Institutional Reform and the Changing Face of Guanxi

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ABSTRACT

History illustrates that different polities adopt different development models in order to achieve modernity. In the case of successful socio-economic and socio-political development, the models that have been adopted have conformed to the paradigms held by the majority of the citizenry, to their cultural values, and to the informal institutions that underpin the sense-making of the citizenry. This paper develops a theoretical framework to better identify potential trajectories of economic development in emerging countries. It draws on Trivers’s theory of reciprocal altruism from evolutionary biology, Berry’s eco-cultural framework from cross-cultural psychology, and North’s framework for analyzing economic and institutional change from new institutional economics. The framework is used in the current study to guide an exploratory empirical examination into how the development models adopted in eight Asian polities influence the reliance by Chinese business people on guanxi (relationships) to manage opportunism and to reduce search and transaction costs and environmental uncertainty. The findings indicate that the nature and practice of guanxi varies from polity to polity, depending on the type of development model adopted.

Keywords: Guanxi, reciprocal altruism, institutional economics, development
1. INTRODUCTION

Many leading scholars (e.g., North, 2005; Redding and Witt, 2007) suggest that a transition from particularistic personal networks and informal institutions, such as guanxi in the Chinese context, to impersonal formal institutions is an essential factor for sustained economic growth in developing polities. Therefore, it is both timely and important to better understand what guanxi is and how and whether it is changing, as Chinese business people are increasingly exposed to more formal “Western” institutions. The latter part of this paper is likely to add to such knowledge through a detailed look at the changing nature of guanxi’s role in Chinese business practices in two Mainland and six overseas Chinese polities. Before beginning to examine the implications of guanxi, however, we need to establish a contextual theoretical framework for analyzing the nature of guanxi and its processes and practices – a framework that allows for comparisons between different polities [Child, 2009].

There is an immense body of literature on institutions, but surprisingly few theoretical or conceptual tools for empirical analysis. Researchers such as Redding [2008], Child [2009], and Hodgson [2010] have made excellent inroads in this regard. We suggest, however, that it is necessary to look deeper into the antecedents of institutions in order to better understand how they evolve and change over time.

This paper first develops a more comprehensive theoretical framework using an interdisciplinary perspective – a perspective that Dunning [1989] and Cheng, Henisz, Roth, and Swaminathan [2009] suggest is important for international business research. To do this, we draw on Trivers’s [1971] theory of reciprocal altruism from evolutionary biology; North’s [1990; 2005] theory of institutional and economic change from new institutional economics; Hodgson’s [2010] work on choice, habit, and evolution; and the eco-cultural framework from cross-cultural psychology [Berry, Portinga, and Pandey, 1997].

The paper then discusses the research methods used in an application of the framework to a case based on an investigation of guanxi. This paper reports on the findings from three research questions. These three questions were developed to elicit perceptions of Chinese business people into how the practice of guanxi might be changing as a consequence of their exposure to a range of socio-economic and socio-political variables. The paper concludes with a discussion of the framework and its strengths and weaknesses, and with a final elaboration on specific research on guanxi and its key implications.
2. THEORETICAL BACKGROUND

Over the last 200 years, international business practices and the institutions that govern them have been dominated mainly by state, private, and public organizations from Western polities. During this period, Western business practice and social reality have evolved from interpersonally based *gemeinschaft*, or a community built on particularistic ties, toward *gesellschaft*, or a society based on more impersonal exchange [Tönnies, 2001 (1887)]. This gradual shift has been accompanied with increasing reliance on formal institutions, or “rules of the game” [North, 2005]. Such a shift assists in managing and preventing opportunism, reducing search and transaction costs, reducing environmental uncertainty, and facilitating knowledge transfer through formally contrived institutions.

Over the last 50 years, and particularly since the early 1980’s, polities such as South Korea, Singapore, Taiwan, China, Malaysia, India, Vietnam, and Thailand have increasingly engaged in international trade and commerce. China and India in particular are rapidly emerging as potential economic superpowers. In comparison with Western polities, constituents of these Eastern polities have quite different value and ethics systems underpinning their formal and informal institutions, and business in these polities is still largely governed by particularistic interpersonal relationships. The increasing levels of regional and global competition and cooperation, coupled with a focus on sustainability, suggest it is of strategic importance that governments and firms better understand Eastern socio-economic and socio-political institutions; how they affect business practices and relationships; and how they may evolve over time. China, by way of example, did not historically develop the rule of law and the commensurate formal institutions that govern Western business practices such as contract law, tort law, capital markets, and property rights. Instead, China developed and relied on the practice of *guanxi*, a uniquely Chinese tradition that fits well with Confucian thought and the rule of man. *Guanxi* and its network of specially developed particularistic relationships [Buttery and Wong, 1999] enable Chinese business people to manage opportunism, reduce search and transaction costs, and, in so doing, reduce environmental uncertainty [Standifird and Marshall, 2000]. Although *guanxi* emphasizes personal exchange over the impersonal (a criticism often leveled by institutional theorists), it does seem to be having reasonable effect.
2.1. New Institutional Economics

New institutional economics (NIE) was a term popularized by Williamson [1975] at a time when he believed “research of the New Institutional Economics had reached a critical mass” [Williamson, 1985: 16] and was further developed and clarified by Langlois [1986]. The intellectual heritage of NIE lies in certain aspects of the property rights literature of Ronald Coase (1937, 1960) … the transaction-cost economics of Oliver Williamson (1975; 1979) and further elaborated upon by Williamson (1985) … [the] evolutionary theory of Nelson and Winter (1982) … Herbert Simon (1955) and the behavioural school … Joseph Schumpeter (1934, 1942) … and the influence of F.A. Hayek, as mediated through the modern Austrian school.

[Langlois, 1986: 1-2]

The school has also been strongly driven by the seminal works of Nobel laureate Douglas North [1990; 2005]. NIE is an evolving branch of economics that specifically investigates how institutions and economies might change over time and “focuses on the beliefs that humans develop to explain their environment and the institutions (political, economic and social) that they create to shape their environment” [North, 2005: 11]. North’s seminal research and theory building [1981, 1990, 1991, 1994, 1995, 2005] and collaborative efforts [North, Summerhill, and Weingast, 2000; North and Thomas, 1973; North and Weingast, 1989] have been motivated by a growing consensus among a number of economists that neo-classical economics fails to explain and predict economic change. North [2005] suggests that, to better understand the processes of economic change, we should focus on formal and informal institutions. Focusing on the essential aspects of social science and human behavior, North [2005] suggests we need to investigate more fully why humans develop rules, norms, conventions, and ways of doing things. He and others such as Hodgson [2010] and Drew and Kriz [2012] point to the importance of biology, habits, and beliefs in structuring human interaction, which in turn shape our informal and formal institutions.

Neo-classical economics focuses on choice and suggests that people make decisions based on rational self-interest in order to maximize fulfilment or satisfaction [Jackson, McIver, Bajada, and Hettihewa 2005]. However, neo-classical economics does not discuss the context in which choices are made [North, 2005; Redding, 2008; Weber, 1930]; specifically, the complex processes
behind such decision making. Economic actors with differing rationales from varying polities are also not properly considered [Weber, 1971; Witt and Redding, 2009]. The complexity of the development of cognitive functioning is ignored [Nisbett, 2003]. Other important oversights that limit such a theory include not accounting for different cultural values [Berry et al., 1997; Geertz, 1973; Hofstede, 2001], socio-ecological factors [Diamond, 1998; Dunbar, Knight, and Power, 1999], psycho-biological factors [Cosmides and Tooby, 1994; Decker, Pierce, and White, 1999], instinct and habits [Hodgson, 2010], historical factors [Diamond, 1998; North, 1990; Sened, 1997], embeddedness and social networks [Granovetter, 1973, 1985, 2005], and genetic factors [Cavalli-Sforza, Menozzi, and Piazza, 1996].

NIE is a theory aimed at understanding mental constructs and the requisite scaffolding as it evolves, in as much as it focuses on the beliefs people develop to explain their environments and the psychological institutions they use to create and shape that environment [North 2005]. However, it is far from a complete theory. Even its main protagonists acknowledge that it is a work in progress. North [2005, vii], for example, asks the rhetorical question, “Can we develop a dynamic theory of change comparable in elegance to general equilibrium theory” [elegance should not be construed as accurate]? The dynamic nature of human development means that North suggests the answer is “probably no,” but he does acknowledge that we can try to understand the underlying processes. If NIE achieves even moderate extensions of our understanding, it may have profound implications for enhancing our understanding of sustainable economic change and for interpreting institutional development in an increasingly global world.

NIE is a relatively new discipline. Thus far, it is based predominantly on limited Western empirical archival research. However, to be successful, such a discipline will likely require a more rigorous and robust underlying theory to meet its purpose.

Developing such a theoretical framework is not a simple task as the processes that underpin human behaviour are often difficult to identify, understand, and explain. Already, Coase [1937], through the nature of the firm, and Williamson [1975; 1979], through transaction cost economics, have added significantly to the body of knowledge. Nevertheless, their contributions are only partial when it comes to the broader objective of a more comprehensive framework for investigating institutional and economic change and the associated underlying processes. Such a framework could increase accuracy in forecasting at which margins – and to what extent – economic and institutional change occurs. North
[2005: 30] himself argues that a framework for discovering and analyzing the complexity of human behaviour is “an important frontier for further research.” North has offered a preliminary path-dependent framework for analyzing economic and institutional change. His preliminary process incorporates five key constructs with an important feedback loop (Figure 1). North [2005: 4] also suggests that “institutions change at the margins.” However, this basic conceptualization of the process does not incorporate the powerful antecedents that underpin perceived reality in decision making processes. In essence, institutions are the informal and formal mechanisms through which people make sense of their surroundings.

![Figure 1. North’s Framework for Analyzing Economic and Institutional Change](image)

North [2005] further argues that institutions are the collectively developed sense-making mechanisms that polities use to reduce personal and group uncertainty regarding behavior. Interestingly, members of polities tend to hold onto existing institutions, even when doing so may lead to economic, social, and political decline. Institutions are therefore quite durable and slow to change (particularly those that are informal). North [2005: 30] suggests that the immense variation between “the performance characteristics of political/economic units over time makes it clear” that both culture and genetics must be central to the
“Decision frameworks” of individuals, groups, and societies, and that “the exact mixture between the genetic predispositions and cultural imperatives is far from resolved.” From the latter statement, it is evident that further theory building and empirical research are required in order to better understand how institutions develop and change over time.

Critical to such an understanding is the interplay of the genetic and biological variables that underpin the formation and modification of institutions. Hodgson [2010] recently presented a conceptual model that is more evolutionary. It alludes to biological and cultural underpinnings, but it does not fully address how and why institutions vary from polity to polity. What has not been discussed as much, even by North, are the cross-cultural and ecological issues that appear central to such a framework. The current study, therefore, attempts to achieve a broader framework and to increase the focus on the latter level of interpretation and analysis.

2.2. Naturally Occurring Institutions

This section discusses the role of free riding in the evolution of social networking and the nature of reciprocal altruism (the so-called biological driver).

2.2.1. Free Riding

Literature from evolutionary ecology suggests that it is quite feasible that the practice of social networking evolved naturally as a universal social institution to manage the problem of free riders. The term free rider refers to those satisfying their own immediate needs and self-interests to the detriment of others, by usurping common pool resources [Hardin, 1968, and Ostrom et al., 1994, cited in Dunbar, Knight, and Powers, 1999: 195]. Evolutionary ecologist Dunbar has drawn on extensive empirical research from biology, anthropology, and economics to suggest that human beings appear to have evolved a number of specific mechanisms designed to overcome, or at least control, the societal problem of free riders. These mechanisms include reliance on close and extended kin, the use of language and specific dialects, the ability to interpret body language and vocal cues, and the use of shared contacts. All of these contribute to how one determines the trustworthiness of third parties. Dunbar et al. [1999] also suggest that the problem of free riding in a society appears to develop only when a society becomes of sufficient size to allow for unrelated individuals to act in their own self-interest at others’ expense. Earlier research [Aiello and Dunbar, 1993] into the number of people an individual can consciously identify with at
one time suggests that the size of a community in which free riding starts to become a problem is about 150.

Social networks (and, in the Chinese context, guanxi) appear to “fit” the criteria of Dunbar et al. [1999]. Accordingly, guanxi seems to have become a naturally evolving institution to manage the problem of free riding in the Chinese context. Guanxi is fundamentally based on kinship ties, geographic specificity, the subtle nuances of a high-context language [Hall, 1989 (1976)] and a preference for undertaking exchange relationships with relatives, friends, or referred contacts. If Dunbar et al. [1999] are correct, social networking is a natural universal institution for the management of the free rider problem in the absence of codified and explicit legal institutions for the management of torts. This propensity to build social networks like guanxi is also strongly supported by research in evolutionary biology.

2.2.2. Reciprocal Altruism, the Biological Driver

Reciprocal altruism is a term originally proposed by evolutionary biologist Robert Trivers [1971]. It developed from an important extension of Hamilton’s [1964] The Genetic Evolution of Social Behaviour I and II. Hamilton’s work explored the nature of kinship and altruism within different species from a genetic perspective. It is important to note that, in biology, the term altruism is not defined in terms of motivating intentions as in the sense of social altruism, but rather in terms of fitness consequences at the genetic level. Species that may not have conscious intentions, such as bees and ants, would therefore only engage in altruism through genetic programming in order to maximize species fitness and longevity. Trivers [1971], like Hamilton [1964], draws on the Darwinian paradigm of natural selection and presents a model that accounts for reciprocally altruistic behaviour. It shows how selection could, in essence, work against a non-reciprocator or cheater in the system. Trivers’s [1971] model has been used to explain behaviors involved in the cleaning symbioses in different fish species, the warning cries of birds, and, more specifically, human reciprocal altruism. In relation to human reciprocal altruism, the model shows that, whereas reciprocal altruism is rooted in genetic evolution and adaptation, the psychological system regulates it through factors such as:

- Friendship and the emotions of liking and disliking
- Gratitude, sympathy, and the cost/benefit ratio of an altruistic act
- Guilt and reparative altruism – making amends for past misdeeds
- Mimicking the altruistic and non-altruistic behaviors of others in a polity


- Detection of the subtle cheater, trustworthiness, trust and suspicion
- Setting up of altruistic partnerships
- Developmental plasticity

Adapted from Trivers [1971: 48-53]

More recently, and of salience to the study of business, Trivers [2006: 67] has suggested that reciprocal altruism is “responsible for the complex economic systems in which we now live,” a position also supported by the concept of the norm of reciprocity [Gouldner, 1960] from social exchange theory. Of the factors noted above, developmental plasticity warrants further note as it suggests, in a similar vein to Dunbar et al. [1997]), that different types of particularistic relationships form from polity to polity. Trivers [1971] noted that the conditions for detecting cheats is likely to differ based on variations in the altruistic “trade” with different wins and losses calculated, based on the stability or lack thereof of the social units or groupings. He further suggests that these characteristics are likely to vary across and within eco-social populations (even if they are small).

2.3. Social-Cum-Business Exchange in Other Polities

Before we discuss the framework developed for this study and its application to guanxi, it is worth enhancing our understanding of the potential variations that have emerged in a number of other polities. These concur well with Trivers’s notion of plasticity and several of the other psychological variations he suggests that one could expect. In a study of the socio-economic development of two villages in rural Lebanon, Makhoul and Harrison [2002: 614] note that, in trying to acquire funding for development purposes, powerful local men often drew on client-patron relationships and the practice of wasta, “the act of accessing material favours” from those with greater political power and financial wealth. Their research indicates that client-patron relationships are an integral part of Lebanese political life at all levels and that the client-patron relationships, “wasta networks,” and the practice of wasta are on-going and a normal part of life.

In an article on cross-cultural training, Hutching and Weir [2006: 272] identified the need for “increased training of international managers to adjust to culture-specific networking in China and the Arab World,” as their research found that the practices of guanxi and wasta were still relevant in relation to social and business life. They liken wasta to guanxi and define it as “a social network of interpersonal connections rooted in family and kinship ties” and
“[i]nvolve the exercise of power, influence and information-sharing through social and politico-business networks” [2006: 278].

In a study of managerial principles in Japan, China, and Korea, Alston [1989: 26] notes that, in Japan, “business relations operate within the group context of wa, which stresses group harmony and social cohesion,” and that, in Korea, “activities involve concern for inhwa, or harmony based on respect for hierarchical relationships including obedience to authority” and is strongly clan- or family-based. In each of these cases, there are subtle variations; however, common to each is the importance of networking and particularistic ties in order to provide stability and reciprocity in relationships.

D’Costa [2003: 70], in reviewing cooperative institutions in India, discusses the constructs of dharma, “which is a social order that calls for individual religious duty within a community context” and discusses its practical application in the jajmani system that institutionalizes giving and receiving and makes kinship ties ‘meaningful centres’ for social and economic transactions.” D’Costa [2003: 70] suggests that jajmani is a hierarchical system based on patron-client relationships that, although largely devoid of religious content today, has carried over into modern patron-client relationships, where “mutual obligations are still prevalent.”

In a discussion of the differences between a gift and second economy, or guanxi versus bribery, Yang [1994: 202] introduced the Russian construct of blat and suggested that, as is the case in guanxi, “in blat, there is a personal basis for expecting a proposal to be listened to, whereas bribery is conceived of as a relationship linked by material interest and characterized by direct and immediate payment.” In view of the above discussion, the authors of the current paper concur with researchers such as Child [2009: 67] that “other societies have similar relational systems” and suggest that “despite the appearance of cultural uniqueness,” they are amenable to valid comparison because they derive from the same source, reciprocal altruism.

The discussion in this and the preceding section suggests that variations in the psychological and behavioral manifestations of reciprocal altruism from polity to polity are primarily due to the ecological and socio-political contexts in which the various polities evolved. This view has strong anthropological as well as evolutionary biological support. Social psychologists have also addressed many of these issues, and it is to this discipline that we now turn to enhance our understanding of institutions and the links to perceived reality, beliefs, and behavior.
2.4. Building on North’s Framework: Lessons from Cross-Cultural Psychology

Cross-cultural psychology is a “systematic” endeavor aimed at understanding the intricacies of culture as it pertains to human development and its “repertoire of individuals” and their ultimate behavior [Berry et al., 1997: viii]. Cross-cultural psychology is therefore an appropriate discipline in which to search for a suitable theoretical framework through which to analyze the evolution of what are inevitably culture-laden functions. Seeking knowledge from other disciplines to enlighten our understanding of institutions is an appropriate pursuit and is not new to the social sciences, although it is an often under-utilized approach in international business [Cheng et al., 2009; Dunning, 1989]. Berry’s eco-cultural framework (Figure 2) attempts to incorporate a range of variables related to cross-cultural psychology and has been acknowledged as a guide for “numerous studies” and “experiments” [Lonner and Adamopoulos, 1997: 65], both qualitative and quantitative.

![Berry's Eco-Cultural Framework](image)

Source: Lonner and Adamopoulos, in Berry et al. [1997: 66]

**Figure 2. Berry’s Eco-Cultural Framework**
Cross-cultural psychologists were challenged about how individuals and cultures develop. They came to the conclusion that “psychological phenomena” stem from “cultural and ecological contexts” [Lonner and Adamopoulos, 1997: 65]. Although the framework is not a theory as such, it has been used to extract propositions and hypotheses, to examine embedded cultural and ecological contexts and their influence on behavior within and between polities, and to “postulate probabilistic relationships” [Lonner and Adamopoulos, 1997: 65].

The ecological context is defined by Berry [in Lonner and Adamopoulos, 1997: 66] as “the setting in which human organisms and the physical environment interact,” and the “central feature of this ecological context is economic activity.” As shown in Figure 2, the flow of the framework is from left to right, indicating that population level variables influence individual outcomes and that group and individual psychological characteristics and behaviors are a function of factors operating at the population level [Berry et al., 1997]. The important influence of the ecological context and the co-evolution of the socio-political context in the development of polities and their institutions has merit as it is also central to much of the works of evolutionary ecologists [e.g., Diamond, 1998; Dunbar et al., 1999; Parker, 1995].

Although the framework does not specifically refer to institutions, it may be deduced that institutions are particular cultural adaptations to the ecology and socio-political context at the group level and are sense-making mechanisms at the individual level. Neither does the eco-cultural framework address the role of reciprocal altruism and its importance in the types of institutions that polities form. Nor does the framework address the key variables in North’s [2005] framework. Consequently, in this study, we have modified the eco-cultural framework to acknowledge reciprocal altruism as a biological driver that adapts to the ecological context and as a background variable that informs genetic transmission. Further, we have inserted institutions at both the population and individual level as they operate collectively and individually. Finally, we have inserted North’s variables at the individual level as this is where their outcomes are expressed. The modified framework is shown in Figure 3.

Based on the literature, the modified eco-cultural framework presented in Figure 3 addresses the key variables that underpin the evolution and development of institutions discussed in previous sections. We propose that this adapted framework is a suitable heuristic device for analyzing how institutions evolve over time and for assessing the direction and margins of change. It also goes somewhat toward resolving one of the key conundrums in the debate between the
new and old schools of institutional economics, in so far as the individual is a function of the socio-economic environment but is equally a contributor to modifying this environment. It is largely irrelevant which came first, but it is important to acknowledge that such a complex emergent and self-organizing system exists [Redding and Witt, 2007].

Adapted for the current study from Lonner and Adamopoulos, in Berry et al. [1997: 66], North [2005], and Trivers [1971, 2006].

**Figure 3. The Modified Eco-Cultural Framework**

### 2.5. Unraveling Guanxi Using the Modified Framework

The Chinese word *guanxi* was introduced into the Western business vernacular in the early 1980s by researchers including Jacobs [1979], Pye [1982], Butterfield [1983], and Gold [1985]. The term describes the Chinese business, political, and social practice of engaging in mutually reciprocal relationships. The word *guanxi* has been variously defined in English as: connections [Bell, 2000; Guthrie, 1998], personal connections [Dunning and Kim, 2007], social connections and social networks [Gold, Guthrie, and Wank, 2002], special relationships [Leung, Wong, and Wong, 1996], social relationships [Guthrie, 1998]; personal relationships [Davies, Leung, Luk, and Wong, 1995], value-laden relationships [Ambler, 1995a], interpersonal connections [Bian and Ang, 1997], interpersonal relationships [Buttery and Wong, 1999], social capital [Carlisle and Flynn, 2005], networking [Qiu, 2005], and cooperative relationships [Pye, 1986]. Variations in interpretation have arguably been due to the perceptions and mental models of those trying to interpret and explain the
practice in a Western context. The current study follows Jacob’s [1979: 242] treatment of the term (see also Gold [1985] and Gold et al. [2002]) in which the Chinese term *guanxi* is used rather than an English derivation for three reasons:

[F]irst…to emphasize the analysis pertains to Chinese particularistic ties and not to particularistic ties in general. Secondly, the most accurate translation, “Chinese particularistic ties,” is quite awkward. Thirdly, non-speakers of Chinese have indicated that such simpler English translations as "relationship" and "connection" confuse more than they enlighten owing to a lack of equivalency between languages.

The importance of the study of *guanxi* is reflected in the number of academic disciplines in which it has been researched. These disciplines include: marketing [Ambler, 1995b], international business [Luo, 1997, 2002], strategy [Hwang and Staley, 2005], institutional economics [Boisot and Child, 1996], sociology [Tong and Yong, 1998], anthropology [Bell, 2000], organizational theory [Redding, 1993], cross-cultural management [Hutchings and Weir, 2006], finance [Batjargal and Liu, 2004], Law [Lo and Everett, 2001], and ethics [Dunfee and Warren, 2001].

It has been argued that *guanxi* is a source of competitive advantage for Chinese firms [Zou and Gao, 2007], but other authors suggest it is not [Tsang, 1998]. It has also been argued that the use of *guanxi* is unethical [Dunfee and Warren, 2001], whereas others suggest that it is just normal business practice [Dunning and Kim, 2007]. Some suggest that *guanxi* is losing relevance in business practice in modern China as more formal institutions for governing economic activity are being developed [Guthrie, 1998; 2002], but others argue that it is not [Hutchings and Weir, 2006].

Some researchers have suggested that *guanxi* is based strongly on Confucian values [Zhang and Zhang, 2006], and others say that it is a unique Chinese cultural phenomenon [Redding, 1993; Yang, 1994]. Others have argued that *guanxi* is the Chinese equivalent of a universal phenomenon for managing in an environment with poor institutional infrastructure [Guthrie, 1998]. Guthrie [2002], drawing on Yang [1994], argues that *guanxi* is simply a product of the cultural revolution. Yang [1994], however, also notes that its actual roots may lie in the ancestor worship tradition of the Xia (2205 BCE –1766 BCE) and Shang dynasties (1766 BCE –1122 BCE) and that it is related to the construct of *renqing* or “personal ties of affect and obligation” [Yang, 1994: 329]. Further,
guanxi is also related to the construct of mianzi and lien, or the giving of face [Hu, 1944; Yau, 1998].

Regardless of the varying views, what is generally agreed is that, without guanxi, one cannot do business in China [Dunning and Kim, 2007]. Perhaps the best definition of what guanxi might be is provided by Wellman, Chen, and Dong [in Gold et al., 2002: 222-223], summarizing the edited works in the book itself. They suggest it is naïve to view guanxi as a good/bad dichotomy with an over-emphasis on corrupt behavior, something perhaps better described through the construct of zho houmen, or back-door dealings. They see guanxi as “a web of interpersonal relations permeating Chinese societies.” They perceive that it is an informal institution that reduces uncertainty and transaction costs and builds interpersonal pleasure and connectedness.

From this brief review of the literature, it is apparent that the formation of particularistic relationships is not just a Chinese phenomenon, but rather a universal one that appears to be biologically rooted in reciprocal altruism. Further, when guanxi is viewed through the lens of the modified eco-cultural framework, it becomes clear that, though rooted in reciprocal altruism, guanxi has evolved to its present form as a consequence of China’s unique ecological and socio-political context, cultural adaptation, cultural transmission, and acculturation. A review on the guanxi literature suggests that guanxi operates as an informal socio-economic and politico-legal institution that can lower search and transaction costs, provide usable resources, and reduce environmental uncertainty and opportunistic behaviour. Guanxi in Mainland and overseas Chinese communities appears to act as an informal proxy for the more formal institutions found in Western polities. Guanxi has also shown itself to be an effective mechanism for facilitating smooth business interactions and business operations along the value chain in the Chinese context [Drew and Kriz, 2012].

Given the nature of guanxi, the question of interest in today’s globalizing economy, therefore, is:

**How is the use of guanxi in Chinese business activity changing in Mainland and overseas Chinese polities, as Chinese business people in these polities are exposed to more formal “Western” socio-economic and socio-political institutions?**

This question is the focus of the current study. We addressed the question by conducting qualitative research using the modified eco-cultural framework. Our
aim was to develop a context-specific research methodology and appropriate research questions for use in investigating the nature and practice of guanxi. The parent study from which this paper has been developed comprised 51 semi-structured interview questions stemming from the overall eco-cultural framework. The variables from the framework were operationalized through the interview questions in order to measure the influence of the ecological context (e.g., ancestral region of origin), the socio-political context (e.g., region of residence), cultural transmission (e.g., perceptions derived from parents), and acculturation (e.g., exposure to Western education and exposure to industry and professional values). The interview protocol comprised 11 demographic questions (region of residence, age, gender, profession, industry, parental ancestry, exposure to Western education), 19 open-ended definitional questions on guanxi posed in Chinese pictograms, and 21 semi-structured open-ended questions on guanxi practice. Responses to three of the most salient business-related questions are discussed in this paper.

3. METHODOLOGY

There has been considerable discussion regarding the appropriateness of using labels to define various philosophical and theoretical perspectives to research [Denzin and Lincoln, 2000; Schwandt, 2000]. Patton [2002: 95] suggests that “labels such as logical positivism, postpositivism, logical empiricism, realism, transcendental realism and objectivism are jargon-ish, have disputed definitions and carry negative connotations for many.” The researchers recognize that, in order to increase the probability of finding the “truth,” a pluralistic approach to research is required, drawing on whichever philosophical approach or theoretical perspective best suits the objectives of study, be they derivations of a positivist philosophy, a phenomenological philosophy, or both.

The design of the current research is philosophically aligned with phenomenology and naturalistic inquiry [Patton 2002: 39]. However, as it is impossible for any researcher to undertake a completely value-free inquiry because of his or her own values, beliefs, and assumptions [Lincoln and Guba, 2000; Patton, 2002; Sarantakos, 2005], the current study follows Patton’s [2002: 93] recommendation of taking stringent methodological and design steps to “mitigate their influences.” Exploratory research – and particularly research into deeply held beliefs, values, and practices – is best undertaken through a qualitative research methodology in order to elicit thick, deep, and rich descriptive responses from respondents [Denzin and Lincoln, 2000; Geertz,
Consequently, in order to better understand how *guanxi* is evolving, we deemed it necessary to explore the perceptions and thoughts of Chinese business people through qualitative techniques. This approach is supported by a number of other social science researchers [Berry et al., 1997; Fang, 1999; Redding, 1993; Weber, 1930], who explain that perceived reality varies from culture to culture (etic variations) and within cultures (emic variations). Given the cultural specificity of *guanxi* and this study’s focus on exploring regional variances in a culturally specific institution, an emic, or a more deeply within-culture analysis has been adopted, as it allows for the study of possible variations within a culturally embedded practice [Granovetter, 1985], across different geographical regions.

### 3.1. Research Strategy

A variety of research strategies can be used to conduct qualitative inquiry, ranging from structured, semi-structured, and unstructured interviews in individual and focus group settings to overt and covert observational case studies and archival research [Patton, 2002; Schwandt, 2007]. What is important is to select the appropriate strategy or combined strategies to best assist in answering the research question. The research question in this study lends itself most appropriately to an ethnographic study, or a study of the culture of a polity [Patton, 2002], as it seeks to understand and explain how *guanxi*, a shared cultural institution, is evolving.

### 3.2. Sample Size and Data Collection Strategy

The parent study of this paper focused on interviewing small homogenous groups of senior business people of Chinese ethnic origin through semi-structured interviews. In relation to the use and the size of the focus groups, the literature [Patton, 2002; Redding, 1993] suggests that the sample size of each focus group should be large enough to facilitate a range of perspectives, but small enough to ensure that all involved have the time, confidence, and opportunity to express their thoughts.

We determined, therefore, that there must be at least three respondents at each focus group interview in order to allow for the triangulation of perceptions and to assist in reducing individual biases, but no more than six, as more than six may not allow all questions to be commented upon by all respondents, may not be manageable from a recording and identification perspective, and may exceed the point of redundancy [Denzin and Lincoln, 2000; Sarantakos, 2005]. In order to
draw a sufficient number of respondents for the focus groups, we drew on our own guanxi with Chinese business people in each region and asked them to inform six business associates who were members of their personal network about the research and to recommend they contact us should they wish to participate in the respective focus groups. As a consequence, nine focus group interviews (comprising 44 participants in total) were conducted in eight cities – Jakarta, Singapore, Kuala Lumpur, Shanghai, Beijing, Taipei, Macau, and Hong Kong (x2). A pilot focus group interview was conducted in Hong Kong in December 2007, and the other interviews were conducted in February and March 2008.

The literature [Cavana, Delahaye, and Sekaran, 2001; Patton, 2002] also suggests that focus group sessions that are complemented with an online survey instrument provide a richer depth of data, especially in relation to personal observations, as opposed to purely group observations. Consequently, the current study included a secondary research phase involving a qualitative online survey instrument based on the focus group interview protocol, in order to facilitate the breadth of data and to lend rigor to the research [Cavana et al., 2001]. In order to increase the number of respondents, we asked participants in the focus group sessions to inform up to ten business associates who were members of their personal network about the research and to recommend they contact us should they wish to participate in the second phase. The online survey was undertaken by 159 business people of Chinese ethnic origin (including those who participated in the focus group sessions) and yielded 121 usable data sets.

This research also drew on a semiotic paradigm and symbolic interaction [Patton, 2002] by using Chinese pictograms in association with the semi-structured questions to ensure that all respondents had the same depth of understanding of the questions being posed. The literature suggests that the use of pictograms is an important part of a research design as it provides the opportunity to investigate shared assumptions and world views [Nisbett, 2003; Patton, 2002] within the context of the collective Chinese psyche related to language. To minimize issues with interpretation, we asked that all respondents be bilingual. The transcripts of both research phases were content-analyzed using NVivo 8 and Microsoft Excel to identify patterns and themes in the responses.
4. RESULTS AND DISCUSSION

This section briefly discusses the current politico-legal framework in each of the polities in which focus group interviews were undertaken and analyzes the findings of the focus group interviews and online survey in relation to the following three questions:

1. How has government policy, legislation, and regulations influenced the practice of *guanxi* and its role in conducting business in the respective polities?
2. How has business practice changed over the previous decade in relation to the balance between formal contractual agreements and *guanxi*?
3. How has competition for business resources (labor, materials, etc.) affected the use of *guanxi*?

4.1. Jakarta

The Indonesian legal system is loosely based on Roman-Dutch civil law, but has been substantially modified by indigenous and Islamic concepts. The nation is also increasingly embracing democratic principles and market reforms after 30 years of quasi-military rule. Respondents in the Jakarta focus group session suggested that Indonesian Chinese experienced periods of severe persecution, to the extent of “being treated like second class citizens” during the Sukarno and Suharto government anti-Chinese periods when the government had an active policy of stifling Chinese business activities. Consequently, the use of *guanxi* was essential in order to conduct business. Today, Indonesia continues to experience extensive levels of poverty, unemployment, corruption, and unequal distribution of resources, inadequate infrastructure, and a very complex regulatory environment [CIA World Factbook, 2008].

Respondents in the focus group interview engaged in considerable conversation about whether the development of government policy, legislation, and regulations to protect commercial interests would reduce the reliance on *guanxi*, but suggested that, even though the government is improving legislation, the problem is in the “execution” of the legislation. Even though laws and regulations are in place, they are not yet well enforced; hence, Chinese people still rely on *guanxi* to protect their interests. With regard to the use of *guanxi* versus contracts, it was generally agreed that, 10 years ago, the preference for *guanxi* “was about 70 – 80%, whereas today it was more likely to be about 50/50.” It was also agreed that, as more formal business protection mechanisms
Institutional Reform and the Changing Face of Guanxi

become established in Indonesia, issues of product quality, price, and reliability would probably become more important than guanxi in determining with whom they would do business.

4.2. Singapore

In contrast to Indonesia, Singapore is one of the world’s most prosperous countries. Singapore’s legal system is based on English common law and the country has a very well-developed free-market economy. Unlike Indonesia, where people of Chinese ethnic origin are a minority, Singapore in 2000 had a population in which the Chinese constituted 76.8% of the total [CIA World Factbook, 2008]. Although Singapore has well-established and effective politico-legal and economic institutions and is a parliamentary republic, it has effectively been ruled by one political party, the People’s Action Party, and has been dominated by one family since 1959.

In response to questions posed on the impact of political and legal forces on the practice of guanxi, the focus group members suggested that government policy, legislation, and regulations have little or no impact on the practice of guanxi and its role in conducting business. In other words, “Guanxi is just a fact of life and everybody does it.” Further, even though businesses in Singapore are subject to more formal instruments and institutions of control, such as contract law and government regulatory authorities, the consensus was that firms owned by Singaporean Chinese are more likely to draw on guanxi or personal networks in order to gain a competitive advantage. One respondent, employed by a Japanese firm, also suggested that Japanese firms operating in Singapore also draw heavily on guanxi. Consequently, even though there are strict requirements for corporate governance and transparency, guanxi is still a very important means of doing business in Singapore.

4.3. Kuala Lumpur

Malaysia is an emerging economy with an estimated GDP per capita (PPP) of $13,300 (2007) and a population (2004) of which only an estimated 23.7% are of Chinese ethnic origin, compared with 50.4% native Malay, 7.1% Indian, and 7.8% others [CIA World Factbook, 2008]. Nominally a constitutional monarchy, Malaysia operates under a bicameral parliamentary system and has been governed by the National Front Party since independence from Britain in 1957. The legal system is primarily based on English common law; however, in matters of family law and religion, Islamic law is applied to people of Islamic faith [CIA
World Factbook, 2008]. Malaysia is an interesting country in which to explore the role of guanxi because government policy favors native Malays of Islamic faith (bumiputeras) in business through an affirmative action process. For example, only firms with bumiputera directors may bid for government contracts.

Respondents in the Kuala Lumpur focus group session strongly agreed that the government’s policy favoring the bumiputeras forces Chinese-owned businesses to rely more on guanxi in order to do business. Similarly, the respondents all strongly agreed that Malaysian Chinese are more likely to draw on guanxi in order to gain a competitive advantage over other firms.

4.4. Hong Kong

Under British occupation from 1841 to 1997, Hong Kong has been exposed to Western-style economic and socio-political institutions as they have evolved. A highly developed free-market economy and, now, a special administrative region of China, Hong Kong maintains a reasonable amount of autonomy in business practices.

Hong Kong respondents in both focus group sessions and in the online survey overwhelmingly noted that government policy, legislation, and regulations, and particularly the ICAC, have reduced many of the negative behaviors associated with guanxi, such as bribery and corruption. They agreed, however, that guanxi is still an important mechanism for doing business and especially for making new business contacts. The majority also noted that, in doing business in China, things are different and that the use of all aspects of guanxi is necessary. On the subject of using guanxi as a source of competitive advantage, despite the presence of more formal institutions, the consensus of the two focus groups was that it would be used, and this position was supported in the online survey, in which 17 respondents answered in the affirmative, seven in the negative and two at “50/50.”

4.5. Macau

Although Macau and Hong Kong have different colonial and politico-legal heritages, Macau is rapidly catching up with Hong Kong in terms of economic and institutional development and has the same high degree of autonomy from China as Hong Kong [CIA World Factbook, 2008].

The responses from the Macau focus group closely mirrored those of the Hong Kong focus group. Specifically, they stated that the negative attributes of bribery and corruption associated with the practice of guanxi have been greatly
reduced and that *guanxi* is used more as a mechanism for developing business contacts and for growing business relationships. They noted, however, that dealings with the Mainland are quite different and that the more negative aspects attributed to *guanxi* are more apparent. With regard to the issue of using *guanxi* for competitive advantage, despite the presence of formal institutions, once again the consensus was in favour of using *guanxi*.

4.6. Taiwan

One of the four Asian tiger economies, Taiwan has a democratic political system, a civil law legal system, and a dynamic capitalist and increasingly free market economy [CIA World Factbook, 2008].

The focus group interview in Taipei also reflected the same conclusions as those in Hong Kong and Macau. Specifically, respondents indicated that legislation and regulations have reduced many of the negative practices associated with *guanxi*, but that *guanxi* is still important for making new contacts. Similarly, despite more formal instruments and institutions of control, such as contract law and government regulatory authorities, Taiwanese firms would use the practice of *guanxi* to gain a competitive advantage, particularly in order to secure scarce resources.

4.7. Shanghai

Since 1978, China has been moving toward a market economy; however, it is apparent from the comments of President Hu that China has no plans to replace socialist ideals with democratic ones. Consequently, China is currently evolving different types of more formal politico-legal institutions compared with those in the West.

In Shanghai, responses to questions on the practice of *guanxi* had a slightly different tone than those in overseas Chinese communities. With regard to whether government policy, legislation, and regulations influenced the practice of *guanxi* and its role in conducting business in the region, the point was made by the respondents that they did not perceive a relationship between *guanxi* and legislation and regulation. From the perspective of the Shanghai group, *guanxi* is much more about an affective relationship with someone a person could trust, more akin to the construct of *renqing*, and that this is a prerequisite prior to engaging in any business relationship. In that sense, legislation and regulation really do not matter. “You simply would not engage in a commercial relationship with someone you did not feel a sense of empathy with,” a respondent stated. It
was also made very clear that, in Shanghai, a person does not even do business unless he or she has *guanxi* first. Despite the evolution of more formal instruments and institutions of control, such as contract law and government regulatory authorities, the respondents agreed that they would also use *guanxi* to gain a competitive advantage, particularly in order to secure scarce resources.

### 4.8. Beijing

The comments made by the Beijing focus group strongly reflected the sentiments in Shanghai. *Guanxi* was perceived as much more of an affective connection with another person in the sense that people with *guanxi* feel obligated to each other. “*Guanxi* is not something you talk about; it is something that you do,” said one respondent. The perception was that government policy, legislation, and regulations would not have any influence on the practice of *guanxi*. As was the case in Shanghai, the Beijing business people interviewed agreed that, despite more formal institutions governing business practices in China today, they would definitely use *guanxi* in order to gain a competitive advantage. In a discussion of the sourcing of supplies, they noted that, if price, quality, and reliability were equal between two prospective suppliers, they would choose the supplier with whom they had the strongest depth of *guanxi*.

### 5. CONCLUSION

The modified eco-cultural framework has enabled a more comprehensive analysis of the practice of *guanxi* in a range of socio-cultural and socio-political settings and has proved extremely useful in this study by assisting us in identifying and analyzing the variables that underpin an institution such as *guanxi*. However, the modified framework requires further investigation and testing within and across a range of different polities in order to determine its overall reliability and validity as a framework for analyzing institutional change outside of a Chinese context. In addition, further research needs to be conducted to identify other variables that might underpin an institution such as *guanxi*. The expansion of North’s [2005] theoretical framework for analyzing economic and institutional change has been of particular importance. Further, the integration of Berry’s eco-cultural framework and the addition of a human biological universal – in this study, reciprocal altruism -- appear to have enhanced the research. Biological and cultural variables are often discussed but rarely applied in the extant literature. The expansion and development of North’s framework have enabled a more holistic investigation of the nature, role, and evolution of *guanxi*. 
From the discussion in Section 4, it is evident that the nature and practice of *guanxi* does vary from polity to polity. On the Mainland, it has a much stronger affective component, perhaps more similar to the related construct of *renqing*; however, it is sometimes used in a very instrumental fashion. In developing countries such as Indonesia and Malaysia, where the Chinese are in the minority and have either been persecuted or discriminated against, the instrumental practice of *guanxi* is much stronger than in polities where the Chinese population is in the majority. The responses from Hong Kong, Singapore, Macau, and Taiwan all indicate that, in the presence of more formal politico-legal institutions, the practice of *guanxi* is moderated to become more of a tool for cultivating new business connections. Responses from all locations, however, indicate that the nature and practice of *guanxi* is still very malleable and that, despite the presence of more formal politico-legal institutions, all respondents agreed that they would use *guanxi* as a source of competitive advantage, particularly in times of scarce resources.

These findings question a simplistic view of the changing nature of *guanxi*. Suggestions that *guanxi* will simply yield to more formal Western institutions as China modernizes should be tempered with a more comprehensive understanding of the antecedents of *guanxi*. Despite more than 30 years of economic reform on the Mainland, *guanxi* remains a powerful force for doing business there. *Guanxi* may have less corrupt implications in polities that have adopted more formal “Western style” institutions, but it remains a key ingredient in terms of making choices about “with whom” you choose to do business.

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