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**Title: The role of Guanxi in buyer-supplier relationships in Chinese small and medium-sized enterprises – a resource based perspective**

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# The role of *Guanxi* in buyer-supplier relationships in Chinese small and medium-sized enterprises – a resource based perspective

## Abstract

This paper examines the role of *guanxi* (personal relationships or connections) in buyer-supplier relationships in Chinese small and medium-sized enterprises (SMEs), through exploratory research that gained access to companies actually using *guanxi*. The resource-based view (RBV) provided a systematic approach for analysing the role of *guanxi* in terms of its potential to be a source of sustained competitive advantage.

Business *guanxi* connections were identified as possessing the potential to be considered an organisational resource. This study identified several valuable attributes of *guanxi* at the organisational level. However, the *guanxi*-based advantage can only be sustained under certain conditions. SMEs should create an organisational environment that encourages their employees to actively establish and maintain *guanxi* connections within the company and beyond. However, companies in China need to recognise that firms that possess superior technological skills or capabilities have a stronger bargaining power, as they are able to deliver quality at competitive prices over the long run.

**Keywords** – *Guanxi*, buyer supplier relationships, resource-based view, China

## 1. Introduction

With a population estimated to be in excess of 1.35 billion, a transition towards a market based economy and apparently permanent positive economic growth, the People's Republic of China (PRC) is reputed to be one of the world's largest and fastest growing emerging and promising markets (National Bureau of Statistics of China, 2012). In the academic literature China is often portrayed as being a relational society, where the cultural concept of *guanxi* (personal relationships or connections) has a major influence on both social and business norms (Tseng *et al*, 1995; Styles & Ambler, 2003). Rooted in the Confucian philosophy *guanxi* practice has been pervasive in the lifeblood of the Chinese business community for more than 2000 years. Personal networks are popular universally, but in China, they have unique, distinct ways of operation (Gu *et al*, 2008) and any business, irrespective of size, local or foreign ownership, inevitably face *guanxi* dynamics in China (Luo, 1997a). So, while similar concepts to *guanxi* can be found in other cultures, we believe that the importance of *guanxi* relationships in Chinese social and business life deserves special attention (c.f. Standifird & Marchall, 2000).

While the Chinese government has pursued its liberalisation reform and promoting foreign investment, it has also encouraged a wide variety of privately owned SMEs to emerge (Carlisle & Flynn, 2005). In the past decade, private SMEs have been starting to gain tremen-

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dous economic momentum and have been playing an important role in the Chinese economy (Cunningham & Rowley, 2010). Particularly, they have been easing employment pressure, encouraging non-governmental investment, contributing significantly to the economy's growth and helping disperse the market prosperity among the broader population (Anderson *et al*, 2003).

The link between *guanxi* and SMEs appears to be driven by a pragmatic desire for advancement and organisation survival. *Guanxi* can be an important business tool to launch new commerce for SMEs because they often have neither a strong brand nor sufficient trust in relationships for doing their business. In addition, many Chinese SMEs face enormous handicaps such as lack of legitimacy, resources and lack of government support. In an environment such as this, *guanxi* becomes crucial in cultivating business relationships, managing scarcity, securing production factors, distribution channels, and institutional support and for that matter the firm's survival (Xin & Pearce, 1996; Carlisle & Flynn, 2005). Su *et al* (2003) suggests that SMEs are perhaps more dependent on *guanxi* and thus might have different needs and capacities than larger companies due to their scarce resource base. They are therefore an import area for research with regards to the application of this business tool (*guanxi*).

The previous academic literature has faced a scarcity of resource-based analysis with sufficient theoretical depth regarding *guanxi* in buyer-supplier relations from the perspective of Chinese SMEs. Adopting the resource-based view (RBV) theory, the role was examined in terms of the potential of *guanxi* to be considered as a source of sustained competitive advantage. Specifically, two research questions were posed for this investigation: *Question 1:*

How does *guanxi* in buyer-supplier relationships act as a source of competitive advantage for Chinese SMEs?; *Question 2:* When is this *guanxi*-based competitive advantage considered to be sustainable? By adopting an exploratory perspective for the research, the semi-structured and in-depth interviews with Chinese managers revealed some interesting insights and conclusions. Business *guanxi* connections were identified to possess the potential to serve as an organisational resource. They constitute a valuable part of the human resource and some of the connections can even be considered as strategically important for SMEs. Furthermore, this study identified several valuable attributes of *guanxi* at the organisational level. According to the RBV framework, *guanxi* can be considered as a potential source of competitive advantage. However, the *guanxi*-based advantage can only be sustained under certain conditions; these are explained further in this paper.

The paper is structured as follows. First, literature on the RBV and aspects of *guanxi* are briefly presented. This literature is used to assist in the research design and qualitative data on China and *guanxi* are presented in the findings. These are then discussed and compared to

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findings from the literature. We finish with conclusions and suggestions for both researchers and practitioners alike.

## 2. The literature

Within this section we briefly present literature on the RBV and aspects of *guanxi*. This has been done to: i) reduce the degree of crossover between the literature and discussion sections; ii) control the word count within reasonable limits; iii) focus more on the ‘value add’ through the defined contribution of the discussion.

Business practices and concepts of relationship management differ in many regions of the world (Hofstede, 1983). In the case of China, a major difference constitutes the concept of *guanxi* which represents an important cultural component of buyer-supplier relationships (Ambler, 1994; Wong, 1998). In Chinese, *guanxi* refers to two characters, *guan* and *xi*, meaning “gate” and “connection” (Wan and Ng, 2013) and Cheng (2007:81) states that “one must pass the gate to get connected to [the] networks”. But what are the differences between *guanxi* and standard relationship management in Western companies? In the West, business relationships are also important resources for creating opportunities. Personal relationships and connections which are similar to *guanxi* exist in any country although definitions do differ from the term *guanxi*. Cheng (2007) identifies the differences between relationship management and *guanxi* in terms of: i) the personal characteristic of *guanxi* and the particular nature of the relationship; ii) trust from *xinyong* (trust); and iii) trust and the unique meaning of *renqing* (favour). *Xinyong* and *renqing* are said to direct behavioural norms in *guanxi*, and this is different from the Western concept of relationship management in terms of the order in which transactions and relationships take place and the short-term versus long-term nature of business transactions (Geddie *et al.*, 2002 and 2005; Sin *et al.*, 2002).

*Guanxi* is therefore complex, multi-faceted and existing definitions in the literature do not capture its true nature (Fan, 2002). Lovett *et al* (1999) and Park and Luo (2001) suggested that i) favour, ii) reciprocity, iii) face, iv) trust and v) affection are the central dimensions of *guanxi*. Please see Table 1.

Table 1 – Aspects of Guanxi

Aspect	Definition	Author(s)
Favour (renqing)	Guanxi relationships are established or strengthened when one party does something, e.g. a favour (renqing), thereby developing an unpaid obligation.	Hwang, 1987
Reciprocity (bao)	Guanxi also embodies reciprocity (bao) of renqing obligations by all parties involved. When one individual receives a favour, he/she is expected to reciprocate the favour in the future.	Hwang, 1987; Luo 1997a; Wong <i>et al.</i> , 2007
Face (mian-)	A key component in guanxi dynamics is defined as “... one’s respect,	Wong <i>et al.</i> , 2007, p.

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zi)	status, and moral reputation and an image of self-delineation in terms of approved social attributes as the recognition by others of one's social standing and situational defined position".	878
Personal trust (xinyong)	Due to the lack of stable political and legal structures in China, personal trust (xinyong) sometimes plays a more salient role than legal contracts among Chinese businessmen. Xinyong is different than the Western concept of trust; it can refer to the integrity, credibility, trustworthiness, or the reputation and character of a person.	Yau <i>et al.</i> , 2000; Wang, 2007; Tong & Yong, 1998; Leung <i>et al.</i> , 2005; Humphreys <i>et al.</i> , 2011
Affection (ganqing)	The Chinese term for affection, sentiment, and a measure for emotional commitment or the degree of closeness. It determines an important dimension of guanxi 'quality'. Building-up ganqing requires prerequisites, such as the experience of sharing and social interactions through the process of living, working or studying together.	Tsang, 1998; Tong & Yong, 1998

Examining a firm's competitive advantage from the RBV perspective allows emphasis of the magnitude of importance placed upon the firm's internal resources, such as capabilities associated with relational assets (Dyer & Sign 1998; Hunt, 1997; Morgan & Hunt, 1999, Yang, 2008). A firm's resources can be perceived as strengths that a firm can use to conceive and implement its strategies (Barney, 1991) and categorised as financial, physical, human, and organisational assets (Barney, 1991; Morgan & Hunt, 1999). *Guanxi* might be considered as part of the firm's human resources (Tsang, 1998; Fan, 2002) and primarily relates to personal relations and exchanges that take place among members of *guanxi* networks (Fan, 2002). Consequently, *guanxi* processes are often represented as a long-term personal investment into ones 'social capital' (Xin & Pearce, 1996; Luo, 1997a; Luo & Chen, 1997; Tsui & Farh, 1997; Nahapiet & Ghoshal, 1998; Fan, 2002; Standifird, 2006). On the other hand, *guanxi* can be perceived as an organisational resource if it is utilised for the purpose of the organisational goal achievement or as a way of finding business solutions (Xin & Pearce, 1996; Yeung & Tung, 1996; Luo, 1997a; Tsang, 1998; Fock & Woo, 1998; Park & Luo, 2001; Standifird, 2006; Gu *et al.*, 2008). *Guanxi* can also be considered to be an organisational strategic resource (Peng & Heath, 1996; Luo 1997a,b; Luo & Chen, 1997; Zhang & Keh, 2010). Furthermore, resource heterogeneity and imperfect mobility represent two core elements of the RBV theory (Barney, 1991). Park and Luo (2001) have empirically proven that *guanxi* utilisation is heterogeneous across firms and depends on the institutional, strategic, and organisational settings of each organisation. Regarding resource mobility, however, *guanxi* that is related to human resources is argued to be mobile in nature (Luo, 1997a; Fan, 2002). Consequently, when an employee leaves the company, the *guanxi* connections leave the organisation with him/her (Fan, 2002). Thus, the imperfect mobility of personal *guanxi* depends upon the extent to which the company can retain its staff (Wright *et al.*, 1994; Barney & Wright 1998; Tsang, 1998). *Guanxi* as an organisational resource, on the other hand, has the characteristic of being imperfectly mobile (Tsang, 1998).

A firm's attributes must be valuable in order to be considered as strategically important

resources under the RBV (Barney, 1991; Yang, 2008). A review of the available literature identified seven *guanxi*-based value drivers. Please see Table 2.

Table 2 – *Guanxi*-based value drivers

Aspect	Definition	Author(s)
Alternative governance mechanism	<i>Guanxi</i> mechanisms such as trust, favour and face giving reduce risks in weak and uncertain legal systems and governmental institutional support	Xin and Pearce, 1996
Gaining access to scarce resources	A primary <i>guanxi</i> function which helps accommodate growth	Davies <i>et al</i> , 1995; Xin & Pearce, 1996; Yi & Ellis, 2000; Pearce & Robinson, 2000; Park & Luo, 2001; Su <i>et al</i> , 2003
Trustworthy, richer, and more useful information	The organisational <i>guanxi</i> network of reliable sources saves search costs, allowing partners to make more informed decisions	Luo, 1997a; Millington <i>et al</i> , 2006
Gain access to new business opportunities	Facilitates ‘back doors’ into the business community, through preferential treatment and mutual support instead of arms length dealings	Yi & Ellis, 2000; Ambler, 1994; Luo 1997a
Corporate reputation enhancement	Development and maintenance of a network of high-quality contacts	Davies <i>et al</i> , 1995; Yi & Ellis, 2000; Standifird, 2006; Fan, 2007
Reduce transaction costs	The potential to reduce opportunistic behaviour	Luo, 1997a; Standifird & Marshall, 2000
Smooth transaction arrangements	E.g. the smoothing of transportation arrangements, procurement of production resources, collection of payments, long-term mutual collaborations between parties	Davies <i>et al</i> , 1995; Leung <i>et al</i> , 1996; Lee & Dawes, 2005; Lee & Humphreys, 2007, Humphreys <i>et al</i> , 2011

*Guanxi* was identified as really providing value. However, investment of resources such as effort, time and money are required for the cultivation, maintaining and utilisation of *guanxi* relationships (Luo & Chen, 1997; Fock & Woo, 1998; Lovett *et al*, 1999; Park & Luo, 2001). An important feature of *guanxi* is therefore that it is an organizational resource which belongs to specific individuals; in this it differs from other resources that can contribute to improved performance, effectiveness and efficiency. In general terms, organizations can accumulate business resources (such as know-how, skills, and capabilities) but *guanxi* is a mobile human specific resource. This means that when an employee leaves the company, the *guanxi* connections leave the organization with him/her (Fan, 2002). *Guanxi* is important for SMEs and business start-ups because they are often struggle to secure excellent human resources.

The RBV literature discusses a variety of isolating mechanisms, which act to preserve

the sustained competitive advantage<sup>1</sup>. Please see Table 3.

Table 3 – A variety of isolating mechanisms that preserve the sustained competitive advantage, according to the RBV

Aspect	Definition	Relevant Author(s)
<i>Guanxi</i> as a rare resource	Businesses may face difficulties in the form of scarcity of appropriate <i>guanxi</i> connections	Tsang, 1998; Dyer & Sign, 1998; Wong & Chan, 1999; Yeung and Tung, 1996
<i>Guanxi</i> as an imperfectly imitable resource. Barney (1991) presented three characteristics of a resource that make it difficult for rivals to imitate	i) unique historical path dependence	Yeung and Tung, 1996; Tsang, 1998; Dierickx & Cool, 1989; Barney, 1991; Luo, 1997a; Fan, 2002
	ii) social complexity	Barney, 1991; Park & Luo, 2001; Ramasamy <i>et al</i> , 2006; Wong <i>et al</i> , 2007; Yeung and Tung, 1996; Dierickx & Cool, 1989; Barney & Hansen, 1994
	iii) casual ambiguity	Barney, 1991; Tsang, 1998
<i>Guanxi</i> as an imperfectly substitutable resource	A review of <i>guanxi</i> literature revealed that the concept of substitutability and non-substitutability of <i>guanxi</i> is not addressed within the academic discussion so far	Barney, 1991

The literature review revealed limited studies (one) that attempted to address *guanxi* from a RBV perspective. Tsang's (1998) analysis came to the conclusion that *guanxi* represents a necessary company resource, but as the sole success factor it is not sufficient for business success in China. However, Tsang's study faced several limitations. First of all, he did not fully apply the RBV framework for his analysis. Particularly, his analysis did not address the substitutability question. Moreover, as with many other *guanxi* studies, there was no distinction made between *guanxi* with the government and the *guanxi* utilised in buyer-supplier relations, which can be different in nature (Park & Luo, 2001). Furthermore, Tsang also did not make the distinction between large and small and medium-sized companies. Finally, similar to the majority of *guanxi* literature, Tsang (1998) emphasised *guanxi* from the perspective of foreign enterprises but did not provide a focus on enterprises with a mainland Chinese background. This is an indication of the paucity of literature regarding a resource-based analysis with a sufficient theoretical depth of the role of *guanxi* in buyer-supplier relations in SMEs in China. Indeed, Wan and Ng (2013) in their paper focused on the significance of *guanxi* in relationship marketing (on perspectives of foreign banks in China) identify a lack of literature on relationships between *guanxi* and marketing/operations and call for further research in this area. Consequently, this investigation intends to cover this research gap.

<sup>1</sup> For assumed mechanisms see above, *guanxi* as a heterogeneous and an imperfectly mobile organisational resource.



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### 3. Research methodology

The aim of this research was to examine the role of *guanxi* in buyer-supplier relationships in Chinese SMEs. Specifically, the role was examined in terms of the potential of *guanxi* to be considered as a source of sustained competitive advantage. By adopting the RBV framework as a theoretical lens, two research questions were identified as appropriate: *Research question 1*: How does *guanxi* in buyer-supplier relationships act as a source of competitive advantage for Chinese SMEs? This question is primarily concerned with the analysis whether *guanxi* can be considered as an organisational resource and what valuable attributes it can provide to Chinese SMEs; *Research question 2*: When is this *guanxi*-based competitive advantage sustainable? This question allowed the analysis of the sustainability mechanism – rareness, imperfect imitability and imperfect substitutability.

A qualitative approach was considered appropriate due to the exploratory nature of the research - it enabled an investigation into areas of socio-cultural life, such as *guanxi* relations, where the collection of quantitative data is difficult or not possible to conduct (Glaser & Strauss, 1967; Bamford, 2008). This method emphasises a more open approach of data collection, which provides the opportunity to acquire in-depth rather than breadth data and understanding over the complex *guanxi* concept (Remenyi *et al*, 1998; Silverman, 2005).

The tentative nature of the research was very much emphasised by the struggle to get managers to take part. Whilst in general conversation people were willing to give an opinion on *guanxi*, once a request for a more formal discussion was made many managers chose not to proceed. Indeed, prior studies showed that Chinese people are reluctant to reveal information about their personal *guanxi* to strangers due to its sensitive nature (Yeung & Tung, 1996; Xin & Pearce, 1996; Fan, 2002).

To try and overcome the difficulty of finding managers willing to talk openly about the sensitive topic of *guanxi*, two methods were adopted. First, following the suggestion of Yeung and Tung (1996) to rely on personal contacts, managers were asked for a favour to establish an initial contact with Chinese managers in Chinese SMEs. The authors did have the restriction that they needed managers able to speak English (interestingly, this did not appear to be a problem at all), and for them to gain permission for an interview with the author (this was a problem). The second method employed relied on the so-called ‘snow-balling’ approach (Remenyi *et al*, 1998); after each interview it was explained to the interviewees the extremely difficult nature of finding Chinese managers willing and able to talk about *guanxi*. Some respondents were cooperative and provided access to further potential respondents. However, following-up on these few recommendations and getting agreement proved very

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challenging indeed. This is an area mentioned within the recommendations for future research within the conclusion section. Furthermore, in order to protect the identity of the respondents and the companies they represented, the authors had to limit the detail presented on the organisations involved. This is a recognised limitation of the transparency of the primary research but could not be done any other way.

The issues of obtaining access to willing respondents and gaining their permission to use the data collected presented real challenges. In-depth interviews therefore provided the best apparent way to elicit information and control the data gathering as well as to provide deeper insights within this obviously highly sensitive area of research (c.f. Brand & Slater, 2003). Furthermore, this paper has been positioned as exploratory research from a methods perspective. To strengthen the validity of the contribution the authors asked additional respondents to recount actual examples of *guanxi*; we have therefore presented several concrete examples in terms of how *guanxi* works as a useful business tool. These are presented in section 4.6.

### *3.1 Sample profile*

The population addressed in this investigation is targeted at SMEs located in China with Chinese ownership. There is no one standard definition for what constitutes an SME. In the UK the Companies Act 2006 defines an SMEs as: i) a small company has a turnover of not more than £6.5 million, a balance sheet total of not more than £3.26 million and not more than 50 employees; ii) a medium-sized company has a turnover of not more than £25.9 million, a balance sheet total of not more than £12.9 million and not more than 250 employees (Companies Act, 2006). For this research project we have applied this definition. Table 4 outlines the main sample profile of this investigation. The interviewees and the companies are coded in letters to preserve confidentiality and anonymity. The participating companies ranged in size in terms of employees from 5 to 140 with a mean of 63. Regarding the annual turnover, all participants indicated a turnover of less than US\$100 million and thus they can be considered as small and medium-sized in nature. Further, five out of six companies were originally privately established with a history of 3 to 20 years. While, two of the companies belonged to the manufacturing sector (A, C), the rest of the firms (B, D, E, F) embodied mainly service providers. All of the interviewees were Chinese nationals with a gender split of one-third female and two-thirds male. Regarding the educational background, all of the participants disclosed that they have achieved a higher educational degree in Anglo-Saxon educational systems. All of the respondents were engaged in either buyer or supplier relations or both. Five out of six interviewees were senior managers and in charge of either the entire company or major departments. This majority also indicated that they possessed some degree of owner-

ship rights in these companies.

Table 4: Main sample profile

Inter- viewee's Code Charac- teristics	A	B	C	D	E	F
<b>Gender*</b>	F	M	F	M	M	M
<b>Nationality**</b>	MC	MC	MC	MC	MC	MC
<b>Educational Back- ground***</b>	PD	PD	UD	PD	UD	UD
<b>Country of Latest Visited Educational Institution</b>	United Kingdom	United Kingdom	United States	Australia	United States	Canada
<b>Position or Function in Company</b>	Sales Manager	Marketing Director	General Man- ager	Managing Di- rector	General Manager	Managing Director
<b>Relation Towards the Company</b>	Senior Manager	One of the Owners	One of the Owners	Founder and Owner	One of the Founders and Owners	Founder and Owner
<b>Nature of Company</b>	Industrial Manufacturing (Electrical Equipment)	Food and Consumer Goods Wholesale Trading	Industrial Man- ufacturing (Apparel Indus- try)	Information Systems and E- Solutions Pro- vider and Con- sultancy	Third Party Logistics Provider	Chemical and Steel Trading
<b>Headquarters Loca- tion</b>	Shanghai	Shanghai	Yancheng, Jiangsu	Shanghai	Yancheng, Jiangsu	Shanghai
<b>Ownership Type****</b>	Private	Private	Private (Originally: State-Owned)	Private	Private	Private
<b>Origin of Compa- ny's Suppliers</b>	Chinese Sup- pliers	Chinese Suppliers	Chinese Suppli- ers	Chinese and Foreign Suppli- ers	Chinese Suppliers	Chinese Suppliers
<b>Origin of Compa- ny's Customers</b>	Chinese and Foreign Cus- tomers	Foreign Customers	Chinese and Foreign Cus- tomers	Chinese Cus- tomers	Chinese and Foreign Customers	Foreign Customers
<b>Number of Employ- ees</b>	140	5	120	33	70	10
<b>Annual Turnover (in Million US Dol- lars)</b>	< 100	< 100	< 100	< 100	< 100	< 100

\*M=Male; F=Female; \*\*MC=Mainland Chinese; \*\*\*PD= Postgraduate Degree; UD= Undergraduate Degree; \*\*\*\*Private; State-Owned; Hybrid

Source: Authors

Furthermore, to provide real life examples of *guanxi* in application a secondary survey was carried out using seven additional SMEs within the Shenzhen Region; with the findings similarly coded. These companies were all Chinese owned and ranged from a pharmacy supplier with just 10 employees to a manufacturer with 45 employees. Please see Table 10.

### 3.2 Data analysis method

With the permission of the interviewees, all interviews were digitally recorded and transcribed verbatim. The analysis of the qualitative reference data was undertaken in the light of the understanding of the key issues regarding the *guanxi* and RBV theory identified previous-

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ly in the literature review. This allowed the coding of the transcription material into categories derived from the literature, especially the RBV theory categories (Fereday & Muir-Cochrane, 2006). Reliability limitations refer to the difficulty of gaining the same results if the same research procedures are repeated. E.g. the semi-structured interview method would be difficult to repeat as the naturally emerged conversations with the respondents are difficult to replicate (Maylor & Blackmon, 2005). The validity limitation refers to the question whether the results are “*generalisable*” to a broader population (Maylor & Blackmon, 2005, p. 363). The main limitation of this research is the small sample size of six, core, in-depth interviewees and the lack of a random selection. Nevertheless, in the case of exploratory research, it is more about gaining insightful evidence regarding attitudes towards a certain topic in order to generalise to theory rather than to population (Miles & Huberman, 1994). Furthermore, there also might be a sampling bias. The sample was composed of Chinese managers who were able to speak English and possessed a Western educational experience. However, this might not apply to the broader population of Chinese managers. To address this concern, following the main data collection, analysis and discussion an electronic survey was conducted involving seven employee staff in small companies within the Shenzhen Region. The results of this survey are presented, with the addition of several concrete examples of the application *guanxi*. Of course, all concerns regarding research methodologies cannot be directly addressed within this paper, we have therefore made suggestions for further research in the conclusion.

#### **4. Findings**

The RBV framework was adopted as a theoretical lens to guide the research and facilitate a systematic analysis of the role of *guanxi*. Interview transcripts provided a rich evidence base to cover the RBV framework categories.

##### *4.1 Guanxi as an organisational resource*

The identified themes for the potential of *guanxi* to be considered as an organisational resource are summarised in Table 5. All respondents indicated that within their daily business practice they rely on *guanxi* when a need arises, problems need to be solved or when help is needed. The common perception is that *guanxi* can provide a higher likelihood of being successful and achieving company goals.

Table 5: Identified themes within the organisational resource category

<b>Guanxi as an Organisational Resource Identified Themes</b>	<b>Cited by Respond- ents</b>	<b>No. of Citations (out of 6)</b>
Importance of <i>guanxi</i> in daily occupational life and for or- ganisational goal achievement	A, B, C, D, E, F	6
Corporate encouragement for utilising and establishing <i>guanxi</i> connections for organisational purpose	A, B, C, D, E, F	6
<i>Guanxi</i> cultivation as personal value enhancement and or- ganisational <i>guanxi</i> as corporate value enhancement	B, C, D, E, F	5
Incentives provision for establishing ‘fruitful’ organisational <i>guanxi</i>	B, C, D, E	4
<i>Guanxi</i> as an evaluation criterion for new employees	B, D	2
<i>Guanxi</i> as a strategic tool for approaching customers	A, B, C, D, E, F	6
Formal budgets for establishing new and maintaining exist- ing <i>guanxi</i> connections to customer companies	B, E	2
<i>Guanxi</i> as a strategic tool for approaching suppliers and se- curing supply	B, D, F	3
Involvement of higher level positioned managers into organ- isational <i>guanxi</i> process	C, E, F	3
Transferring personal <i>guanxi</i> connec- tions to the organisational level	A, B, C, D, E, F	6

Source: Authors

All participating companies encouraged their employees to utilise their *guanxi* for the purpose of company goal achievement. All senior managers (B, C, D, E, F) indicated that *guanxi* of their employees contributes, not only to their personal value enhancement, but also to the enhancement of the company’s value. Four respondents (B, C, D, E) also revealed that their companies provide incentives to their employees to utilise their *guanxi*. The incentives ranged from a *renqing* obligation, dinner with the boss, gifts and also monetary incentives. Respondent F explained:

*“Essentially, every company is encouraging their staff to try to use their own per-  
sonal guanxi. Of course they did not put it in black and white but no boss will be  
against this kind of guanxi. Everybody knows that in this kind of world you have to  
go for the guanxi otherwise you lock [yourself] the door.” - Respondent F*

Some of the participating companies (B, D) even perceived *guanxi* as an important criteri-  
on of human resources in their field of occupation and thus evaluate their potential new em-  
ployees on their *guanxi* before hiring them.

*“Sales people are supposed to have guanxi, because this is a part of their value.  
Why do we hire someone, it’s because, of his personality in the first place, and in  
the second place, because of his or her guanxi. That is going to help a lot to pro-  
mote the sales.” - Respondent D*

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*Guanxi* is also seen as a strategic tool for approaching new and existing customers and suppliers. All respondents said that *guanxi* is very important for suppliers in order to find and establish contacts to potential customers for the purpose of business expansion. Two respondents (B, E) also indicated that their companies have also established a formal budget for establishing new and maintaining existing important *guanxi* relationships with customer companies.

Three other respondents (B, D, F), also referred to the importance of having *guanxi* relationships with suppliers. Having this kind of *guanxi* relationships to the personnel of supplier companies allows them to gain information from suppliers quickly to achieve a safe supply of goods and smooth transactions. Interviewee B explained that some small companies could face the lack of access to goods directly from the manufacturer because of the large minimum order quantities asked by the suppliers. Here *guanxi* connections help to achieve a safe supply of goods though backdoor agreements.

Three interviewees (C, E, F) also highlighted that when new upper level *guanxi* between a customer and supplier is developed, it usually requires the involvement of higher positioned managers from the side of an SME sized supplying company. Even more, in the case of Chinese SMEs the establishment of important *guanxi* connections with key account customers can mean that the owner of the supplying company gets involved in the *guanxi* process. This involvement of senior management or owners into the establishment of important upper level *guanxi* connections has two functions. The first function was indicated by interviewee E:

*“This is more about being convincing and showing respect and about giving face to the other higher positioned managers from the customer side.” - Respondent E*

The other function refers to preserving important *guanxi* connections within the company and making the *guanxi* connections resistant against employees’ movements to other competitor companies. Respondent F described the most common approach mentioned:

*“I recognize that guanxi is the employees’ own personal asset but at the same time I try to switch this personal asset to the company’s asset by encouraging my staff to introduce this kind of guanxi relationship to the other colleagues. In case my staff left the company, I allow [by doing this] that the door is still open.” - Respondent F*

#### 4.2 *Guanxi as a valuable resource*

Table 6 summarises the evidence on value adding benefits and the associated costs of *guanxi*-based buyer-supplier relations. The most cited valuable attribute of *guanxi* based relations is that they provide access to valuable information e.g. about the market, potential business opportunities, customers, suppliers, competitors etc., which can also result in a first-

mover advantage.

Table 6: Identified themes within the value adding attributes category

<b>Valuable Attributes of Business <i>Guanxi</i> Identified Themes</b>	<b>Cited by Re- spondents</b>	<b>No. of Cita- tions (out of 6)</b>
<i>Valuable attributes of organisational guanxi</i>		
Gaining valuable and relevant information (e.g. about market, prices, potential business opportunities, customers, competitors etc.)	A, B, C, D, E, F	6
Enhancing business: acquiring more business, gaining more business opportunities, getting the deals, increasing market share	A, C, D, E, F	5
Decreasing transaction costs	B, C, D	3
Preventing opportunistic behaviour	B, D, F	3
Gain access to resources in general terms	B, D	2
Smoothing transactions arrangements between buyer and supplier	B, F	2
Enhancing corporate reputation	C, B	2
Gaining first mover advantage	A	1
Creating flexible agreements or back door facilitation to suppliers or customers	B	1
<i>Opposing costs of guanxi</i>		
Time input	A, B, C, D, E, F	6
Financial cost	A, B, C, D, E, F	6
Personal effort	A, B, C, D, E, F	6
Pay back of favours	A, B, C, D, E, F	6
Uncertainty of <i>guanxi</i> exchange	A, C, D, E, F	5
<i>Trade off between benefits and costs</i>		
Cost is rather an investment than an expenditure	A, B, C, D, E, F	6
Opportunity cost of <i>guanxi</i> is perceived to be high ( <i>guanxi</i> competition)	A, C, D, E, F	5

Source: Authors

The second most cited (A, C, D, E, F) benefit refers to the enhancement of business in terms of gaining access to new deals and maintaining existing deals. Half of the respondents (B, C, D) also indicated that having the appropriate *guanxi* can contribute to decreasing transaction costs.

Three respondents (B, D, F) have also indicated that *guanxi* can reduce opportunistic behaviour from other parties. The threat of losing good quality *guanxi* with a business partner prevents the other party switching to a competitor. SME suppliers are also unable to secure their position once the purchasing personnel are changed at the customer company. General manager F revealed an example where his company suddenly lost a cooperation contract that lasted successfully for several years with a big foreign company. The newly assigned foreign

purchasing staff just allocated the business to another supplier. However, having the appropriate upper level *guanxi* allowed F to prevent this loss of business.

Table 6 reveals further benefits, nevertheless, all interviewees were also aware of the opposing costs associated with *guanxi* practice. Participant E stated that his company spends between 2 to 5 per cent of total revenue to build-up important *guanxi* connections with customers and maintain existing ones. From the interviews, the costs associated with *guanxi* can be summarised as: (1) time; (2) financial; (3) personal effort, (4) reciprocation of favours; and (5) uncertainty over outcomes and span of time of reciprocation. However, these costs are perceived as an investment rather than expenditure. The common perception was that it is just a matter of time to when the investment was going to yield.

#### 4.3 Guanxi as a rare resource

Table 7: Identified themes within the resource rareness category

<b><i>Guanxi as a Rare Resource Identified Themes</i></b>	<b><i>Cited by Re- spondents</i></b>	<b><i>No. of Citations (out of 6)</i></b>
Perceived scarcity of important business <i>guanxi</i> connections	A, B, C, E, F	5
<i>Reasons for the perceived scarcity</i>		
Difficulty in identifying the right key decision makers	A, B, C, D, E, F	6
Difficulty in establishing new <i>guanxi</i> connections	A, B, C, D, E, F	6
Difficulty due to <i>guanxi</i> competition	A, C, E, F	4

Source: Authors

Table 7 outlines the evidence gained on the scarce nature of *guanxi* connections in inter-firm relations. Five out of six respondents (A, B, C, E, F) revealed that they have been lacking the necessary *guanxi* relationships. Even an experienced managing director (F) revealed:

*“I have been dealing in China for 25 years already, and still feel the lack of guanxi. If you want to work as an agent for those overseas companies and if you don't have this kind of guanxi, you won't get it!” - Respondent F*

Most respondents referred that having *guanxi* with the right decision maker requires access to upper level *guanxi*, which is very difficult to achieve. The first difficulty lies in identifying who makes the required decisions. Respondent D explained:

*“In most of these companies, they don't have only one head. We should first of all make sure we are in the right direction; we are contacting the right person. Otherwise, if you have made this step wrong you may lose the opportunity to have business with this company.” - Respondent D*

Respondent F also referred to the difficulty of identifying the right heads on lower levels:

*“Sometimes the operation department, or the operation managers, they also can do*



*a lot of damage or a lot of interruptions to your supply chain. Unless you know those key persons, there is no chance you can break the icing” - Respondent F*

In case the key decision maker was identified, there is still the difficulty of establishing a *guanxi* relationship to a person they never knew or met before.

*“They don't know you and you don't know them. So normally, they will not trust you and they will ignore you.” - Respondent E*

Moreover, the *guanxi* competition that might have a higher ‘quality’ *guanxi* to key decision makers might also result in a barrier for establishing this kind of influential *guanxi*. The common opinion was that, in a business environment such as PRC, if one does not go the *guanxi* way, the competition would. The opportunity costs of not having this kind of *guanxi* are perceived to be high.

#### 4.4 *Guanxi as an imperfectly imitable resource*

Table 8 provides a summary on the imperfectly imitable nature of business *guanxi*. The evidence was categorised according to the three RBV mechanisms of the imperfect imitability construct: i) historical path dependencies; ii) social complexity; and iii) casual ambiguity.

Table 8: Identified themes within the imperfect imitability category

<b><i>Guanxi as an Imperfectly Imitable Resource</i></b> <b>Identified Themes</b>	<b>Cited by Respondents</b>	<b>No. of Citations (out of 6)</b>
<i>Historical path dependence</i>		
Long-term perspective in <i>guanxi</i> relations	A, B, C, D, E, F	6
<i>Social complexity</i>		
Social interactions as a necessity for maintaining <i>guanxi</i> relations	A, B, C, D, E, F	6
Feelings and emotions can constitute business <i>guanxi</i> relationships	A, C, E, D	4
Blurred boundaries between business and friendship perspective	C, D, E, F	4
Mutual personal trust in long-term oriented <i>guanxi</i>	A, C, D, E	4
‘Quality’ and closeness of <i>guanxi</i> as a barrier mechanism against competition	A, B, C, D, E, F	6
<i>Casual ambiguity</i>		
Situation specific nature of <i>guanxi</i>	E, D, F	3

Source: Authors

All participants provided indications that *guanxi* relationships are long-term in nature. This long-term perspective on *guanxi* relations requires the participants to continuously invest resources such as time, money, and personal effort in order to maintain and strengthen their *guanxi* relations. Some of the respondents (A, B, C, E) also indicated that some of their *guanxi*

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xi-based cooperation has existed since or even before their companies were founded. Interviewee F revealed some common social interaction activities used for strengthening *guanxi*:

*“In China, normally you have to communicate more with the business guanxi partner, you have to be friendly and occasionally you go to have dinner, drinking, and singing with them. This is the time to build, secure and strengthen that kind of guanxi relationships.” - Respondent F*

Five interviewees (A, C, D, E, F) also highlighted some indications for social and cultural complexity of *guanxi* relationships. *Guanxi* is perceived to be more than a relationship as opposed to the Western perspective. It has more social attributes in it, which makes it difficult to distinguish between where business objectives tend to play the role and where friendship starts to emerge. Feelings and emotions can also be a part of the *guanxi*-based exchange. Thus, the boundaries between business and friendship tend to be blurred. Interviewee D emphasised the attitude behind *guanxi*:

*“When we maintain guanxi, business purpose is kind of subconscious. It is not a theme. We just come out and feel happy and are friends. And then in the future, when the time comes and opportunity comes for business, then we talk about business. Then we also help each other.” - Respondent D*

The long-term perspective of *guanxi*-based relationships also has an impact on trust between *guanxi* parties. Four participants (A, C, D, E) revealed a similar pattern of trust development. If the *guanxi* is just built and new in nature, then there tends to be no trust between business *guanxi* partners. However, if it is an existing long-term *guanxi*, with prior cooperation and interactions, then *guanxi* partners usually trust each other. Trust is also perceived to be a mutual product of both parties.

The analysis also proposed that ‘quality’ of *guanxi* tends to influence the *guanxi*-based exchange outcome. All respondents provided indications that high ‘quality’ *guanxi*, e.g. strong and close *guanxi* relationships tend to contribute to a positive achievement of business objectives. Ultimately, high ‘quality’ *guanxi* connections tend also to serve as a barrier for competitors to establish high ‘quality’ *guanxi* connections and conduct exchange with key decision makers.

Finally, respondents E and F indicated that *guanxi* with government officials will be differently approached than *guanxi* with suppliers or customers. Respondent D revealed that *guanxi* in different departments will be utilised for different purposes. For instance, *guanxi* possessed by members of the marketing department is utilised for gaining new and relevant market or competitor information, while *guanxi* possessed in the sales department is utilised

for approaching buyers and gaining new customer contracts and those in purchasing department are primary targeted at suppliers for identifying the relevant suppliers and securing a safe supply of goods.

#### 4.5 Guanxi as an imperfectly substitutable resource

Table 91: Identified themes within the imperfect substitutability category

<b><i>Guanxi as an Imperfectly Substitutable Resource</i></b>	<b><i>Cited by Respondents</i></b>	<b><i>No. of Citations (out of 6)</i></b>
<b><i>Identified Themes</i></b>		
<i>Common perception on replaceability of guanxi</i>		
<i>Guanxi as a cultural product is difficult to replace</i>	A, B, C, D, E	5
<i>Similar guanxi substitutes</i>		
<i>‘Quality’ and closeness on guanxi as a barrier mechanism against competition*</i>	A, B, C, D, E, F	6
<i>Dissimilar substitutes</i>		
<i>Fair deal as potential dissimilar substitute</i>	C, E, D, F	4
<i>*See above - Guanxi as an imperfectly imitable resource.</i>		

Source: Authors

The interview results regarding possible *guanxi* substitutes are summarised in Table 9. On one hand, the majority of interviewees (A, B, C, D, E) felt that there is nothing that can directly substitute the *guanxi* practice. They perceived that *guanxi* is deeply enrooted in their culture and common practice for centuries and thus almost impossible to substitute. Respondent C expressed:

*“It has been done since a long time ago. We cannot change it! It’s ‘Gen Shen Di Gu’.” - Respondent C*

‘Gen Shen Di Gu’ (根深蒂固) is a Chinese idiom and can be translated as ‘it is deeply ingrained in people’s mind’ or ‘such a culture is hard to change’ (Kingsoft Corp, 2010).

On the other hand, some respondents (C, E, D, F) reflected that *guanxi* alone is not sufficient to bring long-term success. In the end it is the product or service, which is sold to the customer for a particular price and with a particular quality. They highlighted that a fair deal, e.g. the right price and quality of a product or service, is still the main selection criterion of most customers. Even if they have some *guanxi* connections to a customer company they still have to deliver a high quality product or service at a right price in order to satisfy the customer, achieve the customer's trust and secure the contracts over the long run. Some of them have concluded that sometimes *guanxi* relationships utilised for the purpose of acquiring contracts with the customer might be substituted by a fair deal.

*“One reason could be the price quote. The potential customers will choose the lower one, so that’s all about business, it is not guanxi.” - Respondent D*

Respondent F also explained under what circumstances the fair deal might be considered as a substitute:

*“In the world there is sometimes a fair deal. If everything is black and white, everything is open and transparent then your good quality, your good service and your good price have a chance to substitute. Then you do not have this kind of guanxi advantage.” - Respondent F*

However, the same interviewee also emphasised that if *guanxi* relationships are accompanying a fair deal, the *guanxi* benefit can always be secured.

*“In a fair deal, the guanxi definitely helps. This is how important the guanxi is. Without this kind of guanxi, then you might lose the business.” - Respondent F*

#### 4.6 Concrete examples

In addition to the above a survey was carried out amongst seven people from different SMEs within the Shenzhen Region. The results from this primary research was coded in the same manner as above (see section 3.2). Please see Table 10 for details of the company size, scope and scale. This additional research allowed the capture of real life examples of *guanxi* in application. Please see the examples listed below the table.

Table 10: Core themes identified by staff in small companies

Small Company Survey Chinese Owned, Shenzhen Region T=furniture, 15 employees U=pharmacy supplier, 10 employees V=accountancy firm, 30 employees W=real estate, 25 employees X=real estate, 10 employees Y=property development, 30 employees Z=manufacturer, 45 employees		Cited by Respondents	No. of Citations (out of 7)
Guanxi as an Organisational Resource			
Utilisation of <i>guanxi</i> contacts in daily business practice		T, U, V, W, X, Y, Z	7
Encouragement for using your <i>own</i> personal <i>guanxi</i> contacts for companies' purposes		U, V, X, Z	4
<i>Guanxi</i> as tool implementing strategies		U, V, W, X, Y, Z	6
Imperfect Mobility			
Preservation of important <i>guanxi</i> connections before employees leave the company		T, V, W, Y, Z	5
Valuable Attributes			
<i>Guanxi</i> with business partners contributes to companies' success		T, U, V, W, X, Y, Z	7
Drawbacks associated with using <i>guanxi</i> in business practice		T, U, V, W, X, Y, Z	7
Sustainability – Rareness			
Difficulties establishing a <i>guanxi</i> connection to the right decision makers		T, U, V, W, X, Y, Z	7

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Lack of necessary <i>guanxi</i> relationships	T, V, X, Y, Z	5
<b>Sustainability – Imperfect Imitability</b>		
Maintenance of <i>guanxi</i> relations to business partners	T, U, V, W, X, Y, Z	7
Importance of trust in <i>guanxi</i> relationships with business partners	V, W, X, Z	4
<b>Sustainability – Imperfect Substitutability</b>		
Other strategies for achieving same results as <i>guanxi</i>	T, U, X, Y	4
Suppliers (or customers) not giving the company preferential treatment	T, U, V, W, X, Y	6

Source: Authors

The table above serves to reinforce the findings from the first phase primary interviews. In addition the participants recounted several concrete examples that explain further how *guanxi* works as a useful business tool:

*“We have a small company and it is very important to have good relationships with our workmates and we have got more choice if we have good relations with our customers and suppliers because they can go to lower price for their products than others and they can sell them at a lower price than others which means that we can earn more money.” Respondent T*

*“A good relationship with a business partner can provide extra profit for the company’s success because they have a strong relationship with customers, suppliers and so they can use this resource to make a strong network and making a strong network is good for the company’s success.*

*If we don’t have strong relationships we can lose the chance to make more customers. Because we just sell the same products we need the necessary *guanxi* relationships with customers and suppliers. For example, for the suppliers, we have strong relation with the suppliers so we can go to lower price on materials to make the product and for the customers we have strong relations with the customers, we can sell more products for them and it’s a good long term development if we have good relationships with suppliers and the customers.” Respondent U*

*“I come from a medical family and my role is tax manager in my company. In China, the interpretation of taxation rules may vary by different tax officers. In order to develop good *guanxi* with them and get most valuable interpretation of taxation rules, I take the in-charge tax officer to see doctors if necessary.” Respondent V*

*“The most important thing is to increase communication, maybe some people they work*

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*for a long time they will become friends from work partners, so they will know each other and maybe they will have dinner, have lunch, they will play together so they build a good relationship with the organisation.” Respondent W*

*“Guanxi means networks for me. It can help you to get things done quicker and better if you use it in the right way. I would feel the need to use my personal guanxi in daily business practice when things are getting out of control under the normal business procedure. For example, something urgent comes up and there is no way you can get it done under normal procedures. Also, I might have to use it when I know it can help me to get things done sooner.*

*Our company has sales team who have good relationship with customers. Therefore they use this relationship to build-up more guanxi relationships which is good for selling properties.” Respondent X*

*“Guanxi connections cannot be made unless you know someone who has guanxi to the right decision makers. So the difficult part of it is finding the person who can provide you meeting chances to talk to the right decision makers. Sometimes, in order to contact with the right decision makers you may have to meet a few people prior to that.” Respondent Y*

*“We should be good friends and not just workmates and have some dinner for example. Sometimes we give them some gifts for our business partners, it is very important you know. For example my workmates (customer) son might get married and we give about 10,000 RMBS. It is very important, you know, to develop a strong relationships.” Respondent Z*

The examples stated above, from the participants, provide some very candid insight into the actual application, use, custom and practice of *guanxi* in China.

## **5. Discussion**

Fundamentally this is a practitioner paper not conceptual one. In order to clearly add value and make a defined contribution within the confines of the necessary word limitation we have arranged the discussion around the research questions and the RBV construct.

### *5.1 Research question 1: How does guanxi in buyer-supplier relationships act as a source of competitive advantage for Chinese SMEs?*

According to Barney's (1991) RBV framework the criteria that constitute a source of competitive advantage are based on strategically important organisational resources that pos-

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sess valuable attributes.

### 5.1.1 *Guanxi as a resource*

*a. Guanxi as an organisational resource:* Similarly to Fan's (2002) argument all senior managers in this study recognised that business *guanxi* cultivation by their employees contributes to their employees' personal value enhancement, which is similar to the notion of the investment into social capital (Luo, 1997a; Tsui & Farh, 1997; Nahapiet & Ghoshal, 1998; Fan, 2002). Moreover, some of the SMEs were identified as evaluating potential employees as to whether they possess any necessary *guanxi* connections before hiring. Consequently, *guanxi* can be perceived as an important attribute of the human resource.

Secondly, *guanxi* was also identified as an organisational resource, which is different to Fan's (2002) argument that *guanxi* is solely personal in nature and cannot be transferred to or sustained on the organisational level. This study strengthened the position of Park and Luo (2001) and Standifird (2006) that *guanxi* can be an organisational resource when it is utilised for the purpose of the organisational goal achievement or as a way of finding business solutions. All of the participating SMEs encouraged their staff to utilise their personal *guanxi*. Some of the companies even provided incentives to their employees for establishing important *guanxi* connections with the potential to generate revenue. The encouragement of the employees to establish more *guanxi* connections may increase the potential to get exposed to more opportunities for exchange and thus increase the value of the human resources and the company.

Luo (1997a) considered business *guanxi* to be an *organisational strategic resource*. Similarly, *guanxi* was identified, on the one hand, as playing an important strategic role in identifying and approaching potential customers (Davies *et al*, 1995; Yeung & Tung, 1996; Luo, 1997b; Luo & Chen, 1997; Fock & Woo, 1998; Yi & Ellis, 2000; Park & Luo, 2001). As *guanxi* connections to customers play an important role, some of the SMEs in China also establish formal budgets for establishing and maintaining this kind of strategically important *guanxi*. *Guanxi* connections to suppliers play also a strategic role. Some of the small-sized companies rely heavily on *guanxi* connections in order to achieve flexible agreements with suppliers in order to secure a safe supply of goods despite a high minimum order quantity required by suppliers. This kind of *guanxi* reliance may also be interpreted as back-door facilitation through creating flexible agreements, long-term cooperation and surpassing arms' length dealings (Ambler, 1994; Xin & Pearce, 1996; Su *et al*, 2003).

*b. Guanxi as a heterogeneous organisational resource:* Similar to Park and Luo's (2001)

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findings, this study revealed that *guanxi* application is situationally dependent, heterogeneous across firms and depends on the institutional, strategic, and organisational settings of each firm (Hunt, 1997; Park & Luo, 2001). For instance, *guanxi* with government officials will be differently approached than *guanxi* with suppliers or customers. *Guanxi* in different departments is utilised for different purposes.

*c. Guanxi as an imperfectly mobile organisational resource:* Fan (2002) argued that *guanxi* is mobile in nature and does not fulfil the RBV requirement. Yet, *guanxi* in this study was identified as possessing the characteristic of being imperfectly mobile when the personal *guanxi* connections are transferred to the organisational level. All companies participating in this study have established a similar approach described initially by Tsang (1998). By involving multiple employees in the *guanxi* process, *guanxi* relationships are transferred from the single *guanxi* ‘gate keeper’ towards multiple ‘gate keepers’ within the company. Consequently, when the ‘gate keeper’, who initially brought the *guanxi* connection into the firm, departs, the *guanxi* connection or the access to it can still remain within the organisation. For strategically important *guanxi* connections, it is usually not enough to transfer the *guanxi* to other staff. Rather top management and, in case of SMEs, even the owners of the company usually engage with the *guanxi* process in order to secure the connection by asking the particular employee to introduce the important *guanxi* contact to him/her and anchor the important *guanxi* connection within the company.

### 5.1.2 *Guanxi as a valuable resource*

According to the RBV theory, company attributes must be valuable in order to be considered strategically important (Barney, 1991; Yang, 2008). In consensus with the academic literature the most cited valuable attribute of business *guanxi* is its function for the attainment of valuable information, e.g. information about the market, potential business opportunities, customers, suppliers, competitors etc., which can result in a first mover advantage if the information is acquired at the right time (Davies *et al*, 1995; Yi & Ellis, 2000). *Guanxi* connections were also confirmed to be useful in gaining important information about suppliers as they serve as an important and reliable source of information (Luo, 1997a; Millington *et al*, 2006). Secondly, another important benefit refers to its potential to enhance business in terms of gaining access to new deals and maintaining existing ones (Yeung & Tung, 1996; Luo, 1997b; Luo & Chen, 1997; Park & Luo, 2001; Gu *et al*, 2008). Further, similar to Standifird and Marshall (2000) the evidence from this study indicates that having the appropriate *guanxi* could reduce opportunistic behaviour. SME suppliers in China are also unable to secure their



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position once the personnel changes at customer companies. Having the appropriate upper level *guanxi*, was shown to help prevent a sudden loss of business to competitors. Moreover, this study also confirmed that *guanxi* has the potential to reduce transaction costs (Standifird & Marshall, 2000; Park & Luo, 2001; Millington *et al*, 2006), a smoothing effect on transaction arrangements between the buying and supplying firms (Davies *et al*, 1995; Leung *et al*, 1996; Nassimbeni & Sartor, 2006; Lee & Humphreys, 2007; Humphreys *et al*, 2011), a potential to enhance corporate reputation through *guanxi* networks (Davies *et al*, 1995; Yi & Ellis, 2000; Standifird, 2006; Fan, 2007), and the capacity to provide access to resources in general terms (Davies *et al*, 1995; Xin & Pearce, 1996; Pearce & Robinson, 2000; Yi & Ellis, 2000; Su *et al*, 2003).

Nonetheless, *guanxi* processes were also identified to have opposing costs such as time input, financial cost, personal effort, the returning of favours, and the bearing of uncertainty about the outcomes and timespan of the return favour (Luo & Chen, 1997; Fock & Woo, 1998; Yi & Ellis, 2000; Fan, 2002). Most participants perceived these opposing costs as an investment rather than expenditure, yielding more advantages than the financial outlay. The opportunity cost of not having particular *guanxi* connections to buying or supplying firms were perceived to be high. The common impression was that if one does not go the *guanxi* way, the competition will and gain the *guanxi*-based advantages, thereby eroding one's potential success factor for a thriving business in China. All in all, *guanxi* was revealed to have the potential to be a strategically important organisational resource with valuable attributes for Chinese SMEs.

## *5.2 Research question 2: When is the guanxi-based competitive advantage sustainable?*

The RBV theory proposes three criteria; resource rareness, imperfect imitability and imperfect substitutability, all of which need to be fulfilled in order to prove the sustainability character (Dierickx & Cool, 1989; Barney, 1991; Yang, 2008).

### *5.2.1 Guanxi as a rare resource*

The majority of managers in this study perceived a lack of necessary *guanxi* relationships which is in analogy with Park and Luo's (2001) point that *guanxi* processes in Chinese society can be found in every corner of daily social life, businesses and that organisations have diverse needs and capacities for cultivating their *guanxi* relationships. Even an experienced managing director (F) with 25 years of work experience in China expressed the lack of necessary business *guanxi* connections.

The difficulty lies in identifying and establishing *guanxi* connections with the 'gate-

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keeper' of the particular business *guanxi* with the necessary relational resources (Yeung & Tung, 1996; Dyer & Sign, 1998; Wong & Chan, 1999). Having *guanxi* with the right decision maker usually requires access to upper level *guanxi*, which is very difficult to achieve (Tsang, 1998). Some study participants stated that it is also necessary to have *guanxi* connections at lower levels, especially to the operations area; decisions in this area can have an impact on the flow of goods between supplying and buying firms. On top of that, even in cases where the *guanxi* 'gate-keeper' was identified a difficulty persists, especially regarding the establishment of a *guanxi* relationship to a person one never knew or met before (Fock & Woo, 1998). Moreover, the difficulty of establishing new and influential *guanxi* can also be traced back to the *guanxi* competition, which might have an existing, stronger and higher 'quality' *guanxi* to the same key decision makers (Fock & Woo 1998; Yi & Ellis, 2000).

#### 5.2.2 *Guanxi as an imperfectly imitable resource*

Imperfect imitability might exist if the resource is shaped by a unique historical path, social complexity or casual ambiguity (Barney, 1991).

*a. Historical path dependence:* The interview findings accentuated the long-term nature of *guanxi* relationships. Some of the *guanxi* connections may even exist from the foundation of the company or, in case of friendship, before that. Consequently, this long-term nature may be subject to what Barney (1991) termed as *historical path dependencies*. Competitors may face the challenging barrier to replicate this kind of historical path, e.g. sharing the same experiences, feelings and long lasting mutual benefits, in order to establish the same 'quality' *guanxi*.

*b. Social complexity:* Establishing a high 'quality' *guanxi* was also confirmed to be a socially complex process which requires continuous communication, face-to-face interaction and a high degree of sociability in order to strengthen the connections and establish the required *ganqing* as well as mutual trust (Yeung & Tung, 1996; Fan, 2002; Ramasamy *et al*, 2006; Wong *et al*, 2007; Humphreys *et al*, 2011).

Social and cultural complexity can also be seen in the common perception that the word 'relationship' by far does not capture the complexity and the obligatory power of *guanxi* as well as the various social attributes such as face giving, personal trust but also mutual *ganqing* (affection), which includes the feelings and emotions of the exchange partners (Tong & Yong, 1998; Yau *et al*, 2000; Fan, 2002). These social attributes make it difficult to distinguish between where business purpose tends to play a role and where friendship starts to emerge.

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Usually, while business purposes tend to be subconsciously present, the time during which *guanxi* maintenance is taking place is more considered to be a friend-to-friend interaction. Thus, in the case of long-term *guanxi* relationships the boundaries between a business relationship and friendship tend to be blurred.

The notion of *time compression diseconomies* embodies the idea that the ‘quality’ of a one-year *guanxi* relationship will be inferior to the ‘quality’ of a ten-year relationship (Dierickx & Cool, 1989; Barney, 1991; Tsang, 1998). Analogically, the research results proposed that the ‘quality’ of *guanxi* tends to influence the *guanxi*-based exchange outcome. The existence of a mutual *ganqing* tends to contribute to the a positive achievement of business objectives. If *ganqing* is developed, the *guanxi* relationship becomes closer, more dependable and valuable for both parties (Tong & Yong, 1998). Ultimately, strong and high ‘quality’ *guanxi* tends also to serve as a barrier for competitors to establish the same high ‘quality’ *guanxi* and conduct exchange (Yi & Ellis, 2000).

Within the literature, mutual trust was also argued to be a further social barrier mechanism (Dierickx & Cool, 1989; Barney & Hansen, 1994; Humphreys *et al*, 2011). While new *guanxi* tends to have no or low trust within the relationship, existing long-term *guanxi*, with several prior cooperations and interactions, tends to have mutual trust in it (c.f. Tong & Young 1998; Leung *et al*, 2005; Lee & Dawes, 2005). Thus, according to Dierickx and Cool (1989) trust between *guanxi* partners, which is cultivated over a longer time period, can be perceived as socially complex.

*c. Casual ambiguity:* Finally, causal ambiguity exists when the link between organisational *guanxi* resource and a firm’s sustained competitive advantage is not understood or understood imperfectly (Barney, 1991). We demonstrated above that *guanxi* application at an organisational level is heterogeneous in nature, situationally dependent and can vary according to different organisational settings. Consequently, the social complexity and situation specific application of *guanxi* at the organisational level can make it casually ambiguous; it is difficult for competitors to understand all the key factors required for cultivating, nurturing and accumulating high ‘quality’ *guanxi* with key decision makers.

### 5.2.3 *Guanxi as an imperfectly substitutable resource*

Answering the sustainability question also requires analysing whether the organisational *guanxi* resource is subject to substitution (Barney, 1991). The common perception among the interviewees was that *guanxi* is deeply ingrained into people’s minds and into Chinese culture as a common practice of doing business for centuries (Luo, 1997a; Park & Luo, 2001). Such

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a cultural product is difficult to change or substitute. However, despite this common perception a deeper analysis of potential similar or dissimilar substitutes was conducted. With regards to similar resource substitutes, one could refer to situations when competitors try to develop *guanxi* with parties similar to or even stronger than the firm's *guanxi* partners (Tsang, 1998). Similarly, competition on *guanxi* was perceived in this study to move towards competing on the strength and 'quality' of *guanxi* that results in a barrier and the ultimate difference to the final outcome of the *guanxi* exchange. Thus, strong and high 'quality' *guanxi*, especially close *guanxi* with a high degree of mutual *ganqing*, tends to have the potential to be imperfectly substitutable and thus sustainable. Weak and distant *guanxi*, on the other hand, tends to be more easily substitutable through stronger *guanxi* and thus is less sustainable.

With respect to dissimilar substitutes, this study highlighted that *guanxi* alone is not sufficient to bring long-term success. In the end, it is the product or service, which is sold to the customer for a particular price and with a particular quality. Thus, the fair deal, especially the right quality at lowest price, remains the main selection criterion for most customers. Consequently, this study found that even when a supplying company has some *guanxi* connections to a customer company it still has to deliver a high quality product / service at the right price to satisfy the customer, achieve the customer's trust and secure the contract over the long run. A fair deal could be considered as a dissimilar substitute for *guanxi* relationships to customers. This point could be analogically linked to Park and Luo's (2001) argument that firms with superior technological skills might have a stronger bargaining power and less need for *guanxi* relations. Here superior technological skills could be regarded as a reflection of the ability to deliver products or services at higher quality and lower prices.

Nevertheless, the authors argue that a fair deal should be considered subject to some restrictions in the business environment. A fair deal might be subject to a perfectly transparent business environment where business decisions are made on the merits of objective performance and not subject to any influence through other factors, especially relational factors, such as *guanxi*. However, as previously mentioned, *guanxi* relationships in the Chinese business environment have been common practice over the centuries (Luo, 1997a; Park & Luo, 2001). On top of that, where a fair deal might still be considered to substitute the *guanxi* relationship for the customer company, it still does not substitute the *guanxi* relationships to the suppliers, which is needed to achieve a safe supply of goods and facilitate back-door access to resources. It also does not substitute *guanxi* used for other purposes such as gaining valuable information and the resulting potential first mover advantage, or other value adding benefits. Where a fair deal is accompanied by *guanxi* relationships and is competing against similar deals, with weaker or without any *guanxi* relationships, the *guanxi*-based advantage can be

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utilized to its full extent.

Finally, we acknowledge that both service and manufacturing companies have been included within this research and that the focus of these two groups strategic attentions, in terms of the point of creating business success and competitive advantage, would be different. For example it is possible that the importance of *guanxi* in service providers is different from that in the manufacturing sector; *guanxi* could be more important for service providers and for business start-ups. However, the authors believe that, in identifying the paper as practitioner based and not fully conceptual, it makes a contribution through examining how *guanxi* works as a resource in business activities of SMEs.

## 6. Conclusions

This paper has enriched the *guanxi* literature with an RBV analysis of the role of *guanxi* in buyer-supplier relations in SMEs with a Mainland Chinese background. The research highlights the ‘how’ question regarding the potential of *guanxi* to be a source of a sustained competitive advantage and also addressed the sustainability question, which previous research failed to address.

Following the theoretical framework of RBV, the discussion revealed that *guanxi* within buyer-supplier relationships can be considered as a strategic organisational resource with valuable attributes and thus as a source of competitive advantage for SMEs in China. However, the *guanxi*-based advantage can only be sustainable under certain conditions. Especially the long-term, strong and high ‘quality’ *guanxi* connections, e.g. close *guanxi*, which is surrounded by mutual *ganqing* (affection), tends to be rare, socially complex and imperfectly substitutable. This kind of *guanxi* serves as an imitation and a substitution barrier for the competition and thus is sustainable in nature. However, a fair deal, e.g. the highest quality at lowest price, might have the potential to substitute *guanxi* with customers for purposes of business enhancement, but not other *guanxi*-based competitive advantages such as information gathering, gaining first mover advantage, reducing transaction costs etc. Thus, the *guanxi*-advantage, in its full extent, can only be sustained over the long term, when it is accompanied by technical capabilities that allow the delivery of a fair deal (e.g. products or services at the right quality and the right price).

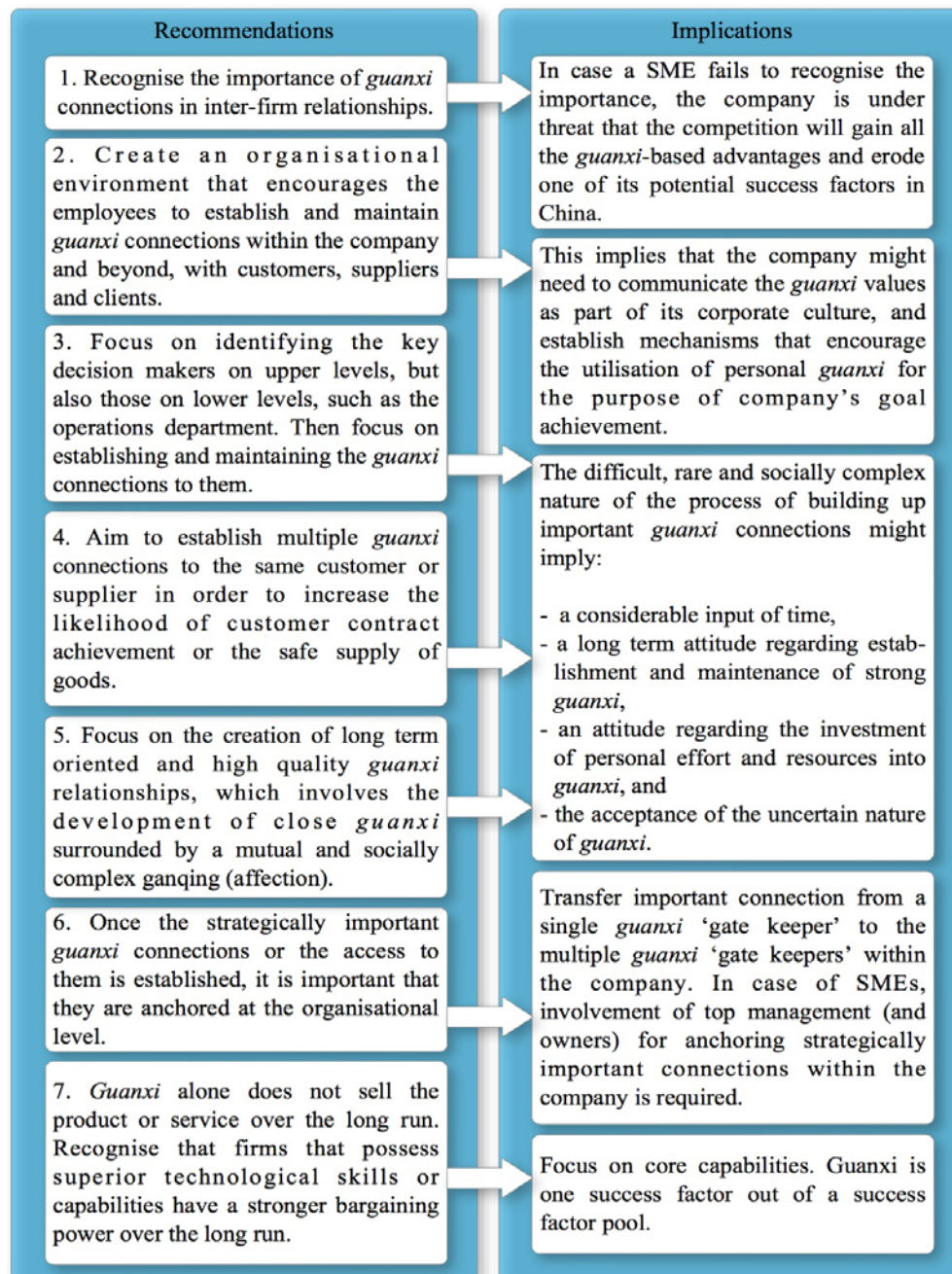
*Guanxi* is therefore used in daily business practice, helps implement strategies, and contributes to company success. There are drawbacks and difficulties associated with using *guanxi* and establishing connections to the right decision makers; plus some suppliers/customers do not automatically give preferential treatment. But company employees appear to strive to maintain *guanxi* relations, despite the interesting perceptions around aspects

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of trust shown in the table. However, *guanxi* should be not considered as the ultimate business solution for everything; *guanxi* alone does not sell the product or service. Consequently, companies in China need to recognise that firms possessing superior technological skills or capabilities may have a stronger bargaining power (Park & Luo, 2001). Superior technological capabilities can be regarded as a reflection of the ability to deliver products or services at higher quality and at a lower price, which results in a higher potential to achieve a fair deal with the customer. Thus, *guanxi* connections should be considered as one success factor within a portfolio, to create a sustained competitive advantage. Hence, it is the combination of success factors which make the ultimate difference. Table 11 highlights the authors recommendations and potential implications for practitioners. SMEs need to recognise the importance of *guanxi* connections for the success of inter-firm relationships in China.

It should be acknowledged that this research faces some limitations commonly found in qualitative studies, and some unique to its setting. Obtaining access to willing respondents proved challenging; gaining their permission to use the data collected was an additional hardship. The small sample size and the lack of a random selection might limit the external validity and generalisability of the research findings. Moreover, the sample was composed of Chinese managers who possessed Western educational experience. This might not apply to the broader population of Chinese managers in SMEs. Finally, SMEs constitute the backbone of the Chinese economy and thus deserve more attention for research. For instance questions such as what is the role of *guanxi* within the corporate culture and how do *guanxi* relations or networks act as an information channel? Furthermore, perhaps there is a change of association between *guanxi* and size (or history) as time passes? Does a dependence on *guanxi* for business decline with the accumulation of business experiences? Is there perhaps a fundamental dynamic change of business process that affects the degree of dependence and importance of *guanxi* by time-series analysis (which is not econometric analysis)? These are still undiscovered areas of research within this fascinating field.

Table 11: Recommendations and implications for practitioners



Source: Authors

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## APPENDIX – INTERVIEW TOPICS

### ***Guanxi* as an organisational resource**

1. What does *guanxi* means to you? *When* do you feel the need to use your personal *guanxi* contacts in your daily business practice?
2. Does your company encourage you using your *own* personal *guanxi* contacts? How do they encourage you? Could you provide an example?
3. When your company is implementing strategies focussing on approaching customers or suppliers. – What role does *guanxi* plays in implementing these strategies? Could you provide an example?

### **Imperfect mobility**

4. How do you think your company preserves important *guanxi* connections within the company beforehand, especially before the employee intends to leave the company?

### **Valuable attributes**

5. How does *guanxi* with business partners contribute to your company's success?
6. From your perception, what are the drawbacks associated with using *guanxi* in business practice?

### **Sustainability – rareness**

7. From your experience, what are the difficulties of establishing a *guanxi* connection to right decision makers?
8. Have you experienced that you (or your company) are (is) lacking the necessary *guanxi* relationships? What do you think are the main reasons for it?

### **Sustainability – imperfect imitability**

9. How do you maintain your *guanxi* relations to business partners?
10. What is the role of trust in your *guanxi* relationships to business partners?

### **Sustainability – imperfect substitutability**

11. Do you think there are any possible substitutes (or strategies) that can help to achieve the same results in business as with *guanxi*? If there are any, could you provide some examples?
12. Consider some of your main suppliers (or customers) who, from your viewpoint, are not giving your company preferential treatment as compared to your competitors. Can you state some reasons for these suppliers (or customers) for not giving preferential treatment to your company?