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Guanxi, structural hole and closure

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Abstract

Purpose — Understanding China's economic success requires insights into its peculiar guanxi-based market. Many scholars are confused how to apply western network theories to the Chinese guanxi-based market. This paper contributes to this comprehensive topic by theoretically exploring the differences among three fundamental network concepts: (1) guanxi, (2) structural hole and (3) closure.

Design/methodology/approach — Following Heide (1994), we categorize a network into three dimensions: (1) network initiation, (2) network maintenance and (3) network termination, based on different time phases. We compare the three fundamental network concepts in every dimension, laying out detailed similarities and dissimilarities among them.

Findings — All three networks are initiated either naturally or artificially, but guanxi is closely embedded in the Chinese institutions. Unlike structural hole and closure, which can be applied at any level, guanxi is a special relation that only exists at the individual level. Structural hole and closure highlight networks' structures which bring them various benefits and constrains. Such merits are not evident in guanxi in which favor exchange plays a crucial role in connecting entities. In addition, guanxi has a special rule to affect the strength of ties.

Originality/value — The purpose of this paper is to articulate the differences among guanxi, structural hole, and closure. With our systematic framework, we offer a platform to scholars who are interested in applying the western network theory to guanxi-based market, and our work also provides non-Chinese who are doing business in China with new insights.

Keywords: Guanxi, Structural Hole, Closure

Paper type: Conceptual Paper

Introduction

During the last decade the world has witnessed an unprecedented shift in economic power from the west to the east. Asian economies represented by rapidly emerging China, have become the world's new economic engine. The global financial crisis did not seem to bite the same way in China as it did in the West. The growth in East Asia is fascinating and is expected to continue in the foreseeable future. These Asian countries (e.g. China, Japan, South Korea, and several Southeast Asian countries), which are deeply affected by Confucian culture, have their own ways to organize business networks and transactions (Luo, 2007). This way is called Guanxi¹. "In China, transactions often follow successful guanxi, while in the west a relationship follows successful transactions" (Park and Luo, 2001:457). In this paper, we will analyze Guanxi-based markets by applying various types of concepts from network theory, trying to solve some Asian puzzles that are hard to understand by western scholars and business people.

Network theory is a hot topic in strategy and management research, and it also provides important insights into business markets (Håkansson *et al.*, 2009). Numerous special issues and edited volumes describe network theory in different ways (Smith-Doerr and Powell, 2003). Thorelli (1986:38) defines network as "consisting of nodes or positions (occupied by firms, households, strategic business units inside a diversified concern, trade associations and other types of organizations) and links manifested by interaction between the positions". Gulati *et al.* (2000:203) state that "Networks encompass a firm's set of relationships, both horizontal and vertical, with other organizations—be they suppliers, customers, competitors, or other entities—including relationships across industries and countries". Since the 1980s, a series of writings from Burt (1987; 1992) and Coleman (1988) have provoked people's attention and let the idea that business network plays critical role in firms' strategy spread widely. Burt's structural hole and Coleman's closure as academic paradigms have been tested by scholars numerous times from a variety of aspects, showing that the theories can be applied in various industries and in different geographic regions (e.g. Ahuja, 2000; Powell *et al.*, 1996).

Therefore, considering that both Burt and Coleman's thoughts are, by and large, established on the western business contexts characterized by "self-seeking and egocentric

¹ Guanxi (Chinese), Kankei (Japanses), and Kwankye (Korean) have similar meanings.

agents with little sense of obligation to others” (Xiao and Tsui, 2007:4), a question occurs that, if business context shifts from western countries to eastern Asian countries, say China, in which collectivism is used to be the backbone of society life rather than individualism, do such network theories still apply?

Although the answers to the question are many (Chua *et al.*, 2009), surprisingly, only a few papers give us a depth of discussion from a basic view point that exploits the essential difference between guanxi and the western network—structural hole and closure. Clearly, clarifying such differences is required in order to develop new understanding of guanxi-based market, as well as to expand network theory itself.

Our paper is designed to uncover such differences. Based on previous works, especially the typology used by Heide (1994) in his transaction cost research in interorganizational governance, we divide network/guanxi into three phases: (1) initiation of network/guanxi, (2) maintenance of network/guanxi, and (3) termination of network/guanxi, and then we systematically compare structural hole, closure and guanxi.

The article is organized as follows: in the next section, we briefly present three definitions of guanxi, structural hole, and closure individually; in section three, we compare the three types of business relationships at every phase. Case illustrations of the network types as applied in a Chinese context are also included; and in the last section we present our conclusions.

Three Definitions

Guanxi—Guanxi is a special relationship, but it is far more than the concept of relationship that is well known to us. An existing relationship may not be a guanxi, for instance, two classmates who never contact each other after graduation have a relationship (at least, a weak tie), but may not have guanxi. For clearly understanding “what is guanxi”, we lay out several definitions of guanxi. Bell (2000:133) calls guanxi “a mechanism by which individuals are able to achieve personal, family, or business objective”. In their writing, Yeung and Tung (1996:55) define guanxi as “the establishment of a connection between two independent individuals to enable a bilateral flow of personal or social transactions. However, both parties must derive benefits from the transaction to ensure the continuation of such a relationship”. Davies (1995:22) defines guanxi as “the social interactions within the network place and its members in the equivalent of an infinitely repeated game with a set of people they know”. Moreover, Yang (1994:1) illustrates that “guanxi means literally a relationship between

objects, forces, or persons. When it is used to refer to relationships between people, not only can it be applied to husband-wife, kinship and friendship relations, it can also have the sense of social connections, dyadic relationships that are based implicitly (rather than explicitly) on mutual interest and benefit. Once guanxi is established between two people, each can ask a favor of the other with the expectation that the debt incurred will be repaid sometime in the future”.

Guanxi generally is classified into three types: family, helper and business guanxi (Fan, 2002). Family guanxi is mostly blood based, like parents, children, brothers, daughters-in-law and so on. Helper guanxi is social based, like relatives, friends, teachers, students, classmates and so forth. Business guanxi is a process that finds solutions for some business through personal connections. Business guanxi is based on personal gain and loss, and examples could be suppliers, customers, business partners etc. Furthermore, Peng and Luo (2000:486) demonstrate that, in business guanxi, the Chinese managers' micro interpersonal ties with government officials help improve organizational performance. Thus business guanxi in the Chinese meaning differs fundamentally from business relationships as commonly conceived in the West.

Closure—“Networks with closure—that is to say networks in which everyone is connected such that no one can escape the notice of others, which in operational terms usually means a dense network—argued to be the source of social capital” (Burt, 2000:351).

Closure has two basic functions. One is that it is close to the source of information. Coleman (1988:104) explains “an important form of social capital is the potential for information that inheres in social relations”. He continues: “A person who is not greatly interested in current events but who is interested in being informed about important developments can save the time required to read a newspaper if he can get the information he wants from a friend who pays attention to such matters” (ibid). The second function is strengthening trust by sanctioning behaviors that benefit decreasing risky within the network. Members who connect to each other with the form of closure in the same network could both monitor and be monitored by others. According to Coleman’s theory, “members of a closely knit network can trust each other to honor obligations, which diminish the uncertainty of their exchanges and enhance their ability to cooperate in the pursuit of their interests” (Gargiulo and Benassi, 2000:184).

Structural Hole—Structural hole is another kind of network. Structural hole as a term was coined by Burt (1992:18) whose definition is “a structural hole is a relationship of non redundancy between two contacts”.

Burt (1992) assumes that effective cooperation between firms is deeply affected by the selection of partners. In Burt's view, benefits would be decreased if a network puts constraint on relationships within it. Firms with structural holes have higher economic gains due to effectively filtering redundant information out and freely choosing tactics and strategies.

The most significant benefit to those who have structural hole at hand is "broker benefit", that is the broker has opportunity to control and spread information within a network for maximizing his benefit. As Gargiulo and Bennis (2000:184) said: "Rather than stressing the utility of consistent norms fostered by cohesive networks, structural hole theory claims that the benefits of social capital result from the diversity of information and the brokerage opportunities created by the lack of connection between separate clusters in a social network".

For clearly presenting the differences among these three concepts, we offer a concrete example about Zhongguancun in Beijing (see Textbox 1), which reflects how the Chinese use guanxi, structure hole, and closure simultaneously.

Textbox 1: Case of Zhongguancun: guanxi, structural hole, and closure

Zhongguancun IT cluster is located in Beijing, China. It is, to a large extent, a closure, as most entrepreneurs in this area have been working before in R&D institutes of the Chinese Academy of Sciences and universities. They possess excellent technological knowledge and use them in creative ways. This is a dense network with guanxi – everybody seems to be connected to everyone to facilitate their success by using guanxi "infrastructure", because most often they are graduates of Peking University and Tsinghua University. However, the dense guanxi network does not hinder CEOs, in particular those startups, from creating and manipulating structure holes by seeking undiscovered business opportunities. Beijing Hi-World Software Technology (BHWST), a company in Zhongguancun, offers us a vivid example. At the beginning, BHWST was a construction company, but its CEO soon realized that "there is no software company in China that writes software for tall buildings. Construction firms do not engage in software development, and software programmers overlook this niche of the market". BHWST's CEO began to "dig a hole" between software business and construction business, which subsequently brought considerable revenues to the company.

Draw on Batjargal (2007:611), and re-edited by the authors

Differences Among Guanxi, Structural Hole, and Closure

Networks could be categorized into three dimensions: (1) network initiation, (2) network maintenance and (3) network termination based on different time phases (Heide, 1994). The first phase is about how to initiate a network. A network may be created by some natural reasons, or may be totally an "artificial product", or a mixed body of both. The second phase — maintaining network includes: (1) positioning roles, meaning how to reasonably specify

and assign entities with certain roles in a network; (2) nature of operation, meaning to make sure the network runs smoothly, and to adjust mistakes made by network participants confronting varying circumstances and contingencies from time to time; (3) in monitoring procedures, participants more or less play the “game” under the third party’s monitoring; (4) incentive system refers to what stimulates participants to maintain relations. The last phase is “how to end a network relation”. Table 1 summarizes the entire process.

Table 1: Dimensions and Types of Networks

Types of Networks	Dimension		
	Guanxi	Structural Hole	Closure
1. Network Initiation	<i>Culture and institution reasons</i>	Objective and subjective reasons	Objective and subjective reasons
2. Network Maintenance			
2.1 Positioning Roles	Individual level; To be broker/friend; Unbalanced power/obligation	Any level; To be broker; Unbalanced power/information	Any level; To be friend; Balanced power/information
2.2 Nature of Operation	To be sensitive of Chinese culture	Content and connection	Build trust and reputation
2.3 Monitoring Procedures	Internal mechanism; “Voluntariness”	Internal mechanism; “Calculation”	External mechanism; “Penalty”
2.4 Incentive System	Long term benefit	Short term benefit	Long term benefit
3. Network Termination	No return favors; Lose face	Costs; Ties’ strength	Violate

Network Initiation

Deeply influenced by traditional Confusion culture, to Chinese initiating guanxi that brings reciprocal benefits is, often superior to constructing structural hole or closure. Under this institution, three types of guanxi are initiated: Family is the first place that generates guanxi, and such guanxi is the most solid and nature, e.g., parent-children, husband-wife etc. Family guanxi is a basic network that supports family member’s development as well as offers a platform for expanding their external network. The second type of guanxi is “helper”. A helper might be contingently formed, like relationships of classmates, colleagues etc. But it may also be artificially formed, like one of your intimate friends introduces one of his (her) friends to you, and then you have close contact with your friend’s friend. The third kind of guanxi is business oriented which is mixed by artificial and natural reasons. A significant example is a purely commercial guanxi between suppliers and retailers, with the sole purpose

of making money. However, business guanxi is unstable, especially if there are few social interactions (e.g., favor exchanges) among business actors. Many Western managers doing business with the Chinese, found that legal contracts were not enough to achieve good business results (Bjorkman and Kock, 1995). Furthermore, managers also found that business guanxi leads actors in the same business treat each other as outsiders, and such kind of guanxi is fragile and can easily be broken (Yau *et al.*, 2000).

Both objective reasons and subjective reasons impose effects on structural holes' initiation. Burt (2005) sketches several reasons why structural holes are naturally formed: (1) information circulates faster within groups than between groups (Burt, 2002); (2) limited time and energy constrain people to maintain connections with all stakeholders (Granovetter, 1983); (3) variations in beliefs and practices occur at individual level, as well as at group level. All in all, people can only "trace" several certain ties, but lose "track" of other people/groups. Furthermore, after people realize that structural hole might benefit themselves from two aspects well-known as "easy access to information" and "control capability", they have momentum to: (1) delay the hole's decay (Burt, 2002); (2) deliberately create and build new bridges with unconnected or remote entities. Although maintaining structural holes to some extent is costly (Burt, 2002), an abundant number of papers has demonstrated that the holes bring vast benefits to people (Burt, 1997; 2007) and to companies (Ahuja, 2000).

Closure, which is similar to structural hole, has been either formed objectively or formed subjectively. Inherently everyone is more or less embedded in some relationships. In particular, those relations people cannot choose but bear naturally, for instance family relations and kinships. You do not choose your family, you are born into it. From another aspect, closures might also be built by objective reasons. With passage of time, brokers may give up structural holes for gaining benefits yielded by closed ties and dense networks which are more stable and involve more trust and reputation. Moreover, those entities, who communicate with each other via the brokers who control and bridge the holes, might also build mutual or multiple relations themselves for virtues like direct information, reducing cost, etc.

The case of Australian Sydney Corporation (see Textbox 2) reveals the different logics of initiating business networks in a Chinese context.

Textbox 2: Case of Australian Sydney Corporation

Australian Sydney Corporation (ASD), a lubricant manufacturing company operating in China, had difficulty finding distributors because of the country's newly developing market infrastructure and the resistance of Chinese to doing business with strangers. ASD's manager described: in the beginning, we advertised heavily in newspapers and magazines, but nothing came of it. We then tried to send sales agents to various cities to push our products. But because we had no established guanxi, the effort was in vain, even though we spent a lot of money on the operation. Later, we developed guanxi with a person in charge of a division in the department of commerce in Beijing. He introduced us to a local distributor who he has guanxi with. Subsequently, the distributor agreed to put our products on the market, but only because of his guanxi with the person in the department of commerce in Beijing. The distributor's personal assessment of the quality of our products was largely immaterial.

Pearce and Robinson (2000:32-33), re-edited by the authors

Network Maintenance

Positioning Roles

Positioning roles concerns two issues. From a macro point of view, the three concepts have various applicable scopes—structural hole and closure assign roles to firms as well as to individuals, while guanxi is only relevant to individuals; from a micro view, under different networks, different entities have different powers and hierarchies.

From a macro aspect, referring to structural hole per se and closure per se Gnyawali and Madhavan (2001:433) clearly point out “the network approach is potential for multi-level analysis—that is actor-level, pair-level, and network-level analyses”. For instance, Coleman (1988) exemplifies that children, whose families are in the community that provides cohesive network connecting local families, have less possibility to drop out of high school (individual level). And in Walker et al. (1997)'s case, biotechnology startups are inclined to form closure rather than to exploit structural holes (group level). Meanwhile, the corresponding findings from the point of view of structural holes show that the holes benefit bankers and managers in their early promotion and income (Burt, 2007); and at group level, for instance, “investment banks benefit from structural hole positions, and that those banks that occupy disadvantaged positions are likely to endeavor to span structural holes to gain network advantage” (Baum *et al.*, 2003:720). But, the Chinese guanxi is barely “pegged” to interpersonal relationships, such as family members, friends, classmates, hometown-mates, business partners, etc. Firms in China do have business relations organized by formal and informal rules and customs, like

written contract and product reputation, but firms do not have guanxi, which relies on guanxi base and involves dyadic and unlimited rounds of favor exchanges.

From a micro aspect, participants in guanxi take unbalanced positions in power and obligation. No matter whether it is the simplest guanxi that merely involves a person who asks a favor and a person who offers a favor, or a complex relation that starts from a favor asker to several “brokers” and finally to favor giver, such unevenness is very prominent. Favor askers use guanxi to fix the problem they have because either they do not know how to get and indentify useful information, or even if they were able to master good information, they might lack capability to fix the problem. Conversely, favor givers, for one thing, have such information and ability to help others maximize profits. Furthermore, favor givers could reassure themselves that they may receive reciprocal returns in future. In real life, by collecting questionnaires from 364 Chinese executives, Luo (2003) points out that such unbalanced guanxi positions are significant especially when the business environment has high uncertainty, high competitive pressure, and low production capacity utilization. Xin and Pearce (1996) have similar opinion, and they show us that the big and state owned firms are superior in guanxi roles, comparing to small and private firms.

The essence of structural hole theory is that entities should position themselves at a place which connects separated parties. Structural holes inherently create advantages in achieving unbalanced information, as well as power. Information advantages consist of three perspectives (Burt, 1992; 1997; 2007): (1) access benefits: the broker reaches a vast number people with direct and indirect means; and furthermore, the information is broad and of high quality as little redundant information would be shared and received by the broker; (2) timing benefits: the broker is the first ones who “touch” the news about new innovation and market demand; (3) referral benefits: the broker is the “candidate for inclusion in new opportunities” (Burt, 1997:342). Besides information advantages, structural holes also provide control benefits: this means the broker could decide and adjust each contract, and he/she is the person who “adds value by brokering the connection between other” (Burt, 1997:342).

The closure stands on the opposite side to structural hole. People in closed networks could be imagined as the relationship between intimate friends: they know each other quite well, and have mutual trust, and there is almost no secret within the network. An extreme case is that when a piece of news enters into a closure, everyone in the network has access to the news; moreover, the news could be spread with only one version (Coleman, 1988).

Nature of Operation

In this sub-section, we will try to shed light on the means with which firms operate their normal business activities and adjust their interactions with others.

Guanxi might be very hard to operate and adjust. Guanxi is a culture, an attitude, and a social custom. It is not like structural hole and closure which are somehow measurable (for more details, see Burt (2001:33), the density table of relations within and between groups). Perhaps one reason is that the change of guanxi network is hard to detect. A guanxi network normally consists of strong ties, weak ties, structural holes, and closure. On one side, such network is too complex to trace trajectory of changing, like strong tie turns to weak tie, and sometimes structural hole is filled up etc; on the other side, even guanxi is a reciprocal relation, it is not a precise mathematical formulation like “investment-return” function. The reciprocal obligation in guanxi is quite vague, and people just deal with it according to their personal experiences. Therefore, we only offer a principle of operating guanxi network, that is, learning more about the Chinese business culture and following Confusion philosophy.

Brokers who control a vast number of structural holes, have two ways to operate their networks. The first way relates to adapting to the shift of properties of ties (Emirbayer and Goodwin, 1994). Content of ties is a broad idea revealing basic issues that affect business networks. For instance, strong or weak relations, and frequent or infrequent ties (Granovetter, 1983); other methods also include that of adapting to environment that contains ties (Adler and Kwon, 2002), learning tacit institutions related to ties (Burt, 1997), and so on. The second way looks much more “aggressive”, that is seeking to modify or change the network’s structures. The premise argues that structural holes might bring monopolistic advantages in information and control for brokers. Therefore, in accordance with network theory (Baum *et al.*, 2003), say two firms belonging to two unconnected groups might “dig” a hole together, either when they hope to integrate their resources and exploit a new market beyond the two groups, or the two firms have incentives to re-locate their positions in their own markets; or if the two firms are big and influential ones, through building structural hole they could create a relatively stable environment that improves their competitiveness. For example, Baum *et al.* (2003) have an example that “commuter airlines that serve (enter) more markets are more likely to have (establish) multi-market ties with other commuter airlines not because of any international effort by their strategists to develop such ties, but because they are more likely to encounter the same competitors in multiple markets than airlines operating in fewer markets” (ibid:704).

Against structural hole, closure emphasizes to build intensive networks. It also has two issues that we need to think about. First, an entity in a closure should know others who are in the same network, the more the better. Therefore, in closure, firms are more well behaved and are less affected by other sources of information that firms in structural hole (Haunschild and Beckman, 1998). Second, the entity should also help the third parties build dyadic or mutual connections, and such network with high density, according to Coleman (1988), would benefit all members in the closure. Closure is relatively simple to adjust, and the core is building trust and reputation. Communication is the most effective “weapon”, through which an entity who masters more information, has a high possibility to become a helper and a medium of information diffusing.

Monitoring Procedures

If only concerned about guanxi without consideration of corruption, monitoring guanxi is a hard and an almost impossible task. External monitoring mechanism (or the third party monitoring mechanism) has little influence on guanxi. No one has the right to interfere in a legal “person to person” relationship. Furthermore, such monitoring mechanism is unfeasible: an individual’s guanxi could be treated as one’s privacy which is normally intangible and would not be shared with the third party. That means it is hard for external mechanism to find “where is guanxi”. Internal monitoring mechanism is applied here. In spite of favor askers having little power to monitor favor givers; and in spite of favor givers, on the other hand, who have places which are superior to those favor askers, have no reason to accept monitoring from the askers. The two sides in one guanxi would be self monitored for keeping a balanced guanxi “trade off” in a long term.

We cannot say that there are no external monitoring impacts which would affect broker’s advantages given by structural holes, like notably a firm’s centrality in its network (Wasserman and Faust, 1994), the network’s density (Coleman, 1990), and cultural institution (Xiao and Tsui, 2007) constrain the firm’s momentum to conduct opportunist behaviors. However, if we only concentrate on the broker, and consider the issue from the micro level, a simple reality is that there is no external monitoring system—such as an exact third party—that has the power to monitor a structural hole network. But, seeing from another side, a broker has some indicators with which he could monitor his own holes. So, this is an internal private monitoring procedure in which two variables are undeniably important: constraints, and structural equivalent. Constraint means the extent to which a firm “is directly or indirectly concentrated in a single contact” (Burt, 1997:347), the more constraint, lesser structural holes

(see Burt, 1992, for details). Structural equivalence exists when relationship patterns that belong to one actor are similar with other actors' patterns (Rice and Aydin, 1991). Unlike variable of constraint which quantitatively sketches structural holes, structural equivalence maps the structural holes' qualities, for instance, structurally equivalent firms have little likelihood to initiate aggressive competitions, as well as to respond positively in the face of business challenges (Dutton and Jackson, 1987).

Closure, usually, relies on external monitoring mechanism. Coleman (1988) shows us that the closure network itself is like a big "monitoring system". Theoretically, every one in a closure network has no privacy, no secret, and any information in closures is equally spread among individuals—every one knows what you are thinking about, your behaviors, as well as you know all others' information in any perspective. Living in a closure network, a person must follow the rules, principles and culture which are well accepted by all members in the network. Besides such kind of self-monitoring, members should also offer information to others who are in the same network, like in Coleman's "parent-children" example, the parents exchange the information they know through frequent contacts.

Incentive System

Structural hole is no doubt a kind of network that puts huge amount of attention on short term benefit. Structural hole can only exist for a short period of time as there are many possibilities that new connections appear between those who do not know each other. Brokers understand that the information advantage and control advantage brought by structural holes could not last forever. Based on the outcome the structural holes yield, brokers make decisions about when and how to give up old structural holes and to develop and organize new holes.

Closure is expected for chasing long term benefit. Coleman (1988:98-100), for instance, portrays a market named Khalili in Cairo, in which "family relations are important in the market, as is the stability of proprietorship". If someone only chases short term benefit but ignores following the principles, rules and culture, he/she may "lose family, religious, and community ties" (ibid) and "in the absence of these ties, elaborate and expensive bonding and insurance devices would be necessary—or else the transactions could not take place" (ibid).

Guanxi is a combination of structural hole and closure in terms of incentive system. Guanxi treats output and behavior equally important. Many scholars agree that guanxi is a long term game (Hammond and Glenn, 2004), and entities must carefully develop, cultivate and maintain it. After all, in Confucian philosophy, a transaction often follows a successful guanxi (but not vice versa). When guanxi is broken, the corresponding businesses easily

come to an end. Additionally, when a guanxi is broken, restoring it is fairly tough work: ending a guanxi implies that the trust between two parties “goes to bankrupt”. Therefore, normally, businessmen wish to develop and maintain long term guanxi, which helps them build their reputation in business.

At the end of this subsection, we use the Motorola case (see Textbox 3) to exemplify how to maintain guanxi in China over time.

Textbox 3: Case of Motorola

Loss of face results in the degradation and possible dissolution of the guanxi relationship. Because guanxi serves as a lubricant for exchange, the cultivating relationships with Chinese bureaucrats. Former CEO Robert Galvin took his first trip to China in October 1986, and since that time, Motorola identified and befriended three generations of potential top leaders. In 1989, Motorola was set to build its first factories in Tianjin. The Tiananmen Square incident leads U.S. government to sever diplomatic relations with China. A corresponding withdrawal by Motorola of its commitment to build in China would have caused the numerous Chinese bureaucrats working with Motorola to lose face. However, unlike many Western companies that decided to remove their Chinese business, although Motorola delayed construction of the factories for two years, it never withdrew its commitment to do so. In order to “re-enter” the Chinese market, Motorola would have had to start completely a new rebuilding the guanxi network it so carefully nurtured. In the realm of guanxi, China never has forgotten Motorola’s loyalty. By 1997, Motorola’s investment in China was \$1.3 billion, double the next largest U.S. investor, Atlantic Richfield. Furthermore, Motorola was the first foreign firm to insist on full-ownership for a manufacturing operation.

Draw on Standifird and Marshall (2000:24-36), and re-edited by the authors

Network Termination

The excuses of ending a guanxi could be many and varied. First, there is no free lunch in the world. Guanxi requires favor askers to return favors and to favor givers in some certain time with some approaches. If someone just wants to receive supports from others, but refuses to provide reciprocal help when others are in trouble, then such kind of “unidirectional” guanxi would soon disappear. Second, some mistakes may also result in guanxi termination, for instance, a common thing is that of letting someone lose “face”². Third, there are still other issues that influence termination of a guanxi, for instance as we have mentioned in prior paragraphs, geographic distance: two intimate friends may have less and less favorable

² lose face means “to not maintain your reputation and the respect of others”
(<http://idioms.thefreedictionary.com/lose+face>)

exchanges after their graduation because they stay in two different continents. In such a situation, the guanxi network between these two persons weakens gradually. In addition, Tsang (1998:70) notes “since guanxi is a crucial company resource, it is worthwhile for senior management to audit their company’s guanxi with its outside stakeholders, such as customers, suppliers, and government bodies”. It is important to note that guanxi is developed by people’s interpersonal relations, not by the companies themselves.

In his article *Bridge Decay*, Burt (2002) outlines his network decay theory, in which he lists some primary factors that might terminate structural holes. The first thing is high maintenance cost. “Research on the tendency for people to have relations with people like themselves implies that bridges require more effort to maintain” (Burt, 2002:344). The second is that such kind of high maintenance cost can only be shared by few people—more precisely, the two parties who are in the two sides of the hole/bridge. On the contrary, in cohesive network, the cost is borne by all parties. The third aspect is about the strength of the tie—is it a strong tie or a weak tie? Normally, strong ties mean heavy interactions between two entities, and weak ties mean that the two entities interact with each other infrequently (Granovetter, 1983). Structural holes characterized by strong ties would survive for a long period of time as “people who have learned to appreciate one another, which increases the probability of relationship continuing into the future” (Burt, 2002:343). Weak ties, vice versa, either weaken holes’ impacts, or develop into strong ties. In addition, in accordance with small world theory (Barabasi and Bonareau, 2003), the network itself roughly keeps balance between structural holes and closure. Baum et al. (2003) exemplify a case: a core firm which connects a lot of peripheral firms enjoys information and controls advantage by owning structural holes. The peripheral firms, for reducing dependence on the core firm, have momentum and motivation to fill in the hole with building direct connections to each other. Such behaviors then naturally deprive the core firm of broker benefits.

Closure generally will last for a long time, but if an entity violates the common principles, rules and culture, then the closure belonging to the entity is gone. In Coleman’s (1988) diamond market story, if someone steals a gemstone from the market, then the person loses his closure—others no longer trust him, and his reputation is ruined.

In Textbox 4, a Chinese manager recalled his experience about a merger between a U.S. and a Chinese company. This case shows how guanxi relations can terminate when confronted with different network logics.

Textbox 4: Case of a merger between a U.S. and a Chinese company

Soon after the merger between a U.S. and our Chinese company the first conflict occurred. Our company's biggest customer in China with whom we have had a very good business relationship for more than 3 years, asked us for an extension of their credit period from 60 to 90 days. Such a request normally was handled by our credit control department according to set procedures and included a review of the creditability record of the respective company. It normally took half a month. After the merger, our U.S. partner handled such requests and refused to extend the credit. The reason given was that it would slow down the company's cash flow. Our customer was angry, and our commercial team was sad that the company gave up the biggest customer so easily in such a competitive market. In addition, our finance manager felt that apparently they did not trust anything she told them regarding local business operations. They always wanted the check with other sources such as lawyers etc. to verify it. We thought this was a waste of time and a sign of not respecting our know-how. More and more Chinese sales managers started to leave the company, and the merger ended in a mess.

Hoivik, (2007:463)

Conclusions

In this paper, we have compared the differences between guanxi, structural hole and closure. Guanxi is based on Chinese interpersonal relations of favors, while structural hole and closure are based on western contractual logic of benefits and costs. Thus, western network concepts cannot easily be applied in Chinese guanxi-based markets. Perhaps this explains why so many western companies initially fail while doing business in China. By the same token, Chinese companies may experience some problems while doing business in the West.

According to our comparative network framework, we would like to highlight several main points:

Institutions—Institutions including custom, religion, and legislation etc. have vast influence on networks. Such influence exists in networks from beginning to end. The Chinese resort to guanxi primarily because of its relatively less sophisticated legal system in which people have no choice but to rely on interpersonal relations to get things done. Further, the principle of doing others a favor when it is necessary, and returning favors to those who helped you, is also advocated by Confucian philosophy. In contrast, western business networks operate within well established legal systems and rely on formally contractual logic. In the western institutional context, contractual business methods become superior to depending on interpersonal relationships.

Scope of application— In accordance with guanxi theory, guanxi only exists at the interpersonal level, or more precisely, guanxi is a rule/custom dealing with interpersonal relationship. Firms which interact with others have business relationships that could be either

formally set down by written contracts or informally built by exchanging tacit knowledge, but they do not have *guanxi*. Nevertheless, structural hole and closure extend from individual level to group level. These two theories treat network participants as nodes which sometimes are homogenous, meaning the node's characteristics to some extent could be ignored.

Position in networks—Structural hole theory requires individual entity to occupy intermediate position for pursuing information and control advantages. In contrast, closure theory pushes individual entity to live in a densely embedded network for cultivating trust and reducing uncertainty and opportunism. Thus, according to these two theories, entities' positions in the network to a large extent determine their benefits. Nevertheless, in *guanxi*, position as a factor does not have any vital effects. *Guanxi* has a peculiar way—favor exchange—to run dyadic or multiple interpersonal relations. Thus, *guanxi* uses psychological distance to initiate relations (Chen and Chen, 2004) which also weakens effects caused by physical position. A salient example is family *guanxi*: imagine that a husband is a broker in a network, and then his wife, even if totally isolated from the network, has a high possibility to access her husband's broker advantages.

Strength of ties—In all three networks the content of the ties is also very important. A notable factor is that the western network theories judge strength of tie by using time and energy, e.g., the indicator of “constraint” quantitatively calculates the degree of “strength”. However, in *guanxi*, the strength is naturally ranked by family member, helper, and business partners in terms of closeness. Thus, *guanxi* as an interpersonal relation is difficult to model quantitatively.

An interesting observation is that the studies of structural hole, closure and Chinese *guanxi* all began in the 1980s—Coleman (1988; 1990) put the foundation stone on closure; and Burt (1987; 1992) stood at the opposite side of Coleman by saying structural hole brings us broker benefit, and China, at that time, was just opening its doors to the world, and such “open door” policy attracted researchers' interest in the Chinese business context. Previous research mostly focuses on differences between social network and the Chinese *guanxi*, or on testing western social network theory in a Chinese context. None of them give us an integrated framework explaining structural hole, closure, and the Chinese *guanxi* simultaneously. Our paper elaborates on such differences with the logic that every network would experience three phases; initiation—maintenance—termination. Although *guanxi* can visually be mapped in the same way as hole or closure structure, the three network concepts are vastly different. Thus, researching and applying network theories in *guanxi*-based market still has a long to go.

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