risks of corruption outweigh the benefits. The role of the media plays an essential role here as the harmful effects of corruption and the hardness of punishments need to be communicated to the public. A further objective is the condemnation of corruption by the public as unacceptable behaviour within society. Singapore and Hong Kong have managed to achieve this more successfully through higher business ethic standards compared to other Confucian countries.

Singapore has successfully realized the determinants and sources of corrupt behaviour and managed to treat the problem at its roots, preventing corruption from occurring in the first place through the determination of the ruling elite²², adding to the good reputation of the “most business-friendly economy in the world” as it is often considered. Further, both Singapore and Hong Kong have obviously effectively implemented an independent anti-corruption agency along with a clear and comprehensive anti-corruption legislation (Quah, 1999), recognized as the least corrupt countries in Asia²³. Although China’s corruption problem has improved during the past 10 years, its corruption level still remains comparatively high²⁴, causing much damage to the national economy and the country’s development. Taiwan is found to lie somewhere in between Singapore and China

²² http://www.transparency.org/news_room/in_focus/2007/nis_in_east_and_southeast_asia (04.02.08, 12:48)

²³ Hong Kong obtained 14th place on the CPI Index with a score of 8.3 and consequently the second least corrupt country in Asia behind Singapore.

²⁴ http://www.transparency.org/news_room/in_focus/2007/nis_in_east_and_southeast_asia (04.02.08, 12:48)

on the Corruption Perception Index, although guanxi is frequently considered just as important for Taiwanese as for Chinese business. However, the extend of guanxi between business players and government officials and the resulting corruption and favouritism may be less in democratic Taiwan compared to communist China with its problems of privileging. Further, living standards are found to be higher in Taiwan than in China (only 0.95% fall below the poverty line in Taiwan, 2007 est., compared to 8% in China, 2006 est.²⁵), which as Quah (1999) has mentioned, is one crucial determinant of corruption. The Taiwanese government has removed the mandatory death penalty from serious currency offences²⁶, perhaps resulting in the perception of a lower risk to corruption compared to Singapore.

The effectiveness of Singapore’s corporate governance system can be illustrated through the fact that firms in Singapore and Hong Kong survived the Asian crisis (1997) better than firms in other countries. This is due to numerous characteristics exhibited by the two countries for instance the openness of the market and consequently market competition as well as comparatively strong banking and financial sectors (Khan, 2003). Especially small Singapore with its lack of natural resources relies on a heavy trade policy and has incorporated a very liberal attitude towards foreign direct investment. Nevertheless, the Asian financial crisis has resulted in the implementation of reforms that improved corporate governance and competitiveness of Singapore including improvements in disclosure, shareholder protection and improved ability of investors to take civil action against insider trading and the establishment of a single securities regulator with widespread power (Teen & Phan, 1999). Generally studies have highlighted the connection between the strength of legal systems and corporate governance ranking (Klapper & Love, 2003), highlighting the connection between Singapore’s strong legal system and relatively good corporate governance implementation.

²⁵ <https://www.cia.gov/library/publications/the-world-factbook/> (10.02.08, 17:27)

²⁶ <http://www.chinapost.com.tw/news/archives/front/20061223/98201.htm> (13.02.08, 12:36).

7. Guanxi and networking

7.1. Guanxi and Western networking

Concerning guanxi's uniqueness as a concept central to China, opinions diverge. According to some, guanxi is a concept deeply rooted in ancient Chinese culture and a highly particular way of forming relationships based on Chinese values. For others, guanxi is simply another word for relationship networking, social capital or gift economy, not actually unique to Chinese (Gold et al., 2005: 3). Whereas gift-giving and entertainment such as dinners is obviously not unique to Chinese culture, some fundamental differences do exist.

Numerous basic differences between the Western and Chinese approaches to business practices exist (Lovett et al., 1999). Whereas Chinese tend to rely on personal relationships, Western businessmen emphasize the support of contractual means. However, in the past years, the concept of relationship marketing has gained significant relevance in Western business and negotiation, stressing the development of a tightly connected, long-term relationship between business partners to achieve comparative advantage by firms (Dunfee and Warren, 2001). Concerning social interaction and relationships, Hofstede's culture dimension "individualism vs. collectivism" has been mentioned. This difference in perception of the role and significance of relationships and groups predetermines the divergence between Chinese guanxi and Western forms of networking.

The importance of trust for guanxi relationships has been discussed before. In the West, business negotiations are conducted quickly and efficiently, their enforcement regulated by commercial law. In China, negotiations require much more time as guanxi first needs to be established and thorough information is sought about the potential business partner in order to draw conclusions about his trustworthiness. The importance of trust is rooted in the ideas of Confucianism, highlighting the rule of man instead of the rule of law. Trust replaced commercial law as it has traditionally not been well developed and can not be relied on for the enforcement of business agreements (Arias, 1998).

The concept of relationship marketing basically follows the same goals as guanxi networking, namely "reduce transaction costs, facilitate cooperation of channel members and retain customers, while emphasising formal contracts and long-term

organizational goals” (Ai, 2006). Comparably, Luo (1997) argues that guanxi shares many common facets with Western relationship marketing. Resources of other network members can be used resulting in competitive advantage and the gap between business people from different nations can be bridged. However, in relationship marketing, exchanges are of economic nature such as of goods or services whereas in guanxi, favours are often exchanged that reach far beyond the economic nature such as the mutual exchange of personal favours or protection. The enhancement of face or reputation through guanxi is another fundamental difference between the two (Arias 1998). Further, Luo (1997) also emphasises the similarity in terms of the long term, continuous (i.e. more than a single transaction) orientation which in turn requires the active and reciprocal participation of both partners. Arias (1998) highlights a differences in the time perspective between relationship marketing and guanxi. Although they are both established with a long term objective in mind, relationship marketing comprises marketing agreements which need to be fulfilled within a certain strict deadline, relationships being evaluated on this short term basis. On the other hand, the return of a favour from guanxi takes place some time in the future when it is needed (Arias, 1998, Yeung and Tung 1996). The concept of reciprocity in the long term (i.e. favours are returned sometime in the future and not immediately) which characterises guanxi, is not realized in relationship marketing. Additionally, what is reciprocated does not necessarily need to be of equal value as in relationship marketing but quite often the weaker part is favoured or more than has been given to is returned in order to continue the guanxi relationship through the creation of feelings of indebtedness (Fock et al., 1998; Yeung and Tung, 1996). “The debit and credit sides of this balance sheet are never in equilibrium since such a status often means the end of a guanxi relationship” (Yeung and Tung, 1996).

Fan (2002b) highlights that guanxi cannot be compared to relationship marketing as these concepts exhibit two fundamental differences. Firstly, guanxi is a highly personal and private relationship established between and belonging to individuals and not to the organization i.e. guanxi is personal not corporate like relationship marketing, although it can be used profitably by an organisation (Zhang and Zhang, 2006). However, Tsang (1998) assumes that guanxi can be “elevated from a personal to an organisational level” if the manager builds guanxi on behalf of the

organization to make the vis-à-vis develop feelings of obligation or reciprocity towards the organization instead of the individual (Dunfee and Warren, 2001). On the other hand, relationship marketing refers to all internal and external relationships produced by an organization (Fock et al, 1998). Consequently, if an employee leaves the company he will take his guanxi connections with him (Fan, 2002b). Secondly, whereas relationship marketing is typically established between buyers and sellers, the relationships in business guanxi are likely to be multi-dimensional rather than just buying.

Business connections do not necessarily lead to the closure of a deal but instead are used to build up and expand guanxi which may prove useful and profitable in future transactions (Pearce and Robinson, 2000). Similarly, Luo (1997) states that, in China, relationships are established first and if successful, transactions will follow whereas in the West, transactions take place first and relationships might be built up if they are successful. Two bases of causality can be identified; in relationship marketing, business relations cause social interactions whereas in China, social interaction is a precondition for guanxi which in turn is a prerequisite for business relationships (Arias, 1998). Guanxi has affective commitment due to the personal involvement and is based on fulfilling a social obligation whereas relationship marketing focuses on economic profitability and is based upon self-interest (Lee and Wong, 2001; Yeung and Tung, 1996). The identities of the counterparts are mostly irrelevant for relationship marketing, whereas guanxi highlights the personal connection based on human feeling and friendship.

Relationships in Western styles of relationship marketing can also be established by images, symbols or brands whereas guanxi is a highly personal concept that can only be established between people (Arias, 1998).

Yau et al. (2000) identify four dimensions required for a true and long-term relationship amongst Chinese: trust, bonding, reciprocity and empathy (see Figure 4). Bonding refers to finding a common ground to built on, similar to the previous mentioned guanxi bases (such as common origin), to eliminate doubt and suspicion. Reciprocity has been mentioned before in connection with Luo's features of guanxi, namely the morally binding obligation to repay one's debts in order not to lose face. As Chinese rely more on people than on law or contracts and as the debt will be returned sometime in the future, trust is essential for a

relationship in order to overcome the uncertainty. Empathy relates to seeing the partner from another perspective and acquire understanding for his needs, desires, strengths and weaknesses as well as personality. Empathy is necessary for reciprocity as only through proper understanding and consideration of the partner can favours be reciprocated appropriately, which will lead to an increase in trust and bonding.

Based on these 4 dimensions, the similarities and differences between guanxi and western relationship marketing can be drawn.

	Western	Chinese
<i>Bonding</i>	<ul style="list-style-type: none"> • Between consumer and supplier • For desired goal 	<ul style="list-style-type: none"> • Blood bases and social bases • For social control and business behaviour
<i>Reciprocity</i>	<ul style="list-style-type: none"> • Long-term with certain deadlines for return • Conversion of value • With specific intention • Specification of the exchanged 	<ul style="list-style-type: none"> • Long-term without time specification for returning favour • Increase of value • No specific intention • No specification of exchanged
<i>Trust</i>	<ul style="list-style-type: none"> • People with promised integrity • Focus on transaction, relationship may be established • More system based, reliance on law 	<ul style="list-style-type: none"> • Kinship or in-group members • Focus on trust and relationship establishment, later on transaction • More personal based, reliance on face
<i>Empathy</i>	<ul style="list-style-type: none"> • Sender-centred communication 	<ul style="list-style-type: none"> • Receiver-centred communication

Figure 4: Comparison of the Four Dimensions of Relationship Marketing Between Western and Chinese (Yau et al., 2000)

7.2. Networking throughout Asia

The teachings of Confucianism have not only had their effect in China but have also spread to and influenced Japan and Korea extensively. In Japan and Korea, the concepts of *kankei* and *inmak* respectively share many similarities with the Chinese *guanxi*, highlighting the principles of interdependency and relationships between individuals. These concepts all represent a form of social or relational capital which is commonly found in Asian companies (Hitt et al., 2002). Although they are very similar, the three exhibit some differences as a result of deviant interpretations of Confucianism and practices. *Kankei* can be defined as a way of granting access through relationships, clearly differentiating between insiders and outsiders. Similar to *guanxi*, *kankei* is used to define who is trustworthy, loyal, committed and valuable to have a relationship with. However, *kankei* is not primarily based on common backgrounds and bases as is *guanxi* but relationships are more logical, rational flexible and situation specific and can be formed without an existing common background. According to Hitt et al. (2002) although trust is important for all these concepts, it is most important for the formation of *kankei*. Trust is more important than existing social or other background commonalities, whereas *guanxi* highlights belongingness to certain groups or social institutions and is more family tie orientated. In spite of these differences, all three concepts are used by Asian companies to gain competitive advantage and reduce transaction and monitoring costs.

Conglomerate organizations are also common in Asian countries, especially in Japan, Taiwan and Korea. In Japan, *keiretsu* networks developed out of large industrial organizations which originated from large groups of family businesses spread over numerous industries (Hitt et al., 2002) and are considered one of the main reasons for strong Japanese presence on global markets as well as competitive advantage (Peng et al., 2001). A *keiretsu* system is best described as a business group consisting of business interrelationships between companies and complex cross-equity ownership with a central bank at the core (Wright, 1990). Through these interrelationships, dynamics are created (Yeung, 2000) such as economies of scope, diversification of new technologies, secure financial base, economic diversification and risk sharing (Wright, 1990; Peng et al., 2001). Especially Japanese *keiretsu* networks were praised to be highly effective means

for the establishment of Japanese companies abroad e.g. North America and Western Europe through competitive advantage until the time of the Asian economic crisis in 1997-1998 which was blamed on networking (Yeung, 2000). Nevertheless, keiretsu systems have helped Japanese companies to achieve competitive advantage through enhanced transactions within the network and easier access to resources especially of financial nature.

Through the closely knitted keiretsu systems which emphasize the helping of others in the network and consequently interdependency, Japanese firms may be missing out on possibilities to establish global networks due to their lack of freedom and dependence on other companies and networks (Hitt et al., 2002). This becomes especially problematic if one member is experiencing great difficulties, harming the other network members through their problems.

During the mid-1980s, the establishment of business groups similar to keiretsu networks in Japan began in China. Through promised protection from shock of reform, reformers encouraged firms to join the groups. Most firms developed some form of trade or lending relation within the groups resulting in the establishment of more than 7000 business groups in China by early 1990. These business groups are similar to business groups in other countries, highlighting extensive corporate ties and conducting business on a long term orientation (Gold et al., 2005: 78).

8. The connection between guanxi and profitability

Due to companies' dependence on their domestic networks, a result of guanxi establishment, Asian firms may be restricted to a certain degree in the establishment of global networks (Hitt et al., 2002). The benefits and drawbacks of guanxi for business have been discussed in a previous chapter. Reduction of transaction costs through diminished monitoring costs and reduced probability of opportunistic behaviour, access to resources and information as well as protection have all been identified as the positive effects of the use of guanxi. Consequently, the question remains whether these benefits in the long-run enhance firm performance or if guanxi's disadvantages such as the time-consuming factor, connection to corrupt behaviour, risk and non-adherence to the principles of fair competition outweigh the advantages. Further, the influence of guanxi on the

economy as a whole is of interest. Here again, opinions are very oppositional. Some believe that guanxi positively influences firm performance and efficiency through the creation of economic value through social capital (Luo, 2000: 41) whereas others consider guanxi establishment a loss of resources.

Lovett et al. (1999) propose a static model to illustrate the relative efficiency between the market system and the guanxi system of conducting business. Within the guanxi system, costs of contracting are zero because business is negotiated based on trust and face, whereas contracting costs exist in the market system. In the guanxi system it is more difficult to become accepted (what Lovett et al. call being a senior), having to prove ones trustworthy in order to become a “senior”. As a result, juniors (which have not completely proven their trustworthiness) cannot trade the full potential of their output (compared to seniors who can) whereas in the market system all individuals are allowed to trade all their output immediately. Which system is more efficient then is a result of the amount of contracting costs and the efficiency of juniors and seniors.

A study by Lee and Wong (2001) investigated antecedents and consequences of guanxi between businessmen. Decision-making uncertainty with which one is confronted as a result of insufficient information and unpredictable outcomes is positively related with the use of guanxi. The more uncertainty a business player is confronted with, the more likely will be the reliance on guanxi relationships in which he trusts and therefore reduce his uncertainty. Perceived similarities between business partners, ideally a common base (e.g. former class mater, neighbours, etc.) have also exhibited a positive relationship with guanxi. Opportunism typically is negatively related to guanxi, in other words, the more opportunistically a person acts, the more he will destroy his face and his guanxi relationships which are based on trust that he loses. Consequences of guanxi on firm performance²⁷ were also analysed. It was found that guanxi has a positive influence on the way relationship quality is perceived which in turn enhances future exchange and efficiency due to trust and thus, firm performance. Business players in a guanxi relationship develop trust and satisfaction which are key elements for successful business performance.

²⁷Sales trend over the last three years from the relationship, the stability of past sales, and the expectation of future sales for the next three years were used as performance measures

Peng and Luo (2000) display the relationship between management connections (guanxi) with other top managers and government officials and firm performance using a survey study. They find a positive correlation between managers' guanxi with other managers and officials and sales growth. Guanxi with government officials also exhibited a strong positive influence on profit growth. This study also highlighted that guanxi is a necessary but not sufficient condition for long-term success. In another study, the connection between guanxi based business determinants such as sales force marketing and credit policy and firm performance was analysed. The results showed a clear positive relationship between guanxi based business variables and business performance in the sense of profitability, asset turnover and domestic sales. This again shows the positive influence guanxi has on efficiency and performance of Chinese firms and foreign-invested enterprises (Luo and Chen, 1997).

If guanxi becomes closely associated with corruption as it often tends to be the case in China, companies that become involved in corrupt activities and scandals will have to deal with a lot more problems than with the penalty imposed by the law. A company that has once been associated with corruption or bribery will come to be considered untrustworthy, as a result losing its trading and business partners. It will take years to re-establish ones relationships and remove the acquired corrupt image. Initiating new business networks also becomes challenging as no firm desires to become involved with a company known for its corrupt practices, the image possibly rubbing off resulting in a loss of face for the other company. Further, through the interconnectedness of guanxi networks, such news spread quickly and far into the guanxi network. However, not only potential business partners will be cautious about doing business with a firm that has a corrupt reputation, also investors will think twice about engaging into business with such a company.

Further, this loss of image might also have an impact on the consumers that purchase the company's products. When a corruption or bribery case becomes public the firm often gains a reputation of poor governance, defective products and the inability to ensure customer service. This reputation is especially important in China as Chinese customers have often suffered from poorly produced products in the past (e.g. fake and dangerous medicine, poisonous toothpaste, etc.). Once the

firm has acquired such a reputation, sales and corresponding growth will be difficult to achieve and survival on the market becomes a challenge (Luo, 2000: 220).

For these reasons, a company doing business in China should beforehand conduct research on the reputation, financial and legal background of potential partners, managers, suppliers etc. before conducting formal business negotiation in order to minimize risks. Also, a pre-employment screening especially for top executive positions might prove to be a worthwhile tactic (Hoenig, 2006).

Guanxi has established as a way to overcome the inefficiencies “inherent in the communist bureaucracy” through networking. Consequently, it may be considered beneficial at a macro-level whereas at the micro-level, inefficiency and the misallocation of resources prevails (Dunfee and Warren, 2001).

Studies have shown that countries with a high degree of corruption tend to have lower GDP going into investment and lower growth rates (Luo, 2000: 212). This is because if a country is abuzz with corruption, the probability that investors will loose money increases which in turn will damage investors’ confidence and lead to a reduction of investment. Not only will present investors consider alternative possibilities for placing their money, future potential investors are also likely to be scared away through these occurrences. The overall image becomes damaged, rendering the quest for new investors challenging.

The problem of favouritism has been discussed in previous chapters. As said, favouritism is not only unfair and harms others but it also stands in conflict with competition and the principles of an open market economy. A few are favoured at the expense of many others that might not have developed such good guanxi. This hurts economic development and in the long-run, society. As guanxi is frequently used by bureaucrats in a corrupt manner to boost their wealth, the social good is reduced since it is split amongst a number of powerful officials instead of the whole society.

9. The connection between guanxi and corporate culture

Pun et al. (2000) argue that national culture can be seen as nurturing the development of corporate culture in organisations and therefore are interrelated. Chinese culture defines values such as honesty, loyalty and obedience (Tan and Shell, 2002) that are commonly believed and shared by its members, inevitably it must also influence corporate culture, i.e. corporate culture of companies reflects Chinese culture (Ip, 2003b). Therefore, Confucian values and the use of guanxi must also be recognized in corporate culture.

Corporate culture can be vital for the attainment of competitive advantage. It shapes the organizational structure, access to and flow of information, the patterns of behaviour, the reward system and other aspects of the organization that make it possible to serve customers (cited in Pun et al., 2000). Further, strong corporate culture creates a complex value system as well as well-defined visions, goals and beliefs for the achievement of these (Ip, 2003b). Difference of corporate culture can be found between varying types of enterprises (e.g. state-owned or private-owned).

The speciality and significance of Chinese guanxi is commonly reflected in Chinese enterprises and management practices, emphasising personal relationships. Chinese management practices and corporate culture underline the importance of personal relationships or connections based on trust, typically exhibiting some kind of paternalistic management (Yang, 1994; Luo and Chen, 1997; Pun et al., 2000; Xin and Pearce, 1996). Working at an enterprise means belonging to a group, a fundamental part of collectivist societies which is used for identification purposes by employees. The in group belongingness is stressed and achieving the groups goals becomes more important than attaining ones own goals. Communication to out-group members is typically restricted or guarded (Pang et al., 1998).

In China, guanxi is not only built up with other businessmen but also with ones employees. Special relationships are found within an organization; it is common for employees to be friends with managers and personal favours are nothing out of the ordinary. This is an extremely important aspect that foreigners should not neglect as Chinese employees are very loyal if guanxi and a feeling of

indebtedness has been established with superiors and management (Yau et al., 2000, Pang et al., 1998). Chinese also score high on Hofstede's dimension of power-distance which implies that they accept difference of power distribution and the resulting hierarchy, willing to subordinate and follow instructions of superiors (Buttery and Wong, 1999). This can also be seen as a result of Confucianism which, as mentioned, places great emphasis on hierarchy and the pursuing of one's role in the society or in this case, in the enterprise. Through the belief in hierarchy, Chinese employees obey their superior even when his behaviour is morally not correct for instance when bribing officials or following opportunistic goals. The employee will keep quiet, believing that it would have a negative effect on their career or might even commence to behave in similar ways, resulting in disastrous effects for corporate governance. Hierarchy and authority are still significant concepts in Chinese enterprises while moral values, benevolence and goodness seem to have been reduced, resulting in corrupt behaviour and bribery (Jing et al., 2005)

Employees play a significant role when it comes to their influence for the construction of a company's widespread guanxi networks. Chinese language skills and an understanding of cultural factors are often considered necessary for the generation of guanxi. As this often poses an obstacle to foreigners, the importance of hiring native Chinese that can establish guanxi and trust is made apparent (Leung et al., 2005). Attention needs to be paid that each employee's guanxi corresponds with the requirements of the tasks, i.e. depending on the position and assignment, different guanxi will have a different significance.

The aim should lie within the establishment of a corporate culture that seeks to continuously improve performance and enhance efficiency (Pun et al., 2000). The concept of morality, which is also a fundamental part of Confucianism, is central to Chinese management culture. The question however then remains, why so many Chinese enterprises are found to be involved with corrupt practices.

10. The changing significance of guanxi and future development

Guanxi is a changing and dynamic process, its significance varying over time. According to guanxi's (future) development, one can analyse how significant this

concept really is to Chinese culture. If it actually originates from Confucianism and is as deeply-rooted as many authors argue, then economic changes should not be powerful enough to cause major changes or extinct this practice. If on the other hand, guanxi is a response to unstable political and social conditions and lack of legal institutions, its significance should rather rapidly diminish as a result of improved institutions and business practices (Dunfee and Warren, 2001).

Hoening (2006) states that over the past five to eight years, guanxi's significance and importance for achieving business success in China has been reduced due to an improvement in market regulations. According to Ai (2006), the significance of guanxi will further be reduced in the future. He bases this conclusion on a study that included college students as well as senior managers in Mainland China and Taiwan. College students rated the importance of the various guanxi maintaining elements such as frequent social activities, gift giving or voluntarily providing favours lower than senior managers. This suggests as today's college students are the future managers, that these aspects of guanxi will become less important. What seems to remain significant for guanxi networking are shared profits from guanxi, frequent mutual help and keeping contact. Ai believes that these results show that guanxi is likely to become more business outcome oriented, less visible and more sophisticated in the future.

Also Vanhonacker (2004) claims that, as China's legal framework and infrastructure will improve, the significance of guanxi will be reduced. Nevertheless, the cultural heritage will remain and guanxi will always be an important and driving factor for doing business in China. Similarly, Arias (1998) states that as legal circumstances will develop, pulling guanxi will become more difficult if not to some extent illegal. Luo (2000: 32) highlights the need for differentiating between socially-based and blood-based guanxi, the former more likely to disappear due to a reduction in its need based on an improvement of institutional law. Correspondingly, Vanhonacker (2004) also believes that blood-based guanxi, a concept deeply rooted in Chinese culture will retain its significance, less likely to be influenced through structural reforms.

Another point stressed by Luo (2000: 32) is the reduction of guanxi with central government officials as more and more decisive power, resources and autonomy are handed to local governments. Consequently, the importance of connections

with local government officials might increase. Further, more advanced Confucian societies such as Japan, Taiwan, South Korea, Hong Kong and Singapore still heavily rely on relationships although their legal infrastructures are further developed, suggesting that even if the development of institutional law is enhanced, these societies will maintain their special way of using relationships instead of or as a complement to law (Tsang 1998, Luo, 2000: 31). Tsang (1998) however also realized that although still important in their home markets, Hong Kong and Singapore managers find it more relevant to establish guanxi with their Chinese business partners instead of within their home country, suggesting the reduction (but not extinction) of guanxi's importance along with the development and advancement of legal institutions.

Remaining uncertainties and distrust of Chinese legal institutions still keeps reliance on personal connection alive, as Chinese feel secure when applying these (Kiong and Kee, 1998). As Millington et al. (2005) have shown, although legal structures have developed and improved, illicit payments remain an important aspect of Chinese business life.

Guthrie's (1998) study on Chinese industrial managers and officials has shown that guanxi plays only a secondary role in market relationships behind competitiveness. The significance of guanxi for the urban industrial economy is changing, managers increasingly distancing themselves from guanxi practices. This is considered a result of China's need for capital which demands higher certainty through regulatory mechanisms. Further, an increase in competition will lead to the reduction of the use of personal connections and an increased reliance on market mechanisms such as price and quality as these tend to be more efficient and are valuable for achieving long-term competitive advantage.

In a previously mentioned interview study on Australian expatriates in China by Hutchings and Murray, respondents employed in larger organizations claimed that through globalization and an increase of market capital guanxi declined as a response. Individuals employed in smaller organization highlighted that guanxi's importance remains strong. Nevertheless, the authors claim that globalization has an influence on the way guanxi works and that the increasing importance and influence of large multinationals might become more significant than national institutional and cultural traditions.

Lovett et al. (1999) feel that western business styles are converging towards a more relationship or guanxi-oriented way. They base their assumption on the increasing significance of relationship marketing and virtual integration in the Western world. Virtual integration refers to the concept of developing tightly coordinated relationships with ones main suppliers. Undeniably, the relevance of these two concepts has advanced over the past years. Networks are becoming more and more important in today's business environment as competition no longer takes place on a firm by firm level but groups of companies compete with each other. Through the creation of social capital which is defined as relationships between individuals or organizations that creates value, firms achieve competitive advantage (Hitt et al., 2002). They suggest that Western firms take this as an example and emphasize the establishment of social capital through business relationships in order to become more competitive on a global market.

11. Meta-analysis

The following table highlights the main opinions, studies and results published in the research area of guanxi.

Topic Area	Author & Date	Title	Core Statement	Analysis
Guanxi on general terms	Ghauri & Fang, 2001	Negotiating with the Chinese: a socio-cultural analysis	<p>Peculiarity of doing business in China analyzed on the basis of the Swedish multinational corporation Ericsson</p> <p>Managerial implications presented as four P’s: Priority, Patience, Price, and People</p> <p>Proposal of a Ping-Pong model to analyze the process of Chinese business negotiation style from the Chinese socio-cultural perspective using indigenous components of Chinese culture</p>	Unsuccessful business operations of foreign firms in China often the result of culture based difference in negotiation styles between Chinese and Westerners
Guanxi on general terms	Buttery and Wong, 1999	The development of a guanxi framework	<p>Analysis of Chinese business culture in terms of Hofstede’s power-distance dimension - differences of power distribution, the resulting hierarchy and subordination to superiors is willingly accepted</p> <p>Potential network members start as "outsiders" aiming to achieve “insider” or old friends status</p>	Highlights the peculiarity of Chinese business based on cultural values and stresses the importance of its consideration for foreigners
Modelling guanxi	Fan, 2002	Questioning guanxi – definitions, classification and implications	<p>Guanxi is defined as the dynamic process of social interaction and classified into the categories of helper, family and business guanxi</p> <p>The potential benefits of guanxi are mainly tactical rather than strategic</p> <p>B2G guanxi is inherently corrupt and ethically</p>	<p>The perception of guanxi as a process enables understanding of the its functionality and ample potential for access to further networks through connections</p> <p>The categorization into three</p>

			<p>questionable</p> <p>The influence of guanxi on all stakeholders needs to be considered</p> <p>It is likely that guanxi’s significance for business will diminish as China moves towards an open market system</p>	<p>basic types of groups is common by numerous authors – despite varying names assigned, the basic properties are usually analogue</p>
Modelling guanxi	Chen and Chen, 2004	On the Intricacies of the Chinese guanxi: a process model of guanxi development	<p>Illustration of a person’s psychological guanxi net space through concentric circles - the shorter the distance between a person and his guanxi partner, the better the quality of their relationship</p> <p>Guanxi viewed as a dyadic relationship whose building process is divided into the three stages of initiating, building and using</p>	<p>Useful demonstration of a persons guanxi network through the model – eases understanding of layout of guanxi network</p>
History/ Roots of guanxi	Dunning and Kim, 2007	The cultural roots of guanxi: An exploratory study	<p>Connection between guanxi and Hofstede’s collectivism dimension is drawn – in-groups are more important than individual resulting in the creation of an interdependent self</p>	<p>One of many papers that analyses guanxi by the means of Hofstede’s culture dimensions</p>
Cultivating guanxi	Pearce and Robinso n, 2000	Cultivating guanxi as a foreign investor strategy	<p>A firm’s ability to cultivate guanxi depends on numerous variables and is one of the most important qualities expatriates need to develop</p> <p>Guanxi members are connected by an unwritten code whose disregard will result in a loss of reputation (face) and prestige</p> <p>Agree that guanxi is the most time intensive part of Chinese business conduct but needed as a social investment for the future to secure resources</p>	<p>Emphasis is placed on the future perspective of guanxi – connections are not necessarily established to close a deal today but might prove profitable in the future</p> <p>Concur on the time intensiveness but necessity of guanxi establishment and maintenance</p>
Necessity for guanxi	Lee and Wong,	A model of close business relationships in	<p>Investigated antecedents and consequences of guanxi between businessmen</p>	<p>The more uncertainty a business player is confronted with, the more likely will be</p>

	2001	China (guanxi)	<p>Decision-making uncertainty and perceived similarities are positively related with the use of guanxi while opportunism typically is negatively related to guanxi</p> <p>Guanxi has a positive influence on the perception of relationship quality which enhances future exchange and efficiency</p> <p>Trust and satisfaction developed by businesses players are key elements for successful business performance</p>	<p>the reliance on guanxi relationships while the more opportunistically a person acts, the more he will destroy his face and his guanxi relationships</p>
Necessity for guanxi	Xin and Pearce, 1996	Guanxi: connections as substitutes for formal institutional support	<p>Guanxi is especially used as a substitute for weak legal frameworks, government and law enforcement, especially by newer, smaller private businesses which are more dependent on guanxi than executives in state-owned or collective-hybrid companies</p> <p>These companies have more government connections and emphasize their importance especially concerning protection from threats such as appropriation and extortion compared to state-owned or collective hybrid companies</p>	<p>Results in accordance with other author’s findings that guanxi is especially important due to lack of legal institutions and law enforcement</p>
Guanxi and firm performance	Luo and Chen, 1997	Does guanxi influence firm performance?	<p>Guanxi based business variables such as the intensity of sales force marketing were found to have a positive influence on the efficiency and growth of Chinese domestic firms as well as on foreign ventures in China</p> <p>Firms and ventures in China need to be aware of the decisive impact guanxi has on business performance variables</p> <p>Guanxi creation and maintenance is determined as a key success factor for business</p>	<p>Analyzed the influence of guanxi business variables on firms performance from a business strategy view and realized the parallels between guanxi and firm performance – the negative effects are completely ignored</p>

Guanxi and firm performance	Peng & Luo, 2000	Managerial ties and firm performance in a transition economy: the nature of micro-macro link	<p>The relationship between management connections (guanxi) with other top managers and government officials is analyzed</p> <p>There is a positive correlation between managers' guanxi with other managers and officials and sales growth</p> <p>Guanxi with government officials also exhibited a strong positive influence on profit growth</p>	This study highlighted that guanxi is a necessary but not sufficient condition for long-term success
Guanxi and firms performance	Luo, 1997	Guanxi and performance of foreign-invested enterprises in China: an empirical inquiry	<p>Analysis of the relationship between guanxi based business variables and the performance of foreign-invested enterprises showed that guanxi-based business variables have a significant positive effect on venture's accounting and marketing performance</p> <p>Entry mode, country of origin of investment and length of operation also have an influence on the guanxi – performance relation</p>	As guanxi is one of the most efficient and effective marketing tool, investors should use it properly to gain competitiveness
Guanxi and firm performance	Yeung and Tung, 1996	Achieving business success in Confucian societies: the importance of guanxi (connections)	<p>Among a list of factors important for long term business success in China, guanxi was the only factor consistently ranked as a key success factor whose importance was attributed to the ambiguity and weakness of legal institutions with numerous loopholes left for interpretation</p> <p>Through the creation of feelings of indebtedness and unspecified time of return, a long term guanxi circle with continuous exchange and mutual assistance is established, the two sides never being in equilibrium</p>	<p>Highlights the importance of guanxi for chief executives of China operations</p> <p>Inequality of favour-return equilibrium desirable and necessary for continuous guanxi exchange</p>
Significance of guanxi	Hitt et al., 2002	The importance of social capital to the management of multinational	<p>Social capital provided through guanxi can supply competitive advantage through access to resources, reduction of opportunism and transaction costs, also on global markets if relations are extended beyond borders</p> <p>Illustration of the similarities and differences between</p>	Social capital is especially needed by firms operating globally to secure enough resources and consequently obtain potential for

		enterprises: relational networks among Asian and Western firms	Chinese guanxi, Japanese kankei and Korean inmak Social capital also creates disadvantages such as opportunity costs and path dependence	competitive advantage The concept of social capital based on close relational ties is common throughout Asian countries, not specific to China alone
Significance of guanxi	Hutchings and Murray, 2002	Working with guanxi: An assessment of the implications of globalization on business networking in China	Appreciation of guanxi for businessmen depends on the time of operation and experience in China and the size of the organization worked at - expatriates in larger organizations claimed that guanxi has no or little significance to them whereas businessmen in smaller organizations stressed the importance of establishing relationships Length of service and language skills give guanxi in a similar way as reputation of working for a big multinational Through globalization and the influence of large multinationals, guanxi declines	This suggests that larger organization automatically have guanxi through their size and international influence whereas smaller organizations need to work hard to obtain guanxi Consent about guanxi's changing significance but as a result of globalization instead of improved legal systems
Implications and benefits of guanxi	Fock and Woo, 1998	The China market: strategic implications of guanxi	Chinese suspicion makes business negotiations a time consuming and wearisome process especially with foreigners however it is vital for competitiveness and attainment of resources of all kinds (ranging from tangible resources to information) to achieve the position of an insider Company image and reputation is greatly influenced through guanxi Absence of commitment distinguishes relationship marketing in the West from guanxi – guanxi relations require continuous effort and involvement	The perceptions and applications of guanxi are analyzed among Hong Kong business executives Highlights that guanxi is a concept which needs to be integrated into the business strategy of foreign business partners in order to attain a competitive position

Benefits of guanxi	Ramasamy et al., 2006	Is guanxi (relationship) a bridge to knowledge transfer?	Trust is so important in Chinese business negotiations because deals often only rely on verbal agreements and face If a guanxi relationship has been established, guanxi can be considered a bridge to knowledge transfer, the information typically being of high value and reliable	Chinese will be reluctant to share valuable information with “outsiders” so a good guanxi relation previously needs to be established – information is treated just as any other, tangible scarce resource
Benefits of guanxi	Tsang, 1998	Can guanxi be a source of sustained competitive advantage for doing business in China?	Timeliness of guanxi one of the main disadvantage – takes years to establish high quality guanxi connections If used correctly guanxi can be a source of competitive advantage but it needs to be rare, valuable and imperfectly imitable Guanxi resembles a risky strategy as guanxi investment can easily be lost – create cost-benefit analysis before guanxi establishment	Highlights that if used correctly, guanxi might very well be a source of competitive advantage but it remains a risky and costly strategy as outcomes and returns are unpredictable and intangible
Benefits of guanxi	Standiford and Marshall, 2000	The transaction cost advantage of guanxi-based business practices	A guanxi network itself considered a sort of insurance against opportunistic behaviour (due to risk of loss of face and exclusion from the network and loss of guanxi based investment) which in turn reduces monitoring costs of transactions If a connection is detached once due to self-interested behaviour it is almost impossible to re-establish Communication of the business partner’s reputation, face and character through the guanxi network, reduces transaction costs concerning screening and identification of an appropriate partner	The tighter connected and richer a guanxi network, the more valuable and consequently the less likely one will be willing to risk it, resulting in a negative interrelationship between value of a guanxi network and opportunism
Benefits of guanxi	Davies et al., 1995	The benefits of guanxi	Guanxi is an important source of information on markets and trends, business opportunities and government	The relevance of guanxi for information attainment has

			<p>policies</p> <p>Generally benefits concerning the smooth operation of routine business (e.g. payment and transport) where seen as the most important guanxi benefits followed by the advantages in securing information on policies and administrative approvals from government officials</p> <p>Guanxi can reduce transaction costs connected to environmental uncertainties such as communication, negotiation and coordination of transactions</p>	<p>been recognized by many authors</p> <p>Information spreads just as other resources through the guanxi network and tends to be of higher quality the better the guanxi relation</p>
Guanxi and reputation	Fan, 2007	Guanxi, government and corporate reputation in China	<p>Despite its rapid transition to a market economy China remains a hierarchical, guanxi-based society, guanxi being a central aspect of “reputation capital”</p> <p>The government or the ruling CCP still plays a major role as a stakeholder which along with the significance of guanxi needs to be recognized by foreign marketers</p>	Guanxi and corporate reputation are linked, the interplay between the two concepts is highlighted as well as the importance of corporate reputation establishment through guanxi
Guanxi and corruption	Steidlmeier, 1999	Gift giving, bribery and corruption: ethical management of business relationships in China	<p>Gift-giving used as a way to strengthen relationships, establish trust and convey respect – frequently interpreted as bribery particularly by foreigners</p> <p>Only a thin borderline separates guanxi from corruption, guanxi is often abused as a cover-up for corrupt practices</p> <p>Differentiation between bribery, gratuity and commission</p>	<p>Draws a distinction between the concepts and explains the importance of gift-giving for guanxi establishment</p> <p>The existence of a fragile borderline between bribery and gift-giving is highlighted</p>
Guanxi and corruption	Vanhoacker, 2004	Guanxi networks in China – How to be the spider not the fly	<p>Social relationships are needed for the definitions of personal identity in China</p> <p>Corruption and guanxi differentiate (corruption is transaction-focused whereas guanxi relation-focused) but guanxi can easily be used to hide corrupt behaviour</p> <p>With the improvement of legal structures guanxi’s</p>	Highlights the central differences between corruption and guanxi, they are based on completely different values nevertheless, the two are often intertwined especially by foreigners which

			significance will be reduced but cultural heritage remains especially in connection with blood-based guanxi	need to learn to distinguish good from bad guanxi
Guanxi and ethics	Lovett et al, 1999	Guanxi versus the market: ethics and efficiency	<p>Through the strategic alliance between individuals and companies, a general access to resources of all kinds is acquired by its members</p> <p>Transaction cost advantage from guanxi in the form of reduced opportunistic behaviour - as a result of basing ones business deals on trust and face, transaction costs are reduced as contracting costs do not exist since contracts do not need to be established</p> <p>Most of the non-western world conducts business using guanxi-based methods but is moving towards a system based more on ability whereas western business styles are converging towards a more relationship or guanxi-oriented way</p>	<p>A static model is proposed to illustrate the relative efficiency between the market system and the guanxi system of conducting business</p> <p>Within the guanxi system, costs of contracting are zero because business is negotiated relying on trust and face, whereas contracting costs exist in the market system</p>
Guanxi and ethics	Dunfee and Warren, 2001	Is guanxi ethical? A normative analysis of doing business in China	<p>Especially B2G guanxi is unethical and results in the elevation of a few above the law at the costs of society</p> <p>Guanxi can also be seen as a way to overcome the inefficiency of the communist bureaucracy</p> <p>If guanxi really is a response to unstable political and social conditions and lack of legal institutions, its significance should rather rapidly diminish as a result of improved institutions and business practices</p>	<p>Takes the negative influence of guanxi onto society as a whole and on the efficiency and development of the economy into consideration</p> <p>Agreement on the diminishing role of guanxi if it is a reaction to political and social changes, if it really is inherited in Confucianism an improved legal framework should not change its significance</p>
Guanxi and ethics	Millington et al.,	Gift-giving, guanxi and	Gift-giving is considered a serious problem by UK companies and often synonymous with illicit payment and	Exploration of the relation between gift-giving, guanxi

	2005	illicit payments in buyer-supplier relations in China: analyzing the experience of UK companies	<p>corruption which firms seek to reduce through various means</p> <p>Illicit payments are not associated with guanxi and companies realize the difference between gift-giving in connection with guanxi relationship to strengthen the bond and trust and on the other hand, illicit payments which are based on personal gain motives but still play an important role in Chinese business</p>	and corruption from the perspective of UK companies
Guanxi and ethics	Su et al., 2003	Is guanxi orientation bad, ethically speaking?	<p>A survey on purchasing managers of various types of Chinese enterprises showed privately owned Chinese enterprises exhibit the strongest level of guanxi orientation, having most government connections and emphasizing their importance the most</p> <p>Investigation between guanxi and cognitive moral development showed that guanxi has little to do with ethical reasoning</p>	This is explained through the assumption that SOEs have direct access to resources whereas privately owned enterprises need to use the “back door” and their relationships to obtain required resources
Guanxi and ethics	Su and Littlefield 2001	Entering guanxi: a business ethical dilemma in mainland China?	<p>Distinction between favour-seeking (Confucian heritage) and rent-seeking guanxi (institutionally defined and often synonymous with corruption)</p> <p>Development of a hybrid socialist market economy in the 1970s through economic reforms problematic since goods are exchanged for goods but also power is exchanged for goods</p>	Many authors agree and believe that economic reforms and the emergence of capitalism are responsible for an increment in the usage of guanxi and consequently, bribery and corruption
Guanxi and relationship marketing	Arias, 1998	A relationship marketing approach to China	<p>Commercial law in China was not well developed and could not be relied on for enforcement, therefore it was replaced by trust and personal connections to achieve ones goals in the highly bureaucratic state</p> <p>Social interaction is a prerequisite for guanxi and business whereas in the West, business causes social</p>	<p>Points out numerous differences and commonalities between guanxi and relationship marketing</p> <p>Agreement with others on the changing significance of</p>

			<p>interaction</p> <p>With improved legal circumstances, pulling guanxi will become more difficult or illegal and previously controlled resources are subject to market forces</p>	<p>guanxi as a result of changing conditions</p>
<p>Guanxi and relationship marketing</p>	<p>Yau et al., 2000</p>	<p>Relationship marketing the Chinese way</p>	<p>Four dimensions are illustrated which are required for long term relationship in China: trust, bonding, reciprocity and empathy</p> <p>Along these dimensions guanxi and Western form of relationship marketing differ significantly</p>	<p>Unique perspective on the peculiarity of marketing relationships the Chinese way along four clear-cut dimensions</p>
<p>Changing significance of guanxi</p>	<p>Guthrie, 1998</p>	<p>Social connections in China – Institutions, culture and the changing significance of guanxi</p>	<p>Guanxi is considered as dependent on the institutional structure of society rather than on culture which changes and adapts according to institutional changes</p> <p>Increased reliance on market mechanisms, need for capital and strong competitive environment are reducing guanxi’s significance and managers willingness to rely on these practices - guanxi plays only a secondary role after competitiveness</p>	<p>Results agree on the changing significance of guanxi with the changing conditions. Through the move towards a market economy, other variables have gained increased significance, whereas guanxi has partially lost relevance</p>
<p>Guanxi’s changing significance</p>	<p>Ai, 2006</p>	<p>Guanxi networks in China: its importance and future trends</p>	<p>Claims that the significance of guanxi will further be reduced in the future on the basis of a study including college students as well as senior managers</p> <p>College students rated the importance of the various guanxi maintaining elements lower than senior managers which suggests a decline in guanxi’s importance</p> <p>Results show that guanxi is likely to become more business outcome oriented, less visible and more sophisticated in the future</p>	<p>Agreement on the reduction of guanxi’s future importance</p> <p>Results based on the lack of guanxi perception of today’s college students but these might not have had enough insights into actual business practices</p>
<p>Changing significance</p>	<p>Yang,</p>	<p>The resilience of guanxi and</p>	<p>Highlights developments in the possibilities of guanxi’s usage (e.g. acquiring exit permits to leave the country and</p>	<p>Changing significance of guanxi is illustrated – with</p>

of guanxi	2002	its new deployments: a critique of some new guanxi scholars	<p>passports, obtaining loans, attracting overseas Chinese investors etc.)</p> <p>Guanxi's usage has moved from simple consumer good acquisition to the business and urban-industrial arena</p> <p>As consumer goods no longer are characterized by shortage and China has developed into a consumer economy, it is now in business where managers still need to deal with the remains of the state economy</p>	further development and changes guanxi should adapt accordingly
Corporate Governance	Clarke, 2003	Corporate governance in China: an overview	<p>Through a deficit of enforcement and minority shareholder protection, resources are tunneled out of SOEs through state shareholders which despite of corporatization frequently remain the controlling shareholder</p> <p>Governmental goals followed instead of those of shareholders which are not necessarily identical</p>	Agreement on the problematic influence of state control and lack of shareholder protection on the tunnelling of resources out of companies
Corporate Governance and ethics	Jing et al., 2005	Corporate governance in China: ethical and legal problems	<p>Giving responsibility for listing to the stock markets themselves would improve performance as stock markets would have an initiative to monitor and attract valuable companies</p> <p>Business ethical standards in China are too low to ensure fair and effective transactions and consequently need to be raised</p> <p>A more stable regulatory framework and proper enforcement of corporate governance codes is required</p>	The impact of Chinese culture and ethics is discussed in relation to corporate governance practices in China
State influence on Corporate Governance	Lui, 2005	Corporate governance in China: current practices, economic effect, and	<p>China exhibits poor shareholder protection, not taking shareholder interest in the form of value maximisation as a priority and insider trading is widespread</p> <p>Firms tightly controlled by the government as a controlling shareholder – harms the development of the stock market</p>	<p>The tight control of the state on public companies seems to be the main problem of Chinese stock market development</p> <p>This in connection with the</p>

		institutional determinants	<p>The state as a controlling shareholder has great influence over the appointment of influential positions such as CEO, senior management, independent directors and chairman resulting in boards dominated by state representatives</p> <p>Politically connected CEOs often to appoint other bureaucrats to other board positions - domination of state representatives on boards</p> <p>78% of listed companies are controlled by some parent company or belong to a group which facilitates tunnelling of resources</p>	importance of social relations leads to a misallocation of (influential) job positions
State influence and CG	Xu and Wang, 1999	Ownership structure and corporate governance in Chinese stock companies	<p>China typically exhibits very concentrated ownership in the hands of the state or institutions</p> <p>Institutional investors are needed for the protection of minority shareholders who have no incentive to monitor on their own, especially in China where the legal protection of minority shareholders is weak due to institutional determinants or historical reasons - institutional investors have the necessary power to control companies</p> <p>An increase in legal person shares is positively correlated with profitability of a firm whereas state control negatively influences market valuation</p>	<p>The assumption that market valuation suffers from the state as the controlling shareholder has been confirmed by many authors</p> <p>Institutional investors are necessary as market mechanisms for corporate control cannot be relied on</p>
Tunnelling	Liu and Lu, 2004	Earnings management to tunnel: evidence from China's listed companies	Especially in emerging markets the concept of tunnelling exhibits particular relevance as inferior corporate governance mechanisms such as lack of independent board members, poor protection of dispersed shareholders, malfunctioning takeover markets and low disclosure quality provide prospects for abuse by controlling shareholders	The reduction of state influence and pyramiding is therefore needed to reduce abuse of shareholders

CG: supervisory board	Dahya et al., 2003	The usefulness of the supervisory board report in China	<p>The usefulness of the supervisory board report depends on the function the board has adopted, whether is preferably independent and actually monitoring managerial practices or if it is merely an “honoured guest”, a “friendly advisory” or a “censored watchdog”, all of which are heavily dependent on the CEO or the board of directors, have little or no expertise and thus almost no monitoring or actual supervisory powers</p> <p>The independence of supervisory boards is common amongst companies predominantly issuing B-shares, H-shares or that are listed in foreign exchanges, as they are confronted with stricter auditing and monitoring</p>	The improvement of the supervisory board report requires and underlying melioration of supervisory boards function, competence and independence
Supervisory board	Xiao et al., 2004	A grounded theory exposition of the role of the supervisory board in China	<p>The board of directors has authority to appoint CEOs and senior management, call shareholders’ meetings, implement resolutions of shareholder meetings, determine internal management systems and undertake necessary decisions</p> <p>Interviews among high executives and board members typically showed that the supervisory board rather fulfilled a subordinated advisory role, typically lacking information from the board of directors and management - the greater their independence the more likely they suffered from lack of insider information and were treated as outsiders</p>	The exchange of Independence for information is a problem that the supervisory board is typically confronted with
Influences on market valuation	Bai et al., 2004	Corporate governance and market valuation in China	<p>Empirically investigated the relationship between governance mechanisms and the market valuation and found a positive effect of a high concentration of non-controlling shareholders and the issuing of shares to foreign investors on market valuation</p> <p>Large holdings by the controlling shareholder, the CEO being the chairman or vice chairman of the board of</p>	This positive effect could be a consequence of increased and effective monitoring by the more sophisticated outsiders and the increased disclosure and financial transparency required for

			directors and the largest shareholder being the state were all found to have negative effects on market valuation	international listing
Business risk	Hoenig, 2006	Managing business risks	<p>One individual often holds all the trivial management and controlling positions of public companies (typically corporatized SOEs) which leaves the manager all possibilities for fraud, without having to bother about internal control</p> <p>Pre-employment screening especially for top executive positions is suggested to explore for any corrupt background</p> <p>Over the past five to eight years guanxi’s significance and importance for achieving business success in China has been reduced due to an improvement in market regulations</p>	<p>Suggestions on how to handle the problem of corruption in China especially as a foreigner not acquainted with Chinese business conduct</p> <p>Agreement on the reduced importance of guanxi due to an improvement of market regulations</p>
Corruption and the state	Yao, 2002	Privilege and corruption: the problems of China's socialist market economy	<p>The core of current Chinese corruption is caused by the government’s struggles against loss of control over certain industries and procedures while at the same time opening the economy - officials are placed at the centre of the market and enabled to draw profits out of companies into their own pockets</p> <p>China’s political system (CCP) which grants and protects privileges (privileged use their monopoly power to exploit the ordinary people’s wealth) causes social unfairness and economic inefficiency and is responsible for China’s corruption problems – unless this is eliminated, China will never dispose of its corruption problem</p>	<p>Highlights the influence of the CCP on the Chinese corruption problem</p> <p>The resulting privileges given to governmental officials grant them monopoly powers to exploit the public good</p>
Corporate culture	Pang et al., 1998	Doing business in China – the art of war?	<p>Working at an enterprise equals group belongingness fundamental to China’s collectivist society - group stands above individual</p> <p>Guanxi establishment between superior and employees -</p>	The importance of relationship establishment not only between business partners but also within an

			employees are very loyal if guanxi and a feeling of indebtedness has been established with superiors and management	organization itself is stressed which secures loyalty and dedication of employees
Corporate culture	Pun et al., 2000	A review of the Chinese cultural influences on Chinese enterprise management	<p>A corporate culture that constitutes to continuous performance improvement is necessary for achieving business success and maintaining competitiveness</p> <p>China’s collectivist culture has a great influence on corporate culture, typically exhibiting a paternalistic management approach stressing the importance of relationships within an organization and the acceptance of hierarchy and obedience to superiors</p>	The particularity of Chinese culture largely influences the management of corporate culture as culture nurtures the development of corporate culture within organizations
Corruption in Singapore and Hong Kong	Quah, 1999	Comparing anti-corruption measures in Asian countries: lessons to be learnt	<p>Singapore and Hong Kong have effectively implemented an independent anti-corruption agency along with a clear and comprehensive anti-corruption legislation.</p> <p>Corruption triggered if salaries are low, opportunities are provided and the probability of getting caught and the punishment is low. The ideal strategy for regulations against corruption should lie in the creation of a high risk-low reward perception of corruption</p>	<p>Efforts by China made to strengthen the high risk-low reward strategy through harsh punishment.</p> <p>China should aim at implementing one independent anti-corruption agency and to strengthen its legislation against corruption</p>

Many authors have modelled the complex concept of guanxi, explaining it as a dynamic and dyadic process of social interaction (Chen & Chen, 2004; Fan, 2002) or highlighted and analysed numerous characteristics of the Chinese phenomenon such as quality determination (Chen & Chen, 2004). Generally, a division into three categories of guanxi is common, including a category for stranger or acquaintances so-called helper-guanxi, family guanxi and business guanxi (Fan, 2002; Yang, 1994). Numerous authors have also attempted to explain Chinese guanxi with Hofstede’s culture dimensions, defining Chinese as a collectivist society (Dunning & Kim, 2007) with a strong power-distance dimension (Buttery and Wong, 1999).

Overall, authors are in accordance with the belief that guanxi is a key determinant of successful business operation in China (Fock & Woo, 1998; Luo & Chen, 1997; Pearce & Robinson, 2000, Tsang; 1998) which has been confirmed by numerous empirical studies (Luo, 1997; Luo & Chen, 1997; Yeung & Tung, 1996; Peng & Luo, 2000).

Guanxi’s importance and development is frequently brought into connection with the lack of legal institutions and problematic law enforcement (Arias, 1998; Dunfee & Warren, 2001; Yeung & Tung, 1996; Xin & Pearce, 1996) due to which people established their own system, relying on trust instead of a false, corrupt and incomplete legal system. Further, it is considered a response to unstable political and social conditions (Arias, 1998; Dunfee & Warren, 2001; Xin & Pearce, 1996), consequently guanxi’s significance should decrease as the situation improves.

Studies have also shown that smaller, private enterprises rely more heavily on guanxi usage than larger multinationals (Hutchings & Murray, 2002) or state-owned or collective hybrid companies (Xin & Pearce, 1996).

The assumption that, if applied correctly, guanxi may reduce transaction costs has also been supported by numerous guanxi scholars which is primarily a result of reduced opportunistic behaviour, guanxi resembling a sort of insurance against opportunistic actions of partners (Hitt et al., 2002; Lee & Wong, 2001; Lovett et al., 1999, Standifird & Marshall, 2000). However, guanxi is also needed to obtain various kinds of resources from tangible to intangible (Davies et al., 1995; Fock & Woo, 1998; Hitt et al., 2002; Lovett et al., 1999, Pearce & Robinson, 2000) and

consequently, to achieve competitive advantage. High quality guanxi connections are also required for receiving valuable and reliable information which is why guanxi is often considered a bridge to knowledge transfer (Ramasamy et al., 2006; Davies et al., 1995). Nevertheless, conformity is also found concerning the existence of negative effects of guanxi. Besides the main disadvantage of guanxi's time consuming nature (Fock & Woo, 1998; Lovett et al., 1999; Pearce & Robinson 2000; Steidlmeier, 1999; Tsang, 1998) reliance on guanxi practices is also considered costly, risky and unpredictable (Fan, 2002; Tsang, 1998).

Authors that have analysed the similarities and differences of guanxi and relationship marketing have agreed that these two concepts are distinctive from one another although they share many similarities (Arias, 1998; Yau et al., 2000). However, it has also been argued that the increased relevance of relationship marketing in the West resembles a movement towards more guanxi orientated business practices (Lovett et al., 1999).

Numerous authors have analysed the problematic relationship between guanxi and corruption (e.g. Luo, 2002; Steidlmeier, 1999; Vanhonacker, 2004). Although most authors agree that corruption and guanxi are based on completely different values and are two different concepts by nature (Vanhonacker, 2004) consensus exists on the thinness of the borderline that separates them (Standifird and Marshall, 2000; Steidlmeier, 1999). Especially the concept of gift-giving, a profound element of guanxi, is often misunderstood and immediately interpreted as bribery (especially) by foreigners although it is necessary to establish trust and convey respect in China (Millington et al., 2005; Standifird & Marshall, 2000; Steidlmeier, 1999; Vanhonacker, 2004). Further, guanxi between business players and government officials is usually considered unethical and corrupt, resulting in the elevation of a few above the law on the costs of the rest of society (Dunfee & Warren, 2001). This privileging is often considered the core of China's corruption problem, causing social unfairness and economic inefficiency (Yao, 2002).

Consensus is found that the peculiar Chinese culture influences corporate culture in China, highlighting group belongingness, acceptance of hierarchy and obedience and management-employee relationship establishment (Pun et al., 2000; Pang et al., 1998).

Conformity also exists to a great extent on the belief that guanxi is a dynamic and changing process whose significance will be reduced in the future with the development of the market economy and an improvement of legal conditions and law enforcement (Arias, 1998; Gurthie 1998; Vahonacker, 2004), which in fact has been illustrated empirically by a number of academics (Ai, 2006; Gurthie, 1998). Further, also the way in which guanxi is used seems to have changed with the development of a consumer economy (Yang, 2002).

Weak shareholder protection and the influence of the government despite corporatization are commonly referred to as the most problematic aspects of Chinese corporate governance (Clarke, 2003; Lui, 2005; Liu & Lu, 2004; Xu & Wang, 1999). As the state consequently is frequently found to be the majority shareholder, great amount of influence lies in its hand concerning the appointment of influential positions, leading to domination by state representatives holding influential board and top management positions (Lui, 2005). Tunnelling resources out of companies is facilitated through unclear or complex pyramidal structures which is also commonly referred to as one of the main problems shareholders are confronted with (Clarke, 2003; Liu & Lu, 2004; Lui, 2005). Studies have shown the negative influence of governmental control on stock market valuation (Bai et al., 2004, Xu & Wang, 1999).

The weakness of the Chinese corporate governance system especially with regard to shareholder protection calls for an increment of institutional investors (Liu, 2005; Wu & Wong, 1999, Xu & Wang, 1999) which would have sufficient power and motivation to monitor the controlling shareholder. Authors agree that an additional burden results from the frequent suppression of the supervisory board which often only fulfils a subordinate, advisory role. The supervisory board is often dependent on the management for insider information and consequently has difficulties effectively monitoring managerial actions (Dahya et al., 2003; Xiao et al., 2004).

Conclusion

Regardless of the drastic changes China has witnessed over the past few decades, relationships still occupy a significant role in Chinese business life which is partially due to the deeply-rooted principles of Confucianism, still having a great influence on Chinese mentality and behaviour and partially due to the imperfect markets that still characterize Chinese economy (Michailova and Worm, 2003). As the legal system in China is still very ill-defined, intransparent and numerous layers of government officials need to be consulted before achieving ones objectives, guanxi can be considered an alternative to the governmental system and a free market economy through the creation of trading associations (Chang, 1993). However, especially between business and government guanxi, the thin borderline between guanxi and corruption needs to be closely monitored as these two concepts are related to each other, guanxi often causing corruption, being used to hide corrupt practices or a euphemism for corruption.

Business guanxi, a way to share scarce resources to enhance business performance (Su et al., 2003) through a network of connections, has become a widely recognized concept. Although its importance varies depending on the type and size of a corporation its importance seems to be undeniable. For the achievement of competitive advantage, successful guanxi needs to be maintained with government authorities, suppliers, buyers and business partners (Luo, 2000: 247). However, as China's markets are advancing and competition is intensified attention needs to be paid also to competitiveness, guanxi resembling a necessary but not sufficient condition for business success (Luo, 2000: 91). Monitoring the balance between costs of guanxi establishment and maintenance and the benefits achieved through the connections is crucial. Attention needs to be paid to not invest too many resources into guanxi as this may crystallise to be a risky and costly strategy as a consequence of guanxi's intangibility, uncertainty and lack of stability.

The opening of the borders and economy and the resulting new business opportunities along with the fact that the government and bureaucrats hold a monopoly position over scarce resources and power leads to the use of bribery and illicit payments by businessmen to attain some of the power held by bureaucrats. The bureaucrats create profits for themselves directing resources into

their own pockets, exploiting the public good and the ordinary person through their actions as well as hurting the effectiveness of competition. The government holds onto control of certain industries and SOEs instead of relying on the governance of market mechanisms that would drive inefficient firms out of the market (Dorn, 1998). This results in a waste of resources that are inserted in inefficient SOEs to follow certain governmental objectives, typically not in accordance with shareholder value maximisation. As Fan (2007) stated, although to some degree an achievement, “the greatest paradox is the co-existence of old communist state politics and a new capitalist economy” characterizes the current special situation of China. Nevertheless, this gradual piecemeal fashion of implementing a free market system from a planned economy has its advantages and evades a lot of risk. However, in order for China to become more efficient it needs to reduce its tight grip and completely privatise SOEs to decrease political influence on economics and reduce corruption. In fact, the negative influence of state control on enterprises has been shown through numerous studies. However, it is not the state ownership de facto that has a negative influence but the exploitation the state exercises. As stated by Harvey (1999), through the socialist market economy the “money-worshipping” has become prevalent and the sense of business morality has diminished.

As the state is frequently the controlling shareholder of listed SOEs, minority shareholder exploitation is common. Managers use company assets in their own interest or direct money to the controlling shareholder through tunnelling. Improvements have been witnessed through enhanced corporate governance regulations, however a lack of enforcement is considered one of the main problems. This lack of enforcement and comparatively low standards of corporate governance leaves room for corrupt behaviour while at the same time, corruption prevents adherence to and implementation of corporate governance codes.

Guanxi can be considered as a way to overcome the inefficiencies of the communist bureaucracy and in fact, studies have exhibited the positive relationship between guanxi and firm performance. However, if guanxi becomes closely related to corruption, the reputation of an enterprise might be seriously hurt. As this spreads quickly through the guanxi network, the company is likely to

loose its business contacts, customers as well as investors possibly resulting in bankruptcy.

Nevertheless, favouritism and privileging are unfair and unethical, conflicting with competition and basic principles of a market economy. In the long-run, this favouring of a few on the expenses of others harms economic development and reduces social well-being. In the future, guanxi’s significance for business in China is likely to survive, although most authors agree that its importance will be reduced through enhanced competition and an improvement of the legal system. This can typically be seen when looking at Singapore or Hong Kong where, despite of well-developed legislation, corporate governance and low levels of corruption, guanxi still exist.

Great opportunities can be expected when doing business in China, but all of the challengers must be aware of the peculiarity of business conduct and the great amount of risk that is included.

II. Appendix I – Deutsche Zusammenfassung

Ziel dieser Diplomarbeit ist es, den Einfluss den das besondere Beziehungssystem namens Guanxi auf die Chinesische Wirtschaft und deren Entwicklung ausübt, anhand einer ausführlichen Literaturrecherche und Metastudie zu analysieren.

Guanxi, welches oft als Erbe Konfuzius und dessen Lehren angesehen wird, ist tief eingewurzelt in der Chinesischen Gesellschaft und übt nach wie vor seinen Einfluss auf Menschen und deren Handlungsweisen aus, nicht nur in der Volksrepublik Chinas sondern auch in der Republik China (Taiwan), Singapur, Hongkong und in ähnlicher Form in Korea und Japan.

Andererseits wird Guanxi auch oft als Resultat zahlreicher Revolten, vor allem der Kulturrevolution (1966-1976), und der folgenden politischen und sozialen Unruhen angesehen, sowie auf ein fehlendes oder lückenhaftes Rechtssystem und auf dessen mangelhafte Durchsetzung zurückgeführt

Die Entwicklung einer marktwirtschaftlich orientierten Gesellschaft unter kommunistischem Regime und die daraus resultierenden Schwierigkeiten mit Unterdrückung beziehungsweise Bevorzugung diverser Gruppen und Schichten, scheint die offensichtlichen und häufig gezogenen Verbindungen zwischen Guanxi und Korruption verstärkt zu haben.

Des Weiteren ist der staatliche Einfluss in teilprivatisierten Unternehmen ein häufiger Konfliktpunkt, da aus diesen oft mit Hilfe unübersichtlicher Konzernbildung und undurchsichtigen Managementpraktiken Ressourcen in privaten Taschen anstatt bei den Aktionären landen.

Guanxi, dessen Anwendung meist als eine der essentiellsten Eigenschaften eines erfolgreichen Geschäftsmannes in China angesehen wird, weist neben Vorteilen wie z.B. der Reduktion von Transaktionskosten vor allem durch Minimierung opportunistischen Verhaltens und erleichtertem Zugang zu Ressourcen und folglich Wettbewerbsvorteilen auch zahlreiche Nachteile auf. Diese spiegeln sich vor allem im erhöhten Zeitaufwand wider sowie in der Risikoreichhaltigkeit dieser Strategie. Vor allem muss aber der negative Einfluss auf die Entwicklung der Wirtschaft und die Schaffung eines unfairen und ineffektiven Marktwettbewerbs bedacht werden, welcher Einigen Vorteile aufgrund ihrer Beziehungen verschafft, die nicht mit Leistung und Konkurrenzfähigkeit im Einklang stehen.

Die Analyse der unterschiedlichen Bedeutung von Guanxi in Taiwan und Singapur zeigt, dass negative Auswirkungen stark von gesellschaftlichen Rahmenbedingungen abhängen und insbesondere durch staatliche Kontroll –und – Sanktionsmechanismen weitgehend verhindert werden können.

Mit der Entwicklung der chinesischen Wirtschaft sowie des Rechtssystems und dessen Durchsetzung und einem steigenden Lebensstandard, scheint Guanxi zumindest teilweise an Bedeutung zu verlieren, wobei Elemente der Konkurrenzfähigkeit wie Qualität und Preis zunehmend wichtiger werden, wenngleich Guanxi noch immer als ein wichtiger und nicht vernachlässigbarer Aspekt der Chinesischen Geschäftswelt anzusehen ist.

III. Appendix II – Lebenslauf

1. Persönliche Daten

Geburtsdatum: 29.06.1984

Geburtsort: Wien

Familienstand: ledig

2. Ausbildung

Schulausbildung

1995-1998: American International School of Zagreb

1998-1999: IB International School in Zagreb

1999-2002: IB International School in Ljubljana, Matura im Juni 2002,
(ausgezeichnet mit Zweisprachigem Diplom)

Studium

Seit 10/2003: Universität Wien, Internationale Betriebswirtschaftlehre (BWZ);

Spezielle: International Marketing (Prof. Diamantopoulos)

Industrial Management (Prof. Wirl)

02/2006 – 06/2006: Auslandssemester in Lissabon; Universität ISCTE

3. Tätigkeiten

07/2004-08/2004: Entertainment Organizer in Rimini, Italien

01/2005-05/2007: Geringfügig Beschäftigt bei der Catering Firma “Table-Service-Team”

06/2007 – 01/2008 Geringfügig Beschäftigt bei Karmasin Motivforschung GmbH

08/2007-09/2007: Praktikum bei Karmasin Motivforschung GmbH

03/2008-04/2008: Volontariat bei der Österreichischen Außenhandelsstelle in Manila, Philippinen

4. Weitere Qualifikationen

Sprachkenntnisse: Englisch (fließend)

Italienisch (fortgeschritten)

Portugiesisch (Anfänger)

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