

DO MANAGERIAL TIES IN CHINA ALWAYS PRODUCE VALUE? COMPETITION, UNCERTAINTY, AND DOMESTIC VS. FOREIGN FIRMS

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While most advocate that foreign firms should utilize managerial ties to conduct business in China, recent literature cautions that such ties may offer only conditional value. This study examines three sources of heterogeneity that may condition the value of ties: firm ownership (foreign vs. domestic), competition, and structural uncertainty. Results from a survey of 280 firms in China indicate that though foreign and domestic firms utilize ties at a similar level, their performance gains from tie utilization differ. Managerial ties have a monotonic, positive effect on performance for domestic firms, whereas the effect is curvilinear (i.e., inverted U-shaped) for foreign firms. Therefore, compared with domestic firms, foreign firms have a competitive disadvantage from tie utilization. Furthermore, managerial ties are less effective for fostering performance when competition becomes more intense. However, ties lead to higher levels of firm performance when structural uncertainty increases. Overall, these results support the contingency view of managerial ties and caution companies about the unconditional use of ties as the market becomes more heterogeneous. Copyright © 2008 John Wiley & Sons, Ltd.

INTRODUCTION

With a history of more than 5,000 years, ties are a deeply ingrained institution in China. Thus, it is not surprising that managerial ties, namely, top managers' boundary-spanning and interpersonal connections, provide a pervasive means to conduct commerce in China (Batjargal and Liu, 2004; Boisot and Child, 1996). For both domestic and foreign firms that seek to prosper in this huge market, cultivating ties with business leaders and government officials is critical, because who you know often is more important than what you know (Tsang, 1998; Xin and Pearce, 1996;

Yang, 1994). These connections help companies gain necessary resources, foster firm growth, and achieve superior performance. Empirical work also demonstrates that managerial ties increase performance for firms operating in China and other emerging economies (Batjargal, 2003; Peng and Luo, 2000). Unknown, however, is whether ties will always generate such returns and therefore remain so pervasive in China. Whereas some argue that this institution will always be an important form of coordination in the Chinese market (Boisot and Child, 1996; Yang, 1994), others beg to differ (Peng, 2003).

Related to this divergence in thought, recent developments in social network theory caution that ties are not always advantageous, that is, the effectiveness of ties may be contingent on important contextual factors. For example, while some argue that ties are an important source of competitive advantage in China, especially for foreign firms

Keywords: managerial ties; guanxi; liability of foreignness; competitive intensity; uncertainty; China

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(Tsang, 1998), foreign firms may be less likely to realize these advantages to the same extent that domestic firms can. That is, a liability of foreignness, the additional costs of a firm operating in an overseas market that a local firm would not incur (Zaheer, 1995), may exist since foreign firms are unfamiliar with the prevailing social and political institutions that coordinate business transactions, and may also receive differential treatment (Dunning, 1993). The scant empirical work confirms a competitive disadvantage: foreign firms operating in financial services have a lower chance of survival (Zaheer, 1995; Zaheer and Mosakowski, 1997) and lower profitability (Miller and Parkhe, 2002). Extending this literature, we suspect that the value created from tie utilization may differ for foreign and domestic firms—thus utilizing political and managerial ties, a common absorption strategy for foreign firms, may not fully overcome a liability of foreignness.

Our review of the literature also reveals a second contingency that may alter the value of ties: market forces. As emerging markets in China become more heterogeneous, two market forces, competition intensity and structural uncertainty, likely influence business decisions and outcomes (Luo, 2003). Unanswered, however, is whether these market changes imply that ties will *NOT* always matter. The market efficiency logic posits that ties become necessarily less efficient as market forces begin to influence business decisions and outcomes (Davies and Walters, 2004; Guthrie, 1998). Peng (2003: 276, *italics added*) argues for example, ‘as emerging economies become more *competitive*, networks and connections, previously thought to be imperative for business success, no longer seem as important as before.’ Yet, a social capital perspective posits that when market uncertainty and competition exist in an emerging economy, ties become more desirable because they enable a firm’s positioning through favored relationships with others in the value chain or through favorable government protections (Luo, 2003; see also Boisot and Child, 1996; Podolny, 1994).

Despite these significant controversies, no studies have assessed such conditional arguments. To fill these research gaps, we examine three untested contingencies: domestic vs. foreign firms, competitive intensity, and uncertainty. First, we extend current theory by arguing that while foreign firms tend to use ties at a similar level as domestic firms, the values created through ties differ. Domestic

firms can realize a monotonic benefit from the use of managerial ties; but for foreign firms, the positive effect of managerial ties will decline after reaching a threshold. That is, foreign firms can achieve a maximum benefit from a moderate level of tie utilization. Second, we examine alternative perspectives based on social capital and market efficiency logics to assess whether the effects of ties on performance depend on two dimensions of market-based economies—competitive intensity and uncertainty (Porter, 1985; Zhou, Yim, Tse, 2005). Thus, our study informs the debate on the value of ties in China as markets become more heterogeneous in terms of competition and uncertainty.

As an emerging economy, China offers an important yet idiosyncratic setting to examine the conditional value of ties. As the largest emerging market in the world, China shares many characteristics with other emerging economies, such as a rapid pace of economic development and policies that favor the adoption of a free-market system. Yet in emerging economies, the rules for market competition remain less predictable and less clear than in most Western economies, because the formal institutions that support free markets, such as effective legal infrastructure, are still evolving (Hoskisson *et al.*, 2000). As a result, ties are prevalent in emerging economies, as the ‘institutional voids’ force managers to rely on personal ties and connections (e.g., *blat* in Russia, *compadre* in Latin America, and *guanxi* in China) to substitute for formal institutional support. At the same time, China possesses its own idiosyncrasies. During its reform, the Chinese government has maintained a central role in guiding the economic transition (Luo, 2005), whereas formerly planned economies in Central and Eastern Europe such as Czech, Hungary, Poland, and Russia decentralized political control and maintained few central policies (Hitt *et al.*, 2004). Further, China has a long tradition of using ties to coordinate transactions, which cause some to refer to ties as the ‘lifeblood’ of business conduct in Chinese society (Xin and Pearce, 1996). Boisot and Child (1996: 623) similarly suggest that what is unique about China’s economic order is not the presence of network ties, but ‘the depth and nature of its social embeddedness.’ The heavy influence of government and long tradition of tie utilization make it unclear whether foreign firms can use ties as effectively as domestic firms and whether the effectiveness of ties declines as

competition intensifies and uncertainty increases. Therefore, China serves as a rich context for testing our contingency logic.

A CONTINGENT VIEW OF MANAGERIAL TIES

Economic action is closely embedded in networks and ties of interpersonal relations (Uzzi, 1997). Managerial ties represent ‘executives’ boundary-spanning activities and their associated interactions with external entities’ (Geletkanycz and Hambrick, 1997: 654). In China, managers build ties not only with managers at other firms (i.e., *business ties*), but also with government officials (i.e., *political ties*) (Peng and Luo, 2000). According to social network theory, managers form networks and ties to obtain access to scarce resources and information and reduce uncertainty (Podolny and Page, 1998). Ultimately, ties should improve important economic outcomes such as firm performance, which empirical studies consistently show (Batjargal, 2003; Peng and Luo, 2000). However, though researchers and practitioners agree that ties matter, less examined is their contingent value (Gulati and Higgins, 2003). Recent developments in social network theory suggest that the value of ties in a given situation is contingent on firm- and market-level characteristics, yet studies addressing this approach are few (Baker and Faulkner, 2004). This gap motivates our assessment of firm ownership (domestic vs. foreign) and market forces as contingencies that provide a means to ‘tackle the harder and more interesting issues of how they [ties and networks] matter, under what circumstances, to what extent, and in what ways’ (Powell, 1996: 297).

Managerial ties: foreign vs. domestic firms

Well established in the international business literature are the challenges that foreign entrants face when adapting their systems to the ‘country-specific economic, legal, political, institutional and cultural differences’ of a host country’ (Dunning, 1993: 195). The complexity of the environment further challenges the adaptive process since firms cannot simply reduce potentially negative forces by codifying or acting directly on them (Boisot and Child, 1999). Rather, when information is not easily codified and predictable, foreign entrants

likely employ an ‘absorption strategy’ to mitigate the potential adverse effects of country-specific differences (Ring, Lenway, and Govekar, 1990: 146–147). Boisot and Child (1999: 248) argue that in China, foreign entrants should absorb the environment by engaging, and thus entering ‘into more intensive relationships (i.e., high relational complexity) with Chinese partners and other significant groups’ (see also Tsang, 1998; Xin and Pearce, 1996). Ties not only enable foreign firms to adapt their business systems to those used in China, but also enhance their legitimacy, in that ties enable foreign firms to be perceived as more ‘desirable, proper, or appropriate’ entities within the system of norms and beliefs that define business conduct in China (Suchman, 1995: 574). Thus, connections and the legitimacy they confer help foreign firms cope with the differences raised by operating in countries with different institutions.

Although developing connections with relevant parties in China is not easy (Boisot and Child, 1999), foreign firms appear to employ this strategy quite readily. Industry observations indicate that similar to their domestic counterparts, foreign firms use managerial ties extensively to obtain scarce resources, garner support from public authorities, and request permission to enter certain business sectors (*BusinessWeek*, 2006; Wang, 2004). For example, the chairman of a European insurance company flew to China 10 times in three years to network with government officials and business leaders in its (ultimately successful) quest to win a license to do business in China (Wang, 2004). Only after making substantial investments and commitments to build strong relationships and ties with Chinese government officials did Microsoft overcome its negative image and improve relations with the public and the media (Gao, 2006). Thus, it is common for foreign firms, similar to their domestic counterparts, to have high-ranking managers specifically responsible for developing ties with the Chinese government and other businesses. Because absorption represents a critical means to do business in China, we predict that foreign firms use ties at similar levels as do domestic firms.

Hypothesis 1a: Foreign firms and domestic firms exhibit a similar level of managerial tie utilization.

While previous work demonstrates the positive effects of ties on firm performance, it is unknown whether foreign firms are able to extract the same value from their use of ties as domestic firms do. Foreign firms operating in China tend to be more familiar with market-based, impersonal transactions and institutions than domestic firms (Boisot and Child, 1999); whereas domestic firms are more accustomed to coordinating exchanges through their connections and are more familiar with the host-country political process (Hillman, Keim, and Schuler, 2004). Consistent with prior studies, we argue that foreign firms can benefit from their use of ties, which provide them the knowledge to overcome the challenges of operating in a country with different institutions and practices. We extend this argument however, that while the effect of tie utilization is monotonic and positive for domestic firms, for foreign firms the positive slope of tie utilization declines after a certain point and therefore reveals an inverted U-shaped relationship between tie utilization and performance. We provide a three-part rationale for this claim.

First, since the mid-1990s, regulatory policies in China have shifted dramatically, enabling local and national governments to interfere and intervene more readily in foreign businesses. For example, policies have shifted from 'entry intervention to operational interference ... from overt control to covert intervention' and from centrally determined to both centrally and locally determined (Luo, 2005: 295–296). These shifts make it easier for government officials to intervene in foreign businesses and potentially limit their opportunities and returns, because ultimately the Chinese government desires globally competitive *Chinese* firms (Nolan, 2001). Thus, domestic rather than foreign firms are more likely to gain benefits or favors from strong political ties. For instance, whereas domestic firms likely can extract favorable terms, protections, opportunities, and resources from their use of ties, foreign firms may encounter adversarial or challenging relationships with host-country governments after a certain point because the two parties have differing objectives. Foreign firms aim for growth and profitability while the Chinese government seeks accelerated learning of advanced technological know-how and management skills through foreign investment. Conflict therefore arises over how

to share the opportunities and economic rents generated by the foreign entrant (Dunning, 1998), and such conflict diminishes the returns from tie utilization.

Second, as cultural differences increase, firm performance may decrease due to greater levels of conflict when implementing strategic decisions (Tihanyi, Griffith, and Russell, 2005). Extending this logic, we suspect that cultural differences between foreign firms and the host country may lower the quality derived from ties after a certain point. In particular, the Chinese favor a clan culture, which honors consensus, tradition, trust, commitment, and long-term orientation; foreign firms tend to be more market oriented and competitive, which drives a short-term, results-oriented culture (Ralston *et al.*, 2006). Because of their short-term orientation, foreign firms have different time expectations than their Chinese counterparts. For example, foreign firms tend to demand a short-term payback for a favor, whereas domestic firms have a much longer time horizon for reciprocation (Yang, 1994). Foreign firms also have no qualms about disagreeing publicly and disrupting harmony, whereas domestic firms value relationship harmony and favor trust in the long term. These short-term orientations and open disagreements likely erode the quality of tie utilization and, thus, its presumed value for foreign firms. In contrast, their long-term orientation enables domestic firms to enjoy the benefits of operating in high-quality networks associated with deeper connections and enduring partnerships.

Third, tie utilization represents a divergent orientation compared with the market-based strategies that foreign firms generally employ (Peng, 2003). Foreign firms are typically characterized by organizational processes and routines that maximize the efficiency and implementation of market-based strategies. The use of ties, however, requires a different mindset that is incompatible with the entrenched, efficiency-based routines of foreign firms (Li, 2005). Thus, even if foreign firms rely heavily on ties, they may not be able to effectively use the information they obtain from it. Because of this organizational incompatibility, foreign firms are likely to realize diminishing returns from their utilization of ties.

In summary, these arguments suggest that ties are differentially effective for foreign and domestic firms: their benefits are initially positive, but then

decrease after a certain threshold for foreign firms, while remaining positive for domestic firms.

Hypothesis 1b: For domestic firms, managerial tie utilization has a positive effect on firm performance.

Hypothesis 1c: For foreign firms, managerial tie utilization has an inverted U-shaped relationship with firm performance, such that the positive effect decreases after a threshold level.

The moderating role of competition and uncertainty

China has been experiencing massive and complex changes in its institutions, including political, economic, and enterprise ownership structures, during its economic reform (Hoskisson *et al.*, 2000). These institutional changes have weakened the constraints of the old economic systems and led to the extensive structural transformations of many industries, namely, greater structural uncertainty. Competition has also intensified in many markets as private enterprises proliferate and the number of enterprises drastically increases (Zhou *et al.*, 2005). Yet the potential influence of these market forces is blurred by the continued role of government in regulating business and the economy through its interference and constraints, as well as favorable protections and support for certain firms.

To address the controversy regarding the role of ties as Chinese markets become more heterogeneous, we focus on whether competitive intensity and uncertainty alter the effectiveness of using ties to conduct business. The market efficiency logic implies ties burden efficiency rather than improve it as more marketized mechanisms, such as sales and profit, determine firm survival (Davies and Walters, 2004). Others, however, counter that ties are becoming more salient during the transition. Boisot and Child (1996: 619), for example, argue that China is 'moving not toward a market order, as it claims, but toward a form that can be labeled network capitalism.' Based on her in-depth interviews with managers, Yang (1994) similarly suggests that the practice of personal ties is becoming more important and prevalent and has increased at an accelerated rate. More recently, Luo (2003) finds that firms in China are more likely to *utilize* managerial ties as uncertainty and competition

increases and as regulation becomes more stringent. No empirical work, to our knowledge, has examined this debate.

Competitive intensity refers to the degree of competition that a firm faces in its industry. Increased intensity often is characterized by greater rivalry among incumbents, which can take the form of price wars, more advertising or product offerings, added services, and increased transactions (Porter, 1985). In less competitive markets, managerial ties are valuable because they facilitate access to key resources, information not widely held, protection, and favors. In addition, because firms have more flexibility in pricing their services and products, they face softer budget constraints and possess greater ability to manage the high costs of tie utilization.

In contrast, as competition intensifies, firms face more constraints in their pricing such that inefficiencies in business practices or operations lower firm performance. According to social network theory, the value of ties stems from their provision of information to which others lack access. As the number of firms in a market increase, information transferred through ties likely becomes redundant, which decreases the information benefits of access, timing, and referrals brokered through ties (Burt, 1997). Further, one benefit of ties is to exchange or broker information in order to minimize multiple prices. Multiple prices are undesirable because if un-coordinated, a firm may price too low, constraining its profit potential (Burt, 1997). Yet, in competitive markets, price is more transparent and efficiently regulated through market competition, which makes this use of managerial ties redundant.

Managerial ties may also be less effective for coordinating the larger scale and scope of transactions in more competitive markets. While ties thrive in small, regional markets (Uzzi, 1997), as markets grow in scale and scope, information processing and enforcement likely become more difficult to coordinate and sanction through ties (Peng 2003). For example, distance makes it harder for parties to communicate effectively and to monitor performance, decreasing the efficiency of ties. Related, a firm may find it harder to observe deviations when managing a larger number of transactions through ties. These limitations increase the likelihood of exploitation and abuse of trust-based relationships, as well as increase the costs of using ties. Consistent with this, Guthrie's

(1998) interviews with Chinese managers indicate that they perceive a declining importance of managerial ties due to increasing competition and greater enforcement of rules. Contrary to the above logic, Luo (2003) argues that firms are more likely to benefit from ties when competition intensifies because these firms can extract more favorable terms or favors than others—in effect they can use the ties to buffer themselves from competitive forces. Our hypothesis however is consistent with the market efficiency logic. Therefore,

Hypothesis 2a: The effect of managerial tie utilization on firm performance is weaker when competitive intensity is high rather than low.

Uncertainty also challenges managers by making it difficult for them to predict the future. We focus on *structural uncertainty*, the extent to which the industry environment is volatile and fast changing, because it creates greater uncertainty about the actions of other economic actors, such as customers, competitors, suppliers, and regulators (Sutcliffe and Zaheer, 1998). Our review of the literature reveals two alternative stances regarding whether uncertainty enhances or hinders the effect of tie utilization on firm performance. A social capital perspective posits that ties are valuable because they grant access to trusted information in China, in which ties traditionally operate as a conduit for information that has not been codified or placed in the public domain (Boisot and Child, 1996). Because ties are embedded in a social context of obligation and trust, this information is deemed trustworthy, especially compared with information from new acquaintances or strangers (Baker and Faulkner, 2004; Uzzi, 1997). Thus, networks enable access to information from reputable sources that those without ties cannot access. Keister (2001) further indicates that the primary reason Chinese managers prefer to transact with parties within their business groups is to gain the benefits of trust.

As uncertainty increases, ties become a natural mechanism to pursue greater levels of information, such as business intelligence that is not widely known, likely changes in government regulations and political favors, and the access to scarce resources, thereby diminishing uncertainty or its adverse effects (Boisot and Child, 1996; Luo,

2003; Podolny, 1994). The trust inherent in these ties enables the parties to feel more confident in their planning and act as if the future is more certain (Zajac and Olsen, 1993). Moreover, tight connections speed up requests for information, tips, or news, and thus facilitate adaptation, given external uncertainty (Kiong and Kee, 1998). Managers also may seek to utilize their ties because if they band together as a collective group, firms can potentially guard against or control the uncertain effects, thereby increasing firm performance. In sum, since ties provide better information about customers' needs and local market conditions, by accessing these ties managers may be able to create better plans to respond to the uncertainty, resulting in greater firm performance. Consistent with this social capital view,

Hypothesis 2b: The effect of managerial tie utilization on firm performance is stronger when structural uncertainty is high rather than low.

Alternatively, the market efficiency perspective suggests that when firms face uncertainty, they require flexibility to search freely and respond quickly to external changes. Because optimal search requires broad access to different sources of information, firms linked tightly to other entities may be less adaptive and constrained in their information searches to solely information in the established network (Weick, 1976). Deviating from this pattern of utilization is difficult because norms, such as social obligations and commitment among network members, leads to network inertia, such that members remain with existing network relations and trade with 'old friends' rather than strangers (DiMaggio and Louch, 1998; Kiong and Kee, 1998). As a result, network ties create social obligations between parties that preclude the firm from searching for new information and exploiting new opportunities outside its current relations (Ahuja, 2000). Partners may become trapped by these relationships and vulnerable to sudden shifts in market demand (Mitchell and Singh, 1996). Thus, an extensive use of ties in times of uncertainty may lead to less effective adaptation and result in poor performance.

Hypothesis 2b_{alt}: The effect of managerial tie utilization on firm performance is weaker when uncertainty is high rather than low.

METHOD

Sampling and data collection

To test the hypotheses, we examine firms in manufacturing sectors located in three major Chinese cities (Beijing, Guangzhou, and Shanghai). These three areas represent the fastest-growing regions during China's transition to a market economy (Zhou, Tse, and, Li 2006), and thus provide an appropriate setting for testing the effectiveness of ties in a more competitive market. Hoskisson *et al.* (2000) suggest that in emerging economies, collaboration with local researchers provides a key means to obtain reliable and valid information, and face-to-face interviews generate more valid information. Therefore, we collaborate with local researchers to conduct the survey using on-site, personal interviews.

An English-language version of the questionnaire was prepared first, then translated into Chinese by two researchers of this project who are competent in both languages. To ensure conceptual equivalence, the Chinese version was back-translated into English by two independent translators. Any conflicts were discussed by the researchers and translators until they reached agreement (see Hoskisson *et al.*, 2000). To ensure the content and face validity of the measures, two researchers conducted five in-depth interviews with senior marketing managers in Chinese (i.e., Mandarin), during which we asked them to check the relevance and completeness of the questionnaire items and took notes on their responses. On this basis, we revised a few questionnaire items to enhance their clarity, translated these revised items into English, and then back-translated them into Chinese to ensure their content validity.

Two researchers then conducted a pilot study in Chinese with 30 senior managers with titles such as CEO, vice president, senior marketing director, and general manager. We asked respondents to not only answer all the questionnaire items but also to provide feedback about their design and wording. To alleviate possible social desirability bias, we informed all respondents in advance of the academic purpose of the project, the confidentiality of their responses, and that their responses would be used only in aggregated analysis. The results of this pilot survey reveal that virtually all the items are understandable and prompt reasonably diverse ranges of responses. On the basis of the pilot test,

we further refined the questionnaire and finalized the survey. The revised items were again translated into English and back-translated into Chinese.

For the final survey, we selected a random sample of 1,000 companies from a list of manufacturing firms located in Beijing, Guangzhou, and Shanghai published in a business directory entitled *22,000 Businesses in the P.R. China*, which is maintained and updated regularly by China International Business Investigation Co. Ltd. These firms span diverse manufacturing industries, such as industrial and commercial machinery, electronic and other electrical equipment and components, chemicals and allied products, fabricated metal products, rubber and miscellaneous plastics products, apparel and other fabric products, furniture, etc. In each firm, we selected a local senior manager (e.g., CEO, vice president, senior marketing manager) as the key informant because foreign firms heavily rely on local managers for network building (Fryxell, Butler, and Choi, 2004; Ralston *et al.* 2006). Our field interviews also reveal that these managers are highly familiar with their firms' tie utilizations and orientations. The final survey was conducted in Chinese (i.e., Mandarin).

With the help of a national research firm, we assigned professional interviewers to contact senior managers and solicit their cooperation via telephone. The interviewers informed the managers of the academic purpose of the project and the confidentiality of their responses and promised them a summary report in return for their participation. From these contacts, 428 firms agreed to participate, and the interviewers then successfully surveyed 306 of them on-site. After eliminating 13 surveys with excessive missing data, we retain 293 complete responses, for a response rate of 29.3 percent (293 of 1,000 firms). According to a multivariate analysis of variance (MANOVA), we find no significant differences (Wilks' $\Lambda = 0.968$; $F = 0.426$; $p = 0.959$) between responding and nonresponding firms in terms of key firm characteristics (firm ownership, firm age, industry type, and profit), which suggests nonresponse bias is not a concern.

All interviewers had at least 10 hours of interview training and had conducted at least three similar projects previously. We also developed detailed instructions and provided a two-hour training session for the interviewers. The telephone conversations between the interviewers and senior managers were recorded by the company's monitoring

system. We also asked the interviewers to collect business cards of the senior managers to make sure that the interview was actually done. In addition to the monitoring mechanisms employed by the research firm, after the fieldwork one of the researchers randomly called 60 respondents to confirm that the interviews had been conducted and asked them to respond orally to 10 question items from the questionnaire. We discovered no evidence of cheating in the fieldwork, and the comparison between the telephone and fieldwork responses suggests no major differences.

To overcome possible common method bias, we collect information from different sources. Specifically, we obtain the measures of managerial tie utilization and a control variable (i.e., entrepreneurial orientation) from the key informant surveys, conducted in early 2003 in reference to the preceding three years (i.e., 2000–2002). We calculate competitive intensity and structural uncertainty on the basis of secondary data from the *China Statistical Yearbook* (2000–2002 editions). Data about firm ownership, firm performance, and the other control variables (i.e., firm age, size, and industry) come from archival data provided in the business directory. Following common practice in longitudinal survey studies (e.g., Rindfleisch and Moorman, 2003), in 2006 we collected information about firm performance (i.e., return on assets [ROA] in 2005) to test the causal link between managerial ties and performance. However, we could not obtain performance data for 13 companies in 2006, so our final effective sample consists of 280 firms. We conducted Harman's one-factor test with all the measurement items in a factor analysis and achieve a solution that accounts for 69.53 percent of the total variance; the first factor accounts for 25.6 percent. Because a dominant, single factor does not emerge, common method bias is unlikely to be a concern in our data (Podsakoff and Organ, 1986).

Because we measure managerial ties and entrepreneurial orientation perceptually, we conducted additional interviews for validation. In 2004, one researcher used the same questionnaire and conducted telephone interviews with 60 senior managers from 30 randomly selected firms that had participated in the 2003 survey (two managers from each firm). Among the 60 senior managers, 30 had responded to the prior survey, and the other 30 were new informants. The correlation

analysis of the 30 managers' responses in the two periods reveals strong consistencies in their responses (all $p < 0.001$), demonstrating the high reliability of the survey (Podsakoff and Organ, 1986). We also use the Spearman-Brown test of interclass correlation (ICC) to examine the interrater reliability between the two managers in the 30 firms (James, 1982) and achieve ICC(2) of 0.759, 0.835, and 0.763 for business ties, political ties, and entrepreneurial orientation, respectively, all of which are well above the 0.60 benchmark. These findings demonstrate the validity of our perceptual measures that use a key informant method.

Measures

We adapt the measures in the survey from established studies and measure all perceptual scales using a seven-point Likert scale (1 = strongly disagree; 7 = strongly agree). The measurement items and their validity assessment appear in the Appendix.

Managerial tie utilization. Network literature often uses name and position generators to measure social networks (Batjargal, 2003; Burt, 1997). However, it is difficult to employ these two approaches in this research context because in China network structures are deemed as business secrets, so managers are very protective of this sensitive information (Peng and Luo, 2000). Therefore, we follow Batjargal and Liu (2004) and Peng and Luo (2000) and use, in particular, Peng and Luo's perceptual measures of tie utilization: we treat managerial ties as a composite factor that consists of business and political ties. Business ties involve three items that assess top managers' use of ties with managers of other firms (i.e., buyers, suppliers, and competitors); political ties contains three items examining top managers' use of connections with political leaders at various levels of government, officials in industrial bureaus, and officials in regulatory and supporting organizations during the past three years.

We measure *structural uncertainty* by calculating the geometric average of the standard deviations in an industry's total output, sales, and profit, such that structural uncertainty = $[\text{Std}(\text{output}) \times \text{Std}(\text{sale}) \times \text{Std}(\text{profit})]^{1/3}$ (cf. Luo, 2003). The information about the structural attributes is obtained from the *China Statistical Yearbook*

(2000–2002 editions). We operationalize *competitive intensity* using the well-known Herfindahl index, a popular indicator of competitive intensity that captures the number and market share distribution of firms in an industry (Kotha and Nair, 1995), computed as the sum of the squared market share of each firm in the industry (i.e., $HHI = \sum \text{market share}_i^2$, where i = number of firms in the industry). We calculate the arithmetic average of Herfindahl indices over three years (2000–2002). More intensive competition implies that an industry has more firms with less market share and thus a smaller index. We use a negative Herfindahl index average in our analysis, such that a larger value reflects higher competitive intensity, to make the interpretation of the results more intuitive.

Firm performance entails a financial indicator: ROA in 2005. We obtain this information from archival data, as we do information about *firm ownership*. Because Sino–foreign joint ventures usually structure their operations and management in parallel with foreign partners, researchers tend to classify them together with wholly foreign-owned firms as foreign firms (Ralston *et al.*, 2006). Therefore, we code firm ownership as a dummy variable, such that 0 = domestic firms and 1 = foreign firms (including both wholly foreign-owned and international joint ventures).

Controls. We include firm size, firm age, and industry type as control variables. We measure *firm size* as the logarithm of the number of employees, *firm age* as the number of years of operation by the firm, and *industry type* as a dummy variable, where 1 = high-tech industry (e.g., computers, electronic equipment), and 0 = otherwise (e.g., apparel, furniture, food). Furthermore, because of

the fast-changing nature of the Chinese environment, entrepreneurial outlook represents an important characteristic of firms in China, so we control for *entrepreneurial orientation* and measure it with four items adapted from Matsuno, Mentzer, and Ozsomer (2002) that reflect a firm's proactiveness toward change and willingness to take risks.

Construct validity. Following Anderson and Gerbing (1988), we refine the perceptual measures and assess their construct validity by running a confirmatory factor analysis with structural equation modeling. The measurement model fits the data satisfactorily ($\chi^2(32) = 82.9$, $p < 0.01$; goodness-of-fit index [GFI] = 0.945, confirmatory fit index [CFI] = 0.940, incremental fit index [IFI] = 0.941; root mean squared error of approximation [RMSEA] = 0.07), and all factor loadings are highly significant ($p < 0.001$), which indicates the unidimensionality of the measures (Anderson and Gerbing, 1988). The composite reliabilities of all multi-item measures (ranging from 0.71 to 0.88) exceed the usual 0.70 benchmark. Thus, these measures demonstrate adequate convergent validity and reliability. We assess the discriminant validity of the latent constructs with chi-square difference tests. In a pairwise test, we compare a restricted model (correlation fixed to 1) with a freely estimated model (correlated estimated freely). The chi-square difference is highly significant (ties vs. entrepreneurial orientation, $\Delta\chi^2(1) = 66.7$, $p < 0.001$), in support of discriminant validity (Anderson and Gerbing, 1988). Taken together, these results show that the measures in this study possess adequate reliability and validity. In Table 1, we present the basic descriptive statistics and correlations of the measures.

Table 1. Means, standard deviations, and correlations

	Mean	s.d.	1	2	3	4	5	6	7	8	9
1. Ties	5.28	0.87	1.00								
2. Competitive intensity	−299.57	296.25	−0.01	1.00							
3. Structural uncertainty	2911.51	4164.90	−0.06	−0.20**	1.00						
4. Firm ownership	0.64	0.48	0.04	−0.08	−0.02	1.00					
5. Firm size	5.57	1.21	0.00	−0.11	0.08	−0.05	1.00				
6. Firm age	1.91	1.79	−0.02	−0.07	0.06	−0.30**	0.44**	1.00			
7. Industry type	0.46	0.50	−0.04	−0.21**	0.15*	0.03	0.02	−0.03	1.00		
8. Entrepreneurship	4.93	0.84	0.26**	−0.08	0.01	0.02	0.02	−0.07	0.01	1.00	
9. ROA	0.20	0.20	0.26**	−0.13*	0.02	−0.13*	−0.15*	0.01	0.04	0.23**	1.00

Note: Sample size = 280

** $p < 0.01$, * $p < 0.05$

ANALYSES AND RESULTS

We use correlations, t-tests, and MANOVA to test Hypothesis 1a and hierarchical moderated regression analysis to test the rest of the hypotheses. For the regression analysis, we split the sample into domestic and foreign firms. To mitigate the potential threat of multicollinearity, we mean-center all independent variables that constitute interaction terms and then create interaction terms by multiplying the relevant mean-centered variables (Aiken and West, 1991). The largest variance inflation factor, a multicollinearity indicator, is 3.28, well below the 10.0 cutoff, so multicollinearity is not a concern. To assess the explanatory power of each set of variables, we include the variables in the model block by block. In Table 2, we report the estimated effects on the ROA of domestic and foreign firms,¹ respectively.

Hypothesis 1a pertains to the degree of tie utilization. As Table 1 shows, firm ownership has no significant correlation with managerial ties

¹ We conduct additional subgroup analyses for joint ventures and wholly foreign-owned firms. The results show similar patterns for both types, so we combine them in the subsequent analysis.

($r = 0.04$, $p > 0.10$), which suggests foreign firms rely on ties (mean = 5.28) to the same extent as do local firms (mean = 5.26). We also break down overall managerial ties into two subdimensions: business and political. The t-test results reveal no difference in their use of either business ties ($m_{\text{foreign}} = 5.28$, $m_{\text{domestic}} = 5.26$, $t = 0.29$, $p = 0.77$) or political ties ($m_{\text{foreign}} = 5.28$, $m_{\text{domestic}} = 5.27$, $t = 0.11$, $p = 0.91$). We further test whether domestic, joint ventures, or wholly foreign-owned firms differ in their use of overall managerial, business, or political ties; the MANOVA results indicate that the three types of firms do not differ (Wilks' $\Lambda = 0.99$, $F = 0.37$, $p = 0.90$), at values of 5.26, 5.37, and 5.29 (ties overall); 5.25, 5.34, and 5.24 (business ties); and 5.27, 5.40, and 5.17 (political ties) for local firms, joint ventures, and wholly foreign-owned firms, respectively. These results fully support Hypothesis 1a.

For Hypothesis 1b, we predict the use of ties has a linear, positive relationship with firm performance for domestic firms. As we show in Table 2 (model 3), ties have a positive effect on domestic firms' ROA ($\beta = 0.30$, $p < 0.05$), but the effect of ties² is not significant ($\beta = -0.10$, $p > 0.10$),

Table 2. Standardized coefficient estimates: multiple moderated regressions

Variables	ROA					
	Domestic firms (n = 101)			Foreign firms (n = 179)		
	M1	M2	M3	M4	M5	M6
<i>Control variables</i>						
Firm size	-0.27*	-0.20*	-0.20*	-0.19*	-0.19*	-0.17*
Firm age	0.09	0.11	0.12	0.04	0.06	0.06
Industry type	0.03	0.09	0.04	0.05	0.10	0.10
Entrepreneurship	0.14	0.13	0.04	0.31**	0.32**	0.30**
<i>Direct effect</i>						
Competitive intensity (CI)		-0.25*	-0.15†		-0.15*	-0.13†
Structural uncertainty (SU)		-0.04	-0.03		-0.08	-0.06
H1b&c: Ties		0.27**	0.30**		0.26**	0.23**
Ties ²		-0.04	-0.10		-0.28**	-0.28**
<i>Interactions</i>						
H2a: Ties × CI			-0.27**			-0.14*
Ties ² × CI			-0.12			-0.07
H2b: Ties × SU			0.31**			0.20**
Ties ² × SU			0.06			-0.15*
R ²	0.05	0.13	0.28	0.12	0.24	0.30
Model F	1.16	1.93	2.76	5.96	6.64	5.71
df	4,96	8,92	12,88	4,174	8,170	12,166
p (ΔR^2)	>0.05	<0.05	<0.01	<0.01	<0.01	<0.01

** $p < 0.01$, * $p < .05$, † $p < 0.10$

in support of Hypothesis 1b. For Hypothesis 1c, we predict an inverted U-shaped relationship characterizes tie utilization and performance among foreign firms. As we show with model 6, managerial ties relate positively to ROA ($\beta = 0.23$, $p < 0.01$), but ties² negatively affects ROA ($\beta = -0.28$, $p < 0.01$). That is, a curvilinear (inverted U-shaped) relationship exists between ties and ROA for foreign firms, indicating the diminishing returns of high levels of tie utilization. Figure 1 further depicts these effects of ties (i.e., the sum of the effects of ties and ties²) on the ROA of domestic and foreign firms. Clearly, domestic firms can obtain a monotonic positive result from tie utilization, whereas foreign firms face a decline in the positive effect of managerial ties on performance after a certain level. These results fully support both Hypotheses 1b and 1c.

For Hypothesis 2a, we posit that ties become less effective as competition intensifies. Because we hypothesized a differential effect of ties for domestic and foreign firms in Hypothesis 1, we

continue to run the analysis for the two groups separately. Consistent with Hypothesis 2a, among domestic firms, the interaction between tie utilization and competitive intensity has a significant negative effect on ROA in model 3 ($\beta = -0.27$, $p < 0.01$). In the sample of foreign firms, the first-order interaction is negative and significant (model 6, ties \times CI: $\beta = -0.14$, $p < 0.05$), whereas the second-order interaction is not significant (model 6, ties² \times CI: $\beta = -0.07$, $p > 0.10$), in full support of Hypothesis 2a.

To gain more insight into these interaction effects, we follow Aiken and West (1991) and decompose the interaction terms. Specifically, we conduct simple slope tests and plot the relationships in Figure 2. In these tests, we split the competitive intensity variable into two groups—low (one standard deviation below the mean) and high (one standard deviation above the mean)—and estimate the effect of ties on ROA for both levels. As we show in Figure 2a, Part (1), for domestic

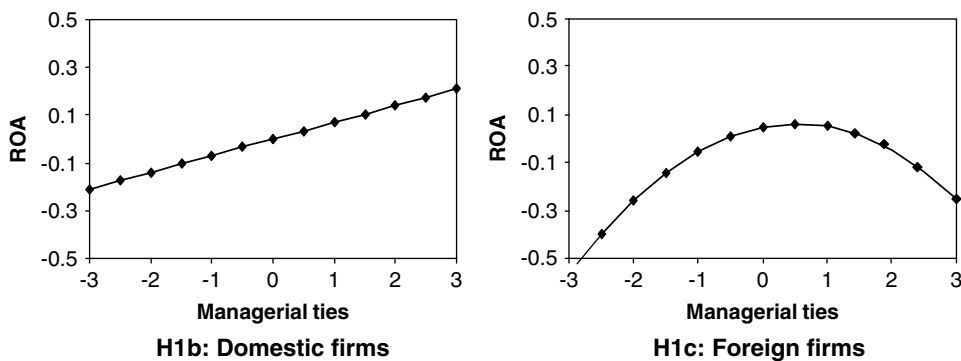


Figure 1. The effect of managerial ties on ROA (H1)

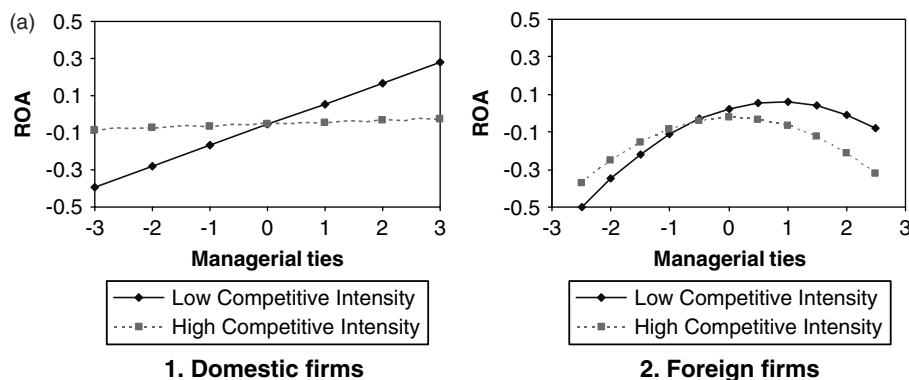


Figure 2a. The interaction of managerial ties and competitive intensity on ROA (H2a)

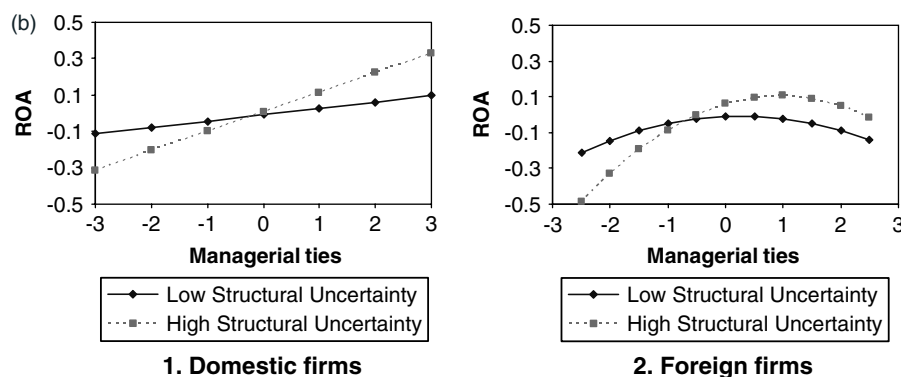


Figure 2b. The interaction of managerial ties and structural uncertainty on ROA (H2b)

firms, the effect of ties on ROA shifts from significantly positive when competition intensity is low (simple slope $b = 0.11$, $p < 0.01$) to insignificant when competition is high ($b = 0.01$, $p > 0.10$). Part (2) of Figure 2a indicates that at high levels of competition intensity, the performance gains from tie utilization decrease more rapidly. Together, these results suggest that managerial ties have a weaker effect when competition intensity is high than when it is low.

Hypotheses 2b and 2b_{alt} provide two competing predictions regarding the moderating role of structural uncertainty. The results show that the interaction terms between structural uncertainty and ties have a significant positive effect on ROA for domestic firms (model 3: $\beta = 0.31$, $p < 0.01$). For foreign firms, the first-order interaction is significant and positive (model 6, ties \times SU: $\beta = 0.20$, $p < 0.01$), whereas the second-order interaction is significant and negative (model 6, ties² \times SU: $\beta = -0.15$, $p < 0.05$), indicating that the curvilinear effect is much stronger when structural uncertainty is high (Aiken and West 1991). These results support Hypothesis 2b but reject Hypothesis 2b_{alt}.

Similarly, we depict the effects of ties on ROA for low and high levels of structural uncertainty. As Figure 2b, Part (1) shows, for domestic firms, the positive relationship between ties and ROA is stronger when uncertainty is high (simple slope $b = 0.10$, $p < 0.01$) than when it is low ($b = 0.04$, $p > 0.10$). Part (2) of Figure 2b suggests ties have a stronger inverted U-shaped effect on ROA with a higher level of uncertainty. In other words, the positive effect of ties endures much longer when structural uncertainty is high. In summary, managerial ties have a greater effect on improving

firm performance for higher than for lower levels of structural uncertainty.

Effects of controls. As we show in Table 2, firm size relates negatively to ROA for both domestic and foreign firms. Small firms may fit the dynamic Chinese environment better than large firms; because large firms are more bureaucratic, they cannot adapt as quickly to changes in the external environment and therefore suffer poorer financial performance. Firm age and industry type have no significant bearings on ROA. Similar to Matsuno *et al.*'s (2002) findings, entrepreneurship orientation has a positive effect on performance for foreign firms, suggesting that foreign firms should be more risk taking to adapt to the dynamic Chinese market. Consistent with the logic that competition erodes firm profitability (Porter, 1985), a highly competitive market relates negatively to performance for both domestic and foreign firms.

DISCUSSION

Prior conceptual and empirical work shows that ties function as a social lubricant, easing coordination and facilitating firm performance: that is, ties matter. Our study advances extant literature by investigating a more complex set of propositions that suggests the value of ties depends on sources of firm ownership (domestic or foreign) and market heterogeneity and therefore may not be equally valuable. We choose China as our research context because the central influence of government and the long tradition of tie utilization make it unclear whether foreign firms can extract as much value

from ties as domestic firms can and whether competition and uncertainty erode the value of ties, as predicted by the market efficiency logic.

Overall, our results endorse the position that though ties still matter, their value is dependent on several factors. While foreign firms tend to use ties to a similar extent as do local firms, their performance gains differ: foreign firms experience diminishing returns (e.g., an inverted U-shaped relationship) from tie utilization, whereas domestic firms enjoy a positive monotonic function, demonstrating a liability of foreignness. We further find that competition and uncertainty have different moderating effects on firm performance. Consistent with the efficient market logic, ties confer less value as competition intensifies. In contrast to this logic (but consistent with the social capital view), ties have a stronger impact on performance when structural uncertainty increases. Overall, these contingencies offer a more refined understanding of the situations and reasons that ties enable firms to gain competitive advantages and superior performance in China.

Managerial ties for foreign vs. domestic firms

Prior empirical work shows that ties are a significant driver of superior performance in China (Li, 2005; Peng and Luo, 2000). Relatedly, some argue that ties are an important source of competitive advantage for foreign firms (Tsang, 1998), because they offer a mechanism foreign entrants can use to understand and adapt to complex external environments (Boisot and Child, 1999; Ring *et al.*, 1990). Consistent with this absorption perspective, we find that foreign firms' use of ties mirrors that of domestic firms, suggesting that foreign firms have assimilated this dominant and pervasive aspect of China's institutional environment and culture.²

More novel and revealing, however, is our finding that though foreign firms use managerial ties to the same extent that domestic firms do, foreign firms suffer a comparative disadvantage in extracting value from their tie utilization: ties have a linear, positive effect on performance for domestic firms but a curvilinear, inverted U-shaped effect for foreign firms. This disadvantage likely arises from political, cultural, and organizational factors. Because the Chinese government desires competitive domestic firms (Nolan, 2001), domestic firms

tend to receive more favorable access, information, and resources from their political ties than do foreign firms. Cultural differences between foreign and domestic firms in China, most notably their long- versus short-term orientations, probably affect relationship quality (Dunning, 1998). These cultural differences increase strategic and operational conflicts, thereby eroding tie quality and its value. Tie-based practices may be inconsistent with the market-based routines deeply entrenched in foreign firms, which make them less willing or able to comply with requests or use information from their ties, leading to diminishing returns from such ties.

Our findings offer some new insights on how ties help foreign firms overcome a liability of foreignness. We suspect that ties can initially help firms assimilate the new environment, become more legitimate, and increase their chances of survival. However, ties do not completely remove obstacles associated with being a foreign firm. Our results show that ties increase return generation only up to a certain level: an inverted U-shape exists between tie utilization and ROA. These results also inform the rather large literature on multinationality and performance, which posits multinational firms should realize superior performance because of superior size, scope, and learning. Empirical support for this position, however, is mixed with studies showing a U-shaped, inverted U-shaped, and an S-curved relationships between multinationality and ROA (Annavarjula and Beldona, 2000; Contractor, Kundu, Hsu, 2003). Recent work further argues that disentangling the unique effects and factors underlying geographic scope may help reconcile these disparate results (Goerzen and Beamish, 2003; Contractor *et al.*, 2003). Our inverted U-shaped finding for foreign firms supports this more microanalytical logic. In particular, our finding implies that when multinational companies enter countries that depend on connections and ties to conduct business, they may realize an upper-bound on returns, but possibly a declining return from the highest level of investment in ties. Further work is needed to examine country differences in the value of ties, especially as they relate to a liability of foreignness and the ultimate value a firm can extract from its multinational strategy.

² We thank an anonymous reviewer for suggesting this insight.

The contingent effects of market forces

As markets emerge and grow in China, competition and structural uncertainty increasingly challenge managerial decisions and firm outcomes (Hoskisson *et al.*, 2000). The market efficiency logic posit that managerial ties may become less effective for coordinating information and transactions (Guthrie, 1998; North, 1990; Peng, 2003). Our findings partially endorse this position. As competition intensifies, the performance gains derived from ties shift from beneficial to neutral for domestic firms and from beneficial to potentially detrimental for foreign firms (see Figure 2a). Thus, ties become less valuable as markets become more competitive. In highly competitive markets, firms that pay excessive fees to build political ties and support local government projects probably cannot pass on this extra cost in the form of higher prices, so their profits may erode. Moreover, the benefits of managerial ties may decline because the information they coordinate becomes redundant in competitive markets. We further suspect that the traditions that underlie the continued use of ties are too costly (e.g., reluctance to try a new, low-cost supplier) and access to resources is no longer useful. When firms cannot pass costs on to customers in the form of higher prices, competitive forces will punish those with inefficient business practices. To mitigate such an outcome, firms should consider more arm's-length relationships based on instrumental and economic needs rather than remaining committed to prior relationships (Hite and Hesterly, 2001). But moving away from committed relationships appears difficult; for our sample of firms, we find no significant correlation between tie utilization and competitive intensity (see Table 1).

However, consistent with a social capital perspective (Boisot and Child, 1996), we find that as uncertainty increases, firms realize a greater return from managerial ties. We infer that ties foster firm performance because they broker trusted information that enables firms to better plan how to adapt to external constraints (Keister, 2001). Ties can also reduce uncertainty through favors, such as access to resources or favorable pricing, which further enable firm performance. These results extend recent empirical work that argues firms tend to reinforce relationships with existing parties in response to high levels of market uncertainty (e.g., Beckman, Haunschild, and

Phillips, 2004) and realize higher returns from tie utilization. Our results are contrary to the market efficiency logic, which states that under uncertainty, personal ties lock-in transactions to existing knowledge and business methods, and therefore make it difficult to capture or respond to uncertain environments. It is possible that deeper levels of radical, non-incremental change, as in technological discontinuity, is required to observe the negative lock-in effect of ties (e.g., Afuah, 2000; Mitchell and Singh, 1996). In our study, we use a broad aggregate measure of uncertainty—namely, volatility in total output, sales, and profits. Further work should measure technological change to examine this logic more closely.

Managerial implications

Our findings also provide some important managerial implications. The traditional wisdom for globalization is that firms will generate greater returns from a multinational strategy: that is, firm performance increases as a function of the level of internationalism or geographic scope. Our study, however, warns that return generation may be more complex than this, and that foreign entrants may not be able to easily overcome political or social obstacles that constrain or may even damage returns. While our results show that foreign firms tend to build strong network ties with local business and political authorities in their attempts to overcome the liability of foreignness and to achieve success, our results further caution that they should not rely on ties too heavily, otherwise they will experience declining returns. Thus, our curvilinear effect provides an obvious warning to foreign firms about the value of ties: high levels of managerial tie utilization will damage their ability to be profitable in the marketplace (see Figure 1). These results imply that foreign firms should consider alternative strategic choices for competing in emerging economies, whether by leveraging their global resources or customizing their operations to the particular country (Boisot and Child, 1999; Ring *et al.*, 1990). Our results also suggest that foreign firms need to be astute in their hiring practices: host-country nationals with international experience and a moderate level of connections are more likely to facilitate value-creation than expatriates that lack host-country experience and connections in China—a country in which the type of

connection or *guanxi* will confer a different level of tie quality and thus influence (Chen, 2001).

In contrast, domestic firms are encouraged to develop managerial ties as tie utilization plays a significant role in enhancing its performance. We suspect this advantage will continue as long as domestic firms occupy a favored-political status. However, even for domestic firms, the benefits of ties are not unconditional. For both domestic and foreign firms, tie utilization does not appear to generate economic value in conditions of high competitive intensity or low structural uncertainty. Therefore, managers should be wary of cultivating ties and connections to achieve better performance as competition increases or industrial conditions are stable—when these conditions exist, managers should rely on impersonal market institutions, such as contracts, courts, and competitive forces to coordinate exchanges.

CONCLUSIONS

Our theoretical approach and empirical results contribute to the literature in two major ways. First, our study offers new insights to international management literature by showing that though foreign firms can infiltrate the Chinese market, they appear unable to realize the same benefits from their managerial ties as domestic firms do. These findings suggest that ties may not fully mitigate a liability of foreignness, and offer possible explanations for why some firms experience negative returns as their level of multinationality increases. Second, our study enriches the development of a contingent view of social network theory by exploring conditions in which managerial ties enhance or hinder performance. In this sense, our analysis of the curvilinear effect of ties extends social network theory, which focuses overly on positive outcomes of ties but neglects serious negative consequences (Batjargal and Liu, 2004). Our investigation of the moderating role of market forces shows that the relationships between tie utilization and returns are more complex than previously thought. Depending on different market conditions, ties can be associated with ‘costs’ (e.g., when markets are competitive) as well as ‘benefits’ (e.g., when structural uncertainty exists).

Our results must be interpreted in light of the limitations of this study. First, because we limit our measurement to a firm’s use of managerial

ties, we cannot account fully for the specific function of ties (e.g., information exchange, access to operational resources, financial resources) or the underlying hierarchy or power dependencies (e.g., structural holes, indirect ties, direct ties) within the network. Second, we infer that high levels of competition imply the normative use of more market-based mechanisms and legal institutions that coordinate and govern exchange; however, we do not directly measure these institutions. Third, ties likely develop and change over time, and though our study captures the causal link between managerial ties and firm performance, it does not address changes in networks or how such changes might affect performance. A longitudinal design is necessary to tackle this intriguing issue. Fourth, we suspect that foreign firms experience diminishing returns for high levels of tie utilization because of political, cultural, and organizational differences. Further work should determine how these mechanisms might limit the returns of tie utilization. Related, our findings show that foreign firms actively play the local game by using tie-based strategies. But it is not clear how such strategies interact with the market-based strategies traditionally employed by foreign firms. Additional research should assess the interplay of network- and market-based strategies and their joint effects on organizational performance.

Given that the political, social, and legal institutions in emerging economies are often complex, idiosyncratic, and dynamic, understanding how to strategize in emerging markets presents critical challenges. Our study informs this intriguing topic by showing how managerial ties interact with market heterogeneity to affect performance of domestic and foreign firms in China. We hope that further research continues to explore and document institutional changes, strategic choices, and their performance implications in emerging economies.

ACKNOWLEDGEMENTS

The authors thank the editor, Professor Dan Schendel, the two anonymous reviewers, and Mike Peng for their insightful and constructive comments on earlier versions. The study was supported by the Strategic Research Grant from City University of Hong Kong (Grant No. 7002147).

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APPENDIX: MEASUREMENT ITEMS AND VALIDITY ASSESSMENT

Managerial ties: Second-order indicator, composite reliability = 0.75	Standardized loading
Business ties: First-order indicator, composite reliability = 0.71	0.773
During the past three years, top managers at our firm have heavily utilized personal ties, networks, and connections with	
1. Top managers at buyer firms.	0.593
2. Top managers at supplier firms.	0.772
3. Top managers at competitor firms.	0.829
Political ties: First-order indicator, composite reliability = 0.88	0.838
During the past three years, top managers at our firm have heavily utilized personal ties, networks, and connections with	
1. Political leaders in various levels of the government.	0.721
2. Officials in industrial bureaus.	0.920
3. Officials in regulatory and supporting organizations such as tax bureaus, state banks, commercial administration bureaus, and the like.	0.882
Entrepreneurial orientation: composite reliability = 0.71	
1. When it comes to problem solving, we value creative new solutions more than the solutions of conventional wisdom.	0.819
2. Our top managers encourage the development of innovative marketing strategies, knowing well that some will fail.	0.627
3. We firmly believe that a change in market creates a positive opportunity for us.	0.677
4. We tend to talk more about opportunities rather than problems.	0.593
Model fit: $\chi^2(32) = 82.9$, $p < 0.01$; GFI = 0.945, CFI = 0.940, IFI = 0.941; RMSEA = 0.07	
Note: Respondents answered these questions in terms of the previous three years	