

## **Guanxi and favor in the People's Republic of China (PRC)**

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## **INTRODUCTION**

Many scholars have repeatedly mentioned the importance of guanxi in China business (Tung 1982a and 1982b, Redding 1993, Hofstede and Bond 1988, Brunner et al 1989, Wong 1998). However, these scholars do not have consensus on the ethical aspect of guanxi. To some commentators, guanxi is ethical (Brunner et al 1989, Buttery and Wong 1999). It generates trust and dependence between negotiators so that they can have mutual understanding to facilitate exchange of favor and product adaptation. As such, guanxi is established on mutual benefits and each negotiating party's bargaining powers is equal. However, these findings contradict with existing surveys on business ethics in China. A survey conducted by the Hong Kong Independent Commission Against Corruption (ICAC) suggested that Hong Kong negotiators used 3 to 5% of their operating costs to cultivate guanxi in China (anonymous author, *Oriental Daily News*, 25/7/93). Hui and Graen (1997) also note that traditional guanxi ethics has been weakening ever since the People's Republic of China (PRC) was established 50 years ago. The inconsistency of results in guanxi research poses challenge to researchers to identify the current guanxi status in China.

## **OBJECTIVES**

This paper attempts to tackle the ethical issue of guanxi in China. Specifically, the paper will investigate the dimensions of guanxi as perceived by Hong Kong business negotiators. It aims at indicating the potential danger in using guanxi as the only strategic tool in business negotiation and attempts to capture different guanxi approach used by Hong Kong business negotiators. Especially, the relationship between guanxi and favour is investigated because their relationship has not been empirically tested. Recommendation will also be made to help foreign negotiators to handle the ethical aspects of guanxi in the PRC.

## **GUANXI LITERATURE REVIEW**

The term *guanxi* is generally translated into "special relationships" or "connections" (Davies et al 1995). It is developed with ingenuity, creativity, supplementing by

flexibility (Leung and Yeung 1995). The concept of "guanxi" is tacitly embedded within the Confucius philosophy and it subtly defines the Chinese moral code (Fock and Woo 1998). The Confucius social hierarchical theory i.e. the five relationships emperor-subject, father-son, husband-wife, brother-brother and friend-friend (pronounced as *wu-lun* in Chinese) perpetuates its influence in modern China (Yau 1994, King 1993, Buttery and Leung 1998). The word "*lun*" is actually a concise description of the *guanxi* among these five relationships (Buttery and Leung 1998). An individual will fall into a natural *guanxi* web in his/her socialization process after he/she is born. If every individual submerges in his/her proper position, social harmonization can be achieved in the vast Chinese continent. This social hierarchical theory has prompted almost all Chinese rulers adopted Confucianism as a strategic tool to achieve social stability in the vast Chinese continent (Man and Cheng 1996).

The development of a *guanxi* web depends upon whether some attributes or a *guanxi* base e.g. clanships, friendships, school mates, teachers and students exist among individuals (Nakane 1970, Brunner et al 1989, Tsang 1998). The extent of *guanxi* cultivation among individuals depends upon their positioning within a frame that is based on some social unit classifications. The social units may be family, work units and social network. The more attributes he/she has, the more capable he/she can establish *guanxi* within the social units he/she belongs to provided that he/she has the time, money, and efforts to navigate through this *guanxi* web (King 1993). In the process of cultivating *guanxi*, gifts are normally used (Brunner et al 1989). Gift giving and wine-and-dine are the means to establish and maintain *guanxi*, but the activities are not equivalent to corruption. Outright bribery may be good enough to get a business transaction done on a one-off basis, but it cannot produce interpersonal attraction which is defined as emotional relationship (pronounced as *ganqing* in Chinese term) (Simons et al 1970, Tsang 1998). One of the major purposes is to generate *ganqing* and become an insider of a group (a person belonging to the same group); then all deals become

easy.

Some authors suggest that guanxi is a form of relationship marketing in China (Wong 1998 Wong and Leung 2001). However, there are at least two differences between guanxi and relationship marketing. First, relationship marketing refers to a particular way of doing business that includes not only the relationships (the domain of guanxi), but also how the business is defined from a service perspective, and the management of the service delivery process (Arias 1996, Gronroos 1996, Low 1999). In this sense, relationship marketing has a broader perspective; it harmonizes the activities between the value chains of two partnering firms and advocates the establishment of an enduring long-term relationship between the customers and the new business entities created by these two firms. Second, guanxi implies personal relationship among individuals and relationship marketing is a marketing philosophy operating at organizational level. As such, guanxi between the two firms will disappear once the key guanxi persons leave the two companies whilst the relationship marketing philosophy remains even if the guanxi persons resign from these two companies. Because of these characteristics, purely relying on guanxi to establish a long-term business relationship may be risky.

Evidence shows that whilst established guanxi can provide foreign firms with competitive advantage in negotiating within the complex human network in China, it cannot eliminate threats and competition (Fock and Woo 1998). Guanxi may even become worthless or turn into a liability once the partner loses power. For example, the former party secretary of Beijing City Chen Xitong was convicted of corruption charges in 1995. As a result, any individual or company that has excellent guanxi with Chen and his associates lost their investments (Tsang 1998). Moreover, guanxi can be positive as well as negative.

Besides the conceptual confusion between guanxi and relationship marketing in the literature, confusion also exists in the recognition of guanxi underlying dimensions. Buttery and Wong (1999) perceive that guanxi has four constructs: favor, trust, dependence and adaptation. However, the import/export environment of this study put forward some fundamental argument. Importers and exporters must have these four characteristics to fulfill the legal aspects such as compliance to terms stipulated on the

letter of credit. Once the exporter obtains order and letter of credit from the importer, the exporter's ability of adapting to the importer's continuous request on product amendment depreciates because exporter needs to commit to rigorous downstream production requirements (Leung and Li 1997). Guanxi between importers and exporters, in this sense, may be short-term; whilst guanxi, according to various authorities is established on a long-term base (Tung 1982a and 1982b, Redding 1993, Hofstede and Bond 1988, Brunner et al 1989).

The above arguments suggest that the traditional Confucius concept and modern practice of guanxi have some drastic differences. The traditional Confucius guanxi concept advocates a set of moral codes that can be manipulated by Chinese political leaders to regulate the Chinese people to achieve the ideal social harmonization whereas the modern practice of guanxi treats it as a strategic tool to achieve business goals. The author of this paper argues that existing guanxi commentators are too ambitious to include both the moral and practical aspects in their discussions and miss out the sensitive issues of foreign business negotiators' perceptions on the moral status of guanxi in China. Can guanxi be that moral and still be practical at the same time? Man and Cheng's (1996) study on guanxi provide some hints. They recognise that the practise of guanxi by Chinese people is situational specific. For example, the guanxi in a brother to brother situation is different from that of a business to business situation. They have classified guanxi into three major categories in their book "the Chinese guanxiology": 1) guanxiology of emperor and subject, 2) guanxiology of government and people, and 3) guanxiology of business and business. The first guanxi category concerns about how the Chinese emperors manipulate the guanxi between them and their subjects to achieve success to rule the country. The second category deals with the guanxi establishment between the government and its people. The last category involves in identifying the complex guanxi issues in a business to business environment.

They have built individual inventories describing guanxi based on traditional Chinese slang for individual categories. This survey attempts to use this business-to-business inventory to identify the perceptions of current business guanxi dimensions in Sino-Hong Kong negotiation environment. It also attempts to capture different guanxi approach used by Hong Kong business negotiators and their concepts of guanxi and favour because the relationship has not been empirically tested (Wong 1997).

## **RESEARCH METHODOLOGY**

This study used the inventory that is contained in Man and Cheng's (1996) "business to business guanxiology" section as a basis to develop a questionnaire or survey instrument. The inventory consists of Chinese slang that describes the complicated guanxi concepts in the Chinese business community. The questionnaire was originally constructed in Chinese language. Statements were firstly translated to English and they were back translated to Chinese by a bi-cultural marketing professor. Inconsistency between the Chinese and English version questionnaire was clarified and both versions are identical in contents. In order to explore the ethical aspect, a section contains statements concerning the Hong Kong negotiators' perceptions on "giving favor" is included.

We used the Chinese version questionnaire for this survey and used the English version for reporting in this article. 5 in-depth interviews were carried out with Hong Kong business negotiators to add depth to the questionnaire. The Chinese version questionnaire was pre-tested with 10 business negotiators in Hong Kong which help further clarification on wordings of the statements in the questionnaires before the actual fieldwork was conducted in February 1999. English statements appear in this article were modified accordingly.

We used a CD-Rom produced by the Hong Kong Chinese General Chamber of Commerce that contains all company data involved in direct foreign investment (DFI) in China and we sent questionnaires to the chief negotiators within these firms. The chief negotiators are of Chinese ethnic origins. This research frame allowed us to have

deeper understanding on the concept of guanxi because the Sino-Hong Kong negotiators have similar ethnic and cultural background.

We assigned a number to each company on the CD-Rom list and we chose companies according to a random table. We contacted the targeted respondents by telephone before sending questionnaires and called them two weeks later to remind them of this survey. At the end of May 1999, 164 completed questionnaires were received after 700 questionnaires were dispatched. The 23% response rate was comparatively lower than surveys in North America. However, it is considered satisfactory because Hong Kong executives are under pressure to work for long hour and are not normally responsive to survey that has no commercial value from their perspectives (Stuart 1993, Yam et al 1992).

## **FINDINGS**

59 respondents (36%) were trading firms; 54 (33%) were manufacturing firms; 48 (29%) were operating in service industries and only 3 (3%) came from other industries. The respondent firms were evenly distributed among small (50, 30.5%), medium (57, 34.8%) and large firm (57, 34.8%).

### **The perception of guanxi in a business negotiation context**

Based on factor analysis of 17 statements in section A of the questionnaire, we identified 4 underlying factors. Items of factor 1 are related to the respondents' perceptions on market behavior and they reflect their attitude in seeking market opportunity. Therefore, this factor is labeled as 'opportunism'. Items related to factor 2 mainly reflect the respondents' dynamic to establish relationship with others and therefore this factor is labeled as 'dynamism'. Items related to factor 3 mainly describe the business contact behavior and therefore it is labeled as 'business interaction'. Items in factor 4 are related to the respondents' perceptions on how to protect themselves in the Chinese market and therefore it is labeled as 'protectionism'. The results are presented in Table 1 below.

**Table 1 – Factor Analysis of the guanxi items**

Item	Loading
Factor 1: Opportunism ( $\alpha = 0.8228$ , variance explained: 24.73%)	
A4. Nine out of ten business are traitors.	0.870
A5. All businessmen are wily, or otherwise they are not doing business.	0.872
A6. To bargain and to haggle.	0.742
A7. Money can work miracles.	0.650
A9. A great man knows how to ride the tide of his time.	0.569
Factor 2: Dynamism ( $\alpha = 0.7436$ , variance explained: 15.75%)	
A14. Providing convenience for others also means giving convenience to you.	0.741
A8. It may be comfortable to meet one another in the future if there is a common thread between them.	0.741
A1. Amiability attracts riches.	0.674
A10. Use courtesy first and weapon later.	0.619
A2. Although we cannot do business together, kindness and justice should always be kept between us.	0.587
A15. Even obtain little grace, return with double.	0.585
Factor 3: Business interaction ( $\alpha = 0.6311$ , variance explained: 9.76%)	
A3. Accounts between blood brothers must be clear.	0.738
A11. Expensive gift can be given because of human sympathy but discount will not be offered for doing business.	0.593
Factor 4: Protectionism ( $\alpha = 0.6130$ , variance explained: 8.77%)	
A13. I will not attack the people who do not attack me, but I will attack	0.756
A12. Do thousand types of different businesses except those that will lose money.	0.755
A17. You can get rich when you get close with officials, and you can get food when you get close to the chefs.	0.631

Analysis on table one suggests respondents understood that guanxi can provide them business dynamics (factor 2- dynamism). All statements especially A15 and A14 suggest that "reciprocity" is the real dynamic behind the practice of guanxi. Also respondents tended to maintain a thread with others for future business development. Factor 1 (opportunism) suggests that respondents rely on guanxi to look for business

opportunity in China. This business opportunity is based on whether the respondents know how to negotiate through the bureaucratic system (statements A5 and A9) and they believe that money can generate miracle (A7). Although the respondents recognize that guanxi can provide them with business dynamic and opportunity, they seem to realize that these two advantages come with potential danger of losing their investments in China. Therefore, they take some precautionary measure to protect themselves (factor 4: protectionism). These actions include close association with high ranking officials (A17) and taking a clear cut approach in "business interaction" (factor 3) that may include clean accounting practice in business transactions with their Chinese counterparts. The potential reason may be due to their in-depth understanding of consequence of practicing unethical guanxi. As mentioned in the literature review, a lot of investors lost their investments when the former party secretary of Beijing City Chen Xitong was convicted of corruption charges in 1995.

### **Different guanxi approach**

One possibility to analyze whether different guanxi approach are being employed by Hong Kong negotiators is to investigate whether respondents can be classified into number of distinct guanxi groups based on respondents' perception on the four factors mentioned above (Dess and Davies 1984, Kim and Lim 1988). If distinct guanxi groups can be identified, comparisons between their perceptions on other Chinese relational element such as "giving favor" to their Chinese counterparts can be made to see if one guanxi group is different from the other groups. Since factor scores and summated scales have their own advantages and disadvantages (Hair et al 1995), cluster analysis was performed on both to examine whether there was any significant different between the two solutions. Because it is always arduous to decide how many clusters are appropriate (Saunders, 1980), a three cluster solution was initially run; a two-cluster and a four-cluster solution were subsequently performed to help determine the optimal number of clusters (Hooley et al 1992).

The cluster solutions generated were checked by commonly suggested methods such as ANOVA and Scheffe's test (Hair et al 1995). The validation result shows that the three-cluster solution was found to outperform the other solutions. Table 2 below summarizes the results of the validation tests. Since the two cluster solutions derived

respectively from factor and summated scores are similar, Table 2 only shows the solution based on summated scales for ease of interpretation (Hair et al 1995).

Guanxi factors	Cluster 1 (Preserver) N=38	Cluster 2 (Wiser) N=65	Cluster 3 (Braver) N=61	F value <sup>a</sup>
Factor 1- Opportunism	3.36 <sup>b</sup>	2.35	2.28	30.250 <sup>c</sup>
Factor 2- Dynamism	2.29	2.27	1.98	30.142
Factor 3- Business Interaction	3.01	2.27	1.70	48.715
Factor 4- Protectionism	3.38	2.06	3.17	86.054

<sup>a</sup> F-value derived from one-way ANOVA test between the three clusters. Although it is not shown in the table, the follow-up Scheffe's test also indicates a significant

difference in means factor 1 to 4 between all possible pairs of clusters at  $\alpha = 0.05$ .

<sup>b</sup> Mean summated scores with 1=strongly agree and 5=strongly disagree

<sup>c</sup> Significant at  $\alpha = 0.05$ .

The three derived clusters are labeled as the *preserver*, the *wiser* and the *braver* respectively. The nomenclatures were given according to each cluster's summated scores in factor 1 (opportunism), factor 2 (Dynamism), factor 3 (Business interaction), and factor 4 (Protectionism). For instance, when examining the scores of cluster 1, the scores of opportunism (3.36) and protectionism (3.38) were considerably higher than the other two scores, i.e. dynamism (2.29) and business interaction (3.01). Also, the dynamism score (2.29) is much lower than the mid-value of 3.0 on a 5-point scale. Finally, the protectionism score (3.01) is almost right situated on the mid-value. This guanxi practitioner group may have more than average dynamics in establishing guanxi with their Chinese counterparts in various activities but they may not put excess amount of effort in their business interaction with their Chinese counterparts. They are relatively inactive to seek business opportunity and intend to install some protection measure around themselves. Therefore, this group is labeled as *preserver*.

Guanxi practitioners in cluster 2 spend considerably effort in every guanxi factor, i.e. opportunism (2.35), dynamism (2.27), business interaction (2.27), and protectionism (2.06). These scores, however, indicate their efforts are not excessive because all scores fall into the slightly agree range on a 5-point scale. In short, this group of guanxi practitioners put more than average efforts in seeking opportunity, activating dynamics, and facilitating business interaction but they also put reasonable effort in protecting themselves in the complicated guanxi scenario. Hence, they are labeled as *wiser*.

Guanxi practitioners in cluster 3 have more courage than the other two clusters because they strongly agreed (on a 5-point scale) that they should spend effort in activating the dynamics (1.98) and establishing business interaction (1.70) in their business encounters in the Chinese market. They also slightly agreed that looking for business opportunities (2.28) in the Chinese market is important. However, they are relatively innocent in protecting themselves (3.17) when compared to the two other two clusters in the Chinese market. This group of guanxi practitioner, therefore, is labeled as *braver* because they closely follow company instructions in developing their guanxi network in China and hence their developing company business without knowing the potential danger of over-emphasizing on using their guanxi network in the Chinese market.

### **Relationship among guanxi, favor and ethics**

Table 3 shows the means and standard deviations of the Sino-Hong Kong negotiators' perceptions on the statements that measure the activities of 'giving favor' to their Chinese counterparts. Reliability test ( $\alpha = 0.7532$ ) showed that these statements measure the same concept. The mean scores of the three clusters are also included.

By using the summated score of eight favor statements as a dependent variable and the summated scores of the four factors i.e. opportunism, dynamism, business interaction and protectionism as independent variables, a multiple regression analysis was performed. Interestingly, the result shows that all independent variables do not have significant influence on the independent variable at  $\alpha = 0.05$  level. As such, Wong's (1997) hypothesis of a direct relationship between guanxi and favor can be rejected. This is further confirmed by looking at partial regression plot of all independent variables with the dependent variable. A potential explanation is that all the

respondents have their own specific company guidelines such as resource utilization to follow when interacting with their Chinese counterparts. Therefore, they will not give favor to their Chinese counterparts without their company consensus. In addition to company guidelines, the differences in legal systems (Leung 1998) between China and western countries also imply that the Hong Kong negotiators must handle the “favor” issues very carefully. In saying that, the respondents may spend time and resources to establish their guanxi with their Chinese counterparts so as to bring the two parties together but they will not give away their resources to facilitate business just because they have good guanxi with their Chinese counterparts.

Table 3

	1=strongly disagree	5=strongly agree	Mean*	S.D.	Guanxi cluster groups****		
					Preserver (N=38)	Wiser (N=65)	Braver (N=61)
B1. You spend extra time on following your partner's project.			3.01	1.29	2.76	3.23	2.93
B2. You would spend extra time on carrying out social activities with your partner.			3.40**	1.26	3.39	3.23	3.59
B3. You would give extra help to solve your partner's problem.			2.79***	1.32	2.68	2.75	2.90
B4. You would give extra high quality of services or product to your partner.			3.09	1.24	3.11	3.09	3.09
B5. You would offer extra high quality of services or product to your partner.			3.16	1.09	3.00	3.23	3.18
B6. You would offer extra discount price to your partner.			2.98	1.30	3.24	2.88	2.93
B7. You would offer extra help to fit with partner's need.			2.95	1.39	3.00	2.98	2.89
B8. You would offer extra knowledge and skills to your partner.			3.34**	1.28	3.18	3.32	3.46

\* reliability test shows the eight statements have a  $\alpha = 0.7532$ .

\*\* t test shows that the respondents tended to disagree with these statements at significant level  $\alpha = 0.05$ .

\*\*\* t test shows that the respondents tended to agree with this statements at significant

level  $\alpha = 0.05$ .

\*\*\*\* ANVOA test shows that the three groups are not significantly different at  $\alpha = 0.05$ .

By performing t-tests on the means of the 8 favor statements using 3 as a reference point, the respondents tended to agree that they would give extra help to solve their Chinese partners' problems (B3). They also tended to disagree that they should spend extra time on carrying out social activities (B2) and offer extra knowledge and skills to their Chinese partners (B8). The message is clear. The respondents would help their Chinese partners to solve their problems on personal ground if there is no extra company resource is concerned! ANVOA test also confirms that there is no significant difference at  $\alpha = 0.05$  level among the three groups of cluster, i.e. the preserver, the wiser and the braver.

Our survey reveals that the three clusters of Hong Kong business negotiators, regardless of their guanxi approach, do not display any difference in the concept of "giving favor" to their Chinese counterparts. This may be because all of them note the potential danger of "giving favor" to their Chinese counterparts deal to their relative innocence in political and legal knowledge in the mainland. Therefore, the authors, base on this survey, conclude that the guanxi practice by foreign negotiator is ethical in China. Nevertheless, there is some evidence suggests that the guanxi practice by Hong Kong negotiators is not as ethical as that in the mainland. For instance, one of the in-depth interviewees mentioned the way his company paid pocket money (or per diem in western term) to his company counterparts. He claimed: "it is illegal when we pay pocket money to our Chinese counterparts in the mainland. But when we pay pocket money to our Chinese counterparts in Hong Kong, they can't get us!" The evidence suggests that the guanxi ethical issue is illusive, it is situational specific and its handling is depended upon whether it is permitted within a legal framework. However, this debate should be solved in future research.

## **CONCLUSION**

This research suggests that guanxi can be used as a positioning strategy in the Chinese

market because four dimensions are embedded within it, i.e. opportunism, business interaction, dynamism, and protectionism. A foreign negotiator can manipulate these guanxi dimensions to position him/her as either preserver, wiser, or braver. Different guanxi positioning may result in different business interaction between foreign negotiators and their Chinese counterparts. The research also reveals that guanxi practice in Chinese is essentially ethical. But the ethical standard varies depending upon the legal framework within a specific location.

### **IMPLICATIONS TO FOREIGN BUSINESS**

This search reveals some implications for Sino-foreign negotiators. In Sino-foreign negotiation, foreign negotiators should manipulate the guanxi dimensions to position themselves as wiser. Cultural training should be given to foreign negotiators on the guanxi dimensions so that they know how to 1) interact with their Chinese counterparts, 2) create dynamic, 3) look for business opportunity, and 4) protect themselves in an unfamiliar cultural environment. It is important for the foreign negotiators to have this understanding to avoid their application of their own Self-reference criterion (Keegan 1995) on their Chinese counterparts. The understanding also helps reduce parochialism and ethnocentrism (Alder 1991) in a Sino-foreign negotiation environment. Clear company guidelines must be given so that the issues of “favor” are properly handled in a Chinese context.

### **FUTURE RESEARCH DIRECTION**

This is an exploratory research on the guanxi dimensions. More research has to be done in Chinese culture as a system. In saying that, other Chinese cultural elements, i.e. face, renqing, reciprocity and trust must be included in future Sino-foreign negotiation research. Also, the concept of favor may vary from one culture to another culture. Therefore, a comparison on “favoritism” across various cultures is anxiously required to add our understanding on Chinese culture.

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